

A 'match made in heaven'

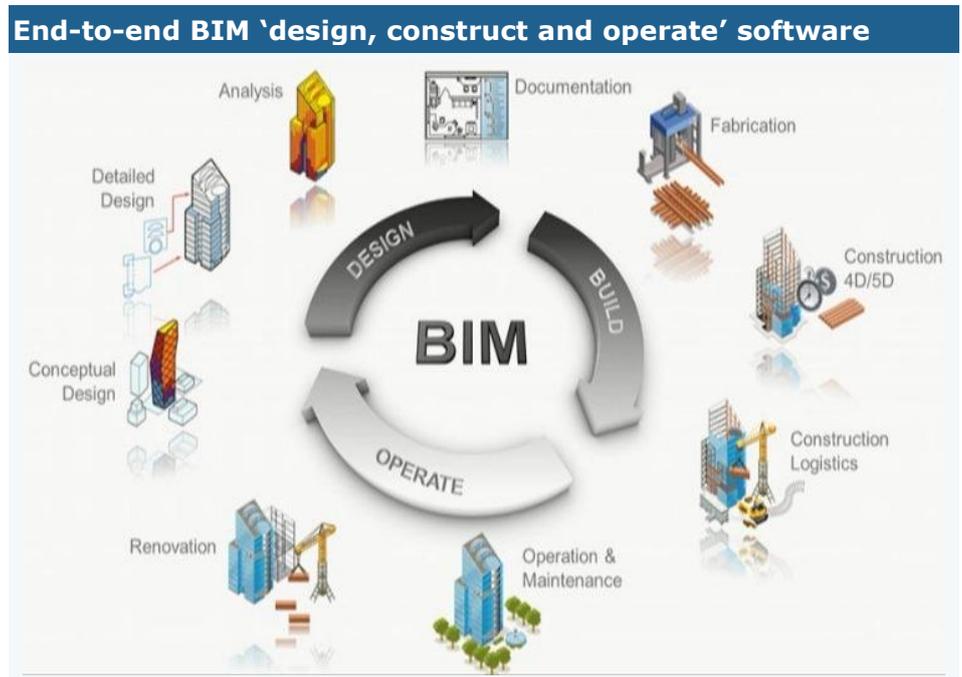
5 July, 2018

M&A is a bit like 'panning for gold'. Most prospectors lose money, but the successful ones do the homework, know where to look and crucially understand their markets inside out. Similarly, we think Elecosoft - following its 'transformational' £2.4m acquisition of BIM (Building Information Modelling) SaaS provider, ICON back in October 2016 - has done it again.

Announcing this morning that it has purchased Shire Systems Limited, a leading UK computerised maintenance management software (CMMS) developer based in Southampton, for £5.1m on a cash/debt free basis. Corresponding to modest 2018 EV/sales, EV/EBIT and PE multiples of circa 2.5x, 6.5x and 8.0x respectively - compared to the sector on 3-5x, 15-25x and 20-30x (see overleaf).

Modest price plus substantial upside synergies

So why are we excited? Well, **the transaction is important on several fronts**. Not least because it materially enhances Elecosoft's capabilities in CMMS, used for say preventative maintenance plans of plant & equipment and facilities management (FM) - shown below under 'operate'.



Source: Internet

What's more, coupled with ICON's cutting-edge BIM solution and the firm's other leading applications (eg PowerProject, BidCon, e-sign, etc), we reckon that there are not only considerable up/X-selling opportunities (Shire has >800 active customers serving numerous industries), but also that strategically Shire will greatly expand the group's post construction expertise.

In turn, offering clients substantial synergies, especially as BIM becomes more ingrained within the FM world.

Company Data

EPIC	AIM: ELCO
Price (last close)	75p
52 week Hi/Lo	91p/41p
Market cap	£58m
ED valuation	90p/share
Avg. daily volume	70k

Share Price, p



Source: Web Financial

Description

Elecosoft is a **developer of on-premise and Cloud/SaaS software** for the Architectural, Engineering, Construction and Operator (AECO) and digital marketing industries. Its award winning 6D solutions (>100,000 users) cover project planning, estimating, design/CAD, visualisation, site operations and Building Information Management (BIM). **BIM acts as the essential lubricant to oil all the connecting parts.**

There are 201 staff: 50 are software engineers, 59 are in client support and 55 sales/marketing. **Visibility is robust with 49% of 2017 revenues recurring maintenance, ~10% SaaS and 90%+ customer retention rates.** Landmark implementations are: The Shard, the BBC Television Centre, Hong Kong International Airport and Berlin's Reichstag Dome.

Next News: H1'18 pre-close update in July

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Here for instance, landlords will be able to manage their property portfolios (Re IoTs) far more efficiently and cheaply by leveraging Elecosoft’s end-to-end software suite and extensive BIM datasets, captured during the original design/construction phase.

Raising forecasts and valuation to 90p/share

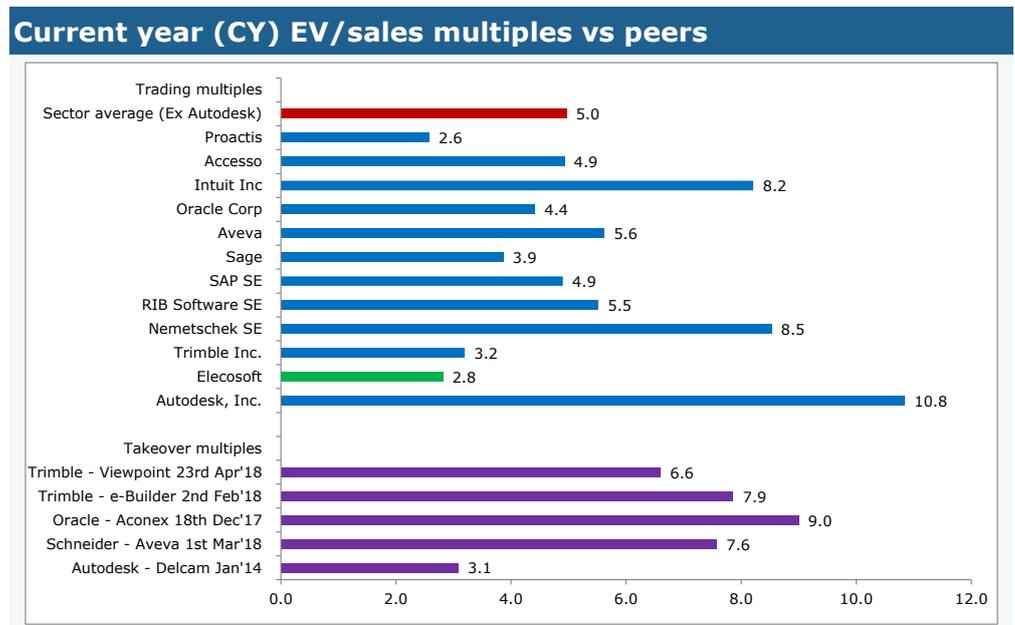
In terms of the numbers, Shire delivered normalised PBT of £0.7m in 2017 on turnover of £1.9m – and YTD is tracking at a slightly higher run-rate of £0.4m and £1.0m for Jan-May’18. Consequently, given this and the newly increased debt facility (from £2m to an £8m 5 year term loan) with Barclays Bank, the Board believes the acquisition **“will be earnings enhancing in H2’18”**.

As such, **we have upgraded our PBT estimates for this year and next** to £3.4m (£3.3m before) and £4.0m (£3.8m) – along with **lifting the valuation from 85p to 90p/share**.

Executive Chairman John Ketteley adding: *"The acquisition of Shire Systems represents another significant milestone in the development of Elecosoft as a leading provider of co-ordinated BIM-led software systems for the construction industry. The addition of Shire Systems computerised maintenance management software to Elecosoft's existing software portfolio will enable Elecosoft to provide construction companies and property investors with a CMMS solution."*

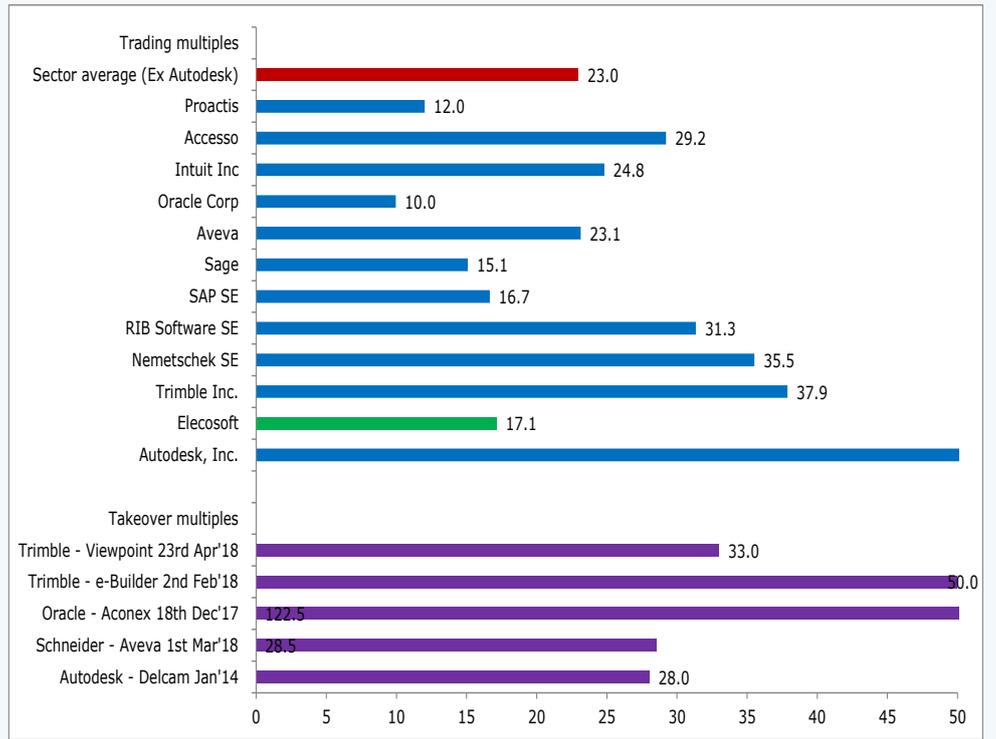
Strategically, Shire appears to be a perfect fit

In our view, today’s acquisition could ultimately generate synergies many multiples higher than the £5.1m price tag. Plus, we understand Shire has an impressive management team, which should assist the integration process, and longer term help shape the future direction of the business as a whole.



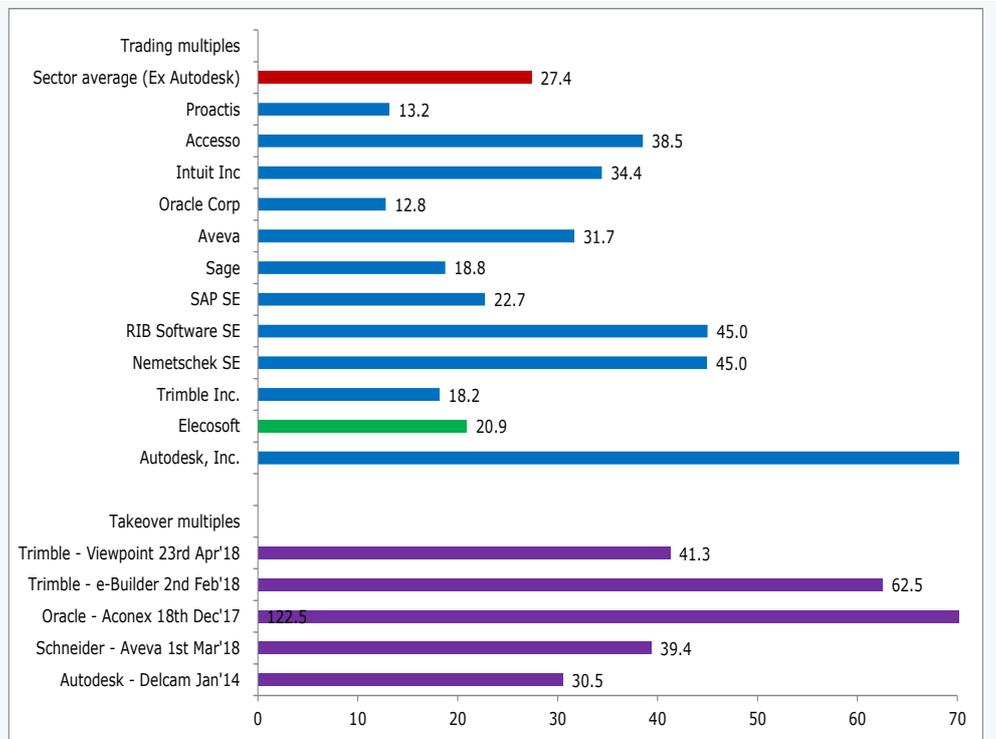
Source: Equity Development, various sites – closing prices as at 4th July 2018

CY EV/EBIT vs peers and M&A multiples



Source: Equity Development, various sites – closing prices as at 4th July 2018

CY PERs vs peers and M&A multiples



Source: Equity Development, various sites – closing prices as at 4th July 2018

Summary financial projections

Elecosoft (Dec yearend)	2014 Act £'000s	2015 Act £'000s	2016 Act £'000s	2017 Act £'000s	2018 Est £'000s	2019 Est £'000s	2020 Est £'000s	2021 Est £'000s	2022 Est £'000s	2023 Est £'000s	2024 Est £'000s
Software licenses (Incl SaaS)	4,008	4,536	4,955	5,775	6,079	6,626	7,422	8,312	9,310	10,427	11,678
Support and maintenance	7,351	7,278	8,622	9,856	10,375	11,309	12,666	14,186	15,889	17,795	19,931
Services	3,813	3,446	4,218	4,365	4,595	4,837	5,092	5,360	5,643	5,940	6,253
Shire - maintenance/FM software					950	2,090	2,341	2,622	2,936	3,289	3,683
Turnover	15,172	15,260	17,795	19,996	22,000	24,863	27,521	30,481	33,778	37,451	41,545
% growth	-7.0%	0.6%	16.6%	12.4%	10.0%	13.0%	10.7%	10.8%	10.8%	10.9%	10.9%
Gross Profit	13,314	13,572	15,560	17,575	19,236	21,740	24,064	26,652	29,535	32,747	36,327
% margin	87.8%	88.9%	87.4%	87.9%	87.4%	87.4%	87.4%	87.4%	87.4%	87.4%	87.4%
Adj. EBITDA (post SBPs)	1,465	1,795	2,753	3,643	4,567	5,392	6,243	7,220	8,338	9,620	11,087
% Margin	9.7%	11.8%	15.5%	18.2%	20.8%	21.7%	22.7%	23.7%	24.7%	25.7%	26.7%
Adj. EBIT (post SBPs)	1,266	1,506	2,207	2,773	3,610	4,310	5,046	5,893	6,869	7,990	9,279
% Margin	8.3%	9.9%	12.4%	13.9%	16.4%	17.3%	18.3%	19.3%	20.3%	21.3%	22.3%
Adj. Profit before Tax	1,046	1,386	2,117	2,666	3,400	4,000	4,786	5,683	6,709	7,990	9,279
Adjusted EPS (p)	1.3	1.5	2.4	2.9	3.6	4.2	4.9	5.8	6.8	8.1	9.3
EPS growth rate		20.1%	58.2%	20.2%	25.0%	16.3%	17.6%	18.2%	17.5%	18.5%	15.6%
Dividend (p)	0.0	0.0	0.4	0.6	0.9	1.0	1.2	1.4	1.7	2.0	2.3
Yield			0.5%	0.8%	1.2%	1.4%	1.6%	1.9%	2.3%	2.7%	3.1%
Recurring maintenance % sales	48.5%	47.7%	48.5%	49.3%	47.2%	45.5%	46.0%	46.5%	47.0%	47.5%	48.0%
Adjusted cash conversion		55.0%	69.8%	102.2%	85.0%	83.1%	84.3%	85.5%	86.4%	87.3%	88.1%
Valuation benchmarks											
P/E ratio	59.7	49.7	31.4	26.2	20.9	18.0	15.3	12.9	11.0	9.3	8.0
EV/Sales	4.1	4.1	3.5	3.1	2.8	2.5	2.2	2.0	1.8	1.7	1.5
EV/EBITDA	42.2	34.5	22.5	17.0	13.6	11.5	9.9	8.6	7.4	6.4	5.6
EV / EBITA	48.9	41.1	28.0	22.3	17.1	14.4	12.3	10.5	9.0	7.7	6.7
Adjusted tax rate	-20.0%	-19.5%	-16.1%	-17.9%	-17.5%	-18.0%	-19.0%	-19.0%	-19.0%	-19.0%	-19.0%
EBITDA drop through rates			37.8%	40.4%	46.1%	28.8%	32.0%	33.0%	33.9%	34.9%	35.8%
Dividend cover			6.0	4.8	4.0	4.0	4.0	4.0	4.0	4.0	4.0
PEG ratio		2.47	0.54	1.30	0.84	1.10	0.87	0.71	0.63	0.50	0.52
Net cash/(debt)	-2,035	-803	-1,304	1,031	-2,800	-1,132	919	3,445	6,516	10,281	14,736
Sharecount (Ks)	66,611	73,971	74,433	76,309	78,244	78,635	79,029	79,424	79,821	80,220	80,621
Shareprice (p)	75.0										

Source: Company historic data, Equity Development estimates

Key risks

- Substantial slowdown in global GDP which could impact the worldwide property, construction and infrastructure markets.
- Anticipated growth/profitability may take longer than envisaged, cost more or not be fully realised.
- Larger license deals can lead to lumpy revenues, albeit this is being equally balanced by recurring revenues from support/maintenance (49% 2017) and another ~10% from SaaS contracts.
- Foreign exchange. However, this is primarily a translation risk with >66% of Elecosoft's turnover being generated outside the UK.
- Regulatory and tax changes.
- Competition may intensify due to new/existing players.
- Being relatively small, Elecosoft could get squeezed by larger rivals, partners and customers.
- Generic risks of retention/recruitment of key staff, etc.
- Potential (yet small) impact from implementing the new "FRS15 sales recognition" accounting standard from 1st Jan'18.
- As with many smallcap AIM stocks, daily trading volumes can occasionally decline, particularly during seasonally quieter periods and/or between newsflow.



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