

PSI AG

Germany / Software
 Primary exchange: Frankfurt
 Bloomberg: PSAN GR
 ISIN: DE000A0Z1JH9

Q3/9M 2019 results

RATING
PRICE TARGET **ADD**
 € 22.40
 Return Potential 17.3%
 Risk Rating Medium

CLIMATE PROTECTION INVESTMENTS ARE MAIN GROWTH DRIVER

Highlights of a strong set of Q3/9M 2019 results were double digit rises in orders and sales at the Energy Management division's electrical energy and oil and gas businesses during the first nine months of the year. One of the main drivers of growth at PSI's electrical energy business is investment in smart grids to accommodate the increasing proportion of electricity generated in Germany through renewable energy sources. 36% of electricity consumed in Germany derived from renewable sources in 2017. The German government's recently published Climate Protection Programme 2030 outlines measures to promote the achievement of a figure of 65% by 2030. Meanwhile, the decision taken earlier this year to cease coal production in Germany by 2038, is boosting investment in PSI's gas network control systems. The order intake in the public transport business was down during the first nine months of 2019 due to an unusually high order figure of €11.4m during 9M/18. However, investments planned by the German government to improve the attractiveness of public transport and electrify the bus fleet suggest a bright future for this business. Against this background we now see Energy Management sales growing at a three year CAGR of 7.0% over the period 2019-2022 (previously 4.4%). Our new price target is €22.40 (previously: €19.00). We maintain our Add recommendation.

9M/19 order intake up despite high prior year public transport bookings
 Q3/19 sales climbed 13.0% to €53.1m (Q3/18: €47.0m) while EBIT came in at €4.0m (Q3/18: €3.9m). Both sales and EBIT were close to our expectations. Stripping out the BTC Smart-Grid division which was acquired on 1 January 2019, Q3/19 sales rose 8.3% to €50.9m while EBIT was €4.3m. The Q3/19 order intake was €40m (Q3/18: €41m) and €182m after nine months (9M18: €176m). The order intake was higher after nine months despite the high order volume in the public transport business in the prior year period. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2017	2018	2019E	2020E	2021E	2022E
Revenue (€m)	186.10	199.16	220.11	232.38	246.48	261.45
Y-o-y growth	5.2%	7.0%	10.5%	5.6%	6.1%	6.1%
EBIT (€m)	13.37	15.45	16.53	20.40	22.80	25.81
EBIT margin	7.2%	7.8%	7.5%	8.8%	9.3%	9.9%
Net income (€m)	9.50	10.59	11.39	14.24	16.31	18.83
EPS (diluted) (€)	0.61	0.68	0.73	0.91	1.04	1.21
DPS (€)	0.23	0.25	0.27	0.29	0.42	0.48
FCF (€m)	-2.92	11.57	0.98	11.22	13.39	15.82
Net gearing	18.7%	9.8%	35.6%	25.1%	16.4%	9.0%
Liquid assets (€m)	38.13	44.58	40.62	47.60	56.44	65.69

RISKS

Risks include a renewed downturn in the prices of oil, gas and steel.

COMPANY PROFILE

PSI makes software control systems, primarily for energy, utility companies and metals producers. Customers also include manufacturers and the operators of transportation networks. The company's control system products are widespread in its core German market.

MARKET DATA

As of 05 Nov 2019

Closing Price	€ 19.10
Shares outstanding	15.70m
Market Capitalisation	€ 299.82m
52-week Range	€ 15.45 / 19.20
Avg. Volume (12 Months)	6,185

Multiples	2018	2019E	2020E
P/E	28.2	26.2	20.9
EV/Sales	1.5	1.4	1.3
EV/EBIT	20.0	18.6	15.1
Div. Yield	1.3%	1.4%	1.5%

STOCK OVERVIEW



COMPANY DATA

As of 30 Sep 2019

Liquid Assets	€ 30.80m
Current Assets	€ 127.73m
Intangible Assets	€ 64.26m
Total Assets	€ 235.82m
Current Liabilities	€ 67.67m
Shareholders' Equity	€ 90.36m

SHAREHOLDERS

InvAG für langfristige Investoren TGV	20.7%
Innogy SE	17.8%
Management and employees	15.0%
Harvinder Singh	8.1%
Free float and other	38.4%



Figure 1: Q3/19 results versus our forecasts

€ 000s	Q3 19A	Q3 19E	Δ Q3 19A vs. Q3 19E	Q3 18A	Δ Q3 19A vs. Q3 18A
External sales	53,086	53,000	0.2%	46,984	13.0%
<i>by division:</i>					
Energy Management	27,812	27,500	1.1%	22,000	26.4%
Production Management	25,274	25,500	-0.9%	24,984	1.2%
EBIT	4,001	4,000	0.0%	3,852	3.9%
margin	7.5%	7.5%		8.2%	
<i>by division:</i>					
Energy Management	1,928	1,800	7.1%	1,766	9.2%
<i>margin</i>	<i>6.7%</i>	<i>1.8%</i>		<i>7.7%</i>	
Production Management	2,551	2,600	-1.9%	2,316	10.1%
<i>margin</i>	<i>9.2%</i>	<i>2.3%</i>		<i>8.5%</i>	
Reconciliation	-478	-400		-230	
EPS (€)	0.18	0.18	0.0%	0.16	12.5%

Source: PSI AG; First Berlin Equity Research estimates

BTC Smart-Grid activities expected to contribute positively in Q4/19 Sales in the Energy Management segment (energy networks, energy trading, public transport) climbed 26.4% to €27.8m in Q3/19 (Q3/18: €22.0m) while EBIT rose to €1.9m (Q3/18: €1.8m). Without the BTC Smart-Grid activities, Q3/19 sales and EBIT would have been €25.6m (+16.4%) and €2.2m respectively. The order intake at the electrical energy business within Energy Management rose by 20% in 2018 and at a double digit rate during the first nine months of 2019. PSI acquired the BTC Smart-Grid division to secure sufficient capacity to work through this order intake. 160 new employees were added through the acquisition. 70 of these are currently working in the electrical energy business' new INFRA division (integrated municipal utilities, infrastructure, industry). Most of the others are working for other electrical energy businesses such as Transmission System Operators and Rail (very high voltage and rail electricity networks), Distribution System Operators (medium and high voltage) and Municipal Utilities (low voltage and multi-utility network control). The cost of integrating/retraining the new employees meant that the new business' contribution to EBIT was €-1.1m in Q1/19, €-0.7m in Q2/19 and €-0.3m in Q3/19. However, management expects it to make a positive contribution in Q4/19.

Coal exit and resurgence of Russian activity boost oil and gas business The oil and gas business within Energy Management also saw a double digit rise in sales during Q3/19 and 9M/19. The German government's decision that coal production in Germany should cease by 2038 at the latest is leading to increased investment in gas networks. Meanwhile, PSI is also benefiting from the return of Russia as a significant source of business. Between 2015 and 2018 sales to Russia almost came to a standstill due to a government-imposed moratorium on the purchase of western software.

Energy Management's Q3/19 performance was also helped by a breakeven result at the energy trading business. Energy trading's figures were in the red during the first half of 2019 due to investment in pilot projects to replace a competitor system. The public transportation business booked an unusually high order intake of €11.4m during the first nine months of 2018 due mainly to a €7m order from the Berlin public transport company, BVG. PSI booked some strategically important orders during 9M/19 including an export order for charging management of electric buses in Q3/19. However, order volume fell short of the 9M/18 total.

Rising U.S. and Chinese activity compensate for lower European orders at PSI Metals Production Management sales climbed 1.2% to €25.3m in Q3/19 (Q3/18: €25.0m) while segment EBIT came in at €2.6m (Q3/18: €2.3m). We gather that Q3/19 order intake, sales and profitability were roughly flat at PSI Metals as growing business volume from the U.S. and China was cancelled out by reduced activity in Europe.

In the U.S. tax cuts and tariffs on imported steel have prompted investment in the domestic industry, while PSI's business in China is benefiting from a state-led investment programme to renew steel plants. In Europe investment is down due to growing imports and uncertainty about the outcome of ongoing tariff negotiations.

Sales in Production Management's logistics business area were up ca. 25% during 9M/19 and EBIT climbed by more than 30%. Meanwhile, automotive and industry sales climbed 10% during the first nine months of 2019 and EBIT was also up by over 30%. The Mines and Roads business burdened EBIT by around €0.3m during 9M/19. The mining part of the business incurred the costs of a transition to a lower risk integration partner-based business while the roads business is currently engaged in several traffic management pilot projects.

Net gearing excluding leasing liabilities stable versus a year ago Net cashflow from operations was up 78.8% at €4.3m in Q3/19 (Q3/18: €2.4m) but was down 52% at €3.7m (Q3/18: €7.8m) at the nine month stage. The divergence is attributable to a €13m increase in working capital in Q2/19 of which net receivables relating to long term contracts were the main element. Cash outflow from investing increased to €7.2m after nine months (9M/18 €4.1m) due mainly to the acquisition of the BTC Smart-Grid division for €3.5m. Cash outflow from financing climbed to €8.4m (9M/18 €5.4m) because of the inclusion of lease liability interest and principle payments totalling a combined €3.5m in connection with IFRS16. Net debt including pension liabilities and leasing liabilities was €42m at the nine month stage equivalent to net gearing of 46.5%. PSI has not provided proforma figures for 2018 including leasing liabilities. If leasing liabilities are excluded from the numbers, 9M/19 net debt was €20.3m, equivalent to net gearing of 22.5% (9M/18: net debt of €15.6m, equivalent to net gearing of 18.8%).

Price target raised to €22.40 (previously: €19.00). Add recommendation retained

Figure 2 shows the impact of the changes to our forecasts for the Energy Management division on our overall group projections. We continue to expect the group EBIT margin to rise over the next three years as R&D costs and cost of goods sold fall as a percentage of sales with the completion of software platform harmonisation. Our new price target is €22.40 (previously: €19.00). We maintain our Add recommendation.

Figure 2: Changes to our forecasts

€m	2019			2020			2021			2022			2019-2022 CAGR	
	New	Old	Δ %	New	Old	Δ %	New	Old	Δ %	New	Old	Δ %	New	Old
External sales	220.1	220.1	0.0%	232.4	227.8	2.0%	246.5	239.1	3.1%	261.5	251.2	4.1%	5.9%	4.5%
by division:														
Energy Man.	115.7	115.7	0.0%	123.8	119.2	3.9%	132.4	125.1	5.9%	141.7	131.5	7.8%	7.0%	4.4%
Production Man.	104.4	104.4	0.0%	108.6	108.6	0.0%	114.0	114.0	0.0%	119.7	119.7	0.0%	4.7%	4.7%
Total EBIT	16.5	17.1	-3.6%	20.4	19.4	4.9%	22.8	21.7	5.0%	25.8	24.1	6.9%	16.0%	12.1%
margin (%)	7.5%	7.8%	-	8.8%	8.5%	-	9.3%	9.1%	-	9.9%	9.6%	-	-	-
by division:														
Energy Man.	7.4	7.7	-4.4%	10.6	9.2	15.0%	12.0	10.5	13.7%	13.8	11.9	16.4%	23.3%	15.5%
margin (%)	6.2%	6.5%	-	8.3%	7.5%	-	8.8%	8.2%	-	9.5%	8.8%	-	-	-
Production Man.	10.7	10.9	-1.7%	11.7	11.9	-1.5%	13.0	13.0	-0.4%	14.4	14.3	0.5%	10.4%	9.6%
margin (%)	9.4%	9.6%	-	9.9%	10.1%	-	10.4%	10.5%	-	11.0%	11.0%	-	-	-
Reconciliation	-1.6	-1.5	-	-1.9	-1.7	-	-2.1	-1.9	-	-2.4	-2.1	-	-	-
EPS (€)	0.73	0.75	-2.8%	0.91	0.87	4.8%	1.04	0.99	5.5%	1.21	1.13	6.7%	18.2%	14.6%

Source: PSI AG; First Berlin Equity Research estimates



Figure 3: Valuation model

€000s	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
Net sales	220,108	232,383	246,478	261,451	274,523	288,249	302,662	316,154
NOPLAT	11,573	14,279	15,962	18,069	18,679	20,127	21,457	22,913
+ Depreciation and amortisation	10,308	10,206	11,318	12,006	12,606	13,237	13,898	14,518
= net operating cash flow	21,881	24,485	27,281	30,075	31,285	33,363	35,355	37,431
- total investments (Capex and WC)	-14,513	-7,334	-9,033	-9,490	-11,415	-10,064	-14,805	-10,882
Capital expenditure	-13,120	-6,195	-7,724	-8,196	-8,284	-8,699	-9,134	-9,351
working capital	-1,393	-1,140	-1,309	-1,294	-3,131	-1,365	-5,671	-1,531
= Free cash flow (FCF)	7,369	17,151	18,248	20,585	19,870	23,299	20,551	26,548
PV of FCF's	7,286	15,753	15,571	16,318	14,632	15,938	13,060	15,673

€000s	
PVs of FCFs explicit period (2019-30)*	241,181
PVs of FCFs in terminal period	153,461
Enterprise Value (EV)	394,642
Net cash/(net debt)	-42,726
Shareholder value	351,916

Value per share (€)	22.40
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WACC	7.65%
Cost of equity	9.5%
Pre-tax cost of debt	3.0%
Normal tax rate	30.0%
After-tax cost of debt	2.1%
Share of equity	75.0%
Share of debt	25.0%
Terminal growth	2.0%

Sensitivity analysis

WACC	Terminal growth rate (%)						Fair value per share
	0.5%	1.0%	1.5%	2.0%	2.5%	3.0%	
4.65%	38.73	41.39	44.89	49.71	56.78	68.15	89.45
5.65%	30.41	31.80	33.53	35.74	38.64	42.65	48.52
6.65%	24.78	25.57	26.53	27.68	29.12	30.95	33.36
7.65%	20.71	21.19	21.76	22.40	23.21	24.17	25.36
8.65%	17.64	17.95	18.30	18.70	19.17	19.72	20.37
9.65%	15.24	15.44	15.67	15.92	16.21	16.54	16.93
10.65%	13.32	13.45	13.60	13.77	13.95	14.16	14.41
11.65%	11.74	11.83	11.93	12.04	12.17	12.31	12.46

*for layout purposes the model shows numbers only to 2026 but runs until 2035

Source: First Berlin Equity Research estimates



INCOME STATEMENT

All figures in €'000	2017	2018	2019E	2020E	2021E	2022E
Revenues	186,096	199,156	220,108	232,383	246,478	261,451
Cost of materials	-27,228	-28,919	-31,916	-33,696	-35,739	-37,910
Gross profit	158,868	170,237	188,192	198,687	210,738	223,540
Total personnel costs	-112,343	-121,279	-129,864	-137,106	-145,422	-154,256
Net other operating costs	-28,809	-28,897	-31,487	-30,977	-31,195	-31,466
Depreciation & amortisation	-4,351	-4,611	-10,308	-10,206	-11,318	-12,006
EBIT	13,365	15,450	16,533	20,398	22,803	25,813
Net interest	-983	-1,061	-460	-261	279	861
Associates	142	134	141	148	155	163
Pretax profit	12,524	14,523	16,214	20,285	23,237	26,837
Income taxes	-3,027	-3,938	-4,822	-6,041	-6,925	-8,002
Net income / loss	9,497	10,585	11,392	14,243	16,313	18,835
EPS (€)	0.61	0.68	0.73	0.91	1.04	1.21
EBITDA	17,716	20,061	26,841	30,604	34,122	37,819
Ratios						
Gross margin	85.4%	85.5%	85.5%	85.5%	85.5%	85.5%
EBIT margin	7.2%	7.8%	7.5%	8.8%	9.3%	9.9%
EBITDA margin	9.5%	10.1%	12.2%	13.2%	13.8%	14.5%
Net income margin	5.1%	5.3%	5.2%	6.1%	6.6%	7.2%
Tax rate	24.2%	27.1%	29.7%	29.8%	29.8%	29.8%
Expenses as % of output						
Personnel	-60.4%	-60.9%	-59.0%	-59.0%	-59.0%	-59.0%
Net other operating income/expenses	-15.5%	-14.5%	-14.3%	-13.3%	-12.7%	-12.0%
Depreciation & amortisation	-2.3%	-2.3%	-4.7%	-4.4%	-4.6%	-4.6%
Y-o-y growth						
Total revenues	5.2%	7.0%	10.5%	5.6%	6.1%	6.1%
EBIT	12.9%	15.6%	7.0%	23.4%	11.8%	13.2%
Net income / loss	11.1%	11.5%	7.6%	25.0%	14.5%	15.5%



BALANCE SHEET

All figures in €'000	2017	2018	2019E	2020E	2021E	2022E
Assets						
Current assets, total	116,463	127,787	132,067	144,146	158,841	174,320
Cash and cash equivalents	38,132	44,579	40,617	47,597	56,436	65,694
Trade accounts and notes receivables	31,611	34,407	38,079	40,202	42,641	45,231
Inventories	7,823	8,712	9,629	10,165	10,782	11,437
Receivables relating to long term contracts	33,118	34,367	37,418	39,505	41,901	44,447
Other current assets	5,779	5,722	6,324	6,677	7,082	7,512
Non-current assets, total	77,547	80,884	111,089	113,143	116,912	120,913
Property, plant and equipment	12,531	13,592	38,522	39,360	41,747	44,283
Goodwill	48,289	48,289	52,837	52,837	52,837	52,837
Other intangible assets	8,200	10,596	11,666	12,316	13,063	13,857
Associates	150	440	581	728	884	1,046
Deferred tax assets	8,377	7,967	7,484	7,901	8,380	8,889
Other non-current assets	0	0	0	0	0	0
Total assets	194,010	208,671	243,156	257,289	275,753	295,233
Shareholders' equity & debt						
Current liabilities, total	59,679	65,960	72,014	74,974	79,521	84,449
Interest bearing debt	2,622	1,795	1,000	0	0	0
Trade accounts payable	14,564	16,440	18,269	19,288	20,458	21,700
Liabilities relating to long term contracts	13,287	16,531	18,269	19,288	20,458	21,700
Provisions	0	0	0	0	0	0
Other current liabilities	29,206	31,194	34,476	36,398	38,606	41,048
Non-current liabilities, total	54,034	56,081	77,292	78,282	80,233	82,292
Interest bearing debt	0	0	0	0	0	0
Leasing liabilities	0	0	23,000	23,500	24,926	26,440
Pension provisions	50,540	51,284	50,000	50,250	50,501	50,754
Deferred tax liabilities	3,494	4,797	4,292	4,531	4,806	5,098
Consolidated equity	80,297	86,630	93,850	104,033	115,998	128,492
Shareholders' equity	80,297	86,630	93,850	104,033	115,998	128,492
Minorities	0	0	0	0	0	0
Total consolidated equity and debt	194,010	208,671	243,156	257,289	275,753	295,233
Ratios						
Current ratio (x)	1.95	1.94	1.83	1.92	2.00	2.06
Quick ratio (x)	1.82	1.81	1.70	1.79	1.86	1.93
Equity ratio	41.4%	41.5%	38.6%	40.4%	42.1%	43.5%
Net gearing	18.7%	9.8%	35.6%	25.1%	16.4%	9.0%
Equity per share	5.12	5.52	5.98	6.63	7.39	8.19
Interest coverage ratio (x)	13.60	14.56	35.96	78.10	-81.73	-29.97
Capital employed (CE)	89,815	95,229	99,681	105,460	108,375	111,808
Return on capital employed (ROCE)	10.4%	11.4%	11.6%	13.5%	14.7%	16.2%



CASH FLOW STATEMENT

All figures in €'000	2017	2018	2019E	2020E	2021E	2022E
Pretax result	12,524	14,523	16,214	20,285	23,237	26,837
Depreciation and amortisation	4,351	4,611	10,308	10,206	11,318	12,006
Other	-1,098	-94	-11,033	-11,939	-12,132	-13,538
Operating cash flow	15,777	19,040	15,490	18,552	22,424	25,305
Investment in working capital	-14,609	-51	-1,393	-1,140	-1,309	-1,294
Net operating cash flow	1,168	18,989	14,097	17,412	21,115	24,011
Cashflow from investing	-4,089	-7,424	-13,120	-6,195	-7,724	-8,196
Free cash flow	-2,921	11,565	977	11,218	13,391	15,815
Dividend paid	-3,439	-3,596	-3,919	-4,238	-4,552	-6,557
Share buy back	-297	-422	-1,020	0	0	0
New share capital	0	0	0	0	0	0
Debt financing	2,622	-827	0	0	0	0
Other	0	0	0	0	0	0
Cash flow from financing	-1,114	-4,845	-4,939	-4,238	-4,552	-6,557
Other	-841	-273	0	0	0	0
Change in cash	-4,876	6,447	-3,962	6,980	8,839	9,258
Cash, start of the year	43,008	38,132	44,579	40,617	47,597	56,436
Cash, end of the year	38,132	44,579	40,617	47,597	56,436	65,694
Free cash flow per share in €	-0.19	0.74	0.06	0.72	0.86	1.01
Y-o-y growth						
Operating cash flow	5%	21%	-19%	20%	21%	13%
Net operating cash flow	-91%	1526%	-26%	24%	21%	14%
Free cash flow	n.m.	n.m.	-92%	1048%	19%	18%

FIRST BERLIN RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	15 July 2003	€4.96	Market Perform	€5.00
2...65	↓	↓	↓	↓
66	5 November 2018	€16.20	Add	€19.00
67	2 April 2019	€17.00	Add	€19.00
68	2 May 2019	€18.45	Add	€19.00
69	Today	€19.10	Add	€22.40

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ASSET VALUATION SYSTEM

First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

RISK ASSESSMENT

The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

INVESTMENT HORIZON

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Legally required information regarding

- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <http://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Lurgiallee 12, 60439 Frankfurt

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