

February 19th, 2018
Research Update

SMC Research
Small and Mid Cap Research



Mensch und Maschine SE

EBITDA margin in the double digits for
the first time

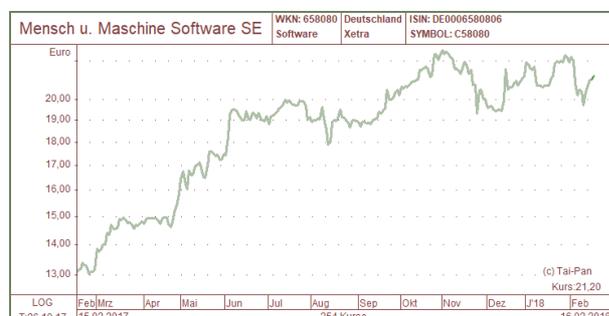
Rating: **Buy** (before: Hold) | Price: **21.20 Euro** | Price target: **25.90 Euro**

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Recent business development



Basic data

Based in:	Wessling
Sector:	CAD/CAM Software
Headcount:	784
Accounting:	IFRS
ISIN:	DE0006580806
Price:	21.20 Euro
Market segment:	Scale / m:access
Number of shares:	16.7 m
Market Cap:	353.7 m Euro
Enterprise Value:	379.0 m Euro
Free Float:	46.9 %
Price High/Low (12 M):	22.80 / 13.01 Euro
Ø turnover (12 M):	171,100 Euro

After a comparatively weak third quarter, where the negative effect of Autodesk's transition of the pricing model made itself felt for the last time in the VAR business, the fourth quarter brought the expected growth acceleration. Overall, the group's sales increased by 14.1 percent and the group's gross profit by 11.2 percent, so that despite a slight drop in sales of 3.9 percent the gross profit increased by 3.7 over the whole year. On this basis and due to a sustained cost discipline, M+M was able to considerably increase margins and to achieve a two-digit earnings growth: EBITDA increased by 14 percent, EBIT by 21.7 percent and the net profit by 29 percent. It was the first time that a two-digit margin was generated on the EBITDA level. M+M remains thus firmly on the path outlined in the course of the transition of the business model in 2011 and intends to double profits by 2020. We think that this forecast is attainable, have aligned our forecasts accordingly and see the fair value now at EUR 25.90. On this basis, we adjust our rating from most recently "Hold" to "Buy".

FY ends: 31.12.	2015	2016	2017	2018e	2019e	2020e
Sales (m Euro)	160.4	167.1	160.5	177.0	195.6	216.1
EBIT (m Euro)	8.5	12.5	15.3	19.3	22.4	26.2
Net profit	3.9	6.6	8.5	11.5	13.6	16.3
EpS	0.24	0.39	0.51	0.70	0.84	1.00
Dividend per share	0.25	0.35	0.50	0.65	0.80	0.95
Sales growth	14.5%	4.2%	-3.9%	10.3%	10.5%	10.5%
Profit growth	4.0%	70.4%	29.1%	34.7%	18.9%	19.9%
PSR	2.16	2.07	2.16	1.95	1.77	1.60
PER	89.5	52.5	40.7	30.2	25.4	21.2
PCR	23.48	23.62	22.76	21.21	18.39	16.06
EV / EBIT	43.8	29.7	24.3	19.2	16.6	14.2
Dividend yield	1.2%	1.7%	2.4%	3.1%	3.8%	4.5%

Jump in sales in the fourth quarter

According to preliminary figures, Mensch und Maschine had sales of EUR 160.5 m in the last financial year. Compared with the previous year, this is a decrease by 3.9 percent that can be attributed to Autodesk's transition of the pricing model implemented in 2016. Accordingly, the decrease affected solely the VAR business, whose sales dropped by nearly 9 percent to EUR 110.1 m. The software business, in contrast, increased considerably by 9 percent to EUR 50.4 m. This pattern had been announced by the company and was indeed to be observed already in the first three quarters. With regard to the future development and to the growth potential of the new license model, it is therefore much more interesting to look at the fourth quarter separately, which is the first one without any distorting effects from previous years. On this basis, M+M can boast a substantial sales growth to EUR 45.0 m, this time sustained to the whole extent by the VAR business. Its quarterly sales rose by 14.8 percent to EUR 30.6 m, while the software segment grew by "merely" 12.6 percent.

Gross margin reaches record high

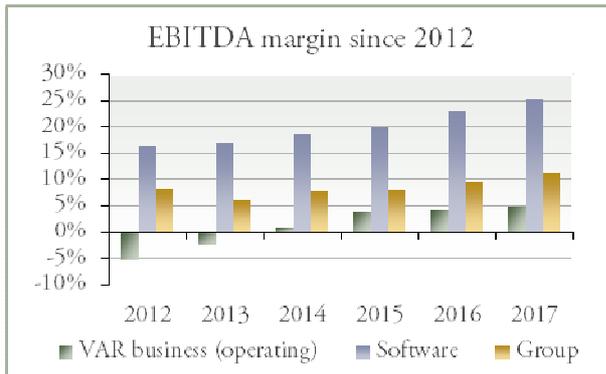
Unlike sales, the gross profit increased in the last financial year. It rose by 3.7 percent to EUR 94.8 m, meeting the company's forecast of EUR 95 m fairly exactly. Our estimate (EUR 98.7 m) had been a little more optimistic and was thus not reached. The resulting gross margin was at 59.1 percent 4.3 percentage points above previous year's figure. This is due to several effects. Firstly, the sales mix has shifted towards the software business that generates a very high gross margin at 97 percent. Secondly, the VAR business has seen an internal structure shift as well. While the gross profit from the business with services (due also to the strong demand for BIM training courses) and with proprietary software solutions rose by 16 percent to EUR 29.9 m, the gross profit contribution of the trade with Autodesk licenses decreased by nearly a quarter to EUR 16 m. Its share in the group's gross profit declined further to just 17 percent.

Business figures	FY 2016	FY 2017	Change
Sales	167.07	160.50	-3.9%
<i>VAR business</i>	120.83	110.10	-8.9%
<i>Software</i>	46.24	50.40	9.0%
Gross profit	91.43	94.80	3.7%
<i>VAR business</i>	46.70	45.90	-1.7%
<i>Software</i>	44.74	48.90	9.3%
<i>Gross margin</i>	54.7%	59.1%	
EBITDA	15.76	18.00	14.2%
<i>VAR business</i>	5.09	5.30	4.0%
<i>Software</i>	10.67	12.70	19.1%
<i>EBITDA margin</i>	9.4%	11.2%	
EBIT	12.49	15.20	21.7%
<i>EBI margin</i>	7.5%	9.5%	
Net profit	6.59	8.50	29.0%
<i>Net margin</i>	3.9%	5.3%	

Profitability considerably improved

Thanks to a sustained cost discipline, M+M was able to convert the gross profit growth into a 14-percent increase of the EBITDA. As an explanation, the company refers for instance to economies of scale of training courses and of customizing projects in which M+M relies on more and more prefabricated sector-specific or individual solutions complementary to the standard Autodesk products. Headcount in the VAR business was kept at a constant level, across the group the increase remained below the gross profit growth. The result of these cost discipline efforts, including also non-personnel costs, shows particularly well in the EBITDA effect from gross profit growth. In the years between 2012 and 2017, M+M was able to convert an average of 53 percent of the additional gross profit into an EBITDA growth. Last year, however, this figure rose to 67 percent. The resulting group EBITDA of about EUR 18 m corresponds to an EBITDA margin of 11.2 percent, reaching thus for the first time a two-digit figure and surpassing last year's figure by 1.8 percentage points. The re-

markable fact is that even the VAR business generated a margin improvement by 0.6 percentage points to 4.8 percent and an EBITDA increase by 4 percent to EUR 5.3 m, in spite of a declining gross profit. In the already highly profitable software business, the EBITDA rose by more than 19 percent to EUR 12.7 m, tantamount to a margin increase from 23.1 to 25.2 percent.



Source: company;

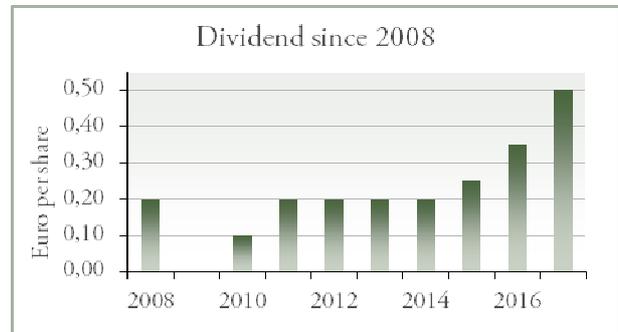
Net profit increases by 30 percent

Combined with declining depreciations, the improved EBITDA led to an EBIT growth of 21.7 percent to EUR 15.5 m, resulting in an increase of the EBIT margin by two percentage points to 9.5 percent. Below the EBIT, an adverse currency effect, which the company estimates year-on-year at EUR 0.4 m, caused a worsening in the financial result. However, after taxes and minorities, there was an overall increase in profit by nearly 30 percent to EUR 8.5 m. Accordingly, the EBITDA hit the middle of the company's target corridor of EUR 17.5 to 18.5 m, while the net profit reached only the lower end of the range (EUR 8.5 to 9.3 m) due to the currency effect.

Cash flows very strong

The operating cash flows improved perhaps not quite as markedly as the profit, but they are still at a high level with EUR 15.2 m (previous year: EUR 14.6m). This is a new record high not only in absolute terms,

but also in relation to sales. The corresponding ratio improved from 8.8 to 9.5 percent.



Source: company; figure for 2017: announcement;

Dividend outlook raised

M+M intends to use the high cash inflow for a high payout ratio. Although the net profit only met the lower end of guidance, M+M plans to pay 50 cents per share for the last year, corresponding with the upper end of dividend forecast. For the current year, the outlook was even raised. Instead of 60 cents, the company offers now the prospect of 62 to 68 cents. Forecasts for other figures have been slightly adjusted as well. While the target figure for gross profit was somewhat reduced from EUR 107 m to 106 m, the previous EBITDA guidance of EUR 22 m is now the lower limit of the new forecast of EUR 22 to 23 m. With regard to net profit, however, the previous target figure of EUR 11.5 m was exchanged for a target range of EUR 11 to 12 m, which actually implies a somewhat higher profit growth considering the 2017 figure that reached the lower end of the forecast. The mid-term profit forecast was phrased a little more offensively as well. While the company had hitherto expected a yearly profit growth of 13 to 20 cents from 2019 on, it is now aiming at a growth of about 20 cents per share. The objective to surpass the profit level of EUR 1.00 per share by 2020 was confirmed. In step with the profit growth, the dividend increase is to be quicker as well. Instead of raising the dividend by 10 to 15 cents annually as announced, it is now intended to rise by about 15 cents p.a.

Estimates slightly modified

Mensch und Maschine reached its own forecasts for 2107. Our estimates, however, which we had based on the expectation of a possible over-achievement and which we ourselves had considered ambitious, have now turned out to be too optimistic. As M+M has, moreover, slightly reduced the forecast for gross profit development in 2018, we lower our gross profit estimate for this year as well. We now expect a gross profit of EUR 104.5 m for 2018. For the subsequent years, we still estimate – in line with company guidance – the growth rates for gross profit at about 10 percent p.a. and our margin expectations remain largely the same. The resulting profit expectations are therefore a little lower than before. For the current year, we calculate with EUR 0.70 per share instead of EUR 0.72, and for 2019, we have lowered the profit estimate by 3 cents to EUR 0.84 per share. The gradual slight lowering of the assumed tax ratio has quite the opposite effect. So far, we had estimated it to be constantly 33 percent from 2018 on, but due to the large contribution of foreign business we now let it gradually decline so that by 2025, it nearly reaches the company's aim of 30 percent. An overview over the data underlying our valuation is to be

found in the table above, a detailed presentation of the model business development up to 2025 is shown in the tables in the Annex.

WACC of 6.5 percent

Subsequently, we assume a “perpetual” cash-flows growth of 1 percent p.a. and an EBIT margin of 10.6 percent that includes a reduced safety discount of 25 percent on the target margin (compared to our last update with 30 percent) at the end of the detailed forecast period. Given the sustained progress in profitability and the already achieved profitability level, we think that this reduction is justified. We have also reduced (from 4.5 to 4.0 percent) the current interest rate on borrowed capital used for determining the discount rate, which resulted in a slightly lower WACC figure of 6.5 percent (so far: 6.6 percent.)

Price target: EUR 25.90 per share

These assumptions result in a market value of equity of EUR 422.8 m or EUR 25.91 per share, from which we derive the new price target of EUR 25.90. The notable increase over our previous research report (EUR 21.80) is due to a combination of the es-

m Euro	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025
Sales	177.0	195.6	216.1	238.8	263.9	291.6	322.2	356.0
Sales growth		10.5%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%
EBIT margin	10.9%	11.5%	12.1%	12.8%	13.4%	13.8%	14.0%	14.1%
EBIT	19.3	22.4	26.2	30.5	35.3	40.1	45.1	50.3
Tax rate	34.0%	33.5%	33.0%	32.5%	32.0%	31.5%	31.0%	30.5%
Adjusted tax payments	6.6	7.5	8.6	9.9	11.3	12.6	14.0	15.3
NOPAT	12.8	14.9	17.6	20.6	24.0	27.5	31.1	35.0
+ Depreciation & Amortisation	3.2	3.3	3.2	3.2	3.3	3.3	3.4	3.5
+ Increase long-term accruals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating Cash Flows	16.0	18.2	20.7	23.8	27.2	30.8	34.5	38.5
- Increase Net Working Capital	1.1	1.3	1.4	1.4	1.5	1.6	1.6	1.7
- Investments in fixed assets	-2.9	-3.0	-3.2	-3.3	-3.5	-3.7	-3.8	-4.0
Free Cash Flows	14.3	16.5	18.9	21.9	25.2	28.7	32.3	36.2

SMC estimation model

estimate adjustments mentioned above and the very strong rollover effect at the turn of the year. The estimation risk, however, remains unchanged at three out of six possible points.

Sensitivity analysis

When the input parameters are varied for the sensitivity analysis (WACC between 5.5 and 7.5 percent, perpetual growth between 0 and 2 percent), the fair value fluctuates between EUR 19.89 and EUR 38.57 per share.

Sensitivity analysis WACC	Perpetual cash flows growth				
	2.0%	1.5%	1.0%	0.5%	0.0%
5.5%	38.57	34.83	31.92	29.59	27.69
6.0%	33.66	30.86	28.62	26.78	25.25
6.5%	29.84	27.68	25.91	24.44	23.19
7.0%	26.78	25.07	23.65	22.45	21.42
7.5%	24.27	22.90	21.74	20.75	19.89

Conclusion

Mensch und Maschine concluded last year with a moderate gross profit growth and a significant profit improvement. Especially encouraging is the fact that these improvements were achieved not only in the already fast-growing and highly profitable software segment, but also in the VAR business. Here, M+M had to cope with considerably lower sales in the trade business with Autodesk licenses as a result of the Americans' transition of the pricing model to a subscription solution. Due to the strong demand for services and proprietary solutions, the company mastered this transition period rather well.

In the fourth quarter, where the new pricing model made itself felt for the first time without the distorting effect of the previous year, the trade business became again more dynamic and enabled a nearly 15-percent growth of sales in the VAR business.

The development is thus reliably progressing within the framework outlined previously by the M+M management; this serves in our opinion to emphasise very strongly the credibility of company forecasts. Although last year and in the forecasts for the next few years M+M has slightly shifted its focus from growth towards profitability and is now working with more ambitious margin targets, we think that the forecasts are well attainable and have aligned our estimates to them.

The resulting fair value has increased over our last update from EUR 21.80 to now EUR 25.90 per share, which is mainly due to the rollover effect at the turn of the year. We think therefore that the M+M share shows again considerable potential, and adjust our rating accordingly from most recently "Hold" to "Buy".

Annex I: Balance sheet and P&L estimation

Balance sheet estimation

m Euro	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025
ASSETS									
I. Total non-current	61.2	60.9	60.6	60.6	60.7	60.9	61.2	61.6	62.1
1. Intangible assets	42.3	41.4	40.5	39.8	39.3	38.7	38.2	37.8	37.4
2. Tangible assets	14.6	15.1	15.7	16.4	17.1	17.8	18.6	19.5	20.4
II. Total current assets	36.9	41.5	43.9	46.8	49.8	59.0	70.0	81.8	94.8
LIABILITIES									
I. Equity	45.3	50.6	53.8	58.3	63.6	70.8	78.3	86.5	95.6
II. Accruals	9.6	10.5	11.3	12.2	13.0	13.9	14.8	15.7	16.6
III. Liabilities									
1. Long-term liabili-	20.6	17.5	14.0	9.9	5.2	4.1	4.1	4.1	4.1
2. Short-term liabili-	22.6	23.9	25.4	26.9	28.7	31.1	34.0	37.1	40.6
TOTAL	98.1	102.4	104.4	107.4	110.5	119.9	131.2	143.4	156.9

P&L estimation

m Euro	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025
Sales	160.5	177.0	195.6	216.1	238.8	263.9	291.6	322.2	356.0
Gross profit	94.8	105.4	115.8	127.3	139.9	153.8	169.0	185.7	204.1
EBITDA	18.0	22.6	25.7	29.4	33.7	38.5	43.5	48.5	53.8
EBIT	15.3	19.3	22.4	26.2	30.5	35.3	40.1	45.1	50.3
EBT	13.9	18.1	21.3	25.4	29.9	35.2	40.3	45.3	50.6
EAT (before minori-	8.8	11.9	14.2	17.0	20.2	24.0	27.6	31.3	35.2
EAT	8.5	11.5	13.6	16.3	19.4	23.0	26.5	30.0	33.8
EPS	0.51	0.70	0.84	1.00	1.19	1.41	1.62	1.84	2.07

Annex II: Cash flows estimation and key figures

Cash flows estimation

m Euro	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025
CF operating	15.2	16.3	18.8	21.5	24.8	28.7	32.5	36.3	40.4
CF from investments	-3.1	-2.9	-3.0	-3.2	-3.3	-3.5	-3.7	-3.8	-4.0
CF financing	-10.6	-11.7	-14.9	-17.1	-20.3	-18.0	-20.0	-23.1	-26.1
Liquidity beginning of	6.4	7.8	9.6	10.4	11.8	12.9	20.2	28.9	38.4
Liquidity end of year	7.8	9.6	10.4	11.8	12.9	20.2	28.9	38.4	48.6

Key figures

Percent	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025
Sales growth	-3.9%	10.3%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%
Gross profit growth	3.7%	11.2%	9.8%	9.9%	9.9%	9.9%	9.9%	9.9%	9.9%
Gross margin	59.1%	59.6%	59.2%	58.9%	58.6%	58.3%	58.0%	57.6%	57.3%
EBITDA margin	11.2%	12.8%	13.2%	13.6%	14.1%	14.6%	14.9%	15.0%	15.1%
EBIT margin	9.5%	10.9%	11.5%	12.1%	12.8%	13.4%	13.8%	14.0%	14.1%
EBT margin	8.7%	10.2%	10.9%	11.8%	12.5%	13.4%	13.8%	14.1%	14.2%
Net margin (after mi-	5.3%	6.5%	7.0%	7.6%	8.1%	8.7%	9.1%	9.3%	9.5%

Disclaimer

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Charts

The charts were made with Tai-Pan (www.lp-software.de).

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- 3) sc-consult GmbH has submitted this report to the customer/ the company before publishing
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7) sc-consult GmbH has included the company's shares in a virtual portfolio managed by sc-consult GmbH

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II) Preparation and updating

The present financial analysis was prepared by: Dr. Adam Jakubowski

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Strong Buy	We expect an increase in price for the analyzed financial instrument by at least 10 percent. We assess the estimation risk as below average (1 to 2 points).
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The expected change in price refers to the current share price of the analyzed company. This price and any other share prices used in this analysis are XETRA closing prices as of the last trading day before publication. If the share is not traded on XETRA, the closing price of another public stock exchange is used with a separate note to that effect.

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Date	Rating	Target price	Conflict of interests
26.10.2017	Hold	21.80 Euro	1), 3), 4)
17.08.2017	Hold	19.80 Euro	1), 3), 4)
25.04.2017	Buy	17.80 Euro	1), 3), 4)
16.02.2017	Buy	16.20 Euro	1), 3)
27.10.2016	Buy	14.80 Euro	1), 3), 4)
29.07.2016	Hold	14.90 Euro	1), 3), 4)
28.04.2016	Hold	12.90 Euro	1), 3)
19.02.2016	Buy	10.50 Euro	1), 3)

In the course of the next twelve months, sc-consult GmbH will presumably prepare the following financial analyses for the company: Two updates, one report.

The publishing dates for the financial analyses are not yet fixed at the present moment

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