

October 26th, 2017
Research Update

SMC Research
Small and Mid Cap Research

Mensch und Maschine SE

Transition period mastered with flying
colours

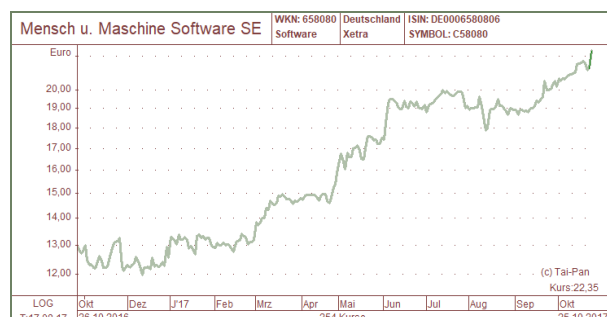
Rating: **Hold** (unchanged) | Price: **22.35 Euro** | Price target: **21.80 Euro**

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Recent business development



Basic data

Based in:	Wessling
Sector:	CAD/CAM Software
Headcount:	790
Accounting:	IFRS
ISIN:	DE0006580806
Price:	22.35 Euro
Market segment:	Scale / m:access
Number of shares:	16.7 m
Market Cap:	372.8 m Euro
Enterprise Value:	398.7 m Euro
Free float:	44.2 %
Price high/low (12 M):	22.45 / 11.87 Euro
Ø turnover (12 M):	192,100 Euro

In the third quarter, the negative effect of Autodesk's pricing model conversion made itself felt for the last time in Mensch und Maschine's VAR segment. This time, the impact was perceptible on the group level as well in terms of a declining gross profit and a weaker operating result. Over the whole nine months, however, M+M was able to achieve a slight increase of the gross profit and a noticeable increase in operating and net profit in spite of the conversion. Accordingly, M+M has confirmed its profit forecast for the whole year. With regard to further prospects, however, we consider it far more important that the company has reported a marked double-digits growth for the trade business adjusted by the transition effect. This supports our expectations that the upward trend will regain momentum in the fourth quarter and that it will continue in the next year. The mid-term forecast assuming a profit doubling by 2020 is in our opinion still achievable as well. However, after this year's price leap, these favourable prospects are already adequately represented in the current share price. We confirm therefore our rating "hold" at a price target of EUR 21.80.

FY ends: 31.12.	2014	2015	2016	2017e	2018e	2019e
Sales (m Euro)	140.0	160.4	167.1	165.7	184.0	202.4
EBIT (m Euro)	6.8	8.5	12.5	16.8	19.5	23.1
Net profit	3.7	3.9	6.6	9.7	11.7	14.2
EpS	0.24	0.24	0.39	0.59	0.72	0.87
Dividend per share	0.20	0.25	0.35	0.50	0.60	0.70
Sales growth	11.3%	14.5%	4.2%	-0.8%	11.0%	10.0%
Profit growth	42.1%	4.0%	70.4%	46.8%	21.0%	21.5%
PSR	2.61	2.28	2.18	2.20	1.98	1.80
PER	98.2	94.4	55.4	37.7	31.2	25.6
PCR	58.04	24.78	24.92	22.04	21.84	18.72
EV / EBIT	57.8	46.1	31.3	23.2	20.1	16.9
Dividend yield	0.9%	1.1%	1.6%	2.2%	2.7%	3.1%

Sales declined

The dampening effect of Autodesk's conversion of the pricing model made itself felt for the last time in the third quarter. Compared to the previous year, where the final sale of one-off licenses led to a temporary boom in July, the VAR sales declined by 28.3 percent to EUR 21.1 m. In contrast, sales in the software segment rose between July and September again, even though the increase was weaker than in previous quarters (4.3 percent to EUR 10.8 m) due to traditionally unfavourable seasonal factors. Across both segments, this resulted in a sales decline by 19.8 percent to EUR 31.9 m.

Slight rise in gross profit after nine months

Unlike in the other quarters, where declining profits were more than compensated for on the level of gross profit through a shift in the sales mix towards higher-margin revenues, in the third quarter this effect was not sufficient anymore. However, the gross profit sank only very moderately by 4.1 percent, and therefore, over the first nine months, despite a sales decline by 9.5 percent there was a slight gross profit growth by 1.1 percent to EUR 68.6 m. An even stronger growth was prevented by the appreciation of the Euro, without which the gross profit increase in the software segment would have been 9.3 percent instead of 7.6 percent.

Turning point in VAR business reached

In the VAR business, gross profit was declining in the first nine months: at EUR 33.6 m, it was 5.2 percent below last year's figure. Of this, EUR 22.7 m or 67.5 percent were attributable to services and M+M's own software solutions, which increased by nearly 16.7 percent. In contrast, the contribution from Autodesk trade dropped by 31 percent to EUR 11.4 m. This figure, however, obscures the fact that the gross profit from maintenance and subscription (which constitute the trade business after the conversion of the pricing model) has already increased by 14 percent. For September, M+M reports a growth of subscription revenues by 20 percent, surpassing

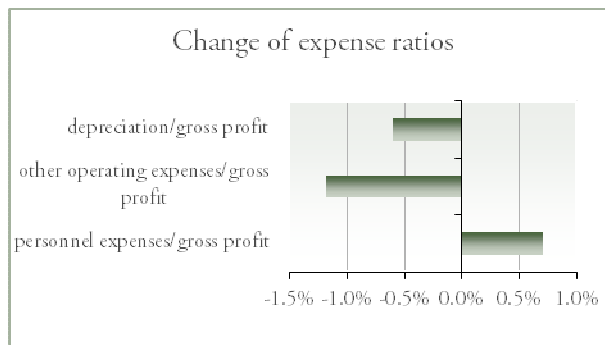
the management's previous expectations (15 percent).

Business figures	9M 2016	9M 2017	Change
Sales	127.59	115.47	-9.5%
<i>VAR business</i>	94.15	79.48	-15.6%
<i>Software</i>	33.45	36.00	+7.6%
Gross profit	67.83	68.56	+1.1%
<i>VAR business</i>	35.44	33.59	-5.2%
<i>Software</i>	32.39	34.97	+8.0%
<i>Gross margin</i>	53.2%	59.4%	
EBITDA	10.80	11.44	+5.9%
<i>VAR business</i>	3.77	3.13	-16.9%
<i>Software</i>	7.03	8.31	+18.2%
<i>EBITDA margin</i>	8.5%	9.9%	
EBIT	8.35	9.37	+12.3%
<i>VAR business</i>	2.25	1.95	-13.5%
<i>Software</i>	6.10	7.43	+21.8%
<i>EBIT margin</i>	6.5%	8.1%	
EBT	7.31	8.63	+18.0%
<i>EBT margin</i>	5.7%	7.5%	
Net profit	4.34	5.31	+22.2%
<i>Net margin</i>	3.4%	4.6%	

Strict cost discipline

M+M was able to convert this slight gross profit growth in an even stronger profit growth. This is partly due to a sustained cost discipline, which resulted in other operating expenses declining by 5 percent and personnel expenses increasing by only 2.2 percent. The EBITDA increased therefore even more disproportionately to the gross profit by 5.9 percent, the growth being achieved solely in the software segment (+18.2 percent). The EBITDA of the VAR business, on the other hand, dropped by 16.9 percent. In relation to the decreased sales, the EBITDA margin improved by 1.4 percentage points to 9.9 percent. Below the EBITDA level, decreasing depreciations and amortizations (-15.8 percent), a

lower interest burden, an assumed improved tax rate and a reduced minority interest resulted in even stronger growth, amounting to 12.3 percent (EBIT), 18.0 percent (EBT) and even 22.2 percent for the net profit.



Source: company

Cash flows very strong

The operating cash flows, increasing year-on-year by 10.4 percent to EUR 13.0 m, saw a much stronger development than the net profit that is still encumbered by depreciations and deferred taxes. In relation to sales, the operating cash flows reached thus a ratio of 11.3 percent. Aside from the higher profit, M+M benefitted here from reduced receivables and inventories. Given an outflow of funds due to investments of EUR 2.8 m (previous year: EUR 2.4 m), the result was free cash flows of EUR 10.2 m, surpassing last year's figure by 9.2 percent.

Balance sheet figures improve further

M+M used the major part of these inflows for dividend payment and repayment of loans, resulting altogether in an increase of liquid funds by EUR 1.9 m to 8.3 m. The net debt (including the property loan and a shareholder loan) was thus reduced to EUR 15.7 m, equaling last year's EBITDA. The equity ratio improved further as well. Although equity rose only by 3 percent to EUR 42.0 m (compared to the beginning of the year) due to the high dividend payment, combined with the balance sheet total reduced simultaneously by 4 percent it resulted in an equity ratio increase by 3 percentage points to 43.5 percent.

Forecasts slightly adjusted

In terms of sales and gross profit, the third quarter lagged a little behind schedule, which is why M+M slightly reduced its own gross profit forecast from previously EUR 98-99 m to now about EUR 95m. In contrast, the profit forecast was confirmed with an EBITDA of EUR 17.5 to 18.5 m and an EPS of 52 to 57 cents, which the company justifies with a markedly improved cost management. The mid-term objective to more than double the profit to 1 Euro per share by 2020 was confirmed as well. M+M intends to increase the net profit to about 70 cents per share at a gross profit growth by 11 to 12 percent already by next year, corresponding with an increase by 30 percent.

Estimates adjusted

As our estimates had been slightly above company guidance so far, we have slightly lowered them in reaction to the nine-month figures. We expect now a gross profit of EUR 98.7 m (previously: EUR 100.5 m), an EBITDA of EUR 19.2 m (EUR 19.5 m), an EBIT of EUR 16.8 m (EUR 17.1 m) and the net profit unchanged at EUR 0.59 per share. As this adjustment continues in the gross profit row into the subsequent years as well, it is now slightly lower than before. Our estimates are nevertheless still a little above the company's forecast, which we think justifiable given that in the past the goals were often surpassed. Although the third quarter was weaker than expected, it should be taken into account that the considerably higher share of services in the VAR business will probably have increased the impact of seasonal factors in the segment. In view of this and of the reported high growth of subscription revenues in September, we are confident that the VAR business will be able to provide a positive surprise in the fourth quarter. In the software segment, the rise of the euro against the yen, the dollar and the British pound has a negative impact, but this is offset by the continuously solid development of the global economy. Altogether, we think therefore that our estimates are attainable, even if a little ambitious with regard to 2017. Further adjustments concern the growth rates of receivables, which seemed too steep after the improvements in the management of work-

m Euro	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024
Sales	165.7	184.0	202.4	222.6	244.9	269.4	296.3	325.9
Sales growth		11.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
EBIT margin	10.1%	10.6%	11.4%	12.4%	13.2%	13.5%	13.7%	13.9%
EBIT	16.8	19.5	23.1	27.6	32.3	36.3	40.6	45.3
Tax rate	35.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%
Adjusted tax payments	5.9	6.4	7.6	9.1	10.7	12.0	13.4	15.0
NOPAT	10.9	13.0	15.5	18.5	21.7	24.3	27.2	30.4
+ Depreciation & Amortisation	2.4	3.2	3.3	3.2	3.3	3.4	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	13.3	16.3	18.8	21.7	24.9	27.7	30.6	33.9
- Increase Net Working Capital	4.1	1.3	1.3	1.4	1.4	1.5	1.6	1.7
- Investments in fixed assets	-3.1	-3.1	-3.2	-3.4	-3.5	-3.7	-3.8	-4.0
Free cash flows	14.3	14.5	16.9	19.7	22.9	25.5	28.4	31.5

SMC estimation model

ing capital. An overview over the data underlying our valuation is to be found in the table below, a detailed presentation of the model business development up to 2024 is shown in the tables in the Annex.

Price target: EUR 21.80 per share

These assumptions result in a market value of equity of EUR 355.9 m or EUR 21.79 per share, from which we derive the new price target of EUR 21.80. The increase over our previous research report is due to a combination of several effects. While the slight reduction in the sales and profits row had a dampening effect on the price target, the adjustments of cash flows estimates and the discounting effect made a positive contribution. In addition, against the continuously high cash surpluses, we have defined for the first time a portion of liquidity as non-operating and have added it to the enterprise value. The esti-

mation 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 5.6 and 7.6 percent, perpetual growth between 0 and 2 percent), the fair value fluctuates between EUR 17.02 and EUR 31.61 per share.

Sensitivity analysis	Perpetual cash flows growth				
	WACC	2.0%	1.5%	1.0%	0.5%
5.6%	31.61	28.73	26.46	24.63	23.13
6.1%	27.86	25.67	23.90	22.45	21.23
6.6%	24.90	23.20	21.79	20.62	19.62
7.1%	22.52	21.16	20.02	19.06	18.23
7.6%	20.55	19.45	18.52	17.72	17.02

Conclusion

Mensch und Maschine is still doing well in this transition year of the Autodesk business. After the expected losses in sales were even better compensated for than expected in the first half-year, the company was not quite able to repeat that in the third quarter as well. Thus, the group's gross profit has declined between July and September in spite of the increases in the software segment and in the proprietary VAR business. Over the whole nine months, however, there was still a minimal gross profit growth and a marked improvement in all earnings figures.

Moreover, we consider it particularly promising that – adjusted by the distorting base effect of last year's final sale – the gross profit in the trade business has again shown double-digits growth. This indicates that plans and expectations resulting from the transi-

tion of the pricing model at Autodesk should well work out. As the other business areas are on track as well and as M+M was able to compensate for the slightly lagging performance of the gross profit by strict cost management, the company has confirmed its profit forecast.

In contrast, we have slightly modified our sales and profit estimates, which was, however, more than offset by other adjustments and by the discounting effect, and the fair value we ascertained rose thus further to EUR 21.80. With regard to the noticeably increased stock price, this indicates a fair valuation of M+M's share, which is why we confirm our rating recently changed to "hold".

Annex I: Balance sheet and P&L estimation

Balance sheet estimation

m Euro	12 2016	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024
ASSETS									
I. Total non-current	62.0	62.7	62.5	62.4	62.6	62.8	63.2	63.6	64.0
1. Intangible assets	42.9	42.3	41.5	40.7	40.1	39.6	39.2	38.8	38.4
2. Tangible assets	13.2	14.6	15.3	15.9	16.6	17.4	18.2	19.0	19.8
II. Total current assets	38.6	39.8	42.7	46.3	51.0	56.7	66.3	76.9	92.0
LIABILITIES									
I. Equity	40.6	47.1	50.6	55.3	61.9	70.3	79.2	89.3	100.8
II. Accruals	8.8	9.6	10.5	11.3	12.2	13.1	14.0	14.9	15.8
III. Liabilities									
1. Long-term liabilities	27.2	21.2	18.2	14.6	10.3	5.3	3.1	0.2	0.2
2. Short-term liabilities	24.0	24.5	26.0	27.5	29.1	30.9	33.2	36.1	39.3
TOTAL	100.5	102.5	105.2	108.7	113.6	119.6	129.4	140.5	156.1

P&L estimation

m Euro	12 2016	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024
Sales	167.1	165.7	184.0	202.4	222.6	244.9	269.4	296.3	325.9
Gross profit	91.4	98.7	109.4	120.1	131.9	144.8	159.0	174.6	191.7
EBITDA	15.8	19.2	22.7	26.5	30.8	35.6	39.7	44.0	48.8
EBIT	12.5	16.8	19.5	23.1	27.6	32.3	36.3	40.6	45.3
EBT	11.1	15.5	18.2	22.1	26.7	32.0	36.4	40.9	45.9
EAT (before minorities)	7.0	10.1	12.2	14.8	17.9	21.4	24.4	27.4	30.8
EAT	6.6	9.7	11.7	14.2	17.2	20.6	23.4	26.3	29.5
EPS	0.39	0.59	0.72	0.87	1.05	1.26	1.43	1.61	1.81

Annex II: Cash flows estimation and key figures

Cash flows estimation

m Euro	12 2016	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024
CF operating	14.6	16.6	16.7	19.5	22.5	26.1	29.2	32.4	35.9
CF from investments	-3.4	-3.1	-3.1	-3.2	-3.4	-3.5	-3.7	-3.8	-4.0
CF financing	-14.5	-10.6	-12.1	-14.2	-16.1	-18.7	-18.0	-20.2	-19.2
Liquidity beginning of year.	9.6	6.4	9.2	10.7	12.8	15.9	19.8	27.3	35.7
Liquidity end of year	6.4	9.2	10.7	12.8	15.9	19.8	27.3	35.7	48.4

Key figures

Percent	12 2016	12 2017	12 2018	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024
Sales growth	4.2%	-0.8%	11.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
Gross profit growth	8.2%	8.0%	10.8%	9.8%	9.8%	9.8%	9.8%	9.8%	9.8%
Gross margin	54.7%	59.6%	59.5%	59.4%	59.2%	59.1%	59.0%	58.9%	58.8%
EBITDA margin	9.4%	11.6%	12.3%	13.1%	13.8%	14.5%	14.7%	14.9%	15.0%
EBIT margin	7.5%	10.1%	10.6%	11.4%	12.4%	13.2%	13.5%	13.7%	13.9%
EBT margin	6.7%	9.4%	9.9%	10.9%	12.0%	13.1%	13.5%	13.8%	14.1%
Net margin (after minorities)	3.9%	5.8%	6.4%	7.0%	7.7%	8.4%	8.7%	8.9%	9.1%

Disclaimer

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Charts

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

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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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Buy	We expect an increase in price for the analyzed financial instrument by at least 10 percent. We assess the estimation risk as average (3 to 4 points).
Speculative Buy	We expect an increase in price for the analyzed financial instrument by at least 10 percent. We assess the estimation risk as above average (5 to 6 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.

The price targets published within the assessment are calculated with common methods of financial mathematics, especially with the DCF (discounted cash flow) method, the sum of the parts valuation and a peer group analysis. The valuation methods are affected by economic framework conditions, especially by the development of the interest rates.

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Date	Rating	Target price	Conflict of interests
August 17th, 2017	Hold	19.80 Euro	1), 3), 4)

April 25th, 2017	Buy	17.80 Euro	1), 3), 4)
February 16th, 2017	Buy	16.20 Euro	1), 3)
October 27th, 2016	Buy	14.80 Euro	1), 3), 4)
July 29th, 2016	Hold	14.90 Euro	1), 3), 4)
April 28th, 2016	Hold	12.90 Euro	1), 3),
February 19th, 2016	Buy	10.50 Euro	1), 3),
November 3rd, 2015	Buy	9.50 Euro	1), 3),

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

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