

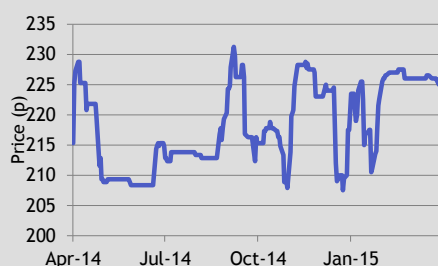
K3 BUSINESS TECHNOLOGY GROUP SOFTWARE AND COMPUTER SERVICES

KBT.L

226p

Market Cap: £71.7m

SHARE PRICE (p)



12m high/low

231p / 208p

Source: LSE Data

KEY INFORMATION

Enterprise value	£85.3m
Index/market	FTSE AIM
Next news	FY15 Results, Sept 15
Gearing	19%
Interest cover	10.4x

**K3 BUSINESS TECHNOLOGY GROUP IS A
RESEARCH CLIENT OF PROGRESSIVE**

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Expanding the offering

K3 has announced the acquisition of Willow Starcom from Access Intelligence. The deal appears sensibly-priced, with scope for both sales and cost synergies. More importantly, it extends K3's hosting and IT support expertise into areas where Microsoft is looking to partner with its ecosystem. We make modest upgrades to our forecasts to reflect the deal, and see this as a good example of the M&A opportunity that the group can enjoy.

- Deal detail:** the Willow Starcom acquisition comprises a subsidiary of Access Intelligence, which is being acquired for £1.75m (debt-funded) with a very modest (£0.075m) retention. The price is just below 5x historic EBITDA, and below 1x sales, which to us appears attractive, and is well below the corresponding multiples for K3.
- Extended offering:** the acquired business is active in the on-site IT support market (break-fix maintenance) and also delivers hosted solutions, with a particular focus on low- and mid-range Microsoft products.
- Logical fit:** the deal brings, in our view, a strong and logical fit with K3's existing business, and delivers both a good number of new customers and a useful expansion of the group's hosting activities. Microsoft has already become a valued relationship for K3, and this deal extends the group's capabilities in a number of important ways. The RNS describes the limited cost of integrating the businesses, and we would expect both revenue cross-sell and cost-related synergies to be features of the deal.
- Upgrades to forecasts:** given the proximity of the group's year-end, the FY15 results are only modestly altered by the transaction, but we upgrade FY16E by some £2.5m in terms of revenue, and £0.45m EBITDA. EPS for FY16E rises from 24.7p to 25.7p. Our net debt assumptions increase from £14.2m to £15.0m for FY15, but remain unchanged for FY16E at just over £9m.

K3 continues to benefit from its existing scale and critical mass; the group's managed services and hosted offerings provide high-value recurring revenue, and this deal is clearly a useful extension of these skillsets. Most importantly, the acquisition shows the earnings-enhancing deals to which the group has access, and which can be made to work through the existing levels of intellectual property and relationships.

FYE JUNE	FY12	FY13A	FY14A	FY15E	FY16E
Revenue	68.0	63.5	72.0	81.7	92.1
Adjusted EBITDA	12.9	7.3	9.9	11.6	13.8
Adjusted PBT	10.0	4.4	6.6	8.1	10.2
Adjusted EPS	24.4	13.9	18.4	20.5	25.7
EV/Sales	1.3x	1.4x	1.2x	1.1x	0.9x
EV/ Adj. EBITDA	6.6x	11.8x	8.7x	7.4x	6.2x
P/E	9.3x	16.4x	12.4x	11.1x	8.9x

Source: Company Information and Progressive Equity Research estimates

FINANCIAL SUMMARY

Year ended Jun	FY-12	FY-13	FY-14	FY-15	FY-16
	£m	£m	£m	£m	£m
Profit & Loss	Act	Act	Act	Est	Est
Revenue £m	68.0	63.5	72.0	81.7	92.1
Adj EBITDA £m	12.9	7.3	9.9	11.6	13.8
Adj EBIT £m	11.4	5.2	7.3	8.9	11.1
Reported PBT	6.0	0.5	1.9	4.9	7.1
PBT before exceptionals and AAG	10.0	4.4	6.6	8.1	10.2
Fully adj PBT	10.1	4.4	6.6	8.1	10.2
NOPAT £m	8.0	3.6	5.1	6.2	7.8
Reported EPS	19.8	4.2	8.1	12.3	17.8
EPS before exceptionals and AAG	24.3	10.4	20.8	20.4	25.6
Fully adj EPS	24.4	13.9	18.4	20.5	25.7
Dividend per share p	1.00	1.00	1.25	1.50	1.75
Cash flow & Balance sheet					
Operating cash flow	7.3	8.0	6.3	7.3	12.5
Free Cash flow £m	3.6	3.9	2.3	2.0	7.1
FCF per share p	12.4	13.2	7.4	6.4	22.3
Capex	-3.2	-4.6	-4.5	-4.0	-4.0
Acquisitions	-7.1	-1.9	-0.1	-1.8	0.0
Net cash flow	-5.4	-0.8	0.0	-1.4	5.3
Shares issued	5.0	2.7	0.3	0.0	0.0
Net cash	-15.7	-13.8	-13.6	-15.0	-9.7

Metrics	FY-12	FY-13	FY-14	FY-15	FY-16
Revenue growth	28.7%	-6.5%	13.3%	13.5%	12.8%
Adj EBITDA growth	22.4%	-43.9%	35.8%	17.9%	18.4%
Adj EBIT growth	18.4%	-54.7%	41.9%	21.8%	24.0%
Adj PBT growth	15.7%	-56.0%	49.1%	22.7%	25.3%
Adj EPS growth	7.2%	-43.2%	32.8%	11.2%	25.3%
Dividend growth	33.3%	0.0%	25.0%	20.0%	16.7%
Adj EBIT margins	16.8%	8.1%	10.2%	10.9%	12.0%
Operating cash conversion	56%	110%	63%	63%	91%
Capex/Depreciation	206%	219%	176%	148%	148%

Valuation	FY-12	FY-13	FY-14	FY-15	FY-16
EV/sales	1.3	1.4	1.2	1.1	0.9
EV/EBITDA	6.6	11.8	8.7	7.4	6.2
EV/NOPAT	10.8	23.8	16.7	13.7	11.1
PER	9.3	16.4	12.4	11.1	8.9
Dividend yield	0.4%	0.4%	0.5%	0.7%	0.8%
FCF yield	5.5%	5.8%	3.2%	2.8%	9.8%

Source: K3 information, Progressive Equity Research estimates

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