

## K3 BUSINESS TECHNOLOGY GROUP

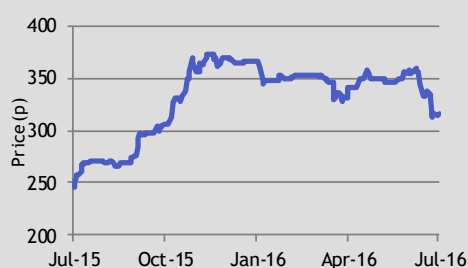
### SOFTWARE AND COMPUTER SERVICES

#### KBT.L

316p

Market Cap: £100.0m

#### SHARE PRICE (p)



12m high/low

372p / 247p

Source: LSE Data

#### KEY INFORMATION

Enterprise value	£110.4m
Index/market	FTSE AIM
Next news	FY16, Sep 16
Gearing	14%
Interest cover	13.1x

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

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### FY16 update in line

K3 has published an in-line trading update for the year to 30 June 2016, with results “broadly in line with expectations”. Trading was strong in the latter part of the year, with performance sufficiently positive across the board to offset the negative impact of a “major” customer entering administration during June. We make no changes to forecasts, other than to reflect the recent acquisition of Merac.

- K3 has today published its FY16 trading update, which details performance “broadly in line with expectations” despite the impact in June of a customer entering administration. We assume that the customer in question is in the UK (the term “administration” is seldom used overseas), and we believe that the debt has been provided for in full, within the FY16 accounts.
- The only specific figure given (as usual at this stage) relates to net debt, which, at £8.9m, is higher than our £6.1m estimate, presumably at least in part due to the customer insolvency mentioned above. The RNS describes a strong flow of deals towards the end of the year; it is unlikely that all (or even many) of these will have generated significant cash flow in the period before the end of June.
- The group has continued to benefit from the switch towards recurring income (which has grown y/y) and a good number of contract wins and renewals.
- In terms of acquisitions, the RNS states that DdD (which was acquired in April) is integrating well. We make upward adjustments of £1.3m to revenues and £0.4m to EBITDA for FY17, to reflect the Merac acquisition announced at the beginning of July – we had waited to see today’s update before altering our estimates. We will refine our FY17 estimates (including the net debt expectations) once we see the full accounts in September.

Overall, a reassuring update from K3, with strong underlying trading offsetting an isolated and external negative impact. We await further detail at the time of full-year results in September. In the meantime, we take comfort from comments around the ongoing success of the transition to greater recurring revenue; it is this, alongside the increase in own-IP product sales, which continues to drive value for shareholders.

FYE JUNE (£M)	FY13	FY14	FY15	FY16	FY17E
<b>Revenue</b>	63.5	72.0	83.4	89.6	96.9
<b>Adjusted EBITDA</b>	<b>7.2</b>	<b>9.8</b>	<b>10.9</b>	<b>13.0</b>	<b>16.2</b>
<b>Adjusted PBT</b>	4.4	6.6	7.2	9.4	12.0
<b>Adjusted EPS (p)</b>	<b>13.9</b>	<b>18.4</b>	<b>19.1</b>	<b>23.6</b>	<b>27.7</b>
<b>EV/Sales</b>	1.7x	1.5x	1.3x	1.2x	1.1x
<b>EV/ Adj. EBITDA</b>	15.4x	11.2x	10.2x	8.5x	6.8x
<b>P/E</b>	<b>22.8x</b>	<b>17.2x</b>	<b>16.5x</b>	<b>13.4x</b>	<b>11.4x</b>

Source: Company Information and Progressive Equity Research estimates

## SUMMARY FINANCIALS

Profit & Loss	FY-12A	FY-13A	FY-14A	FY-15A	FY-16A	FY-17E
<b>Revenue</b>	<b>68.0</b>	<b>63.5</b>	<b>72.0</b>	<b>83.4</b>	<b>89.6</b>	<b>96.9</b>
Adj EBITDA	12.9	7.2	9.8	10.9	13.0	16.2
<b>Adj EBITA</b>	<b>11.3</b>	<b>5.1</b>	<b>7.3</b>	<b>8.2</b>	<b>10.2</b>	<b>12.5</b>
Reported PBT	6.0	0.5	1.9	3.7	5.5	8.8
PBT before exceptionals and AAG	10.0	4.4	6.6	7.2	9.4	12.0
<b>Fully adj PBT</b>	<b>10.0</b>	<b>4.4</b>	<b>6.6</b>	<b>7.2</b>	<b>9.4</b>	<b>12.0</b>
NOPAT	9.3	4.4	6.2	7.0	8.4	10.5
Reported EPS (p)	19.8	4.2	8.1	10.1	13.4	19.5
EPS before exceptionals and AAG (p)	29.5	13.9	18.4	19.1	24.0	27.7
<b>Fully adj EPS (p)</b>	<b>29.5</b>	<b>13.9</b>	<b>18.4</b>	<b>19.1</b>	<b>23.6</b>	<b>27.7</b>
Dividend per share (p)	1.0	1.0	1.3	1.5	1.8	1.9
Cash flow & Balance sheet	FY-12A	FY-13A	FY-14A	FY-15A	FY-16A	FY-17E
Operating cash flow	7.3	8.0	5.4	9.6	8.5	13.0
Free Cash flow £m	1.8	1.1	(0.0)	8.4	1.0	4.6
FCF per share p	6.1	3.7	(0.0)	26.1	2.9	12.8
Acquisitions	(7.1)	(1.9)	(0.1)	(6.6)	(8.6)	0.0
Disposals	0.0	0.0	0.0	0.0	0.0	0.0
Shares issued	5.0	2.7	0.3	0.0	13.5	0.0
<b>Net cash flow</b>	<b>(0.5)</b>	<b>2.0</b>	<b>0.1</b>	<b>5.5</b>	<b>5.9</b>	<b>4.6</b>
Overdrafts / borrowings	(17.8)	(14.1)	(14.3)	(13.9)	(13.9)	(13.9)
<b>Cash &amp; equivalents</b>	<b>2.1</b>	<b>0.3</b>	<b>0.6</b>	<b>1.9</b>	<b>7.8</b>	<b>12.4</b>
<b>Net (Debt)/Cash</b>	<b>(15.7)</b>	<b>(13.8)</b>	<b>(13.6)</b>	<b>(12.0)</b>	<b>(6.1)</b>	<b>(1.5)</b>
NAV and returns	FY-12A	FY-13A	FY-14A	FY-15A	FY-16A	FY-17E
Net asset value	46.9	51.1	52.6	53.5	70.9	77.4
<b>NAV/share (p)</b>	<b>164.7</b>	<b>162.6</b>	<b>165.8</b>	<b>169.2</b>	<b>198.4</b>	<b>216.6</b>
Net Tangible Asset Value	(17.9)	(14.5)	(11.4)	(8.9)	3.5	11.4
<b>NTAV/share (p)</b>	<b>(62.8)</b>	<b>(46.2)</b>	<b>(35.9)</b>	<b>(28.1)</b>	<b>9.9</b>	<b>31.8</b>
Average equity	42.1	49.0	51.9	53.1	62.2	74.1
<b>Post-tax ROE (%)</b>	<b>13.6%</b>	<b>2.5%</b>	<b>4.9%</b>	<b>6.1%</b>	<b>7.1%</b>	<b>9.5%</b>
Metrics	FY-12A	FY-13A	FY-14A	FY-15A	FY-16A	FY-17E
Revenue growth		-6.5%	13.3%	16.0%	7.4%	8.1%
Adj EBITDA growth		-44.1%	36.8%	10.3%	19.7%	24.5%
Adj EBIT growth		-55.1%	43.3%	11.6%	25.0%	22.3%
Adj PBT growth		-56.4%	50.9%	9.5%	30.3%	27.3%
Adj EPS growth		-52.9%	32.8%	4.0%	23.3%	17.3%
Dividend growth		0.0%	25.0%	20.0%	16.7%	5.7%
Adj EBIT margins	16.7%	8.0%	10.1%	9.8%	11.4%	12.9%
Valuation	FY-12A	FY-13A	FY-14A	FY-15A	FY-16A	FY-17E
EV/Sales	1.6	1.7	1.5	1.3	1.2	1.1
EV/EBITDA	8.6	15.4	11.2	10.2	8.5	6.8
EV/NOPAT	11.9	25.2	17.9	15.9	13.1	10.6
PER	10.7	22.8	17.2	16.5	13.4	11.4
Dividend yield	0.3%	0.3%	0.4%	0.5%	0.6%	0.6%
FCF yield	1.9%	1.2%	0.0%	8.2%	0.9%	4.0%

Source: Company information, Progressive Equity Research estimates

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