Research Report (Update)

KPS AG

Internationalisation strategy pays off.
Another major customer was acquired in Scandinavia.

Margin improvements in sight

Target price: 13.20 €
(previously: 13.20 €)

Rating: BUY

IMPORTANT NOTE:
Please take note of the disclaimer/risk warning, as well as the disclosure of potential conflicts of interest as required by section § 85 WpHG und Art. 20 MAR on page 10

Note on research as a "minor non-monetary benefit" according to the MiFID II regulation: This research meets the requirements for being classified as a "minor non-monetary benefit". For more information, see the disclosure under "I. Research under MiFID II"

Date and time of completion of this research: 04/06/2019 (15:00)
Date and time of first distribution: 05/06/2019 (09:00)
Target price valid until: max. 31/12/2019

GBC AG Investment Research

KPS AG*5a;6a;7;11

Rating: Buy
Price target: 13.20 €

Current Price: 6.91 €
03.06.2019 / ETR closing price

Currency: EUR

Key Information:

ISIN: DE000A1A6V48
WKN: A1A6V4
Ticker symbol: KSC

Number of shares³: 37.37
Market Cap³: 258,23
Enterprise Value³: 265,45
³in m. / in m EUR

Free Float: 36.1%

Transparency Level:
Prime Standard

Market Segment:
Regulated Market

Accounting Standard:
IFRS

Financial Year: 30/09/

Designated Sponsor:
Oddo Seydler Bank AG

Analysts:
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Cosmin Filker
filker@gbc-ag.de

* List of possible conflicts of interest on page 18

Company profile

Sector: Services

Focus: consulting for business transformation and process optimisation

Employees : 605 as of 31/03/2019

Established: 2000

Headquarter office: Unterföhring

CEO: Leonardo Musso

KPS is the leading transformation consultancy for companies throughout Europe that want to align their business model to clients within a very short time and implement innovative digital processes and technologies. KPS views companies holistically and combines merchandise management with B2B and B2C e-commerce processes and customer-oriented marketing and sales processes. The KPS rapid transformation method accelerates project initiatives by up to 50 percent. KPS is part of a successful partner network including SAP Gold Partners, SAP Hybris Platinum, Adobe Business, Intershop Premium, SAP ARIBA and SAP Concur Customer Implementation Partners. With around 1,000 consultants in 9 countries, KPS is continuously expanding its market position globally by undertaking trend-setting projects in the field of digital and technological transformation.

P&L in mEUR, financial year-end	30.09.2017	30.09.2018	30.09.2019e	30.09.2020e
Sales	160.30	172.22	179.97	188.97
EBITDA	26.41	20.02	26.47	28.76
EBIT	24.76	16.59	23.17	25.56
Net profit	19.80	9.83	15.31	17.08
Key figures in EUR				
Earnings per share	0.53	0.26	0.41	0.46
Dividend per share	0.35	0.35	0.35	0.35
Key Figures				
EV/Sales	1.66	1.54	1.47	1.40
EV/EBITDA	10.05	13.26	10.03	9.23
EV/EBIT	10.72	16.00	11.45	10.39
P/E	13.04	26.27	16.87	15.11
P/B		3.55		

Financial calendar
09.08.2019: Q3-report

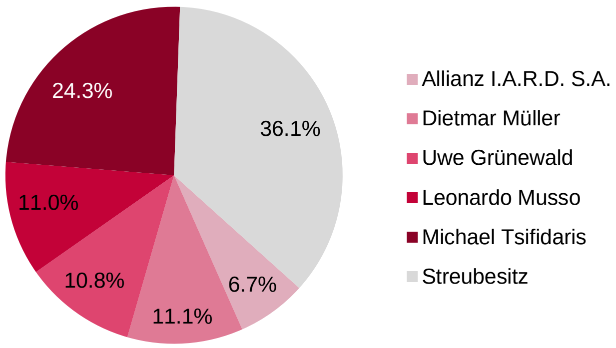
** Last research by GBC:
Date: publication/target price in EUR/rating
06.03.2019: RS / 13.20 / BUY
14.08.2018: RS / 12.50 / BUY
20.02.2018: RS / 16.60 / BUY
28.08.2017: RS / 18.00 / BUY
** The research studies indicated above may be viewed at www.gbc-ag.de, or requested from GBC AG, Halderstr. 27, D86150 Augsburg

COMPANY

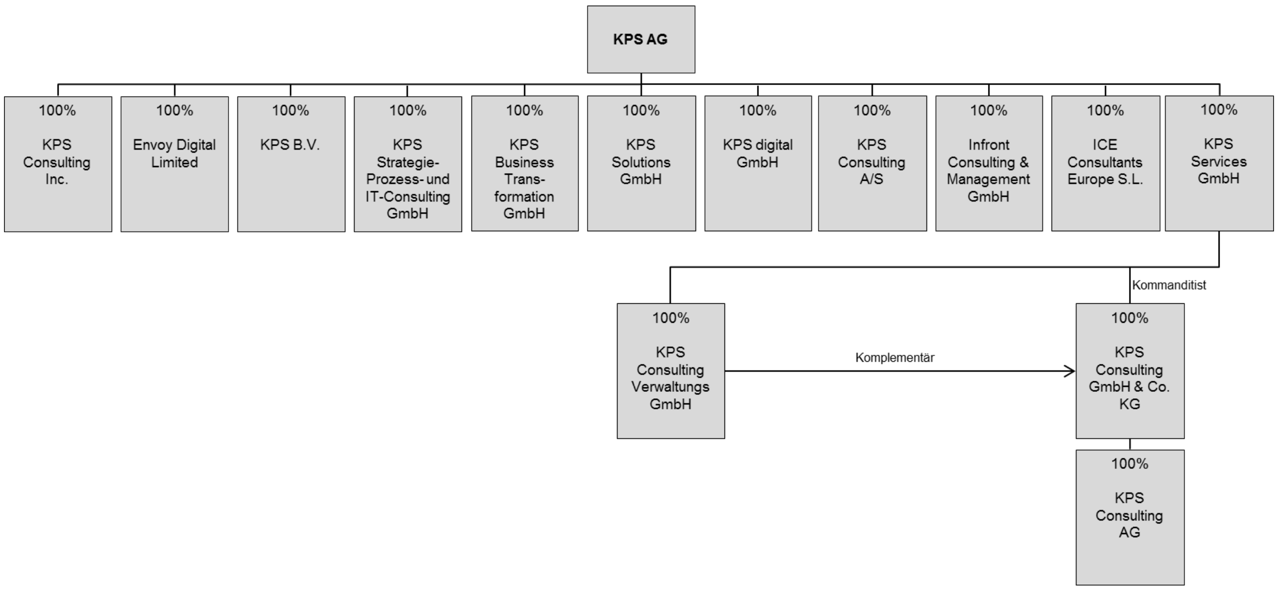
Aktionärsstruktur

Shareholders	
Allianz I.A.R.D. S.A.	6.7%
Dietmar Müller	11.1%
Uwe Grünewald	10.8%
Leonardo Musso	11.0%
Michael Tsifidaris	24.3%
Freeflaot	36.1%
Total	100.0%

Source: KPS AG



Consolidation scope



Source: KPS AG

Significant customers

The customer base of KPS AG includes a number of renowned companies. The focus is on commerce and the consumer goods industry. Below are some selected references:

ESPRIT Dansk Supermarked s.Oliver BOSS HUGO BOSS
FRESSNAPF TROST AUTO SERVICE TECHNIK ESCADA
dodenhof SportScheck Wir machen Sport.
RICHEMONT BESTSELLER Hermes

Source: KPS AG

Business performance HY 2018/19

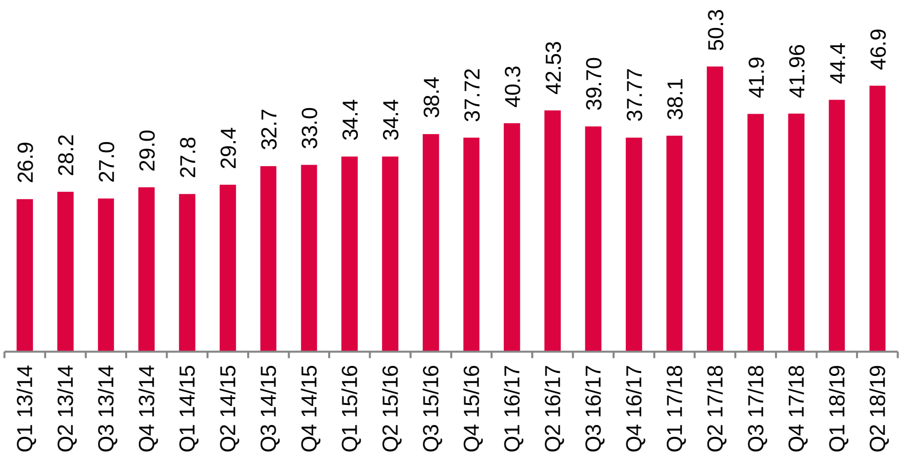
in m €	HY 2016/17	HY 2017/18	HY 2018/19
Sales	82.83	88.37	91.29
EBITDA	13.11	9.37	13.23
EBITDA-Margin	*15.8%*	*10.6%*	*14.5%*
EBIT	12.49	7.51	11.49
EBIT-Margin	*15.1%*	*8.5%*	*12.6%*
Net profit	10.30	5.48	7.40
EPS in €	0.28	0.15	0.20

Source: KPS, GBC

Revenue performance

The first half of the 2018/19 financial year developed very well for KPS AG and was generally in line with our expectations. Revenue increased by 3.3% to €91.28 million (previous year: €88.39 million) despite a larger software deal in the Products and Licences segment which significantly increased revenue in the previous year. The margin did not increase to a proportional extent since this mainly involved the resale of software. According to the management, revenue growth was around 13% when adjusted for this effect.

Revenue development by quarter



Source: KPS, GBC

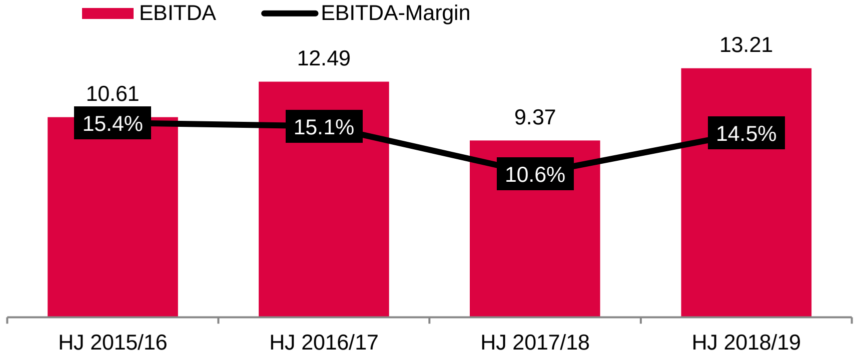
The acquisition of additional transformation projects from existing and new customers was one reason behind the revenue growth. Among other things, a new major customer was acquired in the Scandinavian region. KPS' presence in Denmark is likely to have been an important factor in attracting this customer. In 2016, Danish consulting firm Saphira Consulting (today: KPS Consulting A/S) was acquired in this way, which, as part of the KPS Group, should benefit from the company's size and international direction, making it more attractive for large orders. According to the management, an identical phenomenon has also occurred when recruiting personnel. As a result, it is now easier for acquired companies to recruit qualified personnel because large international companies are generally perceived as being more attractive employers.

At the same time, the company is considerably broadening its customer base. While around 80% of revenue was generated by approx. 15 customers two years ago, the customer base for 80% of the revenue has now risen to 35. This has significantly reduced cluster risk. In parallel to this, the distribution of revenue has also been considerably internationalised. Additionally, the considerable expertise was gradually transferred from the logistics and commerce areas to other sectors in order to expand the range of customers.

Earnings performance

The EBITDA increased by 41.3% to €13.23 million (previous year: €9.37 million). The disproportionate improvement in earnings led to a rise in the EBITDA margin to 14.5% (previous year: 10.6%), with the first six months of 2017/18 being adversely affected by the initial costs of numerous consulting projects in particular. As a result, the company is again approaching the traditionally high EBITDA margin of over 15%. The result could have been even better, however provisions were made for earn-out payments for the acquired subsidiaries. The very good development of the subsidiaries could lead to higher performance-related earn-out payments to the former owners.

Development of EBIT (in € million) and EBIT margin (in %)



Source: KPS, GBC

Furthermore, the cost optimisation strategy is still being implemented successfully within human resources. As a result, employees will undertake an increasing amount of tasks and will gradually decrease their reliance on external services. Material costs therefore fell by 15% to €32.24 million (previous year: €38.00 million), which also resulted from a €5.6 million fall in software acquisitions.

At the same time, more employees were hired so that the project's growing needs could be met. Personnel expenses increased by 9.4% to €33.76 million (previous year: €30.85 million). The regional focus is on Spain in particular, as personnel costs are lower here on average. In addition, the subsidiaries benefit from the KPS acquisition because companies which are under the stewardship of KPS, which is established internationally, are perceived as more attractive and it is therefore easier for them to attract employees. Overall, 16 more employees were hired in Spain, with a further seven added in England. Consequently, the strategy currently seems to have been implemented very successfully and we therefore expect continued margin improvements in the future.

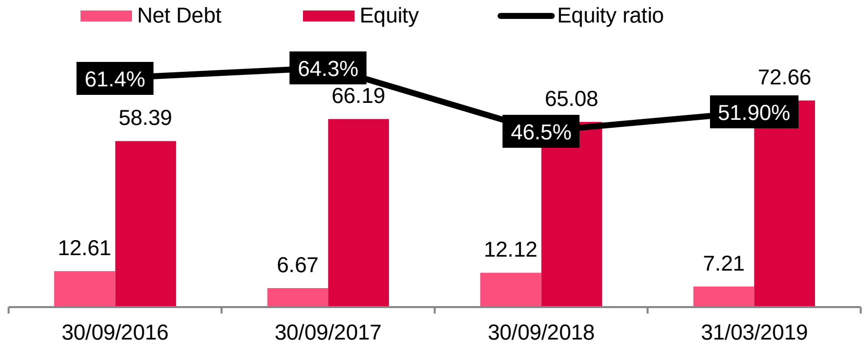
Balance sheet and financial situation

in m €	30.09.2017	31.03.2018	30.09.2018	31.03.2019
Equity	66.19	60.56	65.08	72.66
Equity radtio (in %)	64.3%	39.4%	46.5%	51.9%
Operating Assets	43.28	82.72	79.76	79.80
Working Capital	12.26	15.63	7.51	11.62
Net Debt	-6.67	25.32	12.12	7.21
Cashflow (Operative)	16.79	0.82	17.85	9.41
Cashflow (Investing)	-12.39	-21.57	-24.88	-4.34
Cashflow (Financing)	-12.34	-13.12	2.79	-0.16

Source: KPS, GBC

In terms of the balance sheet, KPS is still in an extremely solid position and as at 31/03/2019, the equity capital was up by 11.6% to €72.66 million (30/09/2018: €65.08 million). However, at the end of the financial year, equity capital was generally reduced by dividend payments. In the same period, the equity ratio increased from 46.5% (30/09/2018) to 51.9% (31/03/2019). As a result, the equity ratio is below the last few years' values as corporate acquisitions were mainly financed using debt capital.

Development of relevant balance sheet ratios (in m €)



Source: KPS, GBC

Overall, non-current liabilities, amounting to €28.53 million, were at the same level as the previous year (30/09/2018: €27.96 million). In addition, current financial liabilities have already begun to be attributed. Current liabilities fell by 17.2% to €38.78 million (30/09/2018: €46.83 million), with financial liabilities in particular down from €8.80 million (30/09/2018) to €4.8 million (31/03/2019).

In the past, KPS AG consistently implemented the high repayment strategy and was therefore able to minimise interest expenses. We assume that, due to the high operating cash flow, interest-bearing liabilities will be cleared in full in the medium term.

Forecasts and model assumptions

P&L (in m €)	FY 2018	FY 2019e	FY 2020e
Sales	172.22	179.97	188.97
EBITDA	20.02	26.47	28.76
EBITDA-Margin	*11.6%*	*14.7%*	*15.2%*
EBIT	16.59	23.17	25.56
EBIT-Margin	*9.6%*	*12.9%*	*13.5%*
Net profit	9.83	15.31	17.08
EPS in €	0.26	0.41	0.46

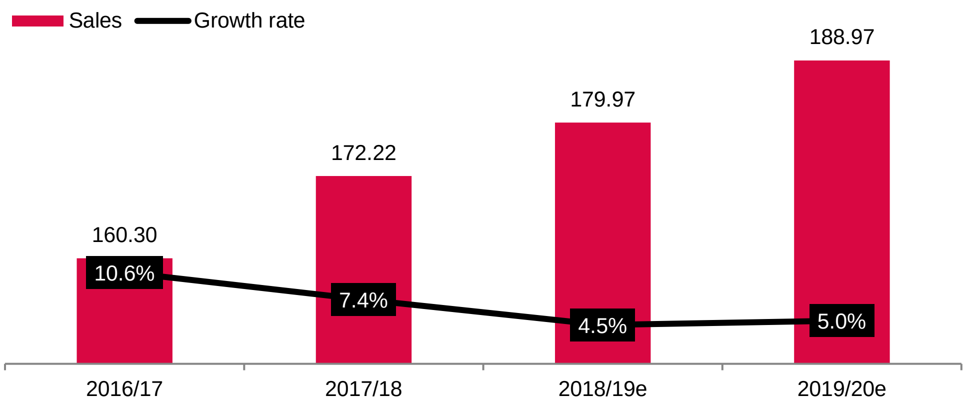
Source: GBC

Revenue forecasts

On the basis of revenue and profit for the first six months of 2018/19, we confirm our forecast. For the current financial year 2018/19, we expect revenue of €179.97 million, with revenue of €188.97 million for 2019/20. Our forecast remains in the limits of the €170.0-€180.0 million revenue guidance and of the €22.0-€27.0 million EBIDTA guidance.

Due to a major customer experiencing a drop in revenue, the company expects moderate growth for the current financial year, below that of the double-digit growth momentum of previous years. In our view, the company should return to a more dynamic growth path in the medium term. However, we expect that the major customer's effect on revenue will still be evident in 2019/20.

Expected revenue development (in € million)



Source: GBC

We regard the internationalisation strategy and the improvements in how the acquired companies address customers in particular as growth drivers in the medium- and long-term. More large-scale projects in Scandinavia or an even greater number of projects in Great Britain could be acquired in this way using Envoy Digital. At present, management does not expect the potential Brexit to negatively impact the company's development. Even in the case of a hard Brexit, digital transformation projects should feel little or no effect.

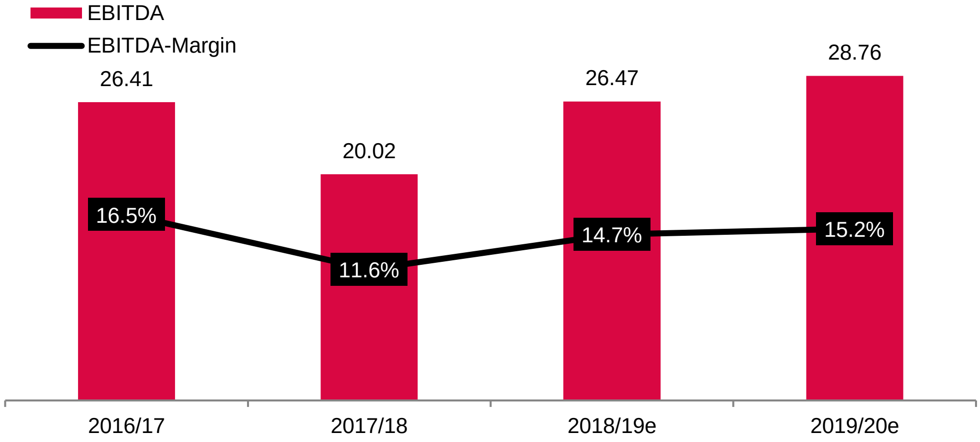
Overall, the company has positioned itself well internationally by means of the acquisitions and we expect a significantly higher growth momentum to once again become apparent in the long term.

Earnings forecasts

In line with the increase in revenue, we expect a disproportionate improvement in earnings. For the current financial year, we expect an EBITDA of €26.47 million, within the guidance of €22.0 million to €27.0 million. Based on the half-year figures (first half-year 2018/19 EBITDA: €13.23 million), we confirm our forecasts are at the upper end of the guidance. For the subsequent year 2019/20, we expect a further disproportionate increase to €28.76 million. This would equate to a margin improvement from 14.7% (2018/19) to 15.2% (2019/20).

The diminishing effect of the major customer's declining revenue is another reason for the margin improvement. This impacted financial year 2017/18 in particular, with gradually lessened effects for 2018/19 and 2019/20.

Expected development of EBITDA and the EBITDA margin



Source: GBC

In our view, the company should once again achieve historically high profitability and reach an EBITDA margin of at least 15% in the medium term. The reasons for this include the switch from using external services to using the company's own employees, plus the increased use of employees from countries with a low wage level.

Furthermore, we should be able to tap into further margin potential by increasing internal digitisation. The company also relies in part on the industrialisation of the consulting approach. In this way, the design centre in Dortmund could help to develop important standard solutions that could be distributed in scalable form.

Consequently, we expect a gradual margin improvement on the whole and we view the company as being very well positioned in an attractive market.

We confirm our forecast and continue to assign it the buy rating with a stock price target of €13.20 per share.

VALUATION

Model assumptions

We rated KPS AG using a three-stage DCF model. Starting with the concrete estimations for 2018/19 and 2019/20 in phase 1, in the second phase, from 2020/21 to 2025/26, our forecast uses value drivers. Here we expect a sales increase of 11.0 %. We have assumed an EBITDA margin target of 17.0%. We have taken into account tax rates of 30.0 %. Additionally, a residual value is determined in the third phase by using the perpetual annuity by the end of the forecast horizon. As the final value, we assume a growth rate of 2.0%.

Determination of capital costs

The weighted average cost of capital (WACC) of KPS AG is calculated using equity costs and debt costs. The market premium, the company-specific beta, as well as the risk-free interest rate have to be determined in order to determine the equity cost.

The risk-free interest rate is derived in accordance with the recommendations of the expert committee for company valuations and business administration (FAUB) of the IDW (Institut der Wirtschaftsprüfer in Deutschland e.V.) from the current interest rate yield curves for risk-free bonds. The zero bond interest rates according to the Svensson method published by the German Federal Bank form the underlying basis. To smooth out short-term market fluctuations, we use the average yields over the previous three months and round up the result to 0.25 basis points. **The value of the currently used risk-free interest rate is 1.00% (before: 1.25%).**

We set the historical market premium of 5.50% as a reasonable expectation of the market premium. This is supported by historical analyses of stock market returns. The market premium reflects the percentage by which the stock market is expected to be more profitable than low-risk government bonds.

According to GBC estimates, we have determined a beta of 1.41 (before: 1.41).

Based on these assumptions, the calculated equity costs amount to 8.8 % (beta multiplied by the risk premium plus the risk-free interest rate). Since we assume a sustainable weighting of the equity costs of 90 %, the resulting weighted average costs of capital (WACC) amount to 8.1%.

Evaluation result

The discounting of future cash flows is based on the entity approach. In our calculation, the result for the corresponding weighted average costs of capital (WACC) is 8.1%. The resulting fair value per share at the end of the 2018/19 financial year corresponds to the target price of € 13.20 (before: 13.20€).

GBC AG Investment Research

DCF-Modell

KPS AG - Discounted cash flow (DCF) model scenario

Value driver of the DCF - model according to estimate phase:

consistency - Phase	
Sales growth	11.0%
EBITDA-Margin	17.0%
Depreciation to fixed assets	6.6%
Working Capital to sales	8.3%

final - Phase	
Eternal growth rate	2.0%
Eternal EBITA - margin	17.0%
Eternal effective tax rate	30.0%

Three phases - Model:

phase	estimate		consistency						final
in €m	FY 19e	FY 20e	FY 21e	FY 22e	FY 23e	FY 24e	FY 25e	FY 26e	Terminal Value
Sales	179.97	188.97	209.72	232.75	258.30	286.67	318.14	353.07	
Sales change	4.5%	5.0%	11.0%	11.0%	11.0%	11.0%	11.0%	11.0%	2.0%
Sales to fixed assets	2.24	2.33	2.65	3.02	3.44	3.92	4.46	5.07	
EBITDA	26.47	28.76	35.65	39.57	43.91	48.73	54.08	60.02	
EBITDA-margin	14.7%	15.2%	17.0%	17.0%	17.0%	17.0%	17.0%	17.0%	
EBITA	23.17	25.56	30.33	34.38	38.87	43.82	49.30	55.35	
EBITA-Margin	12.9%	13.5%	14.5%	14.8%	15.0%	15.3%	15.5%	15.7%	17.0%
Taxes on EBITA	-6.95	-7.67	-9.10	-10.31	-11.66	-13.15	-14.79	-16.61	
Taxes to EBITA	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%
EBI (NOPLAT)	16.22	17.89	21.23	24.07	27.21	30.68	34.51	38.75	
Return on capital	18.6%	19.1%	22.0%	24.9%	28.2%	31.8%	35.6%	39.7%	43.3%
Working Capital (WC)	13.17	15.38	17.41	19.32	21.44	23.79	26.41	29.31	
WC to sales	7.3%	8.1%	8.3%	8.3%	8.3%	8.3%	8.3%	8.3%	
Investment in WC	-5.67	-2.21	-2.03	-1.91	-2.12	-2.35	-2.61	-2.90	
Operating fixed assets (OAV)	80.44	81.24	79.22	77.03	74.98	73.07	71.28	69.61	
Depreciation on OAV	-3.30	-3.20	-5.32	-5.19	-5.05	-4.91	-4.79	-4.67	
Depreciation to OAV	4.1%	3.9%	6.6%	6.6%	6.6%	6.6%	6.6%	6.6%	
Investment in OAV	-3.98	-4.00	-3.30	-3.00	-3.00	-3.00	-3.00	-3.00	
Capital employed	93.61	96.62	96.62	96.34	96.42	96.86	97.69	98.92	
EBITDA	26.47	28.76	35.65	39.57	43.91	48.73	54.08	60.02	
Taxes on EBITA	-6.95	-7.67	-9.10	-10.31	-11.66	-13.15	-14.79	-16.61	
Total investment	-12.87	-9.44	-8.56	-8.14	-8.35	-7.08	-5.61	-5.90	
Investment in OAV	-3.98	-4.00	-3.30	-3.00	-3.00	-3.00	-3.00	-3.00	
Investment in WC	-5.67	-2.21	-2.03	-1.91	-2.12	-2.35	-2.61	-2.90	
Investment in Goodwill	-3.23	-3.23	-3.23	-3.23	-3.23	-1.72	0.00	0.00	
Free cash flows	6.65	11.65	17.99	21.11	23.90	28.51	33.68	37.52	672.43

Value operating business (due date)	513.02	542.81
Net present value explicit free cash flows	122.66	120.92
Net present value of terminal value	390.35	421.89
Net debt	19.85	22.43
Value of equity	493.17	520.39
Minority interests	0.00	0.00
Value of share capital	493.17	520.39
Outstanding shares in m	37.37	37.37
Fair value per share in €	**13.20**	13.92

Cost of Capital:

Riskfree rate	1.0%
Market risk premium	5.5%
Beta	1.41
Cost of Equity	8.8%
Target weight	90.0%
Cost of Debt	2.5%
Target weight	10.0%
Taxshield	28.7%
WACC	**8.1%**

Return on Capital	WACC				
	7.1%	**7.6%**	**8.1%**	**8.6%**	**9.1%**
42.3%	15.77	14.22	12.94	11.87	10.96
42.8%	15.93	14.37	13.07	11.98	11.06
43.3%	16.09	14.51	**13.20**	12.10	11.16
43.8%	16.26	14.65	13.32	12.21	11.26
44.3%	16.42	14.79	13.45	12.32	11.36

ANNEX

I.
Research under MiFID II
1. There is a contract between the research company GBC AG and the issuer regarding the independent preparation and publication of this research report on the issuer. GBC AG is remunerated for this by the issuer.
2. The research report is simultaneously made available to all interested investment services companies.

II.
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Legal information and disclosures as required by section 85 of Securities Trading Act (WpHG) and Financial Analysis Directive (FinAnV)

This information can also be found on the internet at the following address:
http://www.gbc-ag.de/de/Offenlegung.htm

Section 2 (I) Updates
A detailed update of the present analysis/analyses at any fixed date has not been planned at the current time. GBC AG reserves the right to update the analysis without prior notice.

Section 2 (II) Recommendation/ Classifications/ Rating
Since 1/7/2006 GBC AG has used a 3-level absolute share rating system. Since 1/7/2007 these ratings relate to a time horizon of a minimum of 6 to a maximum of 18 months. Previously the ratings related to a time horizon of up to 12 months. When the analysis is published, the investment recommendations are defined based on the categories described below, including reference to the expected returns. Temporary price fluctuations outside of these ranges do not automatically lead to a change in classification, but can result in a revision of the original recommendation.
The recommendations/ classifications/ ratings are linked to the following expectations:

BUY	The expected return, based on the derived target price, incl. dividend payments within the relevant time horizon is >= + 10%.
HOLD	The expected return, based on the derived target price, incl. dividend payments within the relevant time horizon is > - 10% and < + 10%.
SELL	The expected return, based on the calculated target price, incl. dividend payments within the relevant time horizon, is <= - 10%.

GBC AG's target prices are determined using the fair value per share, derived using generally recognised and widely used methods of fundamental analysis, such as the DCF process, peer-group benchmarking and/or the sum-of-the-parts process. This is done by including fundamental factors such as e.g. share splits, capital reductions, capital increases, M&A activities, share buybacks, etc.

Section 2 (III) Past recommendations

Past recommendations by GBC on the current analysis/analyses can be found on the internet at the following address:
http://www.gbc-ag.de/de/Offenlegung.htm

Section 2 (IV) Information basis

For the creation of the present analysis/analyses publicly available information was used about the issuer(s) (where available, the last three published annual and quarterly reports, ad hoc announcements, press releases, share prospectuses, company presentations, etc.) which GBC believes to be reliable. In addition, discussions were held with the management of the company/companies involved, for the creation of this analysis/these analyses, in order to review in more detail the information relating to business trends.

Section 2 (V) 1, Conflicts of interest as defined in section 85 of the Securities Trading Act (WpHG) and in section 20 of Market Abuse Regulation (MAR)

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