

Analyst

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Altium (ALU)

Easy tiger

Recommendation

Hold (Buy)

Price

\$38.25

Target (12 months)

\$40.00 (previously \$37.50)

GICS Sector

Software and Services

Expected Return

| | |
|-----------------------|------|
| Capital growth | 4.6% |
| Dividend yield | 1.3% |
| Total expected return | 5.9% |

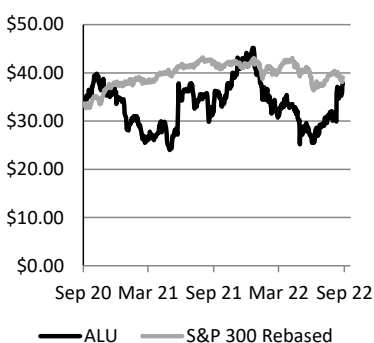
Company Data & Ratios

| | |
|------------------------|-------------------|
| Enterprise value | \$4,760m |
| Market cap | \$5,035m |
| Issued capital | 131.6m |
| Free float | 95% |
| Avg. daily val. (52wk) | \$15.9m |
| 12 month price range | \$24.32 - \$43.50 |

Price Performance

| | (1m) | (3m) | (12m) |
|----------------|-------|-------|-------|
| Price (A\$) | 31.71 | 28.89 | 32.10 |
| Absolute (%) | 19.21 | 30.84 | 17.76 |
| Rel market (%) | 21.60 | 36.16 | 26.93 |

Absolute Price



SOURCE: IRESS

Modest upgrades

We have reviewed our forecasts post the release of the FY22 result last month and put through modest revenue and EBITDA upgrades of 1%, 2% and 3% in FY23, FY24 and FY25. The upgrades have mainly been driven by increases in our subscription and maintenance revenue forecasts given this was the area that positively surprised in the FY22 result and the strong growth looks set to continue with solid increases in the average price for software seats on subscription. We now forecast FY23 revenue and EBITDA margin of US\$264.4m and 36.0% which are still within the guidance ranges of revenue b/w US\$255-265m and an EBITDA margin of b/w 35-37%. We also now forecast FY26 revenue of US\$448.1m which, however, is still short of Altium's aspirational target of US\$500m in this period.

PT up 7% to \$40.00

We have updated each valuation used in the calculation of our price target for the earnings changes as well as market movements and time creep. There are no changes in the key assumptions we apply which are no premium or discount in the relative valuations and a 9.0% WACC and 5.0% terminal growth rate in the DCF. The net result is a 7% increase in the PT to \$40.00 which has been driven by relatively consistent increases of 6-7% in each of the three valuations.

Investment view: Downgrade to HOLD

At our updated PT of \$40.00 the expected excess return is <15% so we downgrade our recommendation to HOLD. We continue to be positive on the outlook for Altium but now see the stock as around fair value trading on an FY23 EV/EBITDA and PE ratio of 36x and 58x. We also see a lack of short term potential catalysts for the stock given Altium does not tend to make many announcements outside of results and we do not expect the company to upgrade its guidance at the AGM in November given it will still be relatively early in the financial year. In our view the key risk to our downgrade is the company makes an accretive and/or strategic acquisition of reasonable size which seems a possibility especially with the strong Balance Sheet.

Earnings Forecast

| Year end 30 June | 2022 | 2023e | 2024e | 2025e |
|-----------------------|--------|-------|-------|-------|
| Total revenue (US\$m) | 220.8 | 264.4 | 319.4 | 380.3 |
| EBITDA (US\$m) | 79.8 | 95.2 | 121.4 | 150.2 |
| NPAT (US\$m) | 55.5 | 62.6 | 82.5 | 104.4 |
| EPS (diluted) (US¢ps) | 42.1 | 47.5 | 62.5 | 78.9 |
| EPS growth (%) | 57% | 13% | 31% | 26% |
| PER (x) | 65.9 | 58.4 | 45.9 | 36.3 |
| Price/CF (x) | 50.5 | 47.0 | 40.3 | 31.4 |
| EV/EBITDA (x) | 43.2 | 36.3 | 29.4 | 23.8 |
| Dividend (A¢ps) | 47.0 | 51.0 | 59.0 | 69.0 |
| Yield (%) | 1.2% | 1.3% | 1.5% | 1.8% |
| ROE (%) | 20.2% | 22.1% | 26.9% | 30.3% |
| Franking (%) | 100.0% | 0.0% | 0.0% | 0.0% |

SOURCE: BELL POTTER SECURITIES ESTIMATES

Forecast and Valuation Changes

Modest Upgrades

We have reviewed our forecasts post the release of the FY22 result last month and put through modest revenue and EBITDA upgrades of 1%, 2% and 3% in FY23, FY24 and FY25. The upgrades have mainly been driven by increases in our subscription and maintenance revenue forecasts given this was the area that positively surprised in the FY22 result and the strong growth looks set to continue with solid increases in the average price for software seats on subscription. We now forecast FY23 revenue and EBITDA margin of US\$264.4m and 36.0% which are still within the guidance ranges of revenue b/w US\$255-265m and an EBITDA margin of b/w 35-37%. We also now forecast FY26 revenue of US\$448.1m which, however, is still short of Altium's aspirational target of US\$500m in this period.

A summary of the changes in our key forecasts is shown below. There are no changes in our DPS forecasts given the relatively modest EPS upgrades.

Figure 1 - Change in key forecasts

| Year end 30 June | FY23e | | | FY24e | | | FY25e | | |
|-----------------------------------|-------|-------|--------|-------|-------|--------|-------|-------|--------|
| | Old | New | Change | Old | New | Change | Old | New | Change |
| Revenue (US\$m) | 262.4 | 264.4 | 0.8% | 314.3 | 319.4 | 1.6% | 370.7 | 380.3 | 2.6% |
| EBITDA | 94.5 | 95.2 | 0.8% | 119.4 | 121.4 | 1.6% | 146.4 | 150.2 | 2.6% |
| NPAT from cont. ops. | 62.0 | 62.6 | 0.9% | 81.0 | 82.5 | 1.8% | 101.5 | 104.4 | 2.8% |
| Diluted EPS from cont. ops. (USc) | 47.1c | 47.5c | 0.9% | 61.4c | 62.5c | 1.8% | 76.8c | 78.9c | 2.8% |
| DPS (Ac) | 51.0c | 51.0c | 0.0% | 59.0c | 59.0c | 0.0% | 69.0c | 69.0c | 0.0% |

SOURCE: BELL POTTER SECURITIES ESTIMATES

7% Increase in PT to \$40.00

We have updated each valuation used in the calculation of our price target for the earnings changes as well as market movements and time creep. There are no changes in the key assumptions we apply which are no premium or discount in the relative valuations and a 9.0% WACC and 5.0% terminal growth rate in the DCF.

The change in each valuation and the impact on our PT calculation is shown below.

Figure 2 - Change in valuations and impact on PT

| Methodology | Old (as at 22-Aug-22) | | | New (as at 13-Sep-22) | | |
|--------------|-----------------------|-------------|----------------|-----------------------|-------------|----------------|
| | Valuation per share | % weighting | Price target | Valuation per share | % weighting | Price target |
| PE ratio | \$37.51 | 33% | \$12.50 | \$40.23 | 33% | \$13.41 |
| EV/EBITDA | \$36.73 | 33% | \$12.24 | \$39.08 | 33% | \$13.03 |
| DCF | \$38.27 | 33% | \$12.76 | \$40.69 | 33% | \$13.56 |
| Total | | | \$37.50 | | | \$40.00 |

SOURCE: BELL POTTER SECURITIES ESTIMATES

The figure shows a relatively consistent percentage increase in each valuation. The net result is a 7% increase in the PT to \$40.00 which is <15% premium to the share price so we downgrade our recommendation from BUY to HOLD.

Altium

Company Description

Altium Limited (Altium) develops and sells software and hardware for the design and development of electronic products. The company has three key products:

- **Altium Designer:** Software for the design of printed circuit boards (PCBs);
- **Nexus:** A collaborative, cloud enabled PCB design solution; and
- **Octopart:** An electronic parts search engine.

Altium is based in San Diego, California and sells its products globally (>95% of revenue is outside Australia). The company is one of the largest providers globally of PCB design software and has an estimated market share of around 25%.

Investment Thesis

We maintain our BUY recommendation on Altium. Our investment thesis is based on:

- **Valuation:** Our 12 month price target for Altium is \$38.00. The price target is generated from a blend of three valuation methodologies we apply to the company: PE ratio, EV/EBITDA and DCF. The price target is a 5% premium to the current share price and the total expected return (including the dividend yield) is 6%.
- **Higher recurring revenue:** Altium has been steadily increasing its recurring revenue base over the past decade or so with a shift to subscription. Recurring revenue represented 75% of total revenue in FY22 which was up from 65% in FY21. Altium has a target of reaching 95% recurring revenue by FY25 (excluding China and developing countries).
- **Potential takeover target:** Altium has already received an unsolicited takeover offer from Autodesk at \$38.50 which was rejected. Our view is Autodesk's Fusion 360 platform is lacking a high powered ECAD offering so we believe Autodesk would still be very interested in Altium and may come back with a revised offer.

Key Risks

Key downside risks to our estimates and valuation include (but are not limited to):

- **Foreign currency fluctuations:** The majority of Altium's sales are in USD and EUR while the majority of Altium's costs are in USD. There is, therefore, a currency risk from fluctuations in the USD/EUR exchange rate. If there is a material appreciation of the USD against then EUR then this would have a negative impact on our forecasts.
- **Increased competition:** Altium is releasing new products to target the low-end and high-end areas of the market and in our forecasts we have assumed some success in penetrating these new areas. A risk is these products are not successful or cause a competitive response from the established players in these areas of the market.
- **Global economy:** The key market for Altium is the global PCB market and the future condition of the global economy will therefore have an impact on Altium and the growth of its key market. A risk for Altium is a downturn in one or both of Europe and the US as these two regions combined represent approximately 80% of Altium's sales.

Table 1 - Financial summary

| Altium (ALU) | | | | | | Share price: | \$38.25 | Target price: | \$40.00 | | |
|-------------------------------|--------|--------|--------|--------|--------|------------------------------|---------|---------------|----------|--------|--------|
| | | | | | | No. of issued shares: | 131.6m | Market cap: | \$5,035m | | |
| Profit & Loss (US\$m) | | | | | | Valuation data | | | | | |
| Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e | Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e |
| Revenue | 180.2 | 220.8 | 264.4 | 319.4 | 380.3 | NPAT from cont. ops. (US\$m) | 35.3 | 55.5 | 62.6 | 82.5 | 104.4 |
| Change | 6% | 23% | 20% | 21% | 19% | Diluted EPS (USc) | 26.9 | 42.1 | 47.5 | 62.5 | 78.9 |
| | | | | | | Change | 71% | 57% | 13% | 31% | 26% |
| Expenses (excl. D&A, int.) | -120.2 | -141.0 | -169.2 | -198.0 | -230.1 | Diluted EPS (Ac) | 35.8 | 58.0 | 65.5 | 83.3 | 105.3 |
| % of revenue | -67% | -64% | -64% | -62% | -61% | P/E ratio (x) | 106.8 | 65.9 | 58.4 | 45.9 | 36.3 |
| EBITDA | 60.0 | 79.8 | 95.2 | 121.4 | 150.2 | CFPS (Ac) | 62.7 | 75.8 | 81.4 | 95.0 | 121.9 |
| Depreciation | -8.5 | -8.4 | -8.1 | -7.9 | -7.7 | Price/CF (x) | 61.0 | 50.5 | 47.0 | 40.3 | 31.4 |
| Amortisation | -3.4 | -3.6 | -3.7 | -3.8 | -3.9 | DPS (Ac) | 40.0 | 47.0 | 51.0 | 59.0 | 69.0 |
| EBIT | 48.1 | 67.9 | 83.3 | 109.6 | 138.6 | Yield | 1.0% | 1.2% | 1.3% | 1.5% | 1.8% |
| Net interest (exp)/rev. | -0.4 | 0.0 | 0.1 | 0.3 | 0.6 | Franking | 8% | 100% | 0% | 0% | 0% |
| Pre-tax profit | 47.7 | 67.9 | 83.5 | 109.9 | 139.2 | EV/Revenue (x) | 19.8 | 15.6 | 13.1 | 11.2 | 9.4 |
| Income tax expense | -12.4 | -12.4 | -20.9 | -27.5 | -34.8 | EV/EBITDA (x) | 59.5 | 43.2 | 36.3 | 29.4 | 23.8 |
| NPAT from cont. ops. | 35.3 | 55.5 | 62.6 | 82.5 | 104.4 | NTA per share (Ac) | 212.1 | 242.3 | 254.1 | 272.4 | 312.9 |
| Profit from discount ops. | 71.7 | -0.1 | 0.0 | 0.0 | 0.0 | Price/NTA (x) | 18.0 | 15.8 | 15.1 | 14.0 | 12.2 |
| NPAT | 107.0 | 55.3 | 62.6 | 82.5 | 104.4 | Performance ratios | | | | | |
| Cash Flow (US\$m) | | | | | | Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e |
| Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e | EBITDA margin | 33.3% | 36.2% | 36.0% | 38.0% | 39.5% |
| EBITDA | 60.0 | 79.8 | 95.2 | 121.4 | 150.2 | EBIT margin | 26.7% | 30.7% | 31.5% | 34.3% | 36.4% |
| Change in working capital | 15.6 | 2.0 | -8.0 | -15.0 | -13.9 | Return on assets | 9.2% | 14.5% | 15.8% | 19.4% | 22.3% |
| Gross operating cash flow | 75.6 | 81.8 | 87.2 | 106.3 | 136.3 | Return on equity | 13.8% | 20.2% | 22.1% | 26.9% | 30.3% |
| Interest received | 0.2 | 0.4 | 0.9 | 1.1 | 1.3 | ROIC | NM | NM | NM | NM | NM |
| Interest paid | -0.7 | -0.5 | 0.1 | 0.3 | 0.6 | Payout ratio | 111.5% | 80.7% | 77.7% | 70.7% | 65.4% |
| Tax paid | -13.4 | -9.2 | -10.4 | -13.7 | -17.4 | Effective tax rate | -26.0% | -18.2% | -25.0% | -25.0% | -25.0% |
| Operating cash flow | 61.7 | 72.5 | 77.7 | 94.0 | 120.9 | Leverage ratios | | | | | |
| Payments for subsidiary | -3.1 | 0.0 | 0.0 | 0.0 | 0.0 | Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e |
| Payments for PPE | -1.7 | -1.0 | -1.5 | -2.0 | -2.5 | Net debt/(cash) (A\$m) | -255.4 | -274.9 | -290.4 | -306.0 | -350.4 |
| Proceeds of sale of PPE | 85.8 | -15.8 | 0.0 | 0.0 | 0.0 | Net debt/equity | NM | NM | NM | NM | NM |
| Investing cash flow | 80.3 | -17.3 | -2.0 | -2.5 | -3.0 | Gearing | NM | NM | NM | NM | NM |
| Proceeds from equity/options | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | Net debt/EBITDA (x) | NM | NM | NM | NM | NM |
| Dividends paid | -37.6 | -40.1 | -64.5 | -72.5 | -84.5 | Net interest cover (x) | >100 | >100 | >100 | >100 | >100 |
| Repayment of borrowings | -5.5 | -5.7 | 0.0 | 0.0 | 0.0 | Segmentals (US\$m) | | | | | |
| Payment for treasury shares | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e |
| Financing cash flows | -43.1 | -45.8 | -64.5 | -72.5 | -84.5 | Revenue | | | | | |
| Net change in cash | 98.9 | 9.4 | 11.3 | 19.0 | 33.3 | Software licence revenue | 79.1 | 85.2 | 95.9 | 107.9 | 121.4 |
| Cash at start of period | 93.1 | 191.5 | 199.3 | 210.5 | 229.5 | Hardware revenue | 2.4 | 1.6 | 1.5 | 1.4 | 1.3 |
| Exchange rate impact | -0.5 | -1.6 | 0.0 | 0.0 | 0.0 | Subscription revenue | 68.7 | 80.4 | 100.5 | 130.7 | 166.6 |
| Cash at end of period | 191.5 | 199.3 | 210.5 | 229.5 | 262.8 | Service revenue | 2.8 | 3.5 | 3.9 | 4.3 | 4.6 |
| Balance Sheet (US\$m) | | | | | | Search advertising revenue | 26.8 | 49.8 | 62.3 | 74.7 | 85.9 |
| Year end 30 Jun | 2021 | 2022 | 2023e | 2024e | 2025e | Other revenue | 0.4 | 0.3 | 0.3 | 0.3 | 0.4 |
| Cash | 191.5 | 199.3 | 210.5 | 229.5 | 262.8 | Sales revenue | 180.2 | 220.8 | 264.4 | 319.4 | 380.3 |
| Receivables | 66.1 | 63.5 | 76.9 | 96.1 | 114.5 | Interest income | 0.3 | 0.7 | 0.9 | 1.1 | 1.3 |
| Inventories | 1.9 | 1.2 | 1.3 | 1.6 | 1.9 | Other revenue | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other current assets | 6.3 | 9.9 | 9.9 | 9.9 | 9.9 | Total revenue | 180.5 | 221.5 | 265.3 | 320.4 | 381.6 |
| PPE | 16.2 | 12.0 | 9.4 | 7.5 | 6.1 | Growth | | | | | |
| Intangibles - Goodwill | 6.0 | 4.9 | 4.9 | 4.9 | 4.9 | Software licence revenue | 0% | 8% | 13% | 13% | 13% |
| Intangibles - Other | 41.1 | 39.0 | 35.8 | 32.5 | 29.1 | Hardware revenue | 0% | 0% | -5% | -5% | -5% |
| Deferred tax assets | 49.5 | 46.7 | 42.7 | 38.7 | 34.8 | Subscription revenue | 9% | 17% | 25% | 30% | 28% |
| Other non-current assets | 4.5 | 4.9 | 4.9 | 4.9 | 4.9 | Service revenue | -21% | 22% | 13% | 10% | 8% |
| Total assets | 383.2 | 381.5 | 396.5 | 425.7 | 469.0 | Sales revenue | 6% | 23% | 20% | 21% | 19% |
| Payables | 20.8 | 20.1 | 26.5 | 32.0 | 38.2 | Interims | | | | | |
| Current borrowings | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | Year end 30 Jun | | 1HFY21 | 2HFY21 | 1HFY22 | 2HFY22 |
| Current lease liabilities | 5.6 | 5.4 | 5.4 | 5.4 | 5.4 | Revenue (US\$m) | | 80.0 | 100.3 | 102.2 | 118.6 |
| Current provisions | 30.6 | 7.5 | 7.5 | 7.5 | 7.5 | Change | | -14% | 31% | 28% | 18% |
| Deferred revenue | 52.4 | 56.4 | 56.4 | 56.4 | 56.4 | EBITDA | | 27.0 | 33.0 | 34.8 | 45.0 |
| Non-current deferred revenue | 7.5 | 8.8 | 8.8 | 8.8 | 8.8 | Depreciation | | -4.4 | -4.1 | -4.0 | -4.3 |
| Non-current borrowings | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | Amortisation | | -1.6 | -1.7 | -1.8 | -1.8 |
| Non-current lease liabilities | 5.5 | 4.1 | 4.1 | 4.1 | 4.1 | EBIT | | 21.0 | 27.1 | 29.0 | 38.9 |
| Non-current provisions | 0.4 | 0.5 | 0.5 | 0.5 | 0.5 | Net interest (exp)/rev. | | -0.3 | -0.1 | 0.0 | -0.1 |
| Other non-current liabilities | 4.6 | 3.8 | 3.8 | 3.8 | 3.8 | Pre-tax profit | | 20.7 | 27.0 | 29.0 | 38.8 |
| Total liabilities | 127.3 | 106.6 | 113.1 | 118.6 | 124.7 | Income tax expense | | -4.1 | -8.3 | -6.1 | -6.2 |
| Contributed equity | 127.7 | 127.7 | 127.7 | 127.7 | 127.7 | NPAT from cont. ops. | | 16.6 | 18.7 | 22.9 | 32.6 |
| Reserves | 22.1 | 25.9 | 25.9 | 25.9 | 25.9 | | | | | | |
| Retained earnings/(losses) | 106.1 | 121.3 | 129.8 | 153.5 | 190.8 | | | | | | |
| Total shareholders' equity | 255.9 | 274.9 | 283.4 | 307.1 | 344.3 | | | | | | |

SOURCE: BELL POTTER SECURITIES ESTIMATES

Recommendation structure

Buy: Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

Hold: Expect total return between -5% and 15% on a 12 month view

Sell: Expect <-5% total return on a 12 month view

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Such investments may carry an exceptionally high level of capital risk and volatility of returns.

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