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Capital Appreciation

ANCHOR STOCKBROKERS

A sharp rise in earnings anticipated

- We adjust the reported FY24 HEPS of 13.6c for the GovChat provisions of R13m, deriving a normalised HEPS of 14.7c (+11%), below our 16.8c estimate. The DPS of 10c (+21%) puts the stock on a favourable 8% dividend yield. The Payment business delivered in line with expectations, however, Software disappointed.
- We reiterate our view that the Payments business has strong underlying growth fundamentals, as evidenced by 9% growth in the terminal estate. Sales revenue has been negatively impacted by the shift towards rentals by certain banks (circa 25% of new business), lower priced Android devices that are growing in popularity given their functionality and the extension of device replacement cycles by banks given capex constraints. Maintenance & Support and Transaction related revenue are less impacted. We believe the above trends are largely cyclical - retailers will not allow themselves to be technologically disadvantaged (security, functionality etc.) with outdated POS devices, requiring replacement from their bankers. The phase out of 2G and 3G networks commencing June 2025 (on which the bulk of issued POS devices are dependent) will also stimulate replacement.
- Payment revenue was up 7.5%, dragged down by terminal sales, down 14.5%. Sales should recover in FY25E as replacements accelerate – several meaningful post year end contracts have been awarded. We forecast sales revenue to rise 21% in FY25E and 38% in FY26E. Maintenance & Support revenue rose 5.4% and should broadly track the growth in the estate, including rentals. Rental income rose 95% and we expect the strong growth to continue with 39% growth in FY25E (we forecast R77m of which R49m is also contracted for). Lastly, Transaction related revenue rose 63%, benefiting from software sales – POS software is now also installed on third party devices. Halo Dot is facing slower than anticipated global adoption of SoftPOS, yet it is consistently winning contracts. LayUp is progressing well and Multi-lane retailing and ACI are gaining traction – these initiatives are not reflected in our revenue outlook but have been expensed in the income statement.
- Payment EBITDA margins rose from 39% to 44%, a level management believes is sustainable going forward. Margins benefited from the sharp rise in Transaction related revenue and increased rentals, which are more profitable than outright sales. To highlight this, there was R50m (R31m + R19m) of rental devices acquired in FY24 and FY23, achieving rental income of R56m in FY24 with further contractual anticipated revenue of R98m over the next three years.
- Software revenue rose 31%, positively impacted by the acquisition of Dariel effective 1 July 2023. Excluding Dariel, revenue was flat, considerably off its historic growth run rate. EBITDA margins declined from 18% to 11% (these tracked above 20% pre FY23) due to idle staff resources as the pipeline of new business is pushed out further. Tenders and contracts are not being lost to competitors, there is merely a delay in IT spend, particularly around value add technology in which Synthesis specializes, hence its high margins. Once again, these delays are not sustainable as technology continues to evolve at a pace.
- We envisage a gradual rebound in Software in FY25E, revenue up 17% with margins widening to 14% given a closer alignment of staff spend to realised projects. Management indicated a circa R100m of pipeline ready to commence. We remain positive on trends in Cloud, digital and data in its key target sectors.
- We revise FY25E & FY26E HEPS down from 23.6c to 18.9c (+29%) and 28.9c to 24.8c (+31%). In our DFCF we calculate a fair value range of 263-297c/share. The balance sheet remains ungeared, and cash represents 37c/share. The stock trades on an attractive 12m fwd. P/E of 6.4x, an EV/EBITDA of 3.2x. We note Lesaka Technologies recent acquisition of a SA payments business on a 9x EV/EBITDA.

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Sven Thordsen, CFA
+44 (0) 752 367 6780
sven.thordsen@anchorsb.co.za

Price (2024/06/19):	R1.21
Market cap	R1585m
Shares in issue	1310mn

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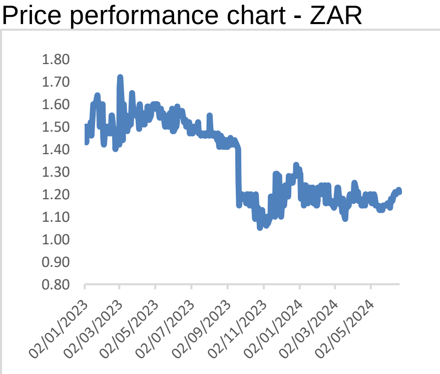
Price performance chart - ZAR



Source: FactSet

Figure 1 Financial summary

Year Ending	FY2021A	FY2022A	FY2023A	FY2024A	FY2025F	FY2026F	FY2027F
Income Statement							
Total Revenue	620	831	996	1,183	1,416	1,736	2,085
Revenue growth (%)	*-11.7%*	*34.2%*	*19.8%*	*18.8%*	*19.7%*	*22.6%*	*20.1%*
Payments revenue	397	534	524	563	679	877	1,099
Growth (%)	*-21.5%*	*34.3%*	*-1.9%*	*7.5%*	*20.6%*	*29.2%*	*25.3%*
Software revenue (incl International)	223	297	472	620	737	859	985
Growth (%)	*14.4%*	*33.2%*	*58.6%*	*31.5%*	*19.0%*	*16.5%*	*14.7%*
EBITDA	173	252	236	269	351	476	619
EBITDA Margin (%)	*28.0%*	*30.3%*	*23.7%*	*22.7%*	*24.8%*	*27.4%*	*29.7%*
Payments EBITDA	147	218	206	248	299	386	484
Margin (%)	*36.9%*	*40.9%*	*39.4%*	*44.1%*	*44.0%*	*44.0%*	*44.0%*
Software EBITDA (incl International)	61	67	83	69	106	148	199
Margin (%)	*27.4%*	*22.4%*	*17.5%*	*11.2%*	*14.4%*	*17.3%*	*20.2%*
Corporate/head office	-35	-33	-53	-48	-53	-58	-63
% Change	*21.3%*	*-4.9%*	*60.4%*	*-8.9%*	*10.0%*	*9.0%*	*9.0%*
EBIT	138	211	193	215	287	404	536
EBIT Margin (%)	*22.3%*	*25.3%*	*19.4%*	*18.2%*	*20.3%*	*23.3%*	*25.7%*
Profit before tax	157	232	156	246	319	438	557
Net profit	126	162	91	171	228	313	398
Net profit post minorities	126	162	91	171	228	313	398
Headline earnings	127	163	162	184	236	313	398
% Change	*-11%*	*28%*	*0%*	*13%*	*28%*	*33%*	*27%*
Diluted EPS (ZAc)	10.2	12.6	6.9	13.0	17.4	23.8	30.2
Headline EPS (ZAc)	10.3	13.3	13.2	14.6	18.9	24.8	31.4
% Change	*-3%*	*29%*	*-1%*	*11%*	*29%*	*31%*	*27%*
DPS (ZAc)	5.5	7.5	8.3	10.0	12.3	16.1	22.0
Payout ratio (%)	*53%*	*56%*	*63%*	*68%*	*65%*	*65%*	*70%*
Balance Sheet							
Cash and Cash equivalents	538	533	495	467	408	475	554
Current asset (ex – cash)	67	146	262	224	304	368	438
Net Fixed assets	26	24	43	72	117	192	284
Intangible assets	61	55	68	106	84	65	50
Investments	42	68	32	60	104	96	87
Other assets	747	773	764	846	847	849	851
Total assets	**1,481**	**1,600**	**1,664**	**1,776**	**1,863**	**2,044**	**2,264**
Debt	9	9	4	6	7	7	7
Current liabilities	71	86	136	116	142	169	200
Other liabilities	25	22	28	71	66	71	77
Total liabilities	**105**	**116**	**169**	**194**	**214**	**248**	**284**
Shareholders' equity	1,376	1,483	1,495	1,582	1,640	1,771	1,928
Total shareholders' equity	**1,376**	**1,483**	**1,495**	**1,582**	**1,640**	**1,771**	**1,928**

BVPS (ZAc)	*105*	*113*	*114*	*121*	*125*	*135*	*147*
ROE (%)	*9.4%*	*11.3%*	*6.1%*	*11.1%*	*14.1%*	*18.4%*	*21.5%*

Year Ending	FY2021A	FY2022A	FY2023A	FY2024A	FY2025F	FY2026F	FY2027F
Cash Flow							
Reported net profit before tax & interest	**138**	**211**	**193**	**215**	**287**	**404**	**536**
Change in net working capital	19	-60	-66	35	-60	-33	-36
Interest (paid)/received	-45	-61	-66	-68	-110	-151	-225
Tax paid	-53	-57	-67	-78	-91	-125	-159
Depreciation	35	41	45	53	64	72	83
Other adjustments	9	13	11	16	-3	3	4
Cash flow from operations	**102**	**86**	**50**	**174**	**87**	**171**	**204**
Net Capex	-7	-17	-33	-45	-71	-104	-125
Capex/sales (%)	*1.1%*	*2.0%*	*3.3%*	*3.8%*	*5.0%*	*6.0%*	*6.0%*
Other investing cash flows	-51	-51	-52	-98	-44	6	6
Cash flow from investing	**-58**	**-68**	**-86**	**-143**	**-115**	**-98**	**-119**
Equity raised/(bought back)	-1	-14	6	-53	-26	0	0
Net inc/(dec) in borrowings	0	0	0	0	0	0	0
Other financing cash flows	-8	-9	-10	-6	-6	-6	-6
Cash flow from financing	**-9**	**-23**	**-4**	**-59**	**-32**	**-6**	**-6**
Net cash flow	**35**	**-5**	**-39**	**-28**	**-60**	**67**	**79**
Free cash flow	**154**	**106**	**72**	**184**	**129**	**215**	**300**
Repayment of lease liabilities	**-8**	**-9**	**-10**	**-6**	**-6**	**-6**	**-6**
Net Free cash flow	**147**	**97**	**62**	**179**	**123**	**208**	**294**
Valuation Summary							
Valuation Metrics							
Share Price (ZAc)	99	185	157	121	121	121	121
P/E (Underlying) (x)	9.6	13.9	11.9	8.3	6.4	4.9	3.9
P/BV (x)	0.9	1.6	1.4	1.0	1.0	0.9	0.8
EV/Sales (x)	1.8	1.3	1.1	0.9	0.8	0.6	0.5
EV/EBITDA (x)	6.4	4.4	4.7	4.1	3.2	2.3	1.8
EV/EBIT (x)	8.1	5.3	5.8	5.2	3.9	2.8	2.1
FCF Yield (%)	9.2%	6.1%	3.9%	11.3%	7.8%	13.2%	18.5%
Dividend Yield (%)	5.6%	4.1%	5.3%	8.3%	10.2%	13.3%	18.2%
Net debt	-502	-506	-457	-414	-353	-344	-441
Net debt/Ebitda	-2.9	-2.0	-1.9	-1.5	-1.0	-0.7	-0.7

Source: Company data, FactSet, ASB Research

Financials

Figure 2 Segmental forecasts

	2023	2024	%	2025E	%	2026E	%
Revenue	996	1,183	19%	1,416	20%	1,736	23%
Payments	524	563	7%	679	21%	877	29%
Sale of terminals	255	218	-14%	265	21%	366	38%
Maintenance & Support Services	177	187	5%	207	11%	231	12%
Terminal rental income	29	56	95%	77	39%	123	59%
Transaction related income/Other	63	102	63%	130	27%	156	20%
Software	472	619	31%	727	17%	844	16%
Services & consultancy fees	305	439	44%	526	20%	621	18%
License & subscription fees	63	75	20%	90	20%	100	12%
Hardware	104	106	2%	111	5%	122	10%
International	1	1	0%	10	>100%	15	50%
EBITDA	236	269	14%	351	31%	476	36%
Payments	206	248	20%	299	20%	386	29%
Software	90	79	-11%	102	28%	143	41%
Corporate	(53)	(48)	-9%	(53)	10%	(58)	9%
International	(7)	(10)	42%	4		5	
EBITDA Margins							
Payments	39.4%	44.1%		44.0%		44.0%	
Software	19.0%	12.8%		14.0%		17.0%	
International		0.0%		40.0%		33.3%	
Depreciation	-43	-53	25%	-64	19%	-72	13%
Net Interest	36	47	29%	39	-16%	31	-20%
Other	73	16	-78%	8		-3	
PBT	156	246	57%	319	30%	438	38%
Tax	-64	-75	17%	-91	21%	-125	38%
PAT	92	171	86%	228	34%	313	38%
Headline earnings	162	184	13%	236	28%	313	33%
HEPS	13.2	14.6	11%	18.9	29%	24.8	31%

Source: Company data, ASB estimates

Comments on financial forecast:

- We assume the terminal estate grows from 357k to 387k in FY25E and 420k in FY26E.

- We assume that 25% of new devices issued are on rental contracts. These range from 3-5 years. We assume a cost of R3200 per rental device in FY24, escalating by 4% in FY25E. We estimate a monthly rental of R200 per device. None of these details are disclosed as management is wary of providing competitive information.
- On our estimates there was circa 18k rental devices in FY24. We forecast this to rise to 32k in FY25E.
- Transaction related income is difficult to forecast as new products are rolled out, for example software installed on third party devices, a trend which is emerging. It is also a reflection of the amount of data passed through the Sim cards in its devices. An immaterial amount of Transaction related revenue relates to devices directly with retailers as the bulk of the estate is sold/rented to banks.
- We anticipate increased activity in Software, however, there remains high forecast risk as at the time of the FY24 results announcement, no material improvement had occurred in deal flow. Our R727m is 10% up on 2H24 annualised, which we believe is conservative.
- Software EBITDA margins have consistently declined since FY18 when 39% was achieved. We don't see these margins ever being achieved again as software reseller margins have declined and a greater component of Software's revenue is from security hardware that attracts considerably lower margins. We believe 20% margins are achievable in the medium term and we glide our margin expansion towards 20% in FY27E.
- Our depreciation charge rises 19% due to the increase in rental devices. These are depreciated over 5 years with a 15% residual value. This implies an annual depreciation rate of 17%. A condition of the rental agreement is that the devices are well maintained during the contract and therefore they should have a useful life beyond 5 years. This would be positive for margins.
- We have net interest declining 16% due to lower anticipated interest rates and a lower average cash balance.
- The company repurchased R44.8m shares in FY24 at an average cost of 130c. A further 9.4m have since been acquired. This represents 4% of shares in issue. The shares are not cancelled, rather treated as treasury stock and utilised for acquisitions and share incentive awards. We forecast further marginal share buy backs in FY25E.
- We assume a further R8m to spent on GovChat in FY25E relating to legal expenses for the potential claim against Meta. We don't include this in our HEPS calculation. There will be a Competition Tribunal heard in April 2025 and the outcome from that will decide on whether further legal action will be instituted, in which case there could be further legal costs and uncertainty relating to GovChat for the next 2-3 years. GovChat is no longer operational.
- Development expenditure on its Multi-lane retail offering (Clicks has already signed up), LayUp, Halo Dot and MicroPOS (it has secured its first banking client), are all expensed upfront. We don't account for these new offerings in our forecasts and therefore there is upside risk to our estimates. To date Halo Dot has secured a major telco (we assume Vodacom). Nedbank, Howler, a local insurer and Telkom as clients with some further success in offshore markets too.
- There is no fixed dividend policy. We estimate a 65% payout in FY25E.
- Dariel contributed R145.9m in revenue and R26m in EBITDA in FY24, effective from 1 July 2023.

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