

OTEXEQUITY RESEARCH

February 2, 2023

Earnings Update

OPEN TEXT CORPORATION

Seasonally Strong FQ2; MCRO Restructuring Begins

Our Conclusion

Open Text reported strong FQ2 results, with revenue 2% and adj. EBITDA 9% above Street expectations, with OTEX continuing to see solid cloud growth. That said, the focus was on updated guidance, which included the Micro Focus acquisition. The F2024 guide was mixed versus our estimates, with adj. EBITDA margins that were 100 bps above our estimate at the mid-point, but FCF that was \$150MM below given restructuring costs and increased investments in R&D. From here, the focus turns to Open Text's ability to return Micro Focus to organic growth in F2025, with management laying out a roadmap to drive renewal rates higher, onboard Micro Focus clients to Open Text private cloud and cross-sell a joint product suite. We retain our Neutral rating and increase our price target to US\$40 (prior US\$35) as we incorporate Micro Focus.

Key Points

FQ2 Results Highlights: Open Text reported revenue of \$897MM versus consensus of \$878MM. Revenues were up 7.8% Y/Y in constant currency. Adjusted EBITDA of \$341MM was well above consensus (\$313MM), with adjusted EBITDA margins of 38% roughly 240 bps above consensus (35.6%). Free cash flow of \$163MM was above consensus of \$143MM.

Cloud Growth Solid Despite Macro Uncertainty: Despite peers noting a weakening cloud environment, Open Text continues to see solid cloud growth (16% in constant currency). The company noted record cloud bookings of \$511MM in FQ2, with demand for digitization services continuing. That said, license revenues appeared to be the delta that drove the FQ2 outperformance versus consensus (\$108MM versus \$92MM) in a seasonally stronger license quarter given the historic year-end budget flush.

F2023 And F2024 Outlook Updated For Micro Focus: The F2023 guide came in below our expectations, although comparability is difficult given the switch from IFRS to U.S. GAAP (we accounted for lease capitalization, but OTEX also noted revenue timing related to license renewals and R&D capitalization). For F2024, organic growth of 1%-2% was on the high end of our estimate (1.1%), while adjusted EBITDA margin guide of 36%-38% was above our expectation (35.5%). Given restructuring costs, investments and interest expenses, Micro Focus is not expected to be additive to FCF for the first six quarters, with the mid-point of the F2024 FCF guide coming in \$150MM below our expectations. With the close of the transaction, Open Text announced an 8% workforce reduction (expected to cost \$70MM-\$80MM) and reiterated its target of \$400MM in cost savings.

Focus Now Turns To Growth: Open Text's guidance assumes that Micro Focus will have flat organic growth by F2024 (vs. mid-single-digit declines prior to the acquisition). OTEX highlighted a plan that includes improving Micro Focus' renewal rates (low-80% range vs. Open Text at 95%), moving Micro Focus clients to the OTEX private cloud and investing in R&D (~15% in the F2023 guide versus ~13% historically) as it cross-sells joint solutions.

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Neutral

OTEX-NASDAQ, Sector: Information Technology

Current Price (2/2/23): US\$33.26
Price Target (12-18 mos.): **↑US\$40.00**
Previous: US\$35.00

CIBC Estimates and Valuation

(Jun. 30)	2021	2022	2023	2024
Adj. EPS	3.28A	3.22A	2.94E	4.93E
Prior			3.25E	3.42E
Adj. EBITDA(mln)	1,315.0A	1,265.0A	1,501.1E	2,199.6E
Prior			1,293.8E	1,351.5E

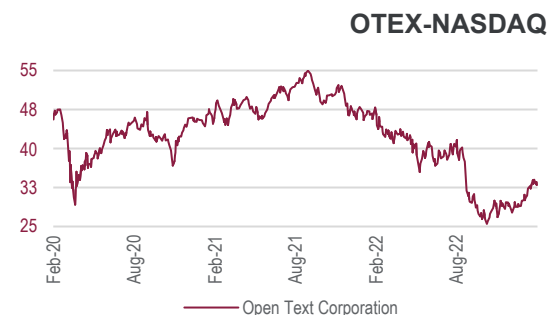
Adj. EPS	Q1	Q2	Q3	Q4
2022	0.83A	0.89A	0.70A	0.80A
2023	0.77A	0.78A	0.56E	0.83E
Prior		0.77E	0.83E	0.89E

Adj. EBITDA(mln)	Q1	Q2	Q3	Q4
2022	323.4A	343.5A	284.5A	313.6A
2023	304.1A	340.9A	387.4E	468.7E
Prior		311.1E	329.5E	349.2E

Valuation	2021	2022	2023	2024
P/E	10.1x	10.3x	11.3x	6.7x
EV/EBITDA	11.5x	11.9x	10.1x	6.9x

Stock Performance and Key Indicators

Enterprise Value:	US\$15,091M	Shares O/S:	270.2M
Market Cap.:	US\$8,985M	Float:	256.4M
52-wk Range:	US\$25.50 - US\$46.51	Div. / Yield:	US\$0.88/2.66%



(Source: FactSet)

All figures in US dollars unless otherwise stated.

Please see "Price Target Calculation and Key Risks to Price Target" information on page 5. For required regulatory disclosures please refer to "Important Disclosures" beginning on page 6.

Open Text Corporation (OTEX-NASDAQ) — Neutral

Price (2/2/23) US\$33.26 12-18 mo. Price Target US\$40.00

Sector: Information Technology

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Peer Comparison	2021	2022	2023E	2024E
P/FCF - Enterprise Information Mai	17.6x	17.6x	-	-
P/FCF - Open Text	11.5x	11.5x	-	-
Key Financial Metrics	2021	2022	2023E	2024E
Net Debt	1,982	2,526	8,241	7,600
Total Debt	3,589	4,220	9,053	8,453
Net Debt/EBITDA	1.5x	2.0x	5.5x	3.5x
Free Cash Flow	812	889	517	880
Sales Growth	8.9%	3.2%	28.9%	35.0%
Per Share Data	2021	2022	2023E	2024E
FCFPS	2.97	3.27	1.92	3.26
Adj. EPS Dil.	3.28	3.22	2.94	4.93
Wgt Avg # of Shares	272.5	271.3	270.1	270.4
FD Number of Shares	273.5	271.9	270.1	270.2
Ratio	2021	2022	2023E	2024E
ROIC	19.2%	16.7%	9.3%	15.0%
Income Statement	2021	2022	2023E	2024E
Revenue	3,386	3,494	4,505	6,084
Cost of Goods Sold	816	864	1,056	1,300
Gross Profit	2,570	2,630	3,449	4,784
Gross Margin %	75.91%	75.28%	76.56%	78.63%
Tot Operating Exp	1,104	1,104	1,104	1,104
Adj. EBITDA	1,315	1,265	1,501	2,200
Adj EBITDA Margin	38.8%	36.2%	33.3%	36.2%
D&A	(521)	(504)	(511)	(547)
Interest Expense	(152)	(158)	(328)	(474)
Pretax profit	651	516	384	1,148
Tax Expense	340	119	107	161
Adjusted Net Income	898	876	793	1,331
Adjusted Net Margin	26.5%	25.1%	17.6%	21.9%
Cash Flow Statement	2021	2022	2023E	2024E
Net CFO	876	982	602	976
Capex	(64)	(93)	(85)	(96)
Free Cash Flow	812	889	517	880
Balance Sheet	2021	2022	2023E	2024E
Cash & ST Investment	1,607	1,694	812	853
Goodwill	5,879	5,245	11,050	10,650
Total Assets	9,609	10,179	15,167	15,635
LT Int-Bearing Debt	3,589	4,220	9,053	8,453
Total Liabilities	5,511	6,148	11,093	10,783
Shareholders' Equity	4,098	4,031	4,074	4,852

Source: FactSet, company reports & CIBC World Markets Inc.

Company Profile

Open Text develops enterprise information management (EIM) solutions, which enable companies to control and better utilize all forms of information.

Investment Thesis

1) Largest Independent EIM vendor 2) Broad range of EIM solutions sold directly and through partnerships 3) Strong track record of Capital Allocation and Acquisition Integration.

Price Target (Base Case): US\$40.00

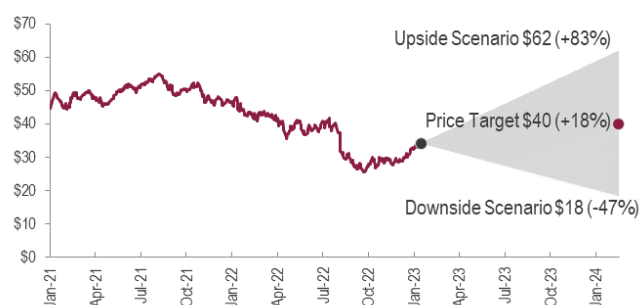
Our price target is calculated using 6.5% revenue growth, 37.3% EBITDA margins and a 6x EV/EBITDA multiple

Upside Scenario: US\$62.00

Our upside scenario is calculated using 12% revenue growth, 38% EBITDA margins and a 10x EV/EBITDA multiple.

Downside Scenario: US\$18.00

Our downside scenario is calculated using a 3% revenue growth, 32% EBITDA margins and a 5x EV/EBITDA multiple.



FQ2 Results

Exhibit 1: Open Text – Financial Summary, Q2/F23 (\$MM except per share)

	Q2/F23		Q2/F22	Y/Y%	Q1/F23	Q/Q%
	Actual	Cons				
Consolidated						
Revenue (\$MM)	897	878	877	2.3%	852	5.3%
Product License	108	92	109	-1.4%	63	72.6%
Cloud	409	396	365	12.0%	405	1.0%
Services	64	65	68	-4.8%	67	-4.7%
Maintenance	317	315	335	-5.5%	317	-0.3%
Adjusted EBITDA	341	313	344	-0.8%	304	12.1%
EBITDA Margin	38.0%	35.6%	39.2%	-3.0%	35.7%	6.5%
Adjusted EPS	\$0.78	\$0.79	\$0.89	-12.6%	\$0.77	1.1%
Cash Flow from Operations	195	150	217	-9.9%	132	47.9%

Source: Company reports, FactSet and CIBC World Markets Inc.

Segmented Results: License revenues of \$108MM were above consensus (\$92MM); Cloud revenues of \$409MM were above consensus (\$396MM). Constant-currency cloud revenue growth was ~16% Y/Y. Services revenue of \$64MM was in line with consensus, while Maintenance revenue of \$317MM was slightly above consensus (\$315MM).

Changes To Our Model: We have updated our model for FQ2 results and have incorporated the Micro Focus acquisition and updated guidance. We are expecting 1% organic growth in F2024, with 36.2% adjusted EBITDA margins.

Exhibit 2: Open Text – Changes To Our Model, 2022 - 2024E

	Revenues (\$MM)	EBITDA (\$MM)	Adjusted EPS	CFO
2022A	3,494	1,265	3.22	981.81
2023E				
CIBC est. – new	4,505	1,501	2.94	602
CIBC est. – prior	3,589	1,294	3.25	808
Consensus	3,470	1,258	3.16	987
2024E				
CIBC est. – new	6,084	2,200	4.93	976
CIBC est. – prior	3,682	1,351	3.42	1,122
Consensus	3,559	1,328	3.43	1,089

Source: Company reports, FactSet and CIBC World Markets Inc.

Environmental, Social and Governance (ESG) Metrics for OTEX-NASDAQ

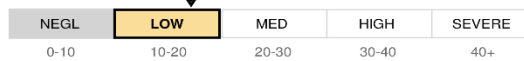
CIBC ESG Metrics					
Governance Metrics	2016	2017	2018	2019	2020
Insider Ownership	1.8%	2.3%	2.0%	1.8%	1.7%
Board Gender Diversity	33.0%	30.0%	27.0%	27%	33%
Separation of Chair & CEO	YES	YES	YES	YES	YES
Dual-class Ownership?	NO	NO	NO	YES	NO
Disclose ESG Data?	NO	YES	YES	YES	YES
Social Metrics	2016	2017	2018	2019	2020
CEO Comp./Mkt Cap*	\$1.4	\$1.7	\$0.9	\$0.9	\$0.9
Diversity Targets	NO	NO	NO	NO	NO
Women Managers	8%	8%	33%	21%	7%
Environmental Metrics	2016	2017	2018	2019	2020
Emissions Intensity**	NA	NA	0	0	0
Net-zero Targets?	NO	NO	NO	NO	NO

* CEO Compensation is shown as per thousand dollars of market capitalization
 ** Emissions Intensity calculated as total emitted CO2e divided by million \$ of CAD revenue

Sustainalytics ESG Risk Rating

17.3 **+2.1** **Low Risk**

Updated on Apr 22, 2022 Momentum



Sustainalytics ESG Risk Rating Ranking

UNIVERSE	RANK	PERCENTILE
	(1 st = lowest risk)	(1 st = lowest risk)
Global Universe	2200/14656	16th
Software & Services INDUSTRY	118/1000	13th
Enterprise and Infrastructure Software SUBINDUSTRY	44/415	11th

Sustainalytics Material ESG Issues

These are the Material ESG Issues driving the ESG Risk Report

Issue Name	ESG Risk Exposure	ESG Risk Management	ESG Risk Rating	Contribution to ESG Risk Rating
	Score Category	Score Category	Score Category	
Corporate Governance	9.0 High	59.6 Strong	3.6 Low	21.1%
Human Capital	8.0 High	57.6 Strong	3.6 Low	21.0%
Data Privacy and Security	7.6 Medium	70.0 Strong	3.3 Low	19.4%
Product Governance	2.2 Low	7.5 Weak	2.0 Low	11.8%
Resource Use	2.0 Low	11.9 Weak	1.8 Negligible	10.5%
Carbon - Own Operations	2.2 Low	27.4 Average	1.6 Negligible	9.3%
Business Ethics	3.0 Low	62.5 Strong	1.2 Negligible	7.1%
Overall	34.0 Low	53.1 Strong	17.3 Low	100%

CIBC Quantitative Scorecard

Within Sector			Within S&P/TSX Comp.		
Style	Rank	Delta	Style	Rank	Delta
Value	3	-1	Value	90	0
Momentum	13	-7	Momentum	226	-37
Quality	7	0	Quality	90	-2
Market	4	0	Market	65	-1
Low Volatility	2	0	Low Volatility	60	-8
Growth	10	0	Growth	169	-1

Note: Ranking out of 16 stocks (Sector) / Note: Ranking out of 239 stocks (S&P/TSX Comp.)

General Notes Behind the Quantitative Scorecard

Delta refers to the change in the ranking over the past month. Number of stocks "Within Sector" is defined by the number within the GICS. In the "Within S&P/TSX" category, we use all stocks in the S&P/TSX Composite. For detail on the Quant Factors included in each style above, please contact the CIBC Portfolio Strategy Team.

The table above is based upon quantitative, statistical, and mathematical analysis and is not intended to serve as a fundamental recommendation.

CIBC Technical Scorecard

Factor	TSM Score	Factor	TSM Score
TSM	-8	Momentum	D
Beta	1.03	MACD	D
Volatility	↓	Alpha (Sector)	A
Trend	↓	Alpha (Index)	D
RSI	Neutral		

General Notes Behind the Technical Scorecard

TSM: The Trendspotting Matrix uses technical factors to score uptrend durability. **Momentum and alpha** metrics compare performance over one-month, one-quarter and one-year timeframes, outputting a rating from A to D. **Trend/Volatility** metrics measure price deviations relative to underlying moving averages. **RSI** is an oscillator that provides mean-reversion estimations. **MACD** is a momentum indicator rated from A to D based off the strength of its signal.

The table above is based upon a technical methodology that examines the past trading patterns and trades and is not intended to serve as a fundamental recommendation.

Source: Sustainalytics, Compustat, FactSet, Bloomberg and CIBC World Markets Inc.

Price Target Calculation

Our price target of US\$40 is calculated using 6.5% revenue growth, 37.3% EBITDA margins and a 6x EV/EBITDA multiple.

Key Risks To Price Target

The risks to our price target include, but are not limited to: the current uncertain economic climate and potential delays in and/or downsized spending on enterprise application software products; increasing competition from other enterprise application software vendors; the company's ability to meet future capital needs in order to support operations; the company's ability to introduce new or updated technology in a timely manner; the company's ability to successfully integrate and operate any current or future acquisitions; and, the loss of key management or other employees.

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Neutral	NT	Stock is expected to perform in line with similar stocks in the coverage universe during the next 12-18 months.
Underperformer	UN	Stock is expected to underperform similar stocks in the coverage universe during the next 12-18 months.
Tender	TR	Shareholders are advised to tender shares to a specific offer as we do not believe a superior offer will materialize.
Not Rated	NR	CIBC World Markets does not maintain an investment recommendation on the stock.
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Marketweight	M	Sector is expected to equal the performance of the broader market averages.
Underweight	U	Sector is expected to underperform the broader market averages.
None	NA	Sector rating is not applicable.

Note: Broader market averages refer to S&P 500 in the U.S. and S&P/TSX Composite in Canada.

CIBC World Markets Inc. Price Chart

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Neutral	134	44%	Neutral	133	99%
Underperformer	7	2%	Underperformer	6	86%
Tender	3	1%	Tender	3	100%
Restricted	9	3%	Restricted	9	100%

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