

# EQUITY RESEARCH

August 4, 2022

Earnings Update

## OPEN TEXT CORPORATION

### FQ4 A Slight Beat; F23 Outlook Highlights Cloud Growth

#### Our Conclusion

Open Text reported FQ4 results that were a slight (2%) beat against consensus, with adjusted EBITDA margins 70 bps ahead of consensus. The company is focusing on cloud growth, with its F23 outlook including constant-currency enterprise cloud bookings growth of 15% and an incremental \$75MM in cloud investments. With the investments, the F23 margin outlook is ~100 bps below Street expectations. While a short-term margin drag, we continue to see upside from cloud offerings with Open Text well positioned to migrate on-premise customers and capitalize on demand for supply chain solutions within its business network. With recent acquisitions, we see the opportunity to gain share in SMB and see upside from the Microsoft channel arrangement. We retain our Outperformer rating and US\$51 price target.

#### Key Points

**FQ4 Results Solid:** Open Text reported revenue of \$902MM, roughly in line with consensus (\$899MM) but below CIBCe (\$913MM). Revenues were up 4.6% Y/Y in constant currency. Adjusted EBITDA of \$314MM was 2% ahead of consensus while adjusted EBITDA margins of 34.8% were ~70 bps above consensus and 120 bps above CIBCe. Cash flow from operations was \$252MM, below consensus of \$265MM, given higher stock-based compensation during the quarter.

**Demand Environment Remains Strong:** Despite a somewhat uncertain macro-environment, Open Text noted continued solid demand, with talent shortages at clients as well as increasing reporting regulations creating secular tailwinds for its cloud business. Migrating current clients to the cloud remains the number one opportunity for Open Text and we expect the secular trends to act as a tailwind for the company to up-sell and cross-sell its cloud solutions.

**F23 Outlook Highlights Solid Cloud Bookings & Investments:** Open Text provided a "constant currency" F23 outlook with FQ4 results. The outlook targeted enterprise cloud bookings of 15% and cloud revenue growth of 6%-8%. Open Text has accelerated its cloud investments and expects \$75MM in incremental R&D spend in F23 that will support the build-out of the cloud offering, with F23 margins expected to be in the 36%-36.5% range (consensus 37.3%).

#### Medium-term Outlook Suggests Improving Cloud Organic Growth:

Open Text also released its medium-term (F25) constant currency aspirations. The F25 outlook targets organic revenue growth of 2%-4% (1.7% in F22) and cloud organic revenue growth of 6%-8% (3.6% in F22) as the company converts its cloud bookings into revenue. The F25 outlook also targets 37%-39% adjusted EBITDA margins, roughly 100 bps below the F24 aspirations as the company continues to invest in cloud.

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### Outperformer

OTEX-NASDAQ, Sector: Information Technology

Current Price (8/4/22): US\$41.63

Price Target (12-18 mos.): US\$51.00

#### CIBC Estimates and Valuation

(Jun. 30)	2020	2021	2022	2023
Adj. EPS	2.89A	3.28A	3.22A	3.34E
Prior			3.17E	3.47E
Adj. EBITDA(mln)	1,148.1A	1,315.0A	1,265.0A	1,329.1E
Prior			1,257.1E	1,371.8E
Adj. EPS	Q1	Q2	Q3	Q4
2021	0.89A	0.95A	0.75A	0.70A
Prior				0.75E
2022	0.83A	0.89A	0.70A	0.80A
Prior				0.75E
Adj. EBITDA(mln)	Q1	Q2	Q3	Q4
2021	342.3A	360.8A	297.1A	314.8A
Prior				
2022	323.4A	343.5A	284.5A	313.6A
Prior				305.7E
Valuation	2020	2021	2022	2023
P/E	14.4x	12.7x	12.9x	12.5x
EV/EBITDA	12.6x	11.0x	11.5x	10.9x

#### Stock Performance and Key Indicators

Enterprise Value:	US\$14,505M	Shares O/S:	272.0M
Market Cap.:	US\$11,325M	Float:	256.4M
52-wk Range:	US\$35.50 - US\$54.98	Div. / Yield:	US\$0.88/2.12%

#### OTEX-NASDAQ



(Source: FactSet)

All figures in US dollars unless otherwise stated.

Please see "Price Target Calculation and Key Risks to Price Target" information on page 4. For required regulatory disclosures please refer to "Important Disclosures" beginning on page 6.

## Open Text Corporation (OTEX-NASDAQ) — Outperformer

Price (8/4/22) US\$41.63 12-18 mo. Price Target US\$51.00

Sector: Information Technology

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Peer Comparison	2020	2021	2022	2023E
P/FCF - Enterprise Information Mai	24.1x	17.6x	17.6x	-
P/FCF - Open Text	10.0x	11.5x	11.5x	-
Key Financial Metrics	2020	2021	2022	2023E
Net Debt	2,501	1,982	2,526	1,834
Total Debt	4,194	3,589	4,220	4,220
Net Debt/EBITDA	2.2x	1.5x	2.0x	1.4x
Free Cash Flow	882	812	889	929
Sales Growth	8.4%	8.9%	3.2%	4.7%
Per Share Data	2020	2021	2022	2023E
FCFPS	3.24	2.97	3.27	3.43
Adj. EPS Dil.	2.89	3.28	3.22	3.34
Wgt Avg # of Shares	270.9	272.5	271.3	270.3
FD Number of Shares	271.9	273.5	271.9	270.4
Ratio	2020	2021	2022	2023E
ROIC	15.8%	19.2%	16.7%	19.7%
Income Statement	2020	2021	2022	2023E
Revenue	3,110	3,386	3,494	3,657
Cost of Goods Sold	798	816	864	904
Gross Profit	2,312	2,570	2,630	2,752
Gross Margin %	74.34%	75.91%	75.28%	75.27%
Tot Operating Exp	1,067	1,104	1,104	1,104
Adj. EBITDA	1,148	1,315	1,265	1,329
Adj EBITDA Margin	36.9%	38.8%	36.2%	36.3%
D&A	(515)	(521)	(504)	(501)
Interest Expense	(146)	(152)	(158)	(158)
Pretax profit	345	651	516	639
Tax Expense	111	340	119	90
Adjusted Net Income	785	898	876	903
Adjusted Net Margin	25.2%	26.5%	25.1%	24.7%
Cash Flow Statement	2020	2021	2022	2023E
Net CFO	955	876	982	1,025
Capex	(73)	(64)	(93)	(96)
Free Cash Flow	882	812	889	929
Balance Sheet	2020	2021	2022	2023E
Cash & ST Investment	1,693	1,607	1,694	2,386
Goodwill	6,285	5,879	5,245	4,834
Total Assets	10,235	9,609	10,179	10,426
LT Int-Bearing Debt	4,194	3,589	4,220	4,220
Total Liabilities	6,229	5,511	6,148	6,142
Shareholders' Equity	4,005	4,098	4,031	4,283

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\$51.00

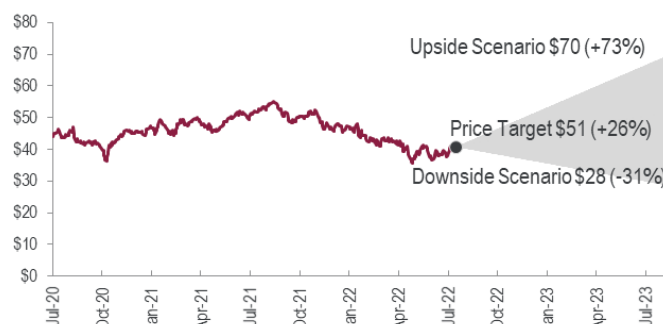
Our price target is calculated using 5% revenue growth, 37.3% EBITDA margins and a 11.0x EV/EBITDA multiple, plus the present value of future acquisitions.

### Upside Scenario: US\$70.00

Our upside scenario is calculated using 13% revenue growth, 38% EBITDA margins and a 13.5x EV/EBITDA multiple, plus the present value of future acquisitions.

### Downside Scenario: US\$28.00

Our downside scenario is calculated using 2% revenue growth, 31% EBITDA margins and a 8x EV/EBITDA multiple.



## FQ3 Results

### Exhibit 1: Open Text – Financial Summary, FQ4/22 (\$MM except per share)

	Q4-F2022			Q4-F2021	Y/Y%	Q3-F2022	Q/Q%
	Actual	CIBC	Cons				
Consolidated							
Revenue (\$MM)	902	913	899	894	1.0%	882	2.3%
Product License	95	105	106	133	-28.6%	81	17.4%
Cloud	412	408	398	360	14.3%	402	2.4%
Services	68	68	67	67	1.9%	67	1.0%
Maintenance	328	332	323	334	-1.8%	333	-1.3%
Adjusted EBITDA	314	306	307	315	-0.4%	284	10.2%
EBITDA Margin	34.8%	33.5%	34.1%	35.2%	-1.4%	32.2%	7.8%
Adjusted EPS	\$0.80	0.75	\$0.77	\$0.70	14.1%	\$0.70	13.3%
Cash Flow from Operations	252	141	265	296	-14.9%	324	-22.1%

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

**Segmented Results:** License revenues of \$95MM was below consensus (\$106MM) and our expectations (\$105MM). Cloud revenues of \$412MM were above consensus and CIBCe (\$398MM/\$408MM); Constant-currency cloud revenue growth was 16.6% Y/Y higher. Services revenue of \$67MM was in line with consensus/CIBCe (\$68MM). Maintenance revenue of \$333MM was in line with consensus (\$334MM) and CIBCe (\$332MM).

**Strong Balance Sheet Position:** Open Text finished the quarter with consolidated net leverage of 2x. At the end of the quarter, the company has total available cash of \$1.7 billion and \$750MM on an undrawn revolver and approximately 75% of the debt is on fixed interest rate.

**Profitability:** Adjusted EBITDA margins in the quarter were 34.8%, 70 bps above consensus (34.1%) and 130 bps above CIBCe (33.5%).

**Capital Allocation:** Open Text spent \$41MM on buybacks in the quarter, repurchasing and cancelling 1 million shares. The company also raised its quarterly dividend by 10% to \$0.24/share with FQ4 results. Open Text continues to target 33% of FCF to dividends and share buybacks.

**Changes To Our Model:** We have updated our model for FQ4 results. We have also reduced our F23 margin assumptions by ~100 bps given increased cloud investments and are introducing our F24 forecast.

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

	Revenues (\$MM)	EBITDA (\$MM)	Adjusted EPS	CFO
2022A	3,494	1,265	3.22	982
2023E				
CIBC est. – new	3,657	1,329	3.34	1,025
CIBC est. – prior	3,682	1,372	3.47	1,074
Consensus	3,639	1,358	3.48	1,074
2024E				
CIBC est.	3,749	1,388	3.54	1,157
Consensus	3,706	1,405	3.57	NA

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

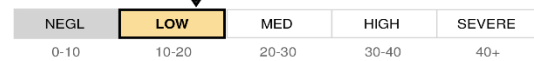
\* CEO Compensation is shown as per thousand dollars of market capitalization  
 \*\* Emissions Intensity calculated as total emitted CO2e divided by million \$ of CAD revenue

Sustainalytics ESG Risk Rating

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

Updated on  
Apr 22, 2022

Momentum



Sustainalytics ESG Risk Rating Ranking

UNIVERSE	RANK (1 <sup>st</sup> = lowest risk)	PERCENTILE (1 <sup>st</sup> = 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 Score   Category	ESG Risk Management Score   Category	ESG Risk Rating Score   Category	Contribution to ESG Risk Rating
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

Note: Ranking out of 239 stocks

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 \$51 is calculated using a 11x EV/F2023E EBITDA basis, using the current capital structure, for the core business. In addition, we add the present value of future acquisition spend.

## 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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Overweight	O	Sector is expected to outperform the broader market averages.
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	131	42%	Neutral	130	99%
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Tender	3	1%	Tender	3	100%
Restricted	7	2%	Restricted	7	100%

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