

EQUITY RESEARCH

February 7, 2023

Flash Research

CONSTELLATION SOFTWARE INC.

Topicus Reports Q4/22 Results

Our Conclusion: Constellation and Topicus announced Q4 results for Topicus this evening. Organic growth of 6% improved sequentially from 3% in the seasonally strong Q4; however, it remained below year-ago levels (10%). All revenue segments grew Y/Y with the exception of License revenue (down 1%), which saw its fourth quarter of Y/Y declines. Margins at Topicus were down 500 bps Y/Y, but were roughly 210 bps above our expectation for Constellation's consolidated margin of 24.9%. Topicus had a relatively low M&A spend (€10.5MM) in the quarter. Overall, we remain comfortable with our Constellation estimates following Topicus' results.

Key Highlights

Demand Environment: Topicus reported revenue of €263.7MM in the quarter, up 27% Y/Y. Organic growth of 6% was down from 10% in the year-ago period. Organic growth was in the mid- to high single digits for most segments. Hardware (+7%), Maintenance (+6%) and Professional Services (+8%) remained solid, while License revenue lagged with a 1% Y/Y decline.

Profitability: EBITDA margin in the quarter was 27%, flat sequentially, but down 500 bps Y/Y. The margin impact appears primarily driven by higher labour costs in the quarter, which came in at 55% of total revenue compared to 51% in the year-ago period.

Cash Flow: Topicus generated free cash flow available to shareholders of €18.6MM in the quarter, down 10% Y/Y, primarily driven by higher interest and lease payments. For the twelve months ended December 31, 2022, FCFA2S decreased 37% Y/Y, mainly driven by the \$66MM of dividends paid to the Preferred Securities holders. Cash flow from operations increased 12% Y/Y in Q4 primarily due to \$2.2MM generated from non-cash operating working capital, compared to €-36.6MM in the prior year, partially offset by higher income tax expense in Q4.

Acquisition Spending: Topicus spent €10.5MM on acquisitions in the quarter, with deferred payments associated with these transactions estimated at €2.9MM. There was one deal announced by Topicus during Q4 - a Dutch student administration system provider for vocational education. During the quarter, the company extended its credit facility with a number of European institutions, allowing borrowings up to €550MM under a revolving loan and €150MM under an additional uncommitted facility.

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Outperformer

CSU-TSX, Sector: Information Technology

Current Price (2/7/23): C\$2,370.01

Price Target (12-18 mos.): C\$2,450.00

All figures in US dollars unless otherwise stated (C\$1.345:US\$1.00).

Please see "Price Target Calculation and Key Risks to Price Target" information on page 2.
For required regulatory disclosures please refer to "Important Disclosures" beginning on page 3.

Financial Summary

Exhibit 1: Topicus – Financial Summary, Q4/22

	Q4/F22				
	Actual	Q4/F21	Y/Y%	Q3/F22	Q/Q%
Consolidated					
Revenue (€M)	263.7	207.6	27%	228.6	15.4%
License	13.5	10.9	23%	6.4	109.9%
Professional services	73.5	55.1	33%	59.6	23.4%
Hardware and other	4.0	2.2	81%	2.0	95.1%
Maintenance and other recurring	172.8	139.3	24%	160.6	7.6%
EBITDA (€M)	71.1	66.3	7%	61.6	15.5%
EBITDA Margin	27.0%	32.0%	(5.0%)	27.0%	0.0%

Source: Company reports and CIBC World Markets Inc.

Price Target Calculation

Our C\$2,450 price target is based on a sum-of-the-parts methodology. We value CSU (ex-TOI) at 22x forward EBITDA multiple, a premium to enterprise software peers, and CSU's 30.35% ownership of TOI at market value.

Key Risks To Price Target

The primary risks to our price target include the following: 1) ability to scale; 2) ability to acquire; 3) vertical market exposure; 4) lack of detailed disclosure.

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None	NA	Sector rating is not applicable.

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CIBC World Markets Inc. Price Chart

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