

# EQUITY RESEARCH

October 5, 2022

Earnings Update

## DYE & DURHAM LTD.

### Model Updates & Product Demo Takeaways

#### Our Conclusion

Following an FQ4 earnings report that mitigated concerns of the impact of slowing housing markets on revenue growth, we have updated our F23 model and introduced F24 estimates. Our updated estimates better reflect the inherent seasonality in the business while also adjusting for the eventual sale of TM Group and factoring in an additional level of conservatism for prolonged weakness in the housing markets. In addition to updating our model, we also had the opportunity this week to view an in-person product demo of DND's eCore and Unity platforms, with the demo highlighting integration capabilities and the value it offers to users by centralizing a variety of conveyancing tasks into a single platform. With the introduction of F24 estimates and the removal of TM Group from our model, we have increased our price target from \$30 to \$33, and retain our Outperformer rating and belief that DND shares are undervalued at current levels.

#### Key Points

**Model Updates:** After Q4 earnings, we have updated our model and introduced our F2024 estimates. The primary changes to our model include factoring in a discounted sale of TM Group at the start of FQ2 and adjusting for seasonality in the business. Prior to F2023, elevated levels of acquired revenue have obscured seasonality in the business, which is predominantly driven by fluctuations in housing market activity. With housing sales slowing in the fall and winter months, we are expecting revenue to be relatively flat Q/Q in FQ1/FQ2 before accelerating in the second half of the year. In addition to updating the model for seasonality, we have also reduced our overall growth estimates to take a more conservative view with regard to continued weakness in housing markets throughout F23, as well as factoring in short-term FX headwinds from a worsening GBP and AUD. The removal of TM Group and other adjustments results in a 12% reduction to our FY23 revenue and EBITDA estimates while our EBITDA margin estimate remains unchanged at 44.7%.

**Valuation Approach:** As we roll forward our estimates to F2024 we are now valuing DND on F2024 unadjusted EBITDA. We also reduce our target multiple from 11x to 10x to account for risk of prolonged weakness in the housing market and uncertainty around the timing of central bank rate decisions. As our model does not include a contribution from unannounced M&A, we also add \$5/share to our target price for contributions from future M&A, calculated using a DCF that assumes 75% of annual FCF is invested in M&A.

**NCIB Details:** DND announced an NCIB that allows it to repurchase 5% of shares outstanding. At the 20-day VWAP price, repurchasing 5% of the outstanding shares would see DND spend ~\$50 million.

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### Outperformer

DND-TSX, Sector: Information Technology

Current Price (10/5/22): C\$15.73

Price Target (12-18 mos.): ↑ C\$33.00

Previous: C\$30.00

#### CIBC Estimates and Valuation

(Jun. 30)	2021	2022	2023	2024
Revenue(mln)	208.95A	474.81A	551.99E	603.91E
Prior		480.47E	629.10E	
EBITDA(mln)	52.9A	193.4A	247.0E	287.4E
Prior		200.5E	281.4E	
Adj. EBITDA(mln)	116.4A	266.9A	312.0E	341.4E
Prior		264.2E	341.4E	

Revenue(mln)	Q1	Q2	Q3	Q4
2024	132.80E	147.46E	156.21E	167.43E
2023	131.36E	131.67E	139.48E	149.49E
Prior	146.69E	158.16E	161.32E	162.93E

EBITDA(mln)	Q1	Q2	Q3	Q4
2024	60.7E	67.8E	75.5E	83.4E
2023	48.9E	59.1E	65.9E	73.0E
Prior	63.5E	70.4E	72.9E	74.6E

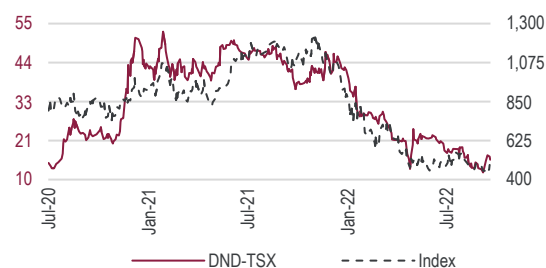
Adj. EBITDA(mln)	Q1	Q2	Q3	Q4
2024	74.2E	81.3E	89.0E	96.9E
2023	73.4E	72.6E	79.4E	86.5E
Prior	78.5E	85.4E	87.9E	89.6E

Valuation	2021	2022	2023	2024
EV/EBITDA	38.7x	10.6x	8.3x	7.1x

#### Stock Performance and Key Indicators

Avg. Dly. Vol.:	222K	Shares O/S:	69.1M
Market Cap.:	C\$1,088M	Float:	56.2M
52-wk Range:	C\$12.06 - C\$46.77	Div. / Yield:	NIL/NIL

#### Inf. Tech. Index vs. DND-TSX



(Source: FactSet)

All figures in Canadian 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 5.

**Dye & Durham Ltd. (DND-TSX) — Outperformer**

Price (10/5/22) C\$15.73 12-18 mo. Price Target C\$33.00

Sector: Information Technology

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Key Financial Metrics	2021	2022	2023E	2024E
Free Cash Flow	-	156	216	262
Sales Growth	219.0%	127.2%	16.3%	9.4%
Per Share Data	2021	2022	2023E	2024E
EPS	(0.72)	0.11	0.07	0.43
Diluted EPS	(0.72)	(0.32)	0.07	0.43
Wgt Avg # of Shares	56.4	68.9	69.4	69.8
FD Number of Shares	56.4	75.5	69.4	69.8
Income Statement	2021	2022	2023E	2024E
<b>Revenue</b>	<b>209</b>	<b>475</b>	<b>552</b>	<b>604</b>
Cost of Goods Sold	28	58	67	73
<b>Gross Profit</b>	<b>181</b>	<b>417</b>	<b>485</b>	<b>531</b>
Tot Operating Exp	65	150	173	189
OpEx (% of Revenue)	30.99%	31.66%	31.39%	31.37%
<b>EBITDA</b>	<b>53</b>	<b>193</b>	<b>247</b>	<b>287</b>
EBITDA Margin	25.33%	40.73%	44.74%	47.59%
<b>Adj. EBITDA</b>	<b>116</b>	<b>267</b>	<b>312</b>	<b>341</b>
Adj EBITDA Margin	55.7%	56.2%	56.5%	56.5%
<b>Net Income</b>	<b>(41)</b>	<b>8</b>	<b>5</b>	<b>30</b>
Net Margin	(19.6%)	1.7%	0.9%	5.0%
Cash Flow Statement	2021	2022	2023E	2024E
<b>Net CFO</b>	<b>79</b>	<b>185</b>	<b>245</b>	<b>291</b>
Capex	2	1	1	1
Acquisitions	767	883	(116)	0
<b>Free Cash Flow</b>	<b>78</b>	<b>156</b>	<b>216</b>	<b>262</b>
Balance Sheet	2021	2022	2023E	2024E
Cash & ST Investment	429	224	454	609
Intangible Assets	564	957	761	609
Goodwill	494	970	912	912
<b>Total Assets</b>	<b>1,558</b>	<b>2,250</b>	<b>2,258</b>	<b>2,281</b>
LT Int-Bearing Debt	222	861	846	816
<b>Total Liabilities</b>	<b>807</b>	<b>1,487</b>	<b>1,473</b>	<b>1,448</b>
<b>Shareholders' Equity</b>	<b>751</b>	<b>763</b>	<b>785</b>	<b>832</b>
<b>Tot Liab &amp; SE</b>	<b>1,558</b>	<b>2,250</b>	<b>2,258</b>	<b>2,281</b>

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

**Company Profile**

Dye & Durham Corporation is a leading provider of cloud-based software and technology solutions designed to improve efficiency and increase productivity for legal and business professionals.

**Investment Thesis**

1) High margin business that generates strong cash flows; 2) Strong track record of realizing synergies on M&A targets; 3) Current valuation providing an attractive entry point; 4) Upside from future M&A

**Price Target (Base Case): C\$33.00**

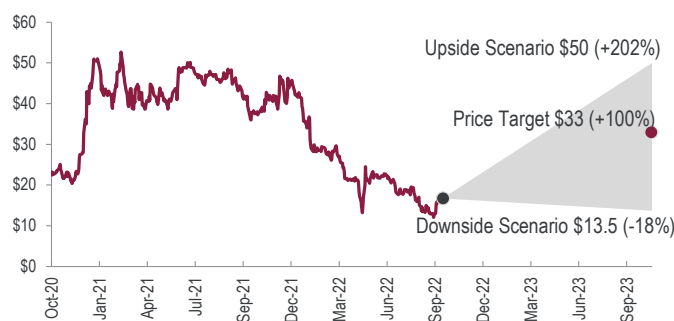
Our base case is calculated using 12% revenue growth, 47% EBITDA margins, a 10.0x EV/EBITDA multiple, and \$5/share to reflect the value of future M&A.

**Upside Scenario: C\$50.00**

Our upside scenario is calculated using estimated 2024E revenue growth of 20%, 55% EBITDA margins and a 12.0x EV/EBITDA multiple

**Downside Scenario: C\$13.50**

Our downside scenario is calculated using 0% revenue growth, 40% EBITDA margins and a 8.5x EV/EBITDA multiple



## Product Demo Takeaways

We visited Dye & Durham's Toronto office, with the product and sales teams walking us through the capabilities of the eCore and Unity platforms. The product demo illustrated the integrative nature of the real estate workflow and conveyancing platforms, giving us a better appreciation of how DND's acquisition approach is well suited to the nature of the platforms.

**Unity Platform Designed For Smooth Integration:** The Unity conveyancing platform, acquired from Teranet in December 2020, is an end-to-end platform that streamlines the real estate conveyancing process. What stood out to us was the number of integrations available in Unity, allowing users to easily pull data from a variety of sources without having to leave the platform. Unity currently has an 85% market share in the Canadian conveyancing market, and after seeing firsthand the ease of use and the amount of time that would be saved by using Unity, we understand why the platform has such widespread adoption.

**Integrations Leading To Acquisitions:** The large number of integrations on the platform also illustrated the value of DND's acquisition approach in the conveyancing and real estate workflow space. As part of the demo we walked through an example of mortgage instruction transfer, a capability that was powered by the Assyst business acquired from TELUS in December 2021. The Assyst example illustrated how DND has the ability to identify assets that are a part of the conveyancing lifecycle before acquiring them and including them as part of the Unity value proposition. During the demo DND noted that its approach has been to partner with integrated providers before, in some cases, eventually acquiring them.

**How Pricing Works:** During the demo we discussed DND's approach to pricing and the process of transitioning customers to a minimum contracted value approach. 30% of DND's customers have moved to a contract structure where they agree to a minimum level of conveyancing transactions for a multi-year period, and if they haven't met those commitments by year-end, are required to pay the difference. Eight of DND's 10 largest conveyancing customers and 49 of the top 100 customers are now on the minimum contract plans, with the pace of conversion expected to slow as the more easily transitioned customers have already been moved over. The minimum level is typically set at 50% of a customer's historical transaction level, insulating against severe weakness in the housing markets.

**Architecture Can Be Expanded To Other Services:** While the Unity and eCore platforms are clear leaders in the Canadian markets, capabilities in the U.K. and Australian markets are less advanced. When asked about the possibility of using the Unity platform in additional geographies, DND noted that the bulk of the development work related to integrating with specific registries and providers, and that the platform was tailored for Canada. That said, DND's experience in building high-end search and conveyancing platforms gives it confidence in improving offerings in the U.K. and Australia, and winning market share. Also, some portions of the tech stack can be used as the building blocks for new platform builds.

### Exhibit 1: DND – Changes To Our Model, F2022-F2024E

	Revenues (\$MM)	EBITDA (\$MM)	Adj. EBITDA (\$MM)	Adj. EPS	CFO (\$MM)	CFO Conversion
<b>F2022A</b>	475	193.4	266.9	-0.32	185	69%
<b>F2023E</b>						
CIBC est. – new	552	247	312	0.07	245	79%
CIBC est. – prior	629	281	341	0.77	228	67%
Consensus	608	NA	347	1.15	266	77%
<b>F2024A</b>						
CIBC est. – new	604	287	341	0.43	291	85%
Consensus	624	NA	363	1.76	329	91%

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

## Price Target Calculation

We derive our price target of \$33 by applying a 10x EV/EBITDA multiple to our F2024 EBITDA estimate based on the current capital structure and sale of TM Group. The 10x multiple is a 1x discount to the peak trading multiple of comparable registry services providers. We also include \$5/share for the value of future M&A. That value is calculated using a DCF that assumes 75% of FCF reinvested in M&A, and average acquisition multiple of 6.5x sales and a 10% discount rate.

## Key Risks To Price Target

The primary risks to our price target include the following: 1) competition and regulatory reviews impact the ability to acquire; 2) regulatory reviews and negative media coverage limit the ability to increase prices on e-conveyancing and transactional services; 3) slowdowns in housing market sales impact transactional revenues, putting organic growth at risk; 4) risks around integration of M&A given the pace of acquisition; and 5) governance concerns in the wake of the stock option grant post the take-private process.

*Note: The CIBC analyst who covers this security visited the company's office in Toronto on October 5. CIBC World Markets was responsible for all transportation costs to and from the location.*

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