

EQUITY RESEARCH

March 6, 2022

Earnings Update

SOFTCHOICE CORPORATION

Benefiting From Solid Demand + Project Monarch

Our Conclusion

Softchoice is seeing solid demand for its software, cloud and services offerings, coupled with the realization of Project Monarch benefits. Gross profit was up 31% Y/Y and the company increased its 2022 gross profit outlook with Q4 results. We see Softchoice as well positioned to benefit from accelerating demand for cloud and digital solutions and see upside as the company expands its relationship with AWS and Google. We retain our Outperformer rating and C\$31 price target.

Key Points

Q4/21 Results Solid, 2022 Guidance Increased: Softchoice reported gross profit of \$85.8 million, roughly 13% above consensus (\$76 million) and 14% above our estimate (\$75.4 million). Adjusted EBITDA of \$26.5 million was above consensus (\$23.6 million) and our estimate (\$23.9 million). Adjusted EBITDA margins (as a percentage of gross profit) were 30.8%, slightly (30 bps) below consensus expectations. Softchoice increased its 2022 financial outlook, with the gross profit guidance increased to over \$320 million (prior over \$300 million). Adjusted EBITDA has been revised from \$90 million-\$100 million to ~30% of gross profit (implying over \$96 million). Adjusted free cash flow conversion of ~90% was unchanged.

Well Positioned In Growth Areas: Softchoice is seeing high demand from three focus areas: 1) hybrid cloud solutions, 2) security software, and 3) software solutions for digital workspaces. Softchoice saw an 86% increase in aggregate public cloud volumes on Microsoft, AWS and Google in 2021, up from a 65% increase in 2020. Softchoice is seeing an acceleration of cloud adoption from clients as they adopt to the changing hybrid work environment and look to save costs.

Solid Growth In Sales Productivity: Softchoice saw its gross profit per executive increase 27% Y/Y to \$751K. The company noted the benefit of Project Monarch efficiencies and an expanded roster of technical experts to aid the sales process. Softchoice expects to reach its target of ~428 Account Executives at the end of 2023, noting that it has not experienced difficulty hiring. With a customer base skewed towards commercial and SMB, we believe that labour challenges at clients could be an incremental positive for Softchoice, driving Services revenue.

Executing On Project Monarch: Softchoice reiterated its expectation of \$25 million in Project Monarch benefits in 2022. The company has seen gross profit benefits in 2021 from pricing alignment and procurement savings, and expects to realize further process streamlining and automation savings in 2022.

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Outperformer

SFTC-TSX, Sector: Information Technology

Current Price (3/4/22): C\$22.81

Price Target (12-18 mos.): C\$31.00

CIBC Estimates and Valuation

(Dec. 31)	2020	2021	2022	2023
Adj. EPS	0.64A	0.65A	0.74E	0.90E
Prior		0.56E	0.82E	
Adj. EBITDA(mln)	65.5A	69.1A	100.2E	113.1E
Prior		66.5E	99.7E	

Adj. EPS	Q1	Q2	Q3	Q4
2021	0.06A	0.23A	0.09A	0.27A
Prior				0.20E
2022	0.16E	0.19E	0.16E	0.23E
Prior	0.12E	0.26E	0.15E	0.29E

Adj. EBITDA(mln)	Q1	Q2	Q3	Q4
2021	10.5A	20.9A	11.3A	26.5A
Prior				23.9E
2022	22.7E	25.0E	23.4E	29.1E
Prior	17.7E	28.6E	20.6E	32.9E

Valuation	2020	2021	2022	2023
P/E	27.9x	27.6x	24.2x	19.9x
EV/EBITDA	15.9x	15.1x	10.4x	9.2x
FCF Yield	NM	5.1%	7.8%	8.8%

Stock Performance and Key Indicators

Enterprise Value:	C\$1,331M	Shares O/S:	63.2M
Market Cap.:	C\$1,442M	Float:	30.9M
52-wk Range:	C\$19.56 - C\$40.00	Div. / Yield:	C\$0.36/1.57%

TSX Composite Index vs. SFTC-TSX



(Source: FactSet)

All figures in US dollars unless otherwise stated (C\$1.277:US\$1.00).

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.

Softchoice Corporation (SFTC-TSX) — Outperformer

Price (3/4/22) C\$22.81 12-18 mo. Price Target C\$31.00

Sector: Information Technology

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Peer Comparison	2020	2021	2022E	2023E
P/E - Softchoice	3.6x	-	-	-
EV/EBITDA - Peer Average	-	23.8x	-	-
EV/EBITDA - Softchoice	0.3x	18.4x	-	-
Key Financial Metrics	2020	2021	2022E	2023E
Net Debt	228	86	20	(54)
Total Debt	229	89	83	78
Net Debt/EBITDA	3.5x	1.2x	0.2x	(0.5x)
Free Cash Flow	(19)	52	89	100
Sales Growth	(12.3%)	7.9%	10.1%	6.0%
Per Share Data	2020	2021	2022E	2023E
FCFPS	(0.33)	0.91	1.40	1.57
Adj. EPS Dil.	0.64	0.65	0.74	0.90
Wgt Avg # of Shares	45.1	53.4	59.7	60.1
FD Number of Shares	56.4	57.2	63.5	63.9
Income Statement	2020	2021	2022E	2023E
Revenue	837	903	994	1,054
Cost of Goods Sold	598	616	672	700
Gross Profit	238	287	322	354
Gross Margin %	28.48%	31.78%	32.37%	33.58%
Tot Operating Exp	223	284	256	274
Adj. EBITDA	65	69	100	113
Adj EBITDA Margin	27.5%	24.1%	31.1%	32.0%
D&A	23	21	22	21
Interest Expense	12	10	2	2
Pretax profit	3	(9)	64	78
Tax Expense	1	1	17	21
Adjusted Net Income	36	37	47	57
Adjusted Net Margin	4.3%	4.1%	4.7%	5.4%
Cash Flow Statement	2020	2021	2022E	2023E
Net CFO	(11)	54	92	103
Capex	(8)	(2)	(3)	(3)
Free Cash Flow	(19)	52	89	100
Balance Sheet	2020	2021	2022E	2023E
Cash & ST Investment	1	3	63	132
Goodwill	139	139	139	139
Total Assets	602	641	645	720
LT Int-Bearing Debt	0	101	82	77
Total Liabilities	630	583	562	605
Shareholders' Equity	(27)	58	82	114

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

Company Profile

Softchoice Corporation is a Canadian IT solutions and managed service provider. The company's technology partners include Microsoft, Cisco, VMware, Google, and AWS.

Investment Thesis

1) Leading North American IT Solutions Provider 2) Focused On High Growth Segments 3) Long Tenured Customer Base And A Focus On Higher Value Solution Sales.

Price Target (Base Case): C\$31.00

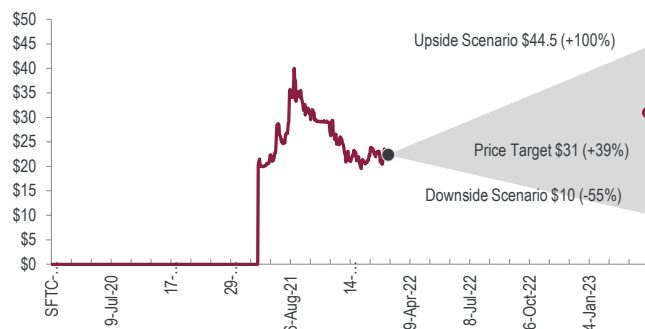
Our Price Target is calculated using 7.9% gross profit growth, 29.4% EBITDA margin as a percentage of gross profit, and a 16x EV/EBITDA multiple.

Upside Scenario: C\$44.50

Our upside scenario is calculated using 24% gross profit growth, 33.50% EBITDA margin as a percentage of gross profit and a 18x EV/EBITDA multiple.

Downside Scenario: C\$10.00

Our downside scenario is calculated using 10.0% gross profit growth, 26.0% EBITDA margin as a percentage of gross margin and a 7x EV/EBITDA multiple.



Financial Summary

Gross Profit By Segment: Softchoice reported gross profit of \$85.8 million (consensus \$76 million). Hardware gross profit of \$25.3 million (our estimate \$21.4 million) was up 1.8% Y/Y, and software and cloud revenue of \$53.2 million (our estimate \$45.6 million) was up 41.5% Y/Y due to strong demand for SaaS and security software solutions and increased public cloud consumption. Professional services gross profit was \$7.3 million (our estimate \$8.4 million), up 70.2% Y/Y from \$4.3 million.

Gross Profit Efficiency Increases: Softchoice reported gross profit per account executive (GP/AE) of \$751,000 (TTM), up 27% Y/Y from \$591,000. Total number of account executives decreased from 404 to 382 (TTM), down 5% Y/Y. Gross profit per customer was up 27% from \$49,000 to \$62,000 (TTM) while the total number of customers decreased by 4% from 4,836 to 4,638.

EBITDA Growth: Adjusted EBITDA of \$26.5 million was above consensus (\$23.6 million) and our estimate (\$23.9 million). Adjusted EBITDA margins (as a percentage of gross profit) were 30.8%, 30 bps below consensus expectations.

Exhibit 1: SFTC – Financial Summary – Q4/21

	Q4-F2021			Q4-F2020	Y/Y%	Q3-F2021	Q/Q%
	Actual	CIBCe	Cons				
Consolidated							
Net Revenue (\$M)	258	264	261	231	11.6%	199	29.7%
Gross Profit (\$M)	85.8	75.4	76.0	65.4	31.1%	65.2	31.6%
Gross Profit Margin	33.2%	28.6%	29.2%	28.3%	17.5%	32.8%	1.5%
Adj. EBITDA (\$M)	26.5	23.9	23.6	26.0	2.0%	11.3	135.1%
Adj. EBITDA Margin	30.8%	31.7%	31.1%	11.2%	174.3%	5.7%	443.8%
Adjusted EPS	\$0.27	\$0.20	\$0.23	\$0.36	-25.0%	\$0.09	205.1%
Adjusted FCF	24.4	13.3	NA	NA	NA	NA	NA

Source: Company reports and CIBC World Markets Inc.

Changes To Our Model: With Softchoice reiterating 2022 guidance, we have made minimal changes to our model. Our updated forecast is found in the table in Exhibit 2.

Exhibit 2: SFTC – Changes To Our Model – 2021A - 2023E

	Revenues (\$mlns)	Gross Profit (\$mlns)	EBITDA (\$mlns)	EPS	CFO (\$mm)
2021A	903	287	69	0.65	54
2022E					
CIBC est. – new	994	322	100	0.74	92
CIBC est. – prior	1,073	315	100	0.82	77
Consensus	1,033	312	95	0.88	71
2023E					
CIBC est. – new	1,054	354	113	0.90	103
CIBC est. – prior	1,158	340	106	0.88	80
Consensus	1,098	344	109	1.09	84

Source: Company reports and CIBC World Markets Inc.

Price Target Calculation

We derive our price target of \$31.00 by applying a 16x EV/EBITDA multiple to our 2023E EBITDA estimate based on the current capital structure. The 16x multiple is in line with software-focused IT Solution providers including Softcat, Crayon, Bytes and SoftwareOne.

Key Risks To Price Target

The primary risks to our price target include the following: 1) volatility in the global IT environment, 2) increasing competition from other IT solutions providers, 3) the company's ability to introduce new or updated technology in a timely manner, 4) the company's ability to partner with leading technology providers, 5) the loss of key management or other employees.

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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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