

EQUITY RESEARCH

September 22, 2022

Flash Research

SOFTCHOICE CORPORATION

Eastern Institutional Investor Conference 2022 Takeaways

Softchoice CEO Vince De Palma presented at a fireside chat at CIBC's Eastern Institutional Investor Conference. Below are some key takeaways:

Solid Demand Environment In SMB/Commercial: Softchoice noted that recession fears have not resulted in any slowdown in spending across its SMB and Commercial customers, which comprise ~90% of overall revenue and 75% of Gross Profit. These companies are typically earlier in their digital journey and rely on Softchoice as an extension of their team, especially given the tight IT labour market. Softchoice has seen some slowdowns in Enterprise (~10% revenue and 25% Gross Profit), but it appears more company-specific (M&A integration, overbuying hardware in F21 etc.) Mr. De Palma noted that enterprise customers typically have robust IT teams and use Softchoice to manage software titles to keep up with compliance, eliminate redundancies, etc. The company is also doing more cloud work with enterprise customers, where it is able to bring its expertise with all hyperscalers (AWS, Azure, Google, etc.), while the enterprise's IT team may have experience with only one or two.

Investing In Growth: The company ended 2021 with 396 Account Executives (AEs), with guidance of 423-433 AE for F22. As of H1/22, the company has 424 AEs, ahead of its target, and now expects to end F22 with 433-435 AEs and in F23 to see a continuation of this ramp-up in the salesforce. At the end of H1/22 the company had its highest-ever salesforce productivity at \$771K per AE. With the salesforce target ahead of expectations, this will put some pressure on EBITDA this year; however, management believes it will ultimately drive future growth for the company.

F22 Guidance: SFTC walked through the F22 guidance change it announced with Q2 results. The F22 gross profit outlook (>\$320MM) is slightly lower than previous expectations, driven mostly by the slowdown in Enterprise spending in some larger customer accounts for company-specific reasons. The company also lowered its adjusted EBITDA expectations to 25-28% for the full year (prev. 30%). This is mostly driven by SFTC's investment to expand its technical experts in the team, which is running ahead of its target timeline. In addition, lower-than-expected spending from Enterprise customers will act as a headwind to EBITDA margins, given the stronger margin profile of Enterprise customers. The company has seen double-digit organic growth from 2017 to 2019, with H1/22 seeing 14% Y/Y GP organic growth. The outlook for this year at the lower end is 11.5% GP Y/Y organic growth.

M&A Environment: While Softchoice has not engaged in any M&A since the company went public, management did note it would be open to acquisitions to deepen the company's technical expertise. We believe the company could look to complete strategic acquisitions that target boutique firms with advanced capabilities in machine learning, AWS, application development and/or Devops.

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Neutral

SFTC-TSX, Sector: Information Technology

Current Price (9/20/22): C\$20.00

Price Target (12-18 mos.): C\$21.00

All figures in US dollars unless otherwise stated (C\$1.328: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.

Price Target Calculation

We derive our price target of \$21.00 by applying a 10.5x EV/EBITDA multiple to our 2023E EBITDA estimate based on the current capital structure. The 10.5x 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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CIBC World Markets Inc. Price Chart

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