October 22nd, 2020
Research update

SMC Research
Small and Mid Cap Research

THOMSON REUTERS ANALYST AWARDS 2018 WINNER
THOMSON REUTERS ANALYST AWARDS 2017 WINNER

Mensch und Maschine SE

On course for record profits despite slightly lower targets

Rating: Hold (unchanged) | **Price:** 55.40 € | **Price target:** 52.30 € (prev.: 52.20 €)

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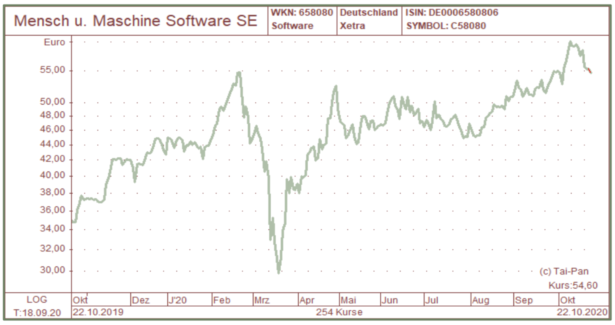
Recent business development



As a result of Covid-19, Mensch und Maschine suffered a decline in sales in the third quarter as well, but in contrast to the second quarter, this was more than compensated for in terms of earnings. Thanks to an improved gross margin and continued cost discipline, Q3 EBIT rose by almost 21 percent. Cumulated over the first nine months, there was a slight increase in sales, an EBIT growth of almost 20 percent and a double-digit increase in net profit, setting again new records. The free cash flows developed even more impressively, almost doubling to over EUR 28 m. M+M is also striving for new earnings records for the entire year, but with reference to the improved visibility it has reduced its specific EPS forecast from EUR 1.17 – EUR 1.23 to EUR 1.07 – EUR 1.18. On the other hand, the dividend is still to be increased to EUR 1.00 – EUR 1.05 per share. The announcement of continued growth in the coming years was also left unchanged. These good prospects are reflected in the fair value of EUR 52.30 per share we have determined, on the basis of which we confirm the previous "Hold" rating.

Basic data

Based in:	Wessling
Sector:	CAD/CAM software
Headcount:	964
Accounting:	IFRS
ISIN:	DE0006580806
Ticker:	MUM:GR
Price:	55.40 Euro
Market segment:	Scale / m:access
Number of shares:	17.2 m
Market Cap:	950.1 m Euro
Enterprise Value:	1,046.6 m Euro
Free Float:	45.0%
Price high/low (12M):	60.60 / 29.50 Euro
Ø urnover (Xetra, 12 M):	444,200 Euro / day

FY ends: 31.12.	2017	2018	2019	2020e	2021e	2022e
Sales (m Euro)	160.9	185.4	245.9	252.1	282.3	313.4
EBIT (m Euro)	15.2	19.7	27.2	31.7	36.2	42.2
Net Profit	9.4	11.7	16.7	18.8	21.8	25.6
EPS	0.56	0.71	0.99	1.12	1.30	1.52
Dividend per share	0.50	0.65	0.85	1.02	1.15	1.30
Sales growth	-3.7%	15.3%	32.7%	2.5%	12.0%	11.0%
Profit growth	42.9%	24.1%	42.6%	12.8%	15.9%	17.5%
PSR	5.79	5.02	3.79	3.69	3.30	2.97
PER	98.9	79.7	55.9	49.5	42.7	36.3
PCR	61.2	61.1	35.3	25.4	26.2	23.7
EV / EBIT	67.4	52.2	37.7	32.3	28.3	24.3
Dividend yield	0.9%	1.2%	1.5%	1.8%	2.1%	2.3%

Nine-month sales slightly up

Following the Covid-19-related decline in sales in the second quarter, sales for the period from July to September were also down on the previous year, although the decline was limited to a comparatively moderate 7.1 percent. The software segment was particularly stable this time, with sales falling by only 0.9 percent in the third quarter, compared with -9.0 percent in the previous three months. M+M is particularly satisfied with the development in the BIM sector and thus also at the subsidiary SOFiSTiK, which almost completely compensated for the somewhat more pronounced weakness in the CAM business. In contrast, the percentage sales decline in the VAR business in the third quarter was slightly stronger (-10 percent) than in the period from April to June. This was due to the Covid-19 pandemic as well as to the end of the exceptional economic boom in the Autodesk business following a special offer for existing customers. In total for the first nine months, however, the two segments recorded sales growth, which adds up to a plus of 3.6 percent to EUR 180.6 m at Group level.

Significant margin improvement in the course of the year

The declining contribution of the trading business with Autodesk licences had a positive effect on the gross margin in the VAR business, which stood at 37.1 percent in the third quarter, almost two percentage points higher than a year ago. Compared with the first quarter, which was very strongly driven by trading business, the difference is even more than five percentage points. This and the higher proportion of sales generated by the software segment meant that the gross margin at Group level also rose by two percentage points to 55.5 percent. In the software segment itself, on the other hand, there was a decline of 1.5 percentage points to 91.2 percent, which – as in the year to date – is attributable to the higher sales contribution of SOFiSTiK. In absolute figures, however, gross profit in the third quarter was still slightly down (-3.6 percent), while a minimal growth of 0.5 percent to EUR 93.5 m was achieved over the whole nine months.

Business figures	**9M 2019**	**9M 2020**	***Change***
Sales	174.27	180.61	*3.6%*
VAR business	119.54	125.68	*5.1%*
Software	54.73	54.93	*0.4%*
Gross profit	93.03	93.54	*0.5%*
VAR business	41.86	43.30	*3.5%*
Software	51.18	50.25	*-1.8%*
Gross margin	*53.4%*	*51.8%*	
EBITDA	25.15	29.66	*17.9%*
VAR business	9.26	11.66	*26.0%*
Software	15.89	18.00	*13.2%*
EBITDA margin	*14.4%*	*16.4%*	
EBIT	18.19	21.76	*19.7%*
VAR business	6.02	8.09	*34.5%*
Software	12.20	13.67	*12.1%*
EBIT margin	*10.4%*	*12.1%*	
EBT	17.55	20.43	*16.4%*
EBT margin	*10.1%*	*11.3%*	
Net profit	11.04	12.63	*14.4%*
Net margin	*6.3%*	*7.0%*	
Free cash flow	14.62	28.12	*92.3%*

In m Euro and percent, source: Company

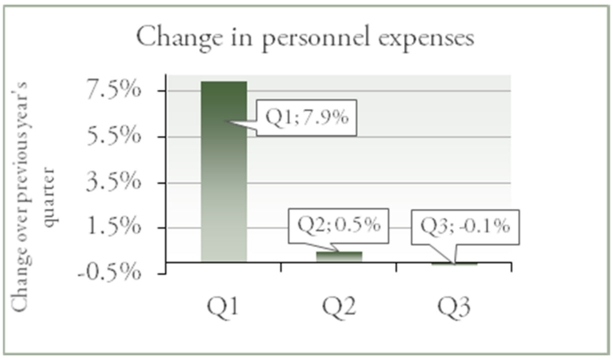
Other expenses significantly reduced

The minimal growth in gross profit in the first nine months was offset by a strong reduction in other operating expenses, which fell by almost 33 percent to EUR 8.9 m. This was due to a combination of M+M's already strong cost discipline, which was further tightened in response to the crisis, and Covid-19-specific savings through the elimination of most of the travel expenses and, temporarily, attendance at events.

Staff recently slightly reduced

By contrast, staff costs for the nine-month period rose by 2.8 percent, i.e. at a faster rate than gross profit, reflecting almost exactly the development in the number of employees, which rose by 3.1 percent to 946 (full-time equivalents) compared with September 2019. However, this comparison conceals the fact that

M+M has also reined in the personnel expenses since the outbreak of the crisis, but this is only reflected in the figures with some delay. For example, between the six-month reporting date and the end of September, the FTE figure was reduced by 1.9 percent, thus completely reversing the growth in personnel in the first half of the year. In the software segment, job cuts in the third quarter were as high as 4 percent. Considered separately, personnel expenses in the third quarter were already slightly below the previous year's level, whereas at the beginning of the year this cost item had risen by 7.9 percent. M+M has also announced that it intends to use natural fluctuation to make very moderate job cuts in the fourth quarter as well.



Source: Company

New records for EBIT…

The combination of the overall decline in costs and the almost 60 percent increase in other operating income (short-time working allowance was booked under this item) enabled the quarterly EBIT to improve by more than a fifth to EUR 5.0 m, thus setting a new record for this time of year. In the software segment, growth was even almost 26 percent, but the operating result in the VAR business also rose by over 6 percent. Cumulative EBIT growth over the three quarters was just under 20 percent (to a new record of EUR 21.8 m), with the VAR business achieving growth of 26 percent and the software segment 13 percent.

… and nine-month earnings

Earnings after taxes and minority interests also reached a new record level of EUR 12.6 m after nine months. Compared to EBIT, however, the growth remained somewhat weaker at 14 percent, which was due on the one hand to negative currency effects leading to a deterioration in the financial result, and on the other hand to the strong increase of the minority share in the group result. This increased by 35 percent (to EUR 1.6 m) and thus significantly stronger than the after-tax result. This strong increase reflects the above-average performance of the 51 percent subsidiary SOFiSTiK, which according to the company, after a slight cooling off in the second quarter, benefited again from very lively demand in the BIM sector in the summer.

Free cash flows almost doubled

As in the first half of the year, the earnings performance, especially impressive in view of the Covid-19 pandemic, was far eclipsed by the cash flow figures after nine months. The operating cash flow increased by more than half to EUR 32.7 m year-on-year, which means that more than 18 percent of the nine-month revenues remained in the till as cash surplus. In addition to the very good earnings development, this was assisted by the change in working capital, the effect of which switched from EUR -0.9 m in the previous year to EUR +8.3 m in the reporting period. The largest item was receivables, which fell by 41 percent to EUR 23.2 m compared to the turn of the year. As investment outflows fell from EUR 6.8 m to EUR 4.6 m at the same time, the improvement in free cash flow was even more impressive at 92 percent or EUR +13.5 m to EUR 28.1 m. EUR 20.9 m of this was used for net financing activities, with the dividend being by far the largest single item at EUR 14.2 m, followed by payments for rent and leasing amounting to EUR 5.0 m. In total, liquidity increased by EUR 7.0 m to EUR 19.9 m in the course of the first nine months.

Equity ratio at almost 50 percent

Since the dividend payment was only distributed in July in contrast to previous years due to the Covid-19-related later date of the Annual General Meeting, equity fell in the third quarter by EUR 7.4 m to EUR 73.5 m despite the profit. Compared to the previous year, however, it is still almost 11 percent higher. The equity ratio also increased slightly year on year (from 48.2 to 48.6 percent).

Earnings forecast reduced, dividend outlook confirmed

For the entire year, M+M intends to increase profits and set a new record. However, the target range for earnings per share has now been reduced from the previous EUR 1.17 − 1.23 to EUR 1.07 − 1.18. Upon enquiry, the management explained this exclusively with the now improved visibility; the question of any business development below plan was explicitly answered in the negative. In contrast, the announcement that the dividend would be raised from 85 cents in the previous year to between 100 and 105 cents was confirmed, as was the objective of returning to growth of 8 to 12 percent p.a. in gross profit and 18 to 24 cents p.a. in earnings per share in the coming years and, on this basis, to increase the dividend by 15 to 20 cents p.a. Looking ahead to the coming year, M+M expects a still subdued development for the first quarter, mainly due to the very high basis of comparison from 2020, but this comparison effect is expected to turn around from Q2 onwards and facilitate sales growth.

Estimates adjusted

We have taken the Q3 figures as an opportunity to modify our estimates in several places. The changes are minor adjustments with partly opposite effects on the fair value. The most striking modification is certainly the reduction of the sales growth forecast for this year from 5.0 to 2.5 percent. Since we have not compensated for this adjustment in subsequent years and have left the growth rates assumed so far unchanged, this results in a slightly lower sales path. For 2027, we now expect sales of EUR 516 m (previously: EUR 529 m). On the other hand, the gross margin appears to be developing better than we had previously expected, which is why we have raised it by one percentage point to 51 percent for the current year. For the years from 2021 onwards, for which we had already anticipated an improvement in gross margin, we have left the assumption unchanged.

Change in expense structure

We were again surprised by the extent of cost elasticity at M+M, which is why we have again lowered our estimates for the development of personnel expenses and other operating expenses. With regard to the latter, however, the reclassification of expenses as a result

m Euro	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales	252.1	282.3	313.4	346.3	382.7	422.8	467.2	516.3
Sales growth		12.0%	11.0%	10.5%	10.5%	10.5%	10.5%	10.5%
EBIT margin	12.6%	12.8%	13.5%	14.1%	14.7%	15.2%	15.7%	16.2%
EBIT	**31.7**	**36.2**	**42.2**	**48.8**	**56.1**	**64.2**	**73.3**	**83.5**
Tax rate	30.0%	31.0%	31.0%	31.0%	31.0%	31.0%	31.0%	31.0%
Adjusted tax payments	9.5	11.2	13.1	15.1	17.4	19.9	22.7	25.9
NOPAT	**22.2**	**25.0**	**29.1**	**33.7**	**38.7**	**44.3**	**50.6**	**57.6**
+ Depreciation & Amortisation	10.9	11.4	11.0	10.7	10.5	10.5	10.4	10.5
+ Increase long-term accruals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating Cash Flows	33.1	36.4	40.1	44.4	49.3	54.8	61.0	68.1
- Increase Net Working Capital	4.8	-0.3	-0.3	-0.4	-0.5	-0.6	-0.8	-0.9
- Investments in fixed assets	-5.6	-2.4	-2.6	-2.7	-2.8	-3.0	-3.1	-3.3
Free Cash Flows	**32.2**	**33.7**	**37.2**	**41.3**	**45.9**	**51.2**	**57.1**	**63.9**

SMC estimation model

of IFRS16 also plays a role. This is reflected in a higher estimate of depreciation and amortisation both in 2020 and in subsequent years.

Profit estimate for 2020 slightly reduced

Cumulatively, the changes for 2020 lead to a EUR 0.5 m higher EBIT estimate of EUR 31.7 m, which is, however, more than offset by the now assumed higher deficit in the financial result as well as a higher share of minority interests in the net profit. All in all, our estimate of earnings per share has been slightly reduced from EUR 1.17 to EUR 1.12. While we have previously expected a result at the lower end of the company's guidance, our new estimate is in the middle of the updated M+M target range. With regard to the next few years, the dampening effects of the slight reduction in the sales projection and the increased depreciation and amortisation are also predominating, so that the new earnings projection is now slightly below the old estimates. The target EBIT margin for 2027 fell from 16.8 to 16.2 percent, mainly due to depreciation and amortisation. As a lower target margin is easier to achieve and maintain, we have, in return, reduced the safety discount, which we apply to the target margin to determine the terminal value, from 15 to 10 percent.

Cash flows higher

We have substantially increased this year's cash flow, which was well above our previous expectations after nine months. Although cash outflows for investments, for which we had assumed greater restraint in view of the Covid-19 pandemic, were also above our estimates, on balance this led to a noticeable increase in the free cash flow estimate. We have taken the very positive cash flows and liquidity development as an opportunity to increase the liquidity defined in the model as not necessary for operations to EUR 15 m. The overall resulting model business performance for the next eight years, which we assume for determining the fair value, is summarized in the table above; further details can also be found in the Annex.

WACC of 6.4 percent

We discount the free cash flows resulting from these assumptions with WACC (Weighted Average Cost of Capital) at an interest rate on borrowed capital of 4.0 percent. The cost of equity is determined using the Capital Asset Pricing Model (CAPM). Our risk-free interest rate is − at 1.0 percent − the long-term average of the German current yield and for the market risk premium we use an above-average value of 6.5 percent (the past-based average market risk premium used for Germany in 2019 was 5.7 percent, source: Pablo Fernandez, Mar Martinez and Isabel F. Acin: Market Risk Premium and Risk-free Rate used for 69 countries in 2019: a survey). Combined with a beta of 1.2 and a target debt ratio of 40 percent, this results in a WACC rate of 6.4 percent.

Target price: EUR 52.30 per share

The model results in a market value of equity of EUR 879.0 million or EUR 52.31 per share, from which we derive the minimally increased price target of EUR 52.30 (previously: EUR 52.20). The assessment of the forecast risk of our estimates remains unchanged at three out of six possible points.

Sensitivity analysis

When the input parameters are varied for our sensitivity analysis (WACC between 5.4 and 7.4 percent and perpetual cash flows growth between 0 and 2 percent), the fair value of the share lies between EUR 39.91 and EUR 79.12.

Sensitivity analysis	Perpetual cash flows growth				
WACC	**2.0%**	**1.5%**	**1.0%**	**0.5%**	**0.0%**
5.4%	79.12	70.94	64.64	59.63	55.56
5.9%	68.76	62.67	57.84	53.90	50.64
6.4%	60.78	56.11	**52.31**	49.15	46.50
6.9%	54.44	50.77	47.72	45.15	42.96
7.4%	49.28	46.34	43.86	41.74	39.91

Conclusion

Following the decline in sales and earnings in the second quarter, the months July to September also brought a drop in revenue for Mensch und Maschine, but this was more than compensated for in terms of earnings. Thanks to the improved gross margin and continued strict cost discipline, EBIT for the quarter rose by almost 21 percent. In total for the first nine months as well, there was an EBIT growth of 20 percent, while sales increased by slightly less than 4 percent.

Once again M+M was able to shine with an excellent cash flow development. After nine months, the operating cash flow amounts to EUR 32.7 m (+53 percent compared to the previous year) or 18 percent of the nine-month revenues.

Based on the new earnings and cash flows records, the company still intends to increase this year's dividend from 85 cents last year to between 100 and 105 cents per share. In contrast, the target range for the profit was slightly reduced. Instead of striving for an EPS increase of between 117 and 123 cents, M+M now considers the range of 107 to 118 cents per share to be realistic. The company emphasises that the reduction is not due to any deterioration in business performance, but merely to the visibility that was previously limited due to Covid-19 and has now noticeably improved.

In response to the nine-month figures, we have modified our estimates in several places, but overall, this has had little effect on the fair value we have calculated. We now see it at EUR 52.30 per share and on this basis confirm our previous "Hold" rating.

Annex I: Balance sheet and P&L estimation

Balance sheet estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
ASSETS									
I. Total non-current	98.7	100.5	98.5	97.1	96.0	95.3	94.8	94.4	94.2
1. Intangible assets	54.1	61.0	60.4	59.7	59.2	58.6	58.1	57.6	57.1
2. Tangible assets	34.0	35.9	34.6	33.7	33.3	33.1	33.1	33.3	33.6
II. Total current assets	60.8	63.5	63.5	71.3	82.4	96.1	111.2	126.2	143.0
LIABILITIES									
I. Equity	73.5	81.4	87.2	94.7	104.1	116.2	129.9	143.5	159.0
II. Accruals	12.2	12.7	13.2	13.8	14.3	14.8	15.4	15.9	16.5
III. Liabilities									
1. Long-term liabilities	34.0	31.0	22.7	20.8	20.8	20.8	20.8	20.8	20.8
2. Short-term liabilities	39.9	38.9	38.9	39.0	39.2	39.5	39.8	40.3	40.8
TOTAL	**159.5**	**163.9**	**162.0**	**168.3**	**178.5**	**191.4**	**206.0**	**220.6**	**237.2**

P&L estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales	245.9	252.1	282.3	313.4	346.3	382.7	422.8	467.2	516.3
Gross profit	127.9	128.6	147.1	163.7	181.3	200.7	222.3	246.2	272.7
EBITDA	36.5	42.6	47.7	53.2	59.5	66.7	74.7	83.7	93.9
EBIT	27.2	31.7	36.2	42.2	48.8	56.1	64.2	73.3	83.5
EBT	26.3	30.0	35.3	41.6	48.3	55.6	63.8	72.9	83.1
EAT (before minorities)	18.3	21.0	24.4	28.7	33.3	38.4	44.0	50.3	57.4
EAT	16.7	18.8	21.8	25.6	29.7	34.1	38.9	44.3	50.4
EPS	0.99	1.12	1.30	1.52	1.76	2.03	2.32	2.64	3.00

Annex II: Cash flows estimation and key figures

Cash flows estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
CF operating	26.4	36.6	35.5	39.3	43.6	48.4	53.8	60.0	66.9
CF from investments	-8.6	-5.6	-2.4	-2.6	-2.7	-2.8	-3.0	-3.1	-3.3
CF financing	-14.5	-24.6	-34.4	-30.5	-31.4	-33.8	-37.8	-44.1	-49.3
Liquidity beginning of year	9.6	12.9	19.4	18.1	24.3	33.8	45.6	58.7	71.4
Liquidity end of year	12.9	19.4	18.1	24.3	33.8	45.6	58.7	71.4	85.7

Key figures

percent	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales growth	32.7%	2.5%	12.0%	11.0%	10.5%	10.5%	10.5%	10.5%	10.5%
Gross profit growth	23.1%	0.5%	14.4%	11.3%	10.8%	10.8%	10.8%	10.7%	10.7%
Gross margin	52.0%	51.0%	52.1%	52.2%	52.3%	52.5%	52.6%	52.7%	52.8%
EBITDA margin	14.9%	16.9%	16.9%	17.0%	17.2%	17.4%	17.7%	17.9%	18.2%
EBIT margin	11.1%	12.6%	12.8%	13.5%	14.1%	14.7%	15.2%	15.7%	16.2%
EBT margin	10.7%	11.9%	12.5%	13.3%	14.0%	14.5%	15.1%	15.6%	16.1%
Net margin (after minorities)	6.8%	7.5%	7.7%	8.2%	8.6%	8.9%	9.2%	9.5%	9.8%

Disclaimer

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Charts
The charts were made with Tai-Pan (www.lp-software.de).

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II) Preparation and updating

The present financial analysis was prepared by: Dipl. Volkswirt Dr. Adam Jakubowski

Participants in the preparation of the present financial analysis: -

The present analysis was finished on 22.10.2020 at 13:15 and published on 22.10.2020 at 13:25.

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Buy	We expect an increase in price for the analysed financial instrument by at least 10 percent. We assess the estimation risk as average (3 to 4 points).
Speculative Buy	We expect an increase in price for the analysed financial instrument by at least 10 percent. We assess the estimation risk as above average (5 to 6 points).

Hold	We expect that the price of the analysed financial instrument will remain stable (between -10 and +10 percent). The forecast risk (1 to 6 points) has no further impact on the rating. The rating "hold" is also used in cases where we perceive a price potential of more than 10 percent, but explicitly mentioned temporary factors prevent a short-term realisation of the price potential.
Sell	We expect that the price of the analysed financial instrument will drop by at least 10 percent. The forecast risk (1 to 6 points) has no further impact on the rating.

The expected change in price refers to the current share price of the analysed company. This price and any other share prices used in this analysis are XETRA closing prices as of the last trading day before publication. If the share is not traded on XETRA, the closing price of another public stock exchange is used with a separate note to that effect.

The price targets published within the assessment are calculated with common methods of financial mathematics, especially with the DCF (discounted cash flow) method, the sum of the parts valuation and a peer group analysis. The valuation methods are affected by economic framework conditions, especially by the development of the interest rates.

The rating resulting from these methods reflects current expectations and can change anytime subject to company-specific or economic changes.

More detailed explanations of the models used by SMC Research can be found at:
http://www.smc-research.com/impressum/modellerlaeuterungen

An overview of the recommendations prepared and distributed by SMC Research in the last 12 months can be found at: http://www.smc-research.com/publikationsuebersicht

In the past 24 months, sc-consult GmbH has published the following financial analyses for the company:

Date	Rating	Target price	Conflict of interests
18.09.2020	Buy	52.20 Euro	1), 3), 4)
24.07.2020	Hold	50.50 Euro	1), 3)
22.04.2020	Buy	50.00 Euro	1), 3), 4)
17.03.2020	Buy	50.00 Euro	1), 3)
17.02.2020	Hold	50.50 Euro	1), 3), 4)
23.10.2019	Buy	38.50 Euro	1), 3)
06.08.2019	Buy	37.10 Euro	1), 3)
02.05.2019	Hold	35.80 Euro	1), 3), 4)
19.02.2019	Buy	35.00 Euro	1), 3), 4)
17.12.2018	Buy	33.70 Euro	1), 3), 4)
23.10.2018	Buy	31.30 Euro	1), 3)

In the course of the next twelve months, sc-consult GmbH will presumably prepare the following financial analyses for the company: one report, two updates

The publishing dates for the financial analyses are not yet fixed at the present moment.

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