

# Nitro Software Ltd (NTO)

Rating: Buy | Risk: High | Price Target: \$4.35

**A solid 1H21 puts NTO in a strong position to deliver on FY21 guidance. Maintain Buy.**

## Key Information

Current Price (\$ps)	3.33
12m Target Price (\$ps)	4.35
52 Week Range (\$ps)	2.16 - 3.75
Target Price Upside (%)	30.7%
TSR (%)	30.7%
Reporting Currency	USD
Market Cap (\$m)	715.1
Sector	Information Technology
Avg Daily Volume (m)	0.4
ASX 200 Weight (%)	0%

## Fundamentals

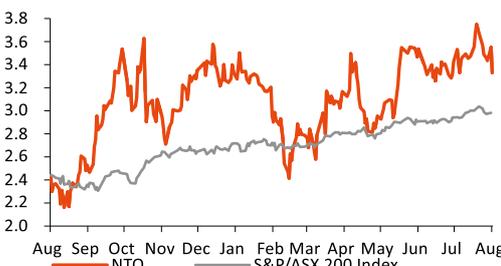
YE 31 Dec (USD)	FY20A	FY21E	FY22E	FY23E
Sales (\$m)	40.2	48.8	59.9	74.5
NPAT (\$m)	(7.5)	(20.1)	(21.9)	(13.8)
EPS (cps)	(3.7)	(9.5)	(9.9)	(6.1)
EPS Growth (%)	(61.9%)	nm	(4.1%)	38.7%
DPS (cps) (AUD)	0.0	0.0	0.0	0.0
Franking (%)	0%	0%	0%	0%

## Ratios

YE 31 Dec	FY20A	FY21E	FY22E	FY23E
P/E (x)	(67.6)	(25.2)	(24.3)	(39.6)
EV/EBITDA (x)	(79.3)	(26.9)	(24.7)	(41.7)
Div Yield (%)	0.0%	0.0%	0.0%	0.0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%

## Price Performance

YE 31 Dec	1 Mth	2 Mth	3 Mth	1 Yr
Relative (%)	(4.0%)	(8.8%)	7.5%	14.2%
Absolute (%)	(2.7%)	(5.8%)	13.8%	36.4%
Benchmark (%)	1.3%	3.0%	6.3%	22.2%



Price performance indexed to 100

Source: FactSet

## Major Shareholders

BROWN MICHAEL M	8.3%
Australian Ethical Investments Ltd. (Inv)	5.4%
Regal Funds Management Pty Ltd.	5.1%
CHANDLER SAM	4.6%
FIL Investment Management (Hong Kong) Lt	2.4%

## Event

NTO has delivered a solid 1H21 result with better than expected revenues delivering a likely “shallower” investment phase. Further, 1H revenue approx. 50% of the mid-point of FY21 revenue guidance (vs 47% in 1H20) puts NTO in a strong positive to deliver, potentially even at the upper end (of the current \$47-49m range). We increase out PT to \$4.35 and maintain the Buy rating.

## Highlights

- A solid 1H21 result** – revenue of \$24.1m (+27% YoY) was 6% better than we forecast (\$22.7m) benefitting from stronger perpetual, maintenance & support revenue, while subscription was in-line with our expectations (and grew an impressive +66% YoY). NTO’s operating EBITDA loss (ex SBP and FX) delivered at -\$3m and was c\$1m better than we expected, benefitting from the stronger revenue. NTO delivered gross free cash flow of -\$5.1m and closed 1H21 with net cash of \$38.6m (c\$33m post the \$6m to be paid for PDFpen in 2H21). NTO remains well funded to reach cash break-even.
- Key positives – strongly positioned to achieve FY revenue guidance, multiple levers to drive ARR growth into FY22 and beyond and outperformance of perpetual maintenance & support delivers a “shallower” investment phase.** 1) 1H revenue of \$24.1m represents 50% of the mid-point of FY21 guidance versus 47% in 1H20. We believe 1H outperformance puts NTO in a strong position to deliver on FY21 revenue guidance, potentially even at the upper end of the current \$47-49m range. 2) on a post result call, NTO management highlighted that incremental ARR from new customers should increase, as recent S&M investment ramps up, despite cycling maintenance transitions and that net revenue retention should improve back towards +120% as NTO benefits from a skew to enterprise, new products and its new “farmer” sales model focussed on expansion. In our view, this would be fantastic outcome and would put NTO in a select group of ASX software companies achieving this sort of existing customer growth, at its relatively high gross margin level. 3) The stronger than expected perpetual, maintenance and support revenues, are resulting in a “shallower” investment phase, and allowing for positive “cash burn” revisions. Overall, we think NTO management are doing a great job, scaling the S&M function, launching new products and pricing plans, and completing the transition of customers to subscription.
- Potential issues – while not really an issue per se, with so many positive announcements recently, this update lacked a big piece of new news to further excite.** As a reminder, this past quarter, NTO have announced: 1) the acquisition of PDFpen, adding native Mac, iPad and iPhone capability; 2) launched Nitro Sign as a stand-alone product and introduced new pricing plans across its whole platform; 3) announced an integration with Salesforce, the world’s leading CRM; and 4) largely completed the scaling of its S&M function. While all these announcements reinforce NTO’s platform strategy and highlight that it is quickly maturing into a globally relevant ASX-listed enterprise software vendor, it can be a tough act to follow, in a short space of time.

## Recommendation

We reiterate our Buy recommendation and increase our PT to \$4.35 (was \$4.20). The key driver of our PT increase is a “shallower” investment phase. Our PT is based on a 10-year discounted cash flow (DCF) analysis that assumes terminal revenue of \$200m, an Adj EBITDA margin of 30%, a terminal EV/FCF multiple of 20x and a discount rate of 8.0%. NTO continues to represent good value trading on an FY21 EV/Revenue multiple of 9.6x vs US peers DocuSign (DOCU-US) and Adobe (ADBE-US) trading on multiples of 30x and 20x respectively.

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**Nitro Software Ltd**  
Information Technology  
Software & Services  
FactSet: NTO-AU / Bloomberg: NTO AU

Key Items	Data
Recommendation	BUY
Risk	HIGH
Price (\$ps)	3.33
Target Price (\$ps)	4.35
52 Week Range (\$ps)	2.16 - 3.75
Shares on Issue (m)	214.8
Market Cap (\$m)	715.1
Enterprise Value (\$m)	678.0
TSR (%)	30.7%

Valuation NPV	Data
Beta	1.10
Cost of Equity (%)	8.0%
Cost of Debt (net) (%)	4.4%
Risk Free Rate (%)	2.3%
Terminal Growth (%)	3.0%
WACC (%)	8.0%
Valuation (\$m)	623.0
Valuation per share (cps) (AUD)	3.80

**Company Description**

Nitro Software Ltd. engages in the development and provision of document productivity and digital signature software to mid-market and enterprise customers globally. It operates under the following key brands: NitroPro and NitroSign. The company was founded in 2005 and is headquartered in San Francisco, USA.

**Financial Year End: 31 December**

Investment Summary (USD)	FY19A	FY20A	FY21E	FY22E	FY23E
EPS (Reported) (cps)	(4.9)	(3.7)	(9.6)	(9.9)	(6.1)
EPS (Underlying) (cps)	(2.3)	(3.7)	(9.5)	(9.9)	(6.1)
EPS (Underlying) Growth (%)	35.3%	(61.9%)	nm	(4.1%)	38.7%
PE (Underlying) (x)	(50.8)	(67.6)	(25.2)	(24.3)	(39.6)
EV / EBIT (x)	(247.2)	(75.2)	(26.4)	(24.4)	(40.6)
EV / EBITDA (x)	(529.9)	(79.3)	(26.9)	(24.7)	(41.7)
DPS (cps) (AUD)	0.0	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%	0%	0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Free Cash Flow Yield (%)	(1.2%)	(0.7%)	(2.0%)	(2.0%)	(0.0%)
Profit and Loss (USD) (m)	FY19A	FY20A	FY21E	FY22E	FY23E
Sales	35.7	40.2	48.8	59.9	74.5
Sales Growth (%)	10.1%	12.7%	21.3%	22.8%	24.5%
EBITDA	(0.9)	(5.9)	(18.1)	(20.1)	(11.9)
EBITDA Margin (%)	(2.5%)	(14.8%)	(37.1%)	(33.6%)	(16.0%)
Depreciation & Amortisation	(1.0)	(0.3)	(0.3)	(0.3)	(0.3)
EBIT	(1.9)	(6.3)	(18.4)	(20.4)	(12.2)
EBIT Margin (%)	(5.3%)	(15.6%)	(37.8%)	(34.0%)	(16.4%)
Net Interest	(0.4)	0.0	(0.1)	(0.1)	(0.1)
Pretax Profit	(3.3)	(7.7)	(19.9)	(21.9)	(13.8)
Tax	(0.4)	0.1	(0.1)	0.0	0.0
Tax Rate (%)	10.7%	(1.5%)	0.6%	0.0%	0.0%
Minorities	0.0	0.0	0.0	0.0	0.0
NPAT Underlying	(3.7)	(7.5)	(20.1)	(21.9)	(13.8)
Significant Items	(4.3)	0.0	(0.2)	0.0	0.0
NPAT Reported	(7.9)	(7.5)	(20.3)	(21.9)	(13.8)
Cashflow (USD) (m)	FY19A	FY20A	FY21E	FY22E	FY23E
EBIT	(1.9)	(6.3)	(18.4)	(20.4)	(12.2)
Tax Paid	(0.1)	(0.1)	(0.1)	0.0	0.0
Net Interest	(0.5)	0.0	(0.1)	(0.1)	(0.1)
Change in Working Capital	1.6	0.9	2.1	4.2	5.4
Depreciation & Amortisation	1.0	0.3	0.3	0.3	0.3
Other	(0.3)	3.5	8.3	8.3	8.3
Operating Cashflow	(0.2)	(1.6)	(7.9)	(7.7)	1.7
Capex	(0.7)	(0.2)	(0.3)	(0.3)	(0.4)
Acquisitions and Investments	0.0	0.0	(6.0)	0.0	0.0
Other	0.0	(0.2)	0.0	0.0	0.0
Investing Cashflow	(0.7)	(0.4)	(6.3)	(0.3)	(0.4)
Free Cashflow	(2.0)	(3.2)	(9.6)	(9.5)	0.0
Equity Raised / Bought Back	48.3	0.1	0.0	0.0	0.0
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Change in Debt	(4.5)	0.0	0.0	0.0	0.0
Other	(1.2)	(1.4)	(1.3)	(1.4)	(1.4)
Financing Cashflow	42.6	(1.3)	(1.3)	(1.4)	(1.4)
Net Change in Cash	41.8	(3.3)	(15.5)	(9.5)	0.0
Balance Sheet (USD) (m)	FY19A	FY20A	FY21E	FY22E	FY23E
Cash	47.0	43.7	28.3	18.8	18.8
Accounts Receivable	6.7	9.5	11.6	14.2	17.7
Other Current Assets	0.1	0.1	0.1	0.1	0.1
PPE	0.6	0.5	0.5	0.6	0.6
Goodwill & Intangibles	0.1	0.0	0.0	0.0	0.0
Total Assets	75.3	60.0	48.3	42.3	46.4
Accounts Payable	3.5	3.9	4.8	5.8	7.3
Short Term Debt	0.0	0.0	0.0	0.0	0.0
Long Term Debt	0.0	0.0	0.0	0.0	0.0
Income Taxes Payable	0.0	0.0	0.0	0.0	0.0
Other	38.5	26.7	31.4	36.9	43.9
Total Liabilities	41.9	30.7	36.2	42.7	51.2
Total Shareholder Equity	33.4	29.3	12.1	(0.4)	(4.8)
Ratios	FY19A	FY20A	FY21E	FY22E	FY23E
ROE (%)	(27.8%)	(24.1%)	(96.8%)	(371.7%)	530.1%
Gearing (%)	345.2%	302.7%	175.1%	98.1%	79.6%
Net Debt / EBITDA (x)	53.2	7.4	1.6	0.9	1.6

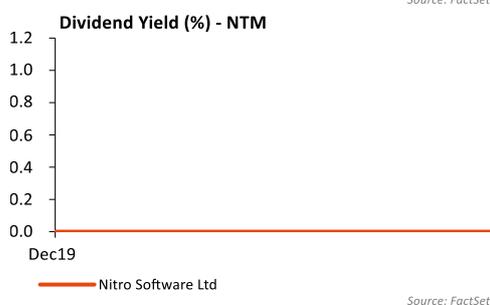


Figure 1: NTO 1H21 result vs Shaw estimates and pcp

	1H19A	2H19A	FY19A	1H20A	2H20A	FY20A	1H21A	1H21F	vs Shaw	vs PCP
	Actual	Actual	Actual	Actual	Actual	Actual	Actual	Fcast		
Subscription	5.7	7.5	13.2	9.1	12.1	21.3	15.1	15.2	-1%	65.6%
Perpetual, maintenance & support	11.0	11.5	22.5	9.9	9.0	18.9	9.0	7.5	20%	-9.4%
<b>Operating revenue</b>	<b>16.7</b>	<b>19.0</b>	<b>35.7</b>	<b>19.1</b>	<b>21.1</b>	<b>40.2</b>	<b>24.1</b>	<b>22.7</b>	<b>6%</b>	<b>27%</b>
Cost of sales	-1.9	-1.8	-3.7	-1.8	-2.0	-3.8	-2.0	-2.0	1%	13%
<b>Gross margin</b>	<b>14.8</b>	<b>17.2</b>	<b>32.0</b>	<b>17.3</b>	<b>19.1</b>	<b>36.4</b>	<b>22.1</b>	<b>20.7</b>	<b>7%</b>	<b>28%</b>
Margin %	88.7%	90.7%	89.8%	90.6%	90.6%	90.6%	91.6%	91.2%	43bps	98bps
Cash opex (expensed)	-15.9	-17.3	-33.2	-17.0	-21.8	-38.9	-25.1	-24.7	2%	48%
<b>Operating EBITDA (ex SBP, non-operat)</b>	<b>-1.1</b>	<b>0.0</b>	<b>-1.2</b>	<b>0.3</b>	<b>-2.7</b>	<b>-2.4</b>	<b>-3.0</b>	<b>-4.0</b>	<b>-25%</b>	<b>1040%</b>
Margin %	-6.8%	-0.2%	-3.3%	1.4%	-12.8%	-6.1%	-12.5%	-17.7%	520bps	-1386bps
D&A	-0.9	-1.1	-2.0	-0.9	-0.9	-1.7	-0.9	-0.8		
Share based payments	-0.3	-0.6	-0.8	-0.7	-2.2	-3.0	-4.1	-3.4		
Other non-operating	-0.1	1.3	1.1	-1.2	0.6	-0.5	-0.1	0.0		
<b>Group EBIT</b>	<b>-2.4</b>	<b>-0.5</b>	<b>-2.9</b>	<b>-2.5</b>	<b>-5.1</b>	<b>-7.7</b>	<b>-8.2</b>	<b>-8.2</b>	<b>0%</b>	<b>225%</b>
Net Interest	-0.3	-0.2	-0.4	0.0	0.0	0.0	0.0	-0.1		
PBT	-2.7	-0.6	-3.3	-2.5	-5.2	-7.7	-8.2	-8.3		
Tax	-0.1	-0.3	-0.4	0.4	-0.3	0.1	-0.1	0.8		
<b>NPAT (pre-significant items)</b>	<b>-2.8</b>	<b>-0.9</b>	<b>-3.7</b>	<b>-2.1</b>	<b>-5.5</b>	<b>-7.5</b>	<b>-8.4</b>	<b>-7.4</b>	<b>12%</b>	<b>304%</b>
Add back acquired amortisation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
<b>NPATA (pre-significant items)</b>	<b>-2.8</b>	<b>-0.9</b>	<b>-3.7</b>	<b>-2.1</b>	<b>-5.5</b>	<b>-7.5</b>	<b>-8.4</b>	<b>-7.4</b>	<b>12%</b>	<b>304%</b>
<b>Rep EBITDA (inc SBP)</b>	<b>-1.5</b>	<b>0.6</b>	<b>-0.9</b>	<b>-1.7</b>	<b>-4.3</b>	<b>-5.9</b>	<b>-7.3</b>	<b>-7.4</b>	<b>-1%</b>	<b>341%</b>
Margin %	-9.1%	3.3%	-2.5%	-8.7%	-20.3%	-14.8%	-30.2%	-32.5%	235bps	-2152bps
<b>Cashflow</b>										
EBITDA	-1.1	0.0	-1.2	0.3	-2.7	-2.4	-3.0	-4.0		
Working capital	0.1	1.5	1.6	-1.6	2.5	0.9	-1.2	-1.7		
<b>Gross operating cashflow</b>	<b>-1.1</b>	<b>1.5</b>	<b>0.4</b>	<b>-1.4</b>	<b>-0.2</b>	<b>-1.6</b>	<b>-4.2</b>	<b>-5.7</b>	<b>-25%</b>	<b>210%</b>
Cash conversion	93%	-3423%	-35%	-516%	7%	63%	140%	141%		
Capex	-0.5	-0.1	-0.7	-0.1	-0.1	-0.2	-0.2	-0.1	40%	64%
Capitalised development	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	na	na
Leases	-0.6	-0.8	-1.3	-0.8	-0.8	-1.5	-0.7	-0.8	-9%	-6%
<b>Gross free cashflow</b>	<b>-2.2</b>	<b>0.6</b>	<b>-1.6</b>	<b>-2.2</b>	<b>-1.1</b>	<b>-3.3</b>	<b>-5.1</b>	<b>-6.6</b>	<b>-23%</b>	<b>130%</b>
<b>Net debt (cash)</b>	<b>0.8</b>	<b>-47.0</b>	<b>-47.0</b>	<b>-43.9</b>	<b>-43.7</b>	<b>-43.7</b>	<b>-38.6</b>	<b>-37.2</b>		

Source: Company reports, Shaw and Partners analysis

For FY21, we forecast: 1) ARR \$41.5m vs guidance \$39-42m ex PDFpen; 2) revenue of \$48.8m vs guidance \$47-49m; and 3) an Operating EBITDA loss of -\$10m vs guidance for a loss between -\$9m and -\$11m.

### Forecast changes

Figure 2: Forecast changes

	FY21			FY22			FY23		
	Old	New	% chg	Old	New	% chg	Old	New	% chg
Revenue	48.0	48.8	+2%	60.0	59.9	-0%	74.9	74.5	-1%
Opex	-64.8	-66.9	+3%	-79.1	-80.0	+1%	-86.2	-86.4	+0%
<b>EBITDA</b>	<b>-16.8</b>	<b>-18.1</b>	<b>+8%</b>	<b>-19.1</b>	<b>-20.1</b>	<b>+5%</b>	<b>-11.3</b>	<b>-11.9</b>	<b>+6%</b>
D&A	-1.6	-1.7	+6%	-1.7	-1.7	+2%	-1.7	-1.8	+1%
EBIT	-18.4	-19.8	+8%	-20.8	-21.8	+5%	-13.0	-13.7	+5%
Net interest	-0.1	-0.1	-10%	-0.1	-0.1	-30%	-0.1	-0.1	-33%
PBT	-18.5	-19.9	+8%	-20.9	-21.9	+5%	-13.1	-13.8	+5%
<b>Norm NPATA</b>	<b>-15.6</b>	<b>-20.1</b>	<b>+28%</b>	<b>-17.1</b>	<b>-21.9</b>	<b>+28%</b>	<b>-11.4</b>	<b>-13.8</b>	<b>+21%</b>
<b>Norm EPS (diluted) (c)</b>	<b>-7.2</b>	<b>-9.5</b>	<b>+33%</b>	<b>-7.6</b>	<b>-9.9</b>	<b>+30%</b>	<b>-4.9</b>	<b>-6.1</b>	<b>+24%</b>
DPS (c)	0.0	0.0	n.a	0.0	0.0	n.a	0.0	0.0	n.a
Gross operating cashflow	-7.8	-7.7	-2%	-8.4	-7.7	-9%	0.2	1.8	+647%
Capex	-0.2	-0.3	+18%	-0.3	-0.3	+16%	-0.3	-0.4	+15%
Capitalised costs	0.0	0.0	n.a	0.0	0.0	n.a	0.0	0.0	n.a
Leases	-1.6	-1.4	-9%	-1.6	-1.5	-9%	-1.7	-1.5	-12%
<b>Gross free cashflow</b>	<b>-9.7</b>	<b>-9.4</b>	<b>-2%</b>	<b>-10.3</b>	<b>-9.5</b>	<b>-8%</b>	<b>-1.7</b>	<b>0.0</b>	<b>-98%</b>
<b>Total opex</b>	<b>-66.6</b>	<b>-68.6</b>	<b>+3%</b>	<b>-81.1</b>	<b>-81.8</b>	<b>+1%</b>	<b>-88.2</b>	<b>-88.3</b>	<b>+0%</b>
<b>Net debt</b>	<b>-28.1</b>	<b>-28.3</b>	<b>+1%</b>	<b>-17.9</b>	<b>-18.8</b>	<b>+6%</b>	<b>-16.1</b>	<b>-18.8</b>	<b>+17%</b>

Source: Shaw and Partners analysis

## Key risks

### Failure to deliver on ARR growth expectations

Investor expectations regarding NTO's ability to deliver superior long run growth have been rising over recent months. While the growth story is compelling, it is not risk free. New products like Nitro Sign, may fail to achieve the take up or usage expected. Competing vendors like DocuSign have strong network effects including incumbency, brand and integrations. In addition, new customer adds may just prove harder, despite efforts to scale the team, which impact efficiency. These potential outcomes, or any others that suggest ARR growth expectations may not be achieved, would likely weigh on the share price.

### Failure to achieve expected long-term margins

NTO adopts a discount pricing strategy vs its market leading competitors, with the goal of increasing customer value over-time via upsell and the cross-sell of additional products. If this can't be achieved then it puts at risk the potential long term margins achievable for the business from its signed customer base.

### Competitive response from dominant category vendors

NTO competes in categories that already have a dominant leader, being Adobe in PDF productivity and DocuSign in eSigning. If those dominant leaders perceive NTO as an increasing threat, then they could aggressively match NTO's pricing, forcing it into a price war and/or retaliate in other ways, like specifically targeting key accounts or staff etc.

### Broader 'Tech' rotation risks may impact sentiment

ASX software stocks have underperformed the broader market CYTD, given historically high valuations and rotation into cyclical/value stocks, as investors have bet on an improving global outlook post COVID vaccines and rising bond yields etc. While software's fundamentals have rarely been better, and in many cases software stocks will benefit from a GDP recovery as well, this may continue to weigh on sentiment.

## Rating Classification

<b>Buy</b>	Expected to outperform the overall market
<b>Hold</b>	Expected to perform in line with the overall market
<b>Sell</b>	Expected to underperform the overall market
<b>Not Rated</b>	Shaw has issued a factual note on the company but does not have a recommendation

## Risk Rating

<b>High</b>	Higher risk than the overall market – investors should be aware this stock may be speculative
<b>Medium</b>	Risk broadly in line with the overall market
<b>Low</b>	Lower risk than the overall market

**RISK STATEMENT:** Where a company is designated as ‘High’ risk, this means that the analyst has determined that the risk profile for this company is significantly higher than for the market as a whole, and so may not suit all investors. Clients should make an assessment as to whether this stock and its potential price volatility is compatible with their financial objectives. Clients should discuss this stock with their Shaw adviser before making any investment decision.

### Distribution of Investment Ratings

Rating	Count	Recommendation Universe
Buy	73	81%
Hold	15	17%
Sell	2	2%

### History of Investment Rating and Target Price - Nitro Software Ltd

Date	Closing Price (\$)	Target Price (\$)	Rating
24-Aug-21	3.33	4.35	Buy
28-Jul-21	3.27	4.20	Buy
21-Jul-21	3.22	3.90	Buy
9-Jul-21	3.24	3.90	Buy
28-Jun-21	3.25	3.90	Buy
29-Apr-21	3.24	3.69	Buy
24-Feb-21	2.64	3.58	Buy
27-Jan-21	3.28	3.45	Buy
18-Nov-20	2.89	3.55	Buy

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