



Computer Services (CSVI)

Updated January 10th, 2019 by Aristofanis Papadatos

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|----------|
| Current Price: | \$45 | 5 Year CAGR Estimate: | 2.0% | Market Cap: | \$1.2B |
| Fair Value Price: | \$32 | 5 Year Growth Estimate: | 7.0% | Ex-Dividend Date: | 11/29/19 |
| % Fair Value: | 141% | 5 Year Valuation Multiple Estimate: | -6.6% | Dividend Payment Date: | 12/26/19 |
| Dividend Yield: | 1.9% | 5 Year Price Target | \$45 | Years Of Dividend Growth: | 48 |
| Dividend Risk Score: | A | Retirement Suitability Score: | B | Last Dividend Increase: | 16.7% |

Overview & Current Events

Computer Services provides regional banks with a wide range of services, such as core processing, digital banking, payments processing, and regulatory compliance solutions. It has a market cap of \$1.2 billion.

In early January, Computer Services reported (1/9/2020) financial results for the third quarter of fiscal 2020. The company grew its revenue by 6.6% thanks to higher sales of core processing, digital banking, regulatory compliance services and managed services. Earnings-per-share rose only 5%, from \$0.41 to \$0.43, as early contract termination fees totaled only \$1.0 million, much lower than the \$3.0 million recorded in last year's quarter. Nevertheless, as early contract termination fees are highly unpredictable and beyond the control of the company, the report should not cause any concerns. Computer Services maintained positive business momentum, with growth prospects remaining strong. The company posted record revenue in the quarter and management expects the strong business momentum to remain in place for the foreseeable future.

Growth on a Per-Share Basis

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$0.71 | \$0.80 | \$0.86 | \$0.88 | \$0.93 | \$0.98 | \$1.03 | \$1.10 | \$1.39 | \$1.61 | \$1.90 | \$2.66 |
| DPS | \$0.18 | \$0.20 | \$0.23 | \$0.26 | \$0.30 | \$0.38 | \$0.47 | \$0.53 | \$0.67 | \$0.72 | \$0.84 | \$1.12 |
| Shares¹ | 30.2 | 29.8 | 29.6 | 29.4 | 28.8 | 28.4 | 28.2 | 28.0 | 28.0 | 27.8 | 27.6 | 26.5 |

Computer Services has grown its sales, earnings, and its dividend for 19, 22 and 48 consecutive years, respectively. Thanks to strong business momentum, management expects to post new all-time highs in the above metrics this year.

Computer Services has grown its earnings-per-share at a rate between 5% and 7% in each of the last five years, excluding the last two years, which benefited from a large decrease in the tax rate. Thanks to sustained momentum in the core business, we continue to expect 7.0% annual earnings-per-share growth for the next five years.

Valuation Analysis

| Year | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | Now | 2025 |
|------------------|------|------|------|------|------|------|------|------|------|------|-------------|-------------|
| Avg. P/E | 9.9 | 12.6 | 16.6 | 19.1 | 16.9 | 18.0 | 20.6 | 17.4 | 20.4 | 16.7 | 23.7 | 16.8 |
| Avg. Yld. | 2.6% | 2.0% | 1.5% | 1.4% | 1.8% | 1.8% | 1.9% | 2.6% | 2.4% | 2.9 | 1.9% | 2.5% |

In the last 12 months, Computer Services has dramatically outperformed the market, with a 79% rally (vs. 26% for the S&P 500). As a result, the stock is currently trading at a price-to-earnings ratio of 23.7, which is much higher than its 10-year average of 16.8. If the stock reverts to its average valuation level in the next five years, it will incur a -6.6% annualized drag due to contraction of its price-to-earnings ratio.

¹ Share count is in millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 |
|---------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|--------------|--------------|
| Payout | 25.2% | 25.5% | 27.3% | 30.1% | 32.4% | 38.6% | 45.4% | 48.0% | 50.2% | 44.6% | 44.2% | 42.1% |

The impressive growth record of Computer Services is a testament to the strength of its business model and the existence of a significant competitive advantage. The company signs multi-year contracts with its customers and offers them a wide range of services. It is thus very costly and inefficient for these customers to stop working with the company, particularly given that they pay appreciable early termination fees. As a result, Computer Services enjoys high renewal rates. In fact, when it loses a customer, the most frequent reason is that the bank has been acquired by another bank that is not a customer of Computer Services.

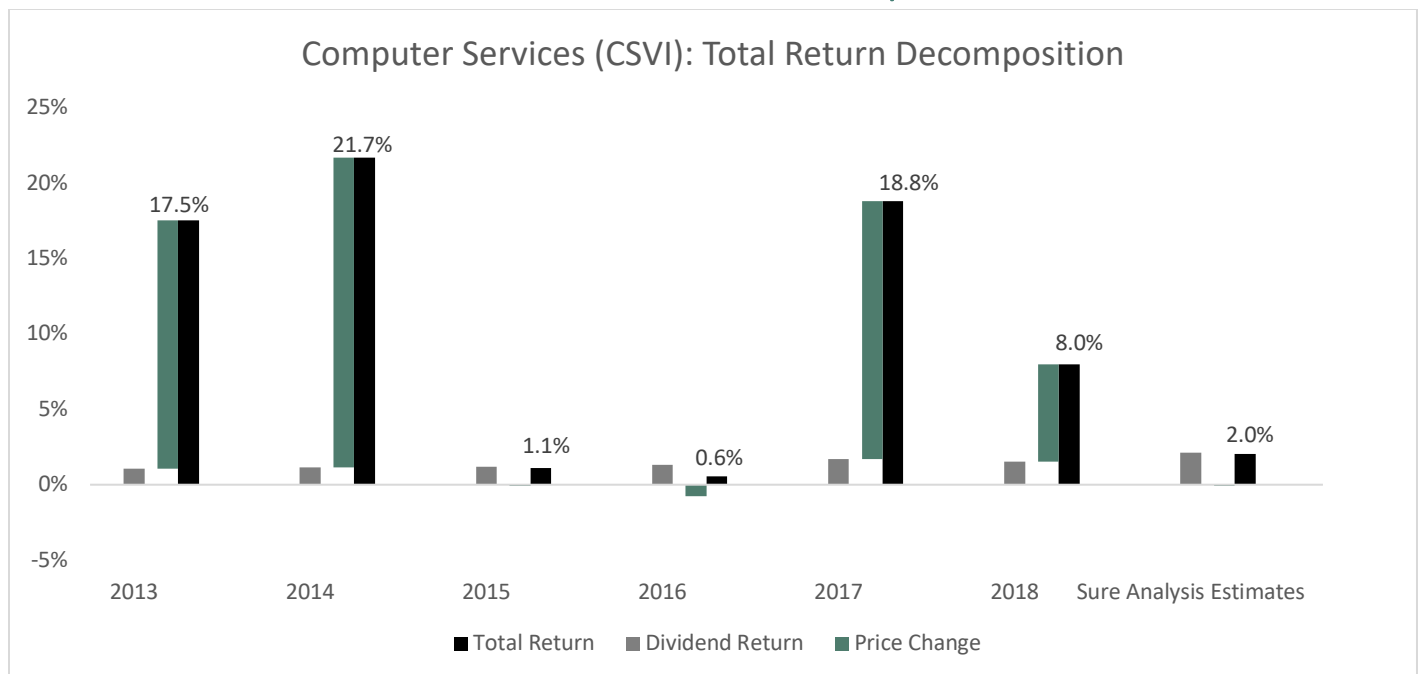
Computer Services does not carry any debt. Instead it has a net cash position of \$5 million. Thanks to its strong balance sheet and its healthy payout ratio, the company can easily keep growing its dividend at a meaningful pace.

Finally, thanks to its long-term contracts and the recurring nature of its revenues, Computer Services is resilient during recessions. In the Great Recession, it grew its earnings-per-share by 17% in 2008 and another 19% in 2009. On the other hand, its price-to-earnings ratio could steeply decline in a recession and the stock price would plunge, just like it did in the Great Recession, when it lost half of its market cap in a year. Nevertheless, those who can focus on the underlying performance and ignore the stock price gyrations could see the stock rebound after an economic downturn.

Final Thoughts & Recommendation

Since it bottomed at the end of 2018, Computer Services has enjoyed an impressive 88% rally, primarily thanks to accelerated earnings growth. While the company has an exceptional growth record and continues to grow without any signs of fatigue, the stock has become richly valued. As a result, it may offer just a 2.0% average annual return over the next five years. While the strong stock price momentum could remain in place in the short run, the stock will have significant downside risk whenever it faces an unexpected headwind. We thus rate it as a sell, despite its high quality.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|------------------|------|------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | N/A | N/A | 178.2 | 198.3 | 212.9 | 221.4 | 224.7 | 234.9 | 249.6 | 266.5 |
| SG&A Exp. | N/A | N/A | 137.8 | 156.4 | 168.8 | 175.6 | N/A | N/A | N/A | N/A |
| D&A Exp. | N/A | N/A | 13.5 | 14.9 | 15.5 | 14.6 | 15.0 | 15.5 | 16.3 | 17.7 |
| Operating Profit | N/A | N/A | 40.4 | 41.9 | 44.1 | 45.8 | 48.1 | 50.0 | 47.7 | 53.2 |
| Operating Margin | N/A | N/A | 22.7% | 21.1% | 20.7% | 20.7% | 21.4% | 21.3% | 19.1% | 20.0% |
| Net Profit | N/A | N/A | 25.5 | 25.8 | 26.7 | 27.8 | 29.1 | 30.9 | 38.8 | 45.0 |
| Net Margin | N/A | N/A | 14.3% | 13.0% | 12.5% | 12.6% | 13.0% | 13.2% | 15.6% | 16.9% |
| Free Cash Flow | N/A | N/A | 35.4 | 20.0 | 23.0 | 26.8 | 25.1 | 35.5 | 25.9 | 37.2 |
| Income Tax | N/A | N/A | 14.8 | 16.0 | 17.4 | 18.0 | 19.0 | 19.2 | 9.0 | 12.2 |

Balance Sheet Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|----------------------|------|------|-------|-------|-------|-------|-------|-------|-------|-------|
| Total Assets | N/A | N/A | 165.0 | 162.0 | 174.9 | 189.2 | 203.2 | 225.2 | 247.0 | 296.5 |
| Cash & Equivalents | N/A | N/A | 8.5 | 0.5 | 1.1 | 11.8 | 17.4 | 34.6 | 40.7 | 56.6 |
| Accounts Receivable | N/A | N/A | 21.3 | 22.0 | 26.0 | 25.7 | 28.0 | 28.2 | 30.5 | 38.7 |
| Goodwill & Int. Ass. | N/A | N/A | 85.8 | 88.4 | 86.3 | 85.0 | 88.2 | 86.0 | 88.6 | 84.4 |
| Total Liabilities | N/A | N/A | 39.1 | 36.6 | 43.6 | 44.8 | 47.2 | 55.2 | 60.5 | 77.7 |
| Accounts Payable | N/A | N/A | N/A | N/A | N/A | N/A | 7.3 | 8.1 | 7.7 | 8.3 |
| Long-Term Debt | N/A | N/A | 0.2 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Shareholder's Equity | N/A | N/A | 125.8 | 125.4 | 131.3 | 144.4 | 156.0 | 170.0 | 186.5 | 218.8 |
| D/E Ratio | N/A | N/A | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |

Profitability & Per Share Metrics

| Year | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|------------------|------|------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return on Assets | N/A | N/A | 16.9% | 15.8% | 15.8% | 15.3% | 14.9% | 14.4% | 16.4% | 16.5% |
| Return on Equity | N/A | N/A | 21.9% | 20.6% | 20.8% | 20.2% | 19.4% | 19.0% | 21.5% | 22.2% |
| ROIC | N/A | N/A | 21.6% | 20.5% | 20.8% | 20.2% | 19.4% | 19.0% | 21.5% | 22.2% |
| Shares Out. | 30.2 | 29.8 | 29.6 | 29.4 | 28.8 | 28.4 | 28.2 | 28.0 | 28.0 | 27.8 |
| Revenue/Share | 5.11 | 5.54 | 6.06 | 6.78 | 7.37 | 7.82 | 7.97 | 8.39 | 8.94 | 9.58 |
| FCF/Share | 0.83 | 0.73 | 1.20 | 0.69 | 0.80 | 0.94 | 0.89 | 1.27 | 0.93 | 1.34 |

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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