

Pivot Technology Solutions Inc.

Smart Edge Sale Crystallizes Value Creation with Intel Partnership
Affirming Longer-Term Value Creation Plan; BUY Rating Reiterated.

PTG-TSX: C\$1.43
Buy
↑ C\$3.30 (prev. C\$2.75) Target

Event: Pivot announced the sale of Smart Edge. All figures are in US\$ unless otherwise noted.

Smart Edge Sale: PTG announced the sale of Smart Edge to Intel (INTC-US, NR) in a \$27M transaction that is expected to close in Q419. In connection with the sale, Pivot and Intel have entered into a three-year preferred channel partner agreement which designates Pivot as a non-exclusive preferred systems integrator and channel partner for Smart Edge based solutions. Under this agreement, Pivot will market Smart Edge solutions and provide customers edge services including: deployment, system integration, monitoring and support services. Approximately 25 employees will join Intel’s Network and Custom Logic Group (NCLG) at close, which is expected in the coming weeks. The expansion of computing in the network and at the edge is an important growth opportunity for Intel – an estimated \$65B silicon addressable market by 2023. Edge computing is an opportunity that is accelerating with the rollout of 5G networks.

Quick Take: We believe this is a great approach for Pivot. Intel is acquiring the Smart Edge software and the developers and the cost to further develop the solution with the software now carrying the Intel brand which helps with adoption. However, Pivot can still resell the software along with design, integrate, support, and manage the software solutions; Pivot’s core competencies. This lowers PTG’s cost basis going forward as well – for context in 2018, Pivot’s net-spend was \$5.1M on Smart Edge. We believe the sale and partnership announcement is value-creative and allows for flexibility in strategic alternatives for the use of proceeds, which we believe can include a combination of debt reduction, common dividend increase, special dividend, and/or a niche services acquisition. For strictly contextual purposes, the \$5.1M net-spend in 2018 on Smart-Edge is more than enough to double 2018’s common dividend spend of \$4.8M. We look for a material one-time EPS gain in Q419 results with an acceleration in services growth as a result of the preferred partnership in 2020 and beyond. We leave our revenue estimates unchanged for now with a slight reduction in SG&A as a result of the lessened expenses and look to fine-tune our 2020+ estimates and valuation after its Q319 earnings call in November.

Leadership Position in Edge Computing: A highlight from the recent AGM was the vision CEO Kevin Shank shared of Pivot becoming the “Number 1 Edge Services Provider in North America”. According to a survey conducted by ZDNet, 75.9% of businesses noted that Edge Computing is Important, Very Important, or Critically Important to improving business processes and productivity. Cisco estimates that there will be 10B mobile connected devices by 2019 and 30B IoT devices connected to internet by 2020. The proliferation of connected devices at the network edge disrupts traditional WAN services and provides a very compelling case for Pivot to have a fortitude in Edge deployed and managed services, complementing its leading position as an Edge software developer in its Smart Edge subsidiary. We look for more on this new service area of Pivot’s and Intel partnership in due course. See our full AGM note [here](#).

Projected Total Return: 142%

Market Data (US\$ Unless Otherwise Noted)

Market Capitalization	43
Net Debt	96
Enterprise Value	139
Basic Shares O/S	39.6
Avg. Daily Volume (M)	0.049
52 Week Range (C\$)	\$1.75 / \$0.83
Dividend Yield	11.2%

Management

CEO	Kevin A. Shank
CFO	David A. Toews, CPA

Top Institutional Ownership

Canoe Financial LP	% Held	2.7%
Dimensional Fund Advisors LP		0.2%

Total Insider Ownership

5.1%

Revisions

	New	Old
2019 Revenue	1,268	1,268
2019 Adj. EBITDA	26	26
2019 EPS	0.34	(0.02)

Financial Metrics (US\$M)

FYE 31-Dec	2018	2019E	2020E
Total Revenue	1,374	1,268	1,307
Adjusted EBITDA	16	26	32
Adjusted EBITDA (%)	1.1%	2.0%	2.4%
Fully Diluted IFRS EPS	(0.11)	0.34	0.23

Valuation Data

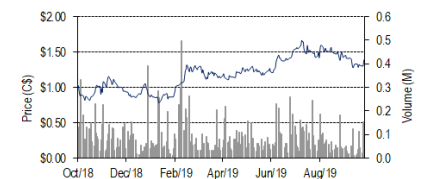
		1.43	3.30
DCF - Current/Target			
EV/Rev	0.10	0.11	0.11
EV/EBITDA	8.9	5.4	4.4
P/E	NM	NM	4.7

Quarterly Data (US\$M)

		Q1	Q2	Q3	Q4
Revenue	2018	369	381	321	302
	2019	296	346	310	317
Adj. EBITDA	2018	1.5	5.1	4.2	4.8
	2019	3.3	9.7	6.2	6.5
EPS	2018	(0.06)	0.01	(0.07)	0.01
	2019	(0.09)	0.04	0.00	0.39

Company Description

Pivot Technology Solutions, Inc. provides information technology services. It designs, sells, and supports information technology (IT) solutions which include hardware, maintenance, and support. It also offers data centre, management, infrastructure management, systems architecture, technical services, and procurement/integration services.



Source: Consensus Data – FactSet,
Historicals – Company Filings,
Forecasts/Estimates – Echelon Wealth
Partners

Impact on Cash Flow: With the announcement today, Pivot realises the net proceeds of \$27M in cash (or C\$0.90/sh) along with annual cost savings from foregoing the \$5M+ net-spend on Smart Edge. As illustrated in Exhibit 4, its current dividend continues to appear secure and payout ratios furthered benefitted from today's news. Our 2019E/2020E payout ratio moves to 19%/24% from 43%/27% prior, respectively.

Cost Reductions: PTG continues to make rapid progress on its cost saving initiatives as part of its transformation, having eliminated over \$8M in annual cost from the business as of Q219 against its initial target of \$5M. We are inclined to believe there is room to cut additional cost from the business. The impact of the cost reduction program on the overall business cannot be understated given the recent weakness in sales to major customers in right sizing Pivot for its current business climate and focusing on profitability. Despite lower revenue numbers in Q318 to-date, gross profit dollars have been relatively consistent due to the offsetting benefits to gross margin.

Majors & Services/Solutions: It is without a doubt that revenue from PTG's major customers has been on a decline since Q318 – majors in Q219 represented 23.0% of revenue compared to 38.0% in Q218, which led to a gross margin of 13.0% vs. 10.6% y/y. While revenue from majors has declined for various reasons beyond control, Pivot has not lost them as customers. Pivot provided services declined 22% y/y in Q219 and attributable to certain workforce services contracts winding down in 2019 as well as a \$3.3M one-time services contract in Q218. The Company has noted its services pipeline has been growing over the past several quarters and will be reflected in H219 results with the profitability of a services dollar improving. We believe the Intel preferred partnership should assist in higher margin revenue growth in 2020 and beyond.

Summary: Pivot continues to deliver robust Adj. EBITDA & cash-flow at a more value-add revenue base with a focus on higher profitability of each revenue dollar. The reductions in operating expenses are impressive, evident and will become ever more obvious if and when major spending returns to levels witnessed in prior years. We believe much of the core legacy/integration issues at Pivot were addressed in 2018 and the Company is in a much better position today to focus on shareholder value creation as evidenced by today's news. We note cash flow and gross profit remain healthy despite fluctuations in quarterly revenue which have become less volatile in the past few quarters. The developments at Smart Edge are material validators and confirmation of value additive, disruptive technology and Pivot now benefits from a preferred partnership agreement with its sale announcement to Intel. The recent credit facility renewal and extension at better terms adds a de-risking element to PTG's balance sheet and should also be viewed as a positive. Our DCF-based PT includes a 20% discount rate and 4.5x terminal multiple. We look for upward mobility in our terminal multiple and consequentially PT with evidence of a growing, higher margin, services moat. **We maintain our BUY rating and raise our 12-month DCF based price target to C\$3.30 from C\$2.75.**

Smart Edge Sale & Intel Partnership

PTG announced the sale of Smart Edge to Intel (INTC-US, NR) in a \$27M transaction that is expected to close in Q419. In connection with the sale, Pivot and Intel have entered into a three-year preferred channel partner agreement which designates Pivot as a non-exclusive preferred systems integrator and channel partner for Smart Edge based solutions. Under this agreement, Pivot will market Smart Edge solutions and provide customers edge services including: deployment, system integration, monitoring and support services. Approximately 25 employees will join Intel's Network and Custom Logic Group (NCLG) at close, which is expected in the coming weeks. The expansion of computing in the network and at the edge is an important growth opportunity for Intel – an estimated \$65B silicon addressable market by 2023. Edge computing is an opportunity that is accelerating with the rollout of 5G networks.

We look for additional commentary at the time of its Q319 earnings with our estimates shown below.

Exhibit 1 – Summary of Results

Forecasts	Q119	Q219	Q319	Q319E	% Diff.	Q419E	Q120E
Revenue (\$M)	\$296	\$346		\$310		\$317	\$311
Adj. EBITDA (\$M)	\$3.3	\$9.7		\$6.2		\$6.5	\$4.8
Basic EPS	(\$0.09)	\$0.04		\$0.00		\$0.39	(\$0.02)
F/D EPS	(\$0.09)	\$0.04		\$0.00		\$0.39	(\$0.02)

Source: Historicals – Company Filings, Forecasts/Estimates – Echelon Wealth Partners

Despite the swings in major customer spending patterns and Smart Edge investments, PTG is still able to generate relatively similar gross profit as in prior quarters where revenue has fluctuated materially. The cost optimization initiatives at PTG that has already generated over \$8M of annual cost savings cannot be understated and will directly benefit Adj. EBITDA and consequentially valuation. The announcement of the sale of Smart Edge to Intel further benefits margins as higher margin edge services revenue are generated and the reduced overall opex as a consequence from selling Smart Edge (\$5.2M net-spend in 2018).

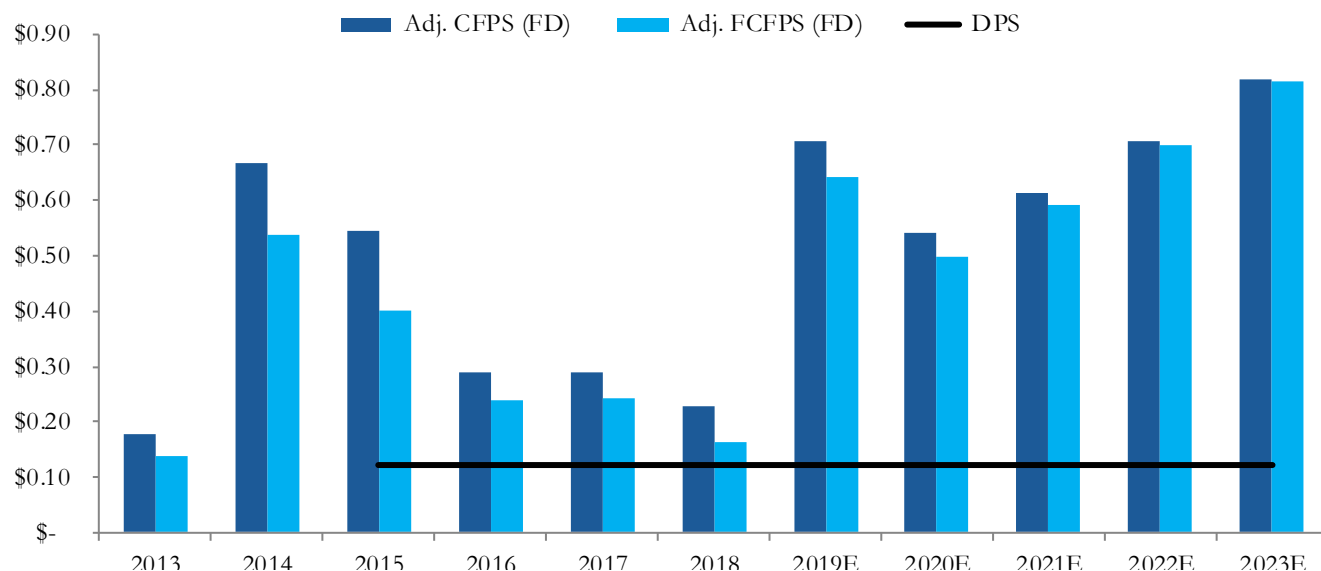
Exhibit 2 – Cost Optimization Efforts Directly Benefiting Margins...Inclusive of Smart Edge Spend!

	Total Revenue	Gross Profit	SG&A	Adj. EBITDA
Q118	\$369M	\$39M	\$38M	\$1.5M (0.4% margin)
Q218	\$381M	\$41M	\$36M	\$5.1M (1.3% margin)
Q318	\$321M	\$41M	\$37M	\$4.2M (1.3% margin)
Q418	\$302M	\$43M	\$38M	\$4.8M (1.6% margin)
Q119	\$296M	\$37M	\$33M	\$3.3M (1.1% margin)
Q219	\$346M	\$45M	\$35M	\$9.7M (2.8% margin)!!

Source: Historicals – Company Filings

PTG continues to have a robust cash flow profile with ability to continue to pay its quarterly dividend of C\$0.04, pay down debt, and make strategic acquisitions. Its \$225M credit facility (with \$75M accordion) is used to finance non-cash working capital.

Exhibit 3 – Adj. Cash Flow, Adj. Free Cash Flow & Dividends per Share



Source: Historicals – Company Filings, Forecasts/Estimates – Echelon Wealth Partners

Taking capital expenditures and our \$25.7M Adj. EBITDA expectation for 2019, we are modeling a 2019 distributable payout ratio of 19%. We expect a steady return to normalisation in 2019 and beyond given the aforementioned efforts/reasons. Our payout ratios are inclusive of the Smart-Edge sale proceeds.

Exhibit 4 – Distributable Payout Ratio*

2016	48%
2017	49%
2018	73%
2019E	19% vs. 43% prior
2020E	24% vs. 27% prior

*Calculated as: Dividends Paid / ((CFOPS before changes in non-cash working capital) - Capital Expenditures)

Source: Historicals – Company Filings, Forecasts/Estimates – Echelon Wealth Partners

Valuation

On 2019E, PTG is currently trading at an EV/Sales and EV/EBITDA of 0.13x and 6.4x, respectively, versus its comparables average of 0.60x, and 10.0x, respectively.

Exhibit 5 – Global Value Added Resellers (VARs) Comparables

GLOBAL VAR / IT SERVICES COMPS

	Ticker	Price	Mkt Cap (Local\$M)	LTM Rev (US\$M)	LTM GM %	EV/Sales			EV/EBITDA			P/E		
						2018	2019	2020	2018	2019	2020	2018	2019	2020
Pivot Technology Solutions, Inc.	PTG-CA	1.50	59	1,265	12.0	0.12	0.13	0.13	10.5	6.4	5.7	NM	NM	6.3
Tech Data Corporation	TECD	109.78	3,908	37,303	6.1	0.13	0.13	0.12	6.2	5.8	5.5	9.6	8.7	8.4
SYNNEX Corporation	SNX	113.64	5,804	22,798	12.0	0.44	0.38	0.38	10.7	7.0	6.6	10.4	9.0	8.6
Insight Enterprises, Inc.	NSIT	56.52	2,023	7,018	14.0	0.32	0.30	0.27	7.9	7.3	6.4	12.2	11.3	10.3
ScanSource, Inc.	SCSC	29.68	749	3,873	10.8	0.29	0.28	0.29	7.6	7.4	8.0	9.5	8.8	9.9
Datatec Limited	DTC-JSE	31.97	6,778	6,083	15.0	NM	NM	NM	NM	NM	NM	NM	NM	NM
Softcat Plc	SCT-GB	9.60	1,902	1,313	18.7	1.71	1.78	1.62	25.9	21.9	20.8	33.3	28.4	27.0
CDW Corp.	CDW	123.51	17,874	17,036	16.7	1.35	1.24	1.18	16.9	15.6	14.7	23.9	21.0	19.3
PC Connection, Inc.	CNXN	38.72	1,019	2,742	14.9	0.35	0.34	0.33	9.4	8.4	8.1	16.3	14.2	13.5
ePlus inc.	PLUS	75.78	1,023	1,387	23.0	0.77	0.72	0.70	10.5	9.9	9.2	14.8	14.6	13.6
AVERAGES:					14.6	0.64	0.60	0.57	11.8	10.0	9.4	16.3	15.5	12.9

Source: Consensus Data – FactSet

Canadian Technology Dividend Stocks

At the current share price, the dividend results in a yield of ~11.1%. If the yield were to move to the average yield shown below (~2.9%), the shares would be trading at the ~C\$5.50 level.

Exhibit 6 – Canadian Technology Dividend Yields

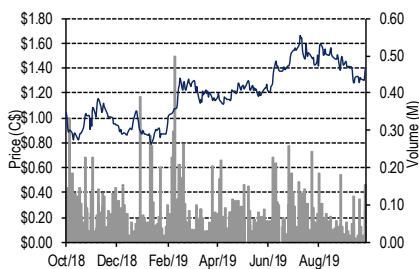
CANADA TECH DIV YIELDS

	Ticker	Price	Mkt Cap (Local)	LTM Rev (US\$)	EV/Sales			EV/EBITDA			P/E			Div Yield
					2018	2019	2020	2018	2019	2020	2018	2019	2020	
Constellation Software Inc.	CSU-CA	1351.00	21,642	3,256	7.1	6.3	5.4	27.9	23.6	20.0	36.0	35.0	28.0	0.4%
Open Text Corporation	OTEX-CA	53.69	10,958	2,870	4.6	4.4	4.2	12.7	11.5	11.0	16.2	14.7	14.1	1.7%
Enghouse Systems Limited	ENGH-CA	36.42	1,506	274	5.4	4.8	4.1	17.6	16.6	14.2	34.5	31.4	26.7	1.2%
Altus Group Limited	AIF-CA	39.90	1,210	403	3.5	3.1	2.8	24.8	20.5	17.7	38.0	28.7	25.4	1.5%
Evertz Technologies Limited	ET-CA	16.34	946	335	2.7	2.6	2.4	10.5	10.2	9.3	16.6	15.7	14.3	4.5%
Pollard Banknote Limited	PBL-CA	19.96	387	271	2.0	1.6	1.5	13.4	10.7	9.6	31.8	20.2	18.7	0.8%
Computer Modelling Group Ltd.	CMG-CA	6.36	386	58	6.7	6.7	6.4	15.9	15.7	14.5	22.7	25.6	23.2	6.4%
Absolute Software Corporation	ABT-CA	7.57	239	99	2.2	2.1	2.0	22.8	10.7	10.1	NM	31.6	28.2	4.2%
Calian Group Ltd.	CGY-CA	34.99	209	250	0.9	0.8	0.7	10.9	9.9	8.3	16.9	16.9	14.7	3.3%
Sylogist Ltd.	SYZ-CA	10.40	186	29	NM	NM	NM	NM	NM	NM	NM	NM	NM	3.8%
TECSYS Inc.	TCS-CA	16.16	160	63	2.9	2.3	2.1	88.4	30.7	20.6	NM	262.1	48.5	1.4%
Vecima Networks Inc.	VCM-CA	9.26	157	64	2.1	1.9	1.7	11.4	20.1	23.5	54.5	NM	NM	2.4%
Quarterhill Inc	QTRH-CA	1.62	145	128	0.8	0.5	0.6	NM	NM	3.5	NM	NM	13.6	3.1%
Mediagrif Interactive Technologies Inc.	MDF-CA	6.62	74	62	1.2	1.4	NM	4.9	6.4	NM	10.3	15.0	NM	6.0%
C-COM Satellite Systems, Inc.	CMI-CA	1.89	54	11	NM	NM	NM	NM	NM	NM	NM	NM	NM	2.6%
Pivot Technology Solutions, Inc.	PTG-CA	1.44	43	1,265	0.1	0.1	0.1	10.5	6.4	5.7	NM	NM	6.0	11.1%
Averages:					3.0	2.8	2.6	20.9	14.8	12.9	27.8	45.2	21.8	3.4%
													Avg (Excl. PTG):	2.9%

Source: Consensus Data – FactSet, Echelon Wealth Partners estimates, note that TCS is covered by Amr Ezzat.

Pivot Technology Solutions Inc. – Tear Sheet

(PTG-TSX, BUY, C\$3.30 PT)



Company Description

Pivot Technology Solutions, Inc. provides information technology services. It designs, sells, and supports information technology (IT) solutions which include hardware, maintenance, and support. It also offers data centre, management, infrastructure management, systems architecture, technical services, and procurement/integration services.

Consensus	Current	Return
Rating:	Buy	
Target:	\$ 3.30	131%
Median:	\$ 2.73	91%
High:	\$ 2.73	91%
Low:	\$ 2.73	91%

Consensus	
Buy	1
Hold	-
Sell	-
# of Ratings	1

Enterprise Value to EBITDA

11-Oct-2016 to 11-Oct-2019 (Daily)



Source: FactSet Fundamentals

Enterprise Value to Sales

11-Oct-2016 to 11-Oct-2019 (Daily)



Source: FactSet Fundamentals

Financial Summary/Key Metrics	2017	2018	Q119	Q219	Q319E	Q419E	2019E	2020E	2021E	2022E
Product Sales	1,356	1,216	261	306	271	273	1,111	1,141	1,164	1,187
Service Revenues	165	158	34	40	39	44	157	166	176	187
Total Revenue	1,521	1,374	296	346	310	317	1,268	1,307	1,340	1,374
Growth y/y		-10%	-20%	-9%	-4%	5%	-8%	3%	3%	3%
Gross Margin	11.1%	11.9%	12.4%	13.0%	12.7%	12.8%	12.7%	12.8%	12.9%	13.0%
Adjusted EBITDA	24.1	15.5	3.3	9.7	6.2	6.5	25.7	31.7	37.2	42.9
Growth y/y		-36%	123%	90%	49%	36%	66%	23%	17%	15%
Fully Diluted IFRS EPS	(0.14)	(0.11)	(0.09)	0.04	0.00	0.39	0.34	0.23	0.46	0.63
Growth y/y		-22%	56%	687%	-102%	3146%	-400%	-33%	102%	37%
Adj. FCFPS (FD)	0.24	0.16					0.64	0.50	0.59	0.70
Net Debt	157	104	145	109	134	96	96	82	64	42
CAPEX	2	3	1	1	0	0	3	2	1	0
Major Customers	39%	35%	10%	23%						

Top Inst. Ownership	% Held
Canoe Financial LP	2.7%
Dimensional Fund Advisor	0.2%

Balance Sheet	2017	2018	Q119	Q219	Q319E	Q419E	2019E	2020E	2021E	2022E
Cash & Equivalents	5	15	5	15	10	27	27	37	51	69
Accounts receivable	293	230	259	268	272	277	277	285	292	299
Inventories	95	54	47	48	43	44	44	45	46	47
Total Current Assets	419	325	339	359	332	376	376	394	417	444
Growth y/y		-22%	-6%	-11%	5%	16%	16%	5%	6%	6%
Total Assets	530	421	453	472	442	462	462	469	486	510
Deferred revenue & customer depos	34	28	29	30	31	31	31	32	33	34
Accounts payable & accrued liability	301	254	244	287	259	264	264	270	277	284
Revolving credit facility	137	100	132	102	101	100	100	96	92	89
Total Current Liabilities	494	401	422	440	411	416	416	420	423	427
Total Liabilities	512	414	451	470	441	446	446	450	453	457
Total Liabilities & Shareholders'	530	421	453	472	442	462	462	469	486	510

Key Statistics	Value
52 Wk High	1.75
52 Wk Low	0.83
YTD Chg.	43%
1 Yr. Chg.	29%
Beta	0.85
Market Cap	57
EV	215
Shares Outstanding	40
LTM Dividend	\$ 0.16
Dividend Yield	11.2%

Valuation	2018	2019E
EV/Rev	0.12	0.13
EV/EBITDA	10.5	6.3
P/E	(9.6)	3.2

Comparables Multiples Analysis	Price	Target	Div Yield	Return			YTD	1 Year	Rev (US\$M)		EBITDA (US\$M)		EPS (US\$)	
				1 Week	1 Month	3 Month			2018	2019	2018	2019	2018	2019
PTG-CA	1.43	3.30	11.2%	9%	-4%	-5%	43%	29%	1,374	1,268	16	26	(0.12)	(0.02)
TECD	109.49		0.0%	5%	4%	9%	34%	57%	37,239	37,382	766	819	11.38	12.56
CDW	123.33		1.0%	0%	10%	6%	52%	50%	16,241	17,599	1,296	1,400	5.17	5.87
SNX	113.46		1.3%	0%	17%	18%	40%	52%	20,054	23,164	823	1,261	10.89	12.60
NSIT	56.41		0.0%	0%	8%	-1%	38%	15%	7,080	7,538	285	306	4.63	4.98
SCSC	29.30		0.0%	-1%	-6%	-9%	-15%	-19%	3,846	3,921	144	149	3.11	3.36

Comparables Multiples Analysis	EV	FCF Yield		EV/Rev		EV/EBITDA		P/E	
		2018	2019	2018	2019	2018	2019	2018	2019
PTG-CA	164	15.2%	59.5%	0.1	0.1	10.6	6.4	NM	NM
TECD	4,701	--	19.5%	0.1	0.1	6.1	5.7	9.6	8.7
CDW	21,840	4.6%	4.6%	1.3	1.2	16.9	15.6	23.9	21.0
SNX	8,830	7.5%	11.8%	0.4	0.4	10.7	7.0	10.4	9.0
NSIT	2,233	--	--	0.3	0.3	7.8	7.3	12.2	11.3
SCSC	1,091	2.7%	#N/A	0.3	0.3	7.6	7.3	9.4	8.7

Source: Consensus Data – FactSet, Historicals – Company Filings, Forecasts/Estimates – Echelon Wealth Partners

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ANALYST CERTIFICATION

Company: Pivot Technology Solutions Inc. | PTG:TSX

I, Gianluca Tucci, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities or issuers. I also certify that I have not, am not, and will not receive, directly or indirectly, compensation in exchange for expressing the specific recommendations or views in this report.

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Is this an issuer related or industry related publication?	Issuer
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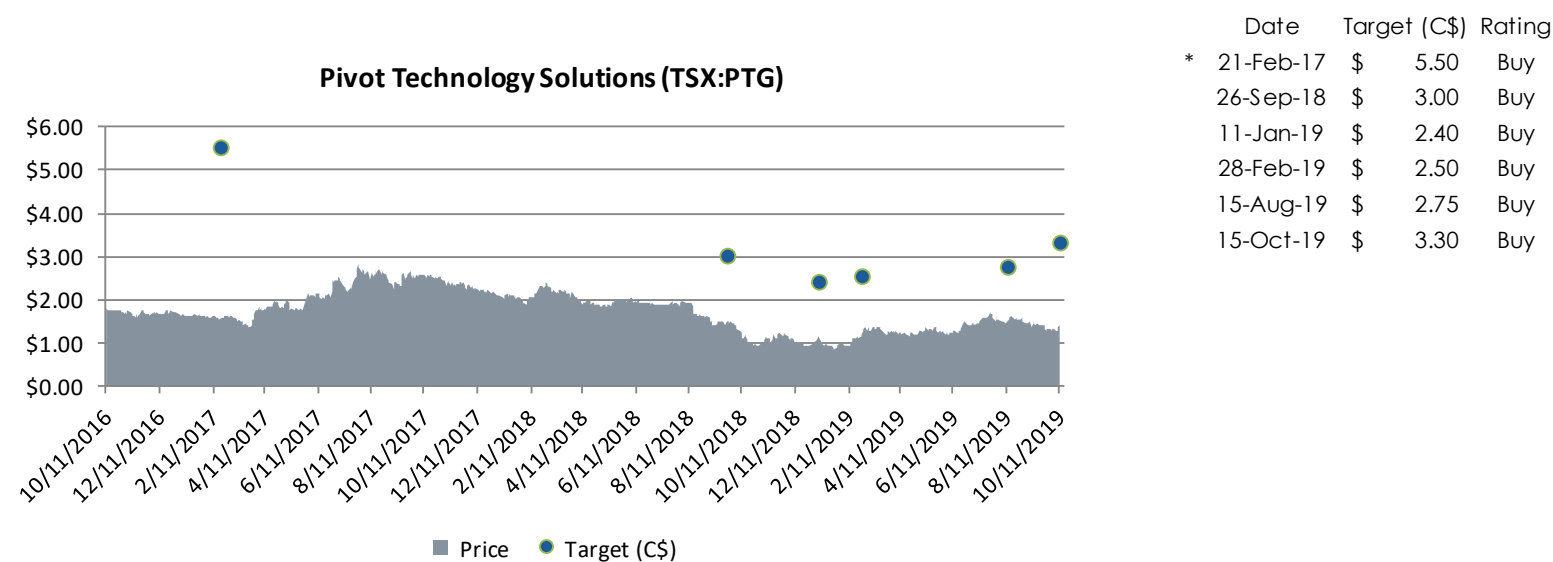
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Buy	The security represents attractive relative value and is expected to appreciate significantly from the current price over the next 12 month time horizon.
Speculative Buy	The security is considered a BUY but in the analyst's opinion possesses certain operational and/or financial risks that are higher than average.
Hold	The security represents fair value and no material appreciation is expected over the next 12-18 month time horizon.
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Under Review	While not a rating, this designates the existing rating and/or forecasts are subject to specific review usually due to a material event or share price move.
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Recommendation Hierarchy	Buy	Speculative Buy	Hold	Sell	Under Review	Restricted	Tender
Number of recommendations	50	42	15	1	7	1	2
% of Total (excluding Restricted)	43%	37%	13%	1%	6%		
Number of investment banking relationships	13	16	4	0	2	0	0
% of Total (excluding Restricted)	37%	46%	11%	0%	6%		

PRICE CHART, RATING & PRICE TARGET HISTORY



Coverage initiated: 02/21/2017
*Prior Analyst PT

Data sourced from FactSet

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