

SAP SE

Q4 preview: all eyes on 2024 acceleration

Maintain Rating: BUY | PO: 173.00 EUR | Price: 148.88 EUR

Setting the scene for business acceleration

SAP will report FY 2023 results on Wed Jan 24th at 6am CET (call 7am CET). We expect Q4 to show improving Cloud revenue, but with Cloud to come in at the low-end of 2023 guidance. We also expect a slowdown in EBIT in Q4 based on comp / one-off timings – see details below. Going ahead however, we expect SAP to post accelerating cloud and total revenue, EBIT and FCF in both 2024 and 2025. With increasing visibility on revenue growth, we expect the shares to continue to outperform as (1) Cloud momentum remains solid in an uncertain macro backdrop, with the current cloud backlog to continue to grow >20% in 2024, driven by new wins and modules upsell, (2) EBIT accelerates to double digit in 2024-2026, supporting multiple expansion., and (3) an unlevered balance sheet allows for enhanced shareholder returns – absent M&A, SAP could return €6.8bn or 4% of its market cap by YE 2025 on top of the existing dividend and €5bn buy back while staying debt free. Maintain Buy.

Q4: expect improving Cloud growth, but softer EBIT

Our Q4 forecasts are 2% below consensus on revenues (cloud), 3% on EBIT and 3% above on FCF. For Q4, we forecast an improvement in Cloud revenue growth to +24% (vs +23% in Q3), leading to 23% cloud growth for the year, at the low-end of its +23-24% guidance range. In Q3 SAP flagged macro-related pressure to certain transactional-based cloud revenue streams such as Fieldglass which we believe will continue into Q4. In addition, SAP has cautioned for a soft Q4 EBIT, implied by its FY guidance. In particular, Q4 will be impacted by the Litmus sale gain in Q4 2022 (€100m headwind) and incremental sales commission amortisation (€61m headwind), altogether a 6pp drag on Q4 EBIT growth, while Cloud Gross margins should slightly contract QoQ; we therefore forecast a 2.7% EBIT decline YoY, ex FX

Setting the stage for 2024 and 2025 acceleration

With SAP RISE's launch, we expect Cloud momentum to accelerate, with AI providing an additional mid-term route to revenue expansion. With Cloud now accounting for over 50% of Software revenues (2023) and growing close to 25% (last cloud backlog +25% YoY), we expect group revenue growth to accelerate to 8.7% c.c. in 2024 and 10.5% c.c. in 2025. Alongside this, SAP should reap the benefits of its migration to a single cloud delivery platform and extract operating leverage, driving margins to expand c 130bps per annum in the coming three years. For 2024 we forecast 8.7% top line revenue growth (including 24% cloud growth), 15% EBIT growth, and a FCF of €5.8bn, impacted by the reversal of factoring policy announced in Dec 2023. Although our revenue and EBIT forecasts are broadly aligned with consensus, our FCF is 6% below, not reflecting yet the factoring unwind.

22 January 2024

Equity

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Stock Data

Price (Common / ADR)	148.88 EUR / 163.45 USD
Price Objective	173.00 EUR / 186.00 USD
Date Established	8-Jan-2024 / 8-Jan-2024
Investment Opinion	B-1-7 / B-1-7
52-Week Range	101.46 EUR-149.18 EUR
Market Value (mn)	175,678 EUR
Shares Outstanding (mn)	1,180.0 / 1,180.0
Average Daily Value (mn)	270.27 USD
Free Float	86.8%
BofA Ticker / Exchange	SAPGF / GER
BofA Ticker / Exchange	SAP / NYS
Bloomberg / Reuters	SAPGY / SAPGF
ROE (2023E)	11.0%
Net Dbt to Eqty (Dec-2022A)	12.2%
ESGMeter™	High

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Refer to important disclosures on page 4 to 7. Analyst Certification on page 3. Price Objective Basis/Risk on page 3.

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Timestamp: 22 January 2024 12:30AM EST

Exhibit 1: BofA vs. 4Q23 consensus for SAP

BofAe c.2% below consensus on Q4'23 revenues, c.3% below on operating profit

In €mn (except per share values)	Q4'23E				Δ (%)	2023E				Δ (%)	Cons. vs. Guidance
	Act. Q4 2022	BofA Q4 2023E	YoY	Cons. Q4 2023E		BofA	Cons.	Guidance	BofA vs. Cons.		
Current Cloud Backlog	24%	25%	100 bps								
Licences	907	649	-28.5%	618	4.9%	1,575	1,546		1.9%		
Maintenance	2,993	2,855	-4.6%	2,867	-0.4%	11,504	11,516		-0.1%		
Cloud Subscription	2,970	3,555	19.7%	3,719	-4.4%	13,520	13,686	13,757	-1.2%	-1.7%	-0.5%
Cloud and software revenue	6,870	7,058	2.7%	7,220	-2.2%	26,600	26,763	26,438	-0.6%	0.6%	1.2%
% YoY growth reported		2.7%		5.1%	-235 bps	5.2%	5.9%	4.6%	-64 bps	64 bps	128 bps
Services revenue	1,042	1,083	3.9%	1,104	-1.9%	4,280	4,303		-0.5%		
Total Revenue	€ 7,912	€ 8,141	2.9%	€ 8,324	-2.2%	€ 30,880	€ 31,066		-0.6%		
Adjusted Operating profit	€ 2,560	€ 2,388	-6.7%	€ 2,473	-3.5%	€ 8,600	€ 8,687	€ 8,480	-1.0%	1.4%	2.4%
Adj. EBIT margin	32.4%	29.3%	-302 bps	29.7%	-38 bps	27.8%	28.0%		-12 bps		
Adjusted EPS (basic)	€ 0.37	€ 1.86	404.8%	€ 1.64	13.5%	€ 3.84	€ 5.22		-26.5%		
FCF*	€ 1,806	€ 1,447	-19.9%	€ 1,405	2.9%	€ 4,950	€ 4,834	€ 4,900	2.4%	1.0%	-1.4%

Source: BofA Global Research estimates, Company / Visible Alpha consensus, Company guidance (mid-point of range), Company report

BofA GLOBAL RESEARCH

Exhibit 2: BofA vs. FY'24/25 consensus for SAP

BofAe c.1% below consensus on revenues, in line on operating profit, 2024 FCF not fully reflecting change in factoring policy

In €mn (except per share values)	2024E		Δ (%)	2025E		Δ (%)
	BofA	Cons.		BofA	Cons.	
Current Cloud Backlog						
Licences	1,088	1,121	-2.9%	816	872	-6.4%
Maintenance	11,108	11,173	-0.6%	10,711	10,586	1.2%
Cloud Subscription	16,702	17,000	-1.8%	20,701	21,197	-2.3%
Cloud and software revenue	28,898	29,188	-1.0%	32,228	32,456	-0.7%
% YoY growth reported	8.6%	9.1%	-42 bps	11.5%	11.2%	33 bps
Services revenue	4,457	4,568	-2.4%	4,627	4,849	-4.6%
Total Revenue	€ 33,354	€ 33,756	-1.2%	€ 36,855	€ 37,305	-1.2%
Adjusted Operating profit	€ 9,861	€ 9,862	0.0%	€ 11,296	€ 11,463	-1.5%
Adj. EBIT margin	29.6%	29.2%	35 bps	30.6%	30.7%	-8 bps
Adjusted EPS (basic)	€ 4.62			€ 5.44		
FCF*	€ 5,784	€ 6,020	-3.9%	€ 7,506	€ 7,389	1.6%

Source: BofA Global Research estimates, Visible Alpha consensus, Company report

BofA GLOBAL RESEARCH

Price objective basis & risk

SAP SE (SAPGF / SAP)

Our price objective is based on Sum of the Parts model, valuing Cloud, on-prem and services separately. We use a 25x 2024E EV/EBITDA for the Cloud business, in line with US peers. We value the on-prem business using a DCF (-8% revenue growth to 2031, terminal growth 0%, 40% terminal EBIT margins, WACC 6.7%), while we value the services business at a 14x EV/EBITDA multiple, in line with IT Services peers. This results in a €173 (US\$186) price objective.

Upside risks to our price objective are (1) a faster multiple re-rating as the market prices in a successful cloud transition, and (2) slower erosion in the core licence business.

Downside risk include increased competition esp from Cloud native peers, and execution challenges leading to a weaker than expected growth or margin profile.

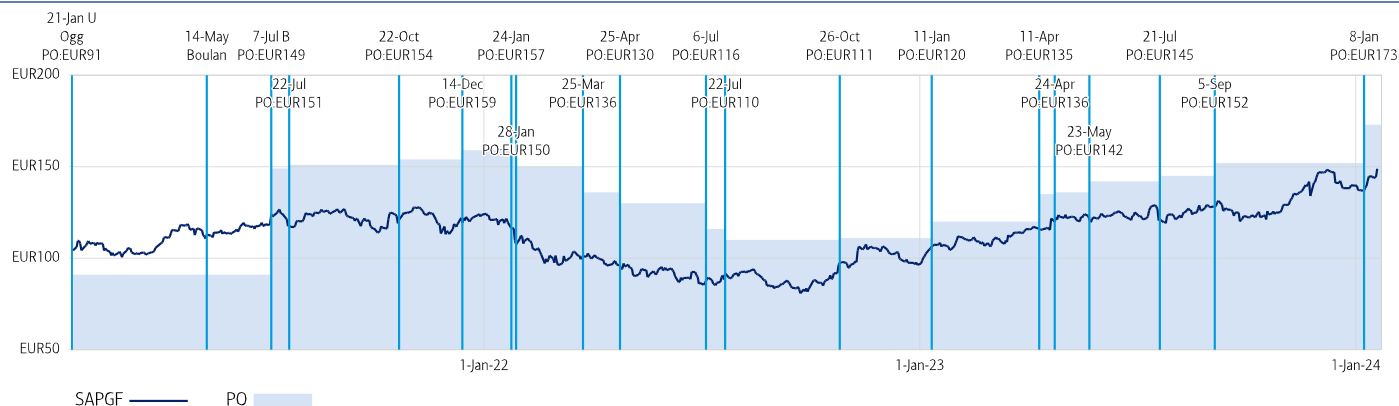
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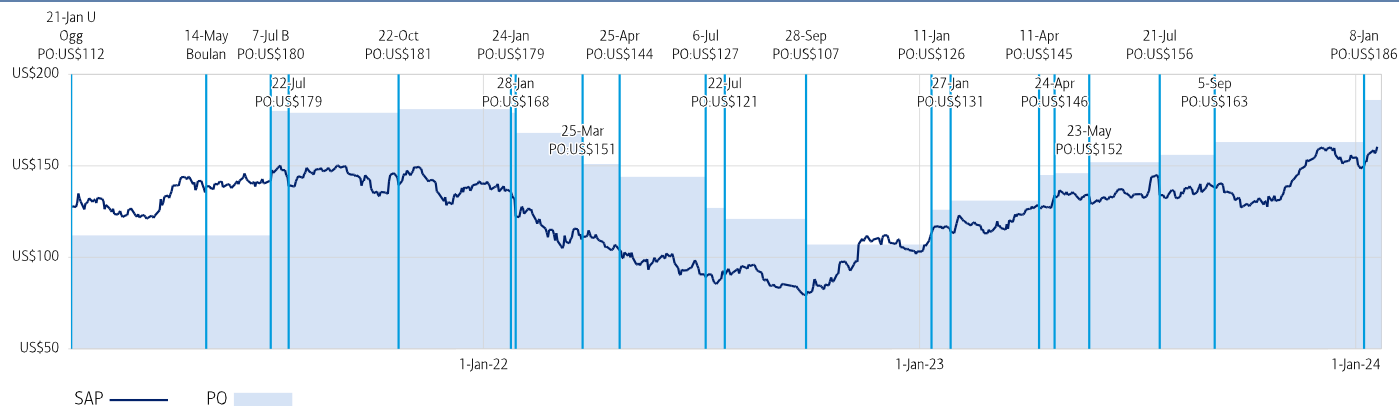
SAP (SAPGF) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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SAP (SAP) Price Chart



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Equity Investment Rating Distribution: Technology Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2}Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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