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CPT Global Limited

ASX code: CGO **BUY**

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Forecasts FY2001

Profit after tax	$m	2.7
EPS pre amort (undiluted, due to the long-dating and price hurdles)	¢	8.1
PER pre amort	x	12.3
Dividend	¢	5.0
Yield	%	5.0
Franking	%	100

Last sale price	$1.00
Issued shares	33.0 m
Options (details page 3)	7.0 m
Market capitalisation	$33.0 m
Share price high	$1.28
Share Price low	$1.00

CPT was listed in September 2000, following an issue of 6.0 million new shares to the public. **The issue price was $1.00.**

Pre-IPO and consultant shareholders have entered into voluntary escrow for at least 12 months and periods up to 36 months.

Shareholder details:

Gerry Tuddenham	35.4%
Peter Corrigan	14.7%
Michael Slattery	1.0%
Consultants & staff	30.7%
Public & institutions	18.1%

CPT is a strongly positioned, specialist IT services company – with a clear market niche in consulting. CPT is distinguished from speculative (non-profitable) technology companies, as the business is profitable and growing rapidly. This growth is maintainable, as CPT services are deemed essential, such as in system assurance (contrasting with discretionary or new computer services that can be deferred by companies). CPT also offers its customers a cost reduction solution, which is attractive in all economic conditions.

While investment values in the *technology-related* sector have fallen drastically, astute investors will identify the companies delivering genuine profit growth hold the most upside. Such companies will be the early beneficiaries of a recovery in sentiment in the sector.

We categorise CPT as an investment that will continue to deliver profit growth, based on its strong intellectual capital and unique consulting service expertise and industry position.

Valuation: **12 month target of $1.30, based on the FY2001 EPS forecast of 8.1¢ and PER of 16.0 x. The upside is CPT's success in winning further major contract work - which will drive the stock value.**

- Despite the volatility of recent months, technology remains a key driver of the economy, albeit now tempered by more realistic future investor expectations.

- The focus has shifted to companies that have real businesses and are delivering profits. CPT's expertise is regarded at the highest level domestically and internationally.
- Its consulting services are primarily targeted at larger companies, where it has a quality client list, including six of the 'top 10' companies in Australia.
- CPT has established a track record of strong, consistent growth. This has been achieved with minimal marketing and reflects management's success in building the business. CPT is positioned in the Professional Services segment of the domestic IT market, which has been forecast (by independent researchers) to grow at rates in excess of 20% per annum.
- CPT met its initial prospectus forecasts. **The key focus is to achieve the FY2001 growth step, representing a profit increase of over 80%.** Management reiterated the company is on-track to achieve prospectus targets (AGM statement for first four months of trading of FY01).

Company profile

CPT is a high-end consulting business focussed on providing specialist services to a range of customers including a number of Australia's Top 20 companies. The computer systems of attention are mainframes (such as large IBM computers) and mid sized systems (such as Unix and Oracle applications). CPT's particular expertise is in capacity planning, performance tuning and testing, and training. CPT has over 160 employees and consulting professionals, with an average industry experience of the consultants of over 13 years. Many of the personnel have considerably longer industry experience. CPT's expertise is to assess an organisation's computer systems from a top-down level, and through its highly skilled diagnostic ability, organise existing systems to extract higher performance and optimise performance**.**

A significant portion of CPT's work is the fundamental testing of systems to ensure operational robustness and assurance (similar to internal compliance auditing)**.** With the importance of IT systems, this is considered an essential function which is maintained irrespective of the economic conditions. This contrasts with a new system purchase decision (and consulting) that may be deferred. The CPT approach provides the ability to unlock and harness the full potential of systems. This frequently negates a need to purchase equipment to meet additional processing demand. The consulting base is skewed toward larger organisations with substantial and complicated computer systems, where a decision to expand a system may sometimes not even be realistic. **The CPT service has the dual powerful benefits of achieving greater functionality and realising cost savings.** The range of services provided include:

▪ Technical Reviews	Architecture Services	Testing Services
▪ Capacity Planning	Cost Reductions	Stress and Volume Testing
▪ Senior Project Management	Tuning Services	Database Management
▪ Technical Support Services	Web Load Testing	

The services create a range of benefits that can be measured in immediate financial terms (in many cases), and in system improvements – that have longer-term underlying benefits. The gains include greater **efficiency and stability** of key systems and identifying and preventing possible areas of system weakness. This includes **prevention of IT system failure** and business disruption, and enhanced **reliability -** with attention to end-to-end cross platforms (testing different system components). **Cost savings** are a clear benefit that CPT can demonstrate.

Proprietary tools CPT holds a number of tools that have been developed by its principals, which its consultants market to clients and use in project applications. These add a further ability to achieve a superior customer solution, reinforcing the advantage over mainstream IT consultants. The proprietary skill set includes providing consulting support for the Mercury Interactive product suite (described in a following section).

Human skill base – the key issue. **CPT's executive and consultant team represent the company's major asset.**

Director's details and experience:

Gerry Tuddenham – Executive Chairman 28 years experience in the IT industry and an international standing in the expertise of computer testing, particularly in IBM mainframe.

Peter Corrigan – Managing Director 17 years background in the IT industry, specialising in the mid-range area. He is the co-author of the well-known industry text of "Oracle Performance Tuning" (sales in excess of 100,000 copies and translated into a number of languages).

Chris Gillies – Non executive Current Group executive services at St George Banking, which includes responsibility for Human Resources.

Glenn Fielding – Non executive A founding member of SMS Consulting Group (one of Australia's largest IT consultants) and was a director of SMS from 1992 until 1999.

Michael Slattery – Executive director Over 38 years in the IT industry, including various consulting roles. Formerly National General Manager for Consulting Architecture at Telstra. Responsible for operational design and tactical frameworks, for the Business Processes and Information Divisions.

High quality consulting At the heart of CPT's service capability is a skilled personnel contractor base. The profile of the personnel is at the top echelon of the IT industry in experience and expertise. The personnel are employed as contractors as a matter of preference, to retain their sense of identity as being 'independent'. While the working relationships are flexible in this regard, the consultants are typically contracted for lengthy periods. The majority of the personnel have been with CPT for long periods, and the arrangements resemble an employee type commitment. The attraction for consultants is the challenge and variety of work that CPT provides. **The critical issue from CPT's perspective, is that the personnel are at the top of their field.** They provide the knowledge and experience in their areas, which forms CPT's 'human capital'. Both Gerry Tuddenham and Peter Corrigan are also highly respected and recognised IT industry individuals. With their understanding of the area, they are able to communicate effectively with the consultants and establish the bond that has been critical in building a highly professional organisation. The ability to motivate and provide the work challenges are a fundamental factor in attracting and retaining the consultants. CPT's success in this area is evident in low staff turnover - in contrast to that typical in the IT sector.

Performance options issued to executives, key staff and other personnel: 7,025,000
With the exception of 600,000 shares issued at 50¢ to Michael Slattery as a remuneration component for assuming his position with CPT (exercisable only after 18 months of service), all other executive options are exercisable at or above $1.00 and for periods from 12 months service with the company. Woodland Software has been granted 4.2 million options over a staggered 5 year period, with specific share price hurdles from $1.50 to $8.00 for the options to be exercised. Woodland has introduced an area of business, which is the basis of this arrangement.

Client list and industry position

CPT's customer list evidences the level at which it operates. Major clients include ANZ Bank, Telstra, Australian Tax Office, Coles Myer, IBM GSA, National Australia Bank, Qantas, DMR Consulting and St George Bank, and it is accredited as an Endorsed Federal Government Supplier. CPT also won a contract with UBS Warburg UK, against international competition. This provides a healthy market verification of the expertise of the company.

In terms of the concentration of the client base, Telstra represents a considerable portion of the contract base, approximately 65%. While this represents a risk, the contracts are spread across a number of divisions that are autonomous business units and the contracts are independent. Moreover, CPT has never lost a contract with Telstra for non-performance. CPT points out that due to Telsta's domestic size and demand for IT services, this situation was a natural outcome in a small local market. As CPT grows, this concentration will decline. **The client list is one measure of the quality of the business which has been established, and the prospects and capability of CPT in winning further contract work.**

In addition, CPT has a strong record of client retention, and typically, once the company is involved with an initial area of work with a customer, the breadth of consulting expands to cover a greater range of areas. CPT believes its personnel have a unique focus and set of competencies, which differentiate the company in the market place and in competing with other firms. CPT's business is distinct from mainstream-type consulting. While it is unrealistic to suggest CPT has no competitors, its set of skills and proprietary testing methodology create a distinct niche. The evidence of this specialisation strength is that CPT constantly works with mainstream IT consulting firms that call on its particular expertise.

Mercury Technology – a major market opportunity

In building CPT's service capability, a relationship has been established with a leading US system testing company Mercury Technology (capitalised at over US$5 billion on the NASDAQ). Mercury has developed a leading global solution in 'pressure' testing major Internet sites for e-transaction capacity and processing of large numbers of users. This is particularly critical for a new site prior to going live, and where a large number of users will access the site (the response time in responding to customers is a critical success factor in e-business). The Mercury product has found ready acceptance with large corporations in the US (such as in financial services), where an online presence has become an integral part of their customer link. CPT's role is the primary service provider for the Mercury product range in Australasia (Mercury is purely a product seller). This will be a major part of CPT's offering in the e-business area, where there is a rapidly growing demand by companies. The first Point of Presence for the Mercury product was established in October 2000 as a joint venture with CPT, with CPT providing facilities management. Strong interest has been shown in the Mercury application in the Australian market. **The link with Mercury positions CPT at the leading edge of technology and offers the potential to leverage new business with existing and new customers.**

Growth strategy

CPT is pursuing a number of strategies to maintain growth, with the cornerstone of growing profitability. Becoming a public company has enhanced CPT's development, with the injection of capital supporting the expansion of the business, particularly into new markets. There is also the ability to fund future acquisitions. CPT has gained a higher profile following listing, resulting in the company being asked to bid on an increasing range of projects. In addition, there is the advantage of offering equity as an incentive in attracting and retaining personnel. CPT adopted a deliberate approach of offering equity to staff in the IPO – to cement their commitment to the company. A substantial number of the staff took up equity in CPT. The specific growth objectives to build the company include:

- CPT has developed contacts in other state markets – through its existing business contacts. Building an on-the-ground presence in interstate locations will strengthen the local knowledge with customers and expand the presence in targeting new customers.
- This includes the possibility of acquisitions to grow interstate and offshore offices.
- Pursuing new business opportunities that a broader network can identify.
- Strengthening the consulting team through selective additions of personnel.
- Developing a training unit for internal and external personnel development. While this unit is not a major profit driver, there is a spin-off benefit in developing existing and new staff, and in external training support. This provides an additional service to customers, while recouping costs.
- Longer term, CPT has developed a business model that can be replicated internationally, in creating a top-level, specialist service. This process has begun in the London market. The key is to bring together the personnel required to provide the type of service offered by CPT. Management will thus be diligent in choosing the right personnel.

Financial projections

CPT has a solid track record from which to build, including the initial prospectus period:

Year ended $'000 30 June	1999 (A)	2000 prospectus forecasts	2000 (A)	JTP 2001	Forecasts 2002		% change FY 01 / 00
Revenue	**16.6**	**21.5**	**22.3**	**28.5**	**33.5**		**27.8**
EBITA	**2.1**	**2.38**	**2.44**	**3.8**	**4.4**		**55.7**
EBITA % margin	**12.6**	**10.7**	**9.4**	**12.0**	**12.2**		**-**
EBIT	**1.86**	**1.88**	**2.1**	**3.45**	**4.1**		**64.3**
Profit after Tax	**1.1**	**1.2**	**1.2**	**2.45**	**2.8**		**104.2**
Profit after Tax (pre amortisation)	**1.36**	**1.55**	**1.5**	**2.7**	**3.15**		**80.0**

*** amortisation relates to a change in economic entity from trust to company structure as part of the IPO and no underlying generation of goodwill.**

The FY2000 result maintained the trend in building CPT's revenue and profit base, which is projected to continue strongly into FY2001. Non-recurring factors held back the full profit benefit. Y2K was an adverse factor in CPT's revenue growth as the company is not engaged in consulting in this area and CPT absorbed a consultant rate increase to prevent a personnel leakage to the lucrative contracts being offered in the industry. This resulted in lower margins in the period.

CPT used the IPO process and issue of incentive shares to lock-in consultants. This is aimed at returning margins to historic levels. CPT also absorbed marginally higher costs in opening new offices, as part of building the company's presence in Sydney and London.

Key forward assumptions

- **Revenue growth** The growth in CPT's business is from identified customers that the company has secured. This work has flowed through according to prospectus projections.
- **Margins** Margins are a key factor in CPT's profitability. CPT maintains a comfortable profit level on its contract work. As the profit level is now transparent to its customers, management believes that the rate level is at a sustainable level for the long term. CPT believes that other consulting companies (with higher rates) may not be able to sustain such rates as industry competition and account transparency increases.
- Margin recovery has been factored into future projections, based on the more normal industry conditions. Customer contract rates have edged up on recent work won by CPT.
- **Future contracts** No major additional contracts have been factored into the projections. However with the expanded market presence, it is realistic to anticipate CPT winning further work. Additional contracts provide the upside to the revenue projections.
- **Financial structure and profile** Post IPO, CPT is financially strongly placed, with no debt and $4 million in cash. The nature of the business is that there is a strong and regular cash flow. Moreover the business is not capital intensive. Accordingly, CPT is anticipated to generate a high level of surplus cash, to support dividends and fund expansion.

Valuation and assessment

We believe the prospectus profit forecasts are achievable and our own projections are slightly above management targets, with a modestly higher margin expectation. Our PER is in recognition of CPT's growth performance, and on a comparative basis to the small cap sector and specifically the IT consulting-related sector. **We have ascribed a prospective PER of 16.0 x in our target value.** This is in line with the prevailing trading of listed peers:

FY01 (e)	**PER x**
Kaz Computer services	15.8
Powerlan	23.7
Oakton Computing	15.9

We regard CPT's valuation of $1.30 as representing a solid fundamental level, with none of the premium the broader technology sector has carried in the last 12 months. Valuations of peer stocks have fallen in line with the market move in technology to discounted levels, which is reflected in our valuation. The investment fundamentals are reinforced by the attractive forecast dividend yield of 5.0%. The markets` reassessment of technology stocks in the latter part of CY2000 was rapid and non-discriminatory. Companies with a 'technology' tag have suffered. However, the significance of technology in the economy remains and the investment case for *real* businesses continues. We believe that there will be increasingly a differentiation of the companies that are delivering on growth objectives, and in particular - meeting profit growth targets. **We believe that CPT will be recognised as a company with the attributes to succeed and earn investor support.** The confidence in recommending a BUY on CPT Global is driven by:

- Its distinct position in the IT sector, supported by world class expertise.
- Providing consulting service to major companies, with a consistent level of work through different market conditions.
- Meeting its prospectus forecasts. We forecast that further confirmation of this trend will occur in the interim result, with CPT maintaining a strong growth path.
- Maintaining a leading edge through its proprietary tools and technology to support its consulting service.
- CPT has corporate appeal for potential multinational and large domestic IT services companies, due to the niche focus of its business and quality client list. An offer would need to be highly attractive to induce the present owners to sell.

CPT is building a strong and sustainable business, which we believe, will deliver on the growth promise.