

## MORNING NOTE

**Buy** **241.0p**  
(Remains Unchanged) (Priced at close 3/7/08)

Target Price: 292p  
(290p)

Stock Codes: MCRO.L / MCRO LN

EPS

Apr 2008 A 32.46¢

Apr 2009 E 33.30¢

Apr 2010 E 36.65¢

Panmure Gordon Estimates  
Market Cap: £483m

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## Micro Focus International

### Ahead of teach-in

We expect a confident management team to take to the podium at the forthcoming analyst/investor teach-in. Given continued strong -typically better than expected- operating results, good disclosure and a willingness to engage the investment community has been warming to the share – in the last month the share outperformed FTSE All Share by 11.1%. A robust performance should widen the fan base, in our view. We retain our Buy.

■ **Analyst/Investor teach-in.** While we have yet to see a set agenda we anticipate that the event will concentrate on Micro Focuss' current strategy and a market overview, the Microsoft alliance, the product roadmap. We expect updates on customer case studies and greater detail about NetManage.

■ **Microsoft alliance.** Announces that itself and Microsoft have signed a strategic relationship to provide customers with advanced levels of integration and utilisation of the Windows platform and the Microsoft toolset. Micro Focus is going to extend its Windows-based technology portfolio, which already includes Net Express, SOA Express and Enterprise Server products, to provide customers with managed-code, 64-bit solutions that will take advantage of Microsoft .NET Framework. This will appear to customers interested in modernising COBOL applications and sharing data from Cobol while developing new applications in Microsoft. Strategically the announcement helps to paint in investors minds that Micro Focus is linked in with modern as well as vintage computing environments.

■ **Why do we like Micro Focus? Management.** For the first time in years (decades) Micro Focus is being driven by a sales-led software management team who have not only churned and restructured the sales organisation but also identified new co-related markets (such as APM) and attractive drop-in acquisitions. *Earnings momentum.* The new sales execution model, combined with conservative guidance, makes for a company with the potential to deliver positive earnings surprises – we acknowledge that management has been hinting that revenue growth looks more like double digit percentages. In addition to creating a sharper front end the back-end of the organisation has been changed by consolidating disparate offices and streamlining the R&D process, making for a reduced cost base. *Viable end market.* More than 80 percent of the world's corporate and government data resides on mainframes and IBM has focused on making its mainframes open servers that run open technologies such as Linux and Java. Mainframe enhancement software should remain a viable sub-segment, despite decades of alternative technologies. Micro Focus message on lower operating costs is attuned with the mood of the end customers. Indeed the new Microsoft alliance changes to complexion of the company to being better associated with a 'modern' computing environment. *The financial model.* This is cash generative business with the FCF yield is 6.1%. *Valuation* is attractive. Micro Focus shares are trading on a P/E of 16.1x for the current year. The EV/EBITDA is 10.6x and the EV/Sales is 3.7x. The dividend yield is 2.3%, the dividend is 2.4x covered.

■ **Diary date.** Teach-in 11 July

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Overall Global Distribution (Banking Client*)		
Buy	Hold	Sell
61% (33%)	26% (10%)	13% (0%)

\* Indicates the percentage of each category in the overall distribution that were banking and/or corporate broking clients

## Rating: GUIDELINE (return targets may be modified by risk or liquidity issues)

Buy	Expected to produce a total return of 15% or better in the next 12 months
Hold	Fairly valued: total return in the next 12 months expected to be $\pm 10\%$
Sell	Stock is expected to decline by 10% or more in the next 12 months

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