Outlook

Edison investment research

11 March 2010

SQS Software Quality Systems AG

Year End	Revenue (€m)	PBT* (€m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/08	142.9	13.1	39.1	10.0	5.5	4.6
12/09	134.3	7.0	19.1	6.3	11.3	2.9
12/10e	141.0	8.8	20.5	6.3	10.5	2.9
12/11e	154.2	11.4	26.0	7.7	8.3	3.6

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, share-based payments and exceptional items. Translated at £1=€0.906

Investment summary: Recovery underway

Despite weaker than expected revenues, SQS reported slightly better than forecast FY09 earnings and has seen signs of recovery in several markets. We see FY10 as a recovery year, followed by a year of stronger growth as the company's managed services business gains momentum and the IT services environment improves. The stock trades at c 11x FY10E adjusted EPS with a 3% dividend yield.

FY09 results: Mixed fortunes

Revenues fell 6% y-o-y, with the UK showing the biggest decline. Adjusted PBT was in line with our forecast, and lower tax drove adjusted EPS of €0.21 versus our €0.19. Despite a small h-o-h revenue decline in H2, better utilisation drove gross margins from 29.4% in H1 to 33.9% in H2. Several markets (UK, Germany, Other) saw a resumption in orders in H2 and managed services continued to win new business.

FY10: Recovery year

For FY10, SQS is cautiously optimistic, although it does not expect to reach pre-recession gross margins in the year. We forecast 4.9% revenue growth in FY10, driven by recovery in the UK and Other markets and more modest growth in Germany and Switzerland. We expect margin improvement in the UK and Other, driving a normalised EPS of €0.23.

FY11: Return to stronger growth

We forecast that the continuing trend towards independent testing bolstered by the company's diversification into higher recurring revenues from managed testing will drive stronger revenue growth of 9.4% in FY11 and normalised EPS of €0.29.

Valuation

The stock is up over 60% from its lows and trades at 10.5x FY10E and 8.3x FY11E adjusted EPS; the rebased dividend offers a yield of c 3%. As confidence in the recovery of SQS's business increases, we believe the stock has the potential to rerate. Our DCF analysis calculates an equity value of 278p, 29% above the current share price.

Price	215p
Market Cap	£59m

Share price graph

Share details

Code	SQS
Listing	AIM
Sector	Software & IT Services
Shares in issue	27.26m

Price

	High	Low
52 week	242.5p	137.5p

Balance Sheet as at 31 December 2009

Debt/Equity (%)	N/A
NAV per share (c)	224.7
Net cash (€m)	1.6

Business

SQS is the world's biggest provider of independent software testing and quality management. The majority of the group's revenue is derived from consultancy services to a client base including a long list of blue chip customers.

Valuation

	2009	2010e	2011e
P/E relative	109%	72%	68%
P/CF	6.8	5.0	4.3
EV/Sales	0.4	0.4	0.4
ROE	9%	10%	12%

Revenues by geography

UK	Europe
25%	75%

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SQS Software Quality Systems is a research client of Edison Investment Research Limited

Investment summary: Recovery underway

Company description: Leader in independent software testing

SQS is Europe's largest provider of independent software testing and quality management. The vast majority of the group's revenues are derived from consultancy services to a client base that now includes 20 FTSE 100 companies and half the DAX 30. SQS also generates revenues from its training and conference business and the development of specialised software tools. SQS was founded 28 years ago in Germany by the current CEO and former COO, and although Germany remains the largest market, the UK has become increasingly important. There are operations in a number of other European markets, including Scandinavia, as well as South Africa and India.

Valuation

The stock has rebounded c 60% from its low of 137.5p in August 2009 and is currently trading at 10.5x our FY10 and 8.3x our FY11 forecasts. This is marginally below its peer group – we expect that as confidence in the recovery of SQS's business increases, the stock has the potential to rerate. Although the dividend has been rebased to reflect the fall in FY09 earnings there is still some support in a yield of c 3%. Our DCF analysis based on our typically ultra-conservative discount rate of 15% reveals an equity value of 278p, 29% above the current share price.

Sensitivities

When assessing the potential factors which can affect the investment case, the following four sensitivities should be considered. **Cyclicality:** despite its advantages, external testing represents an initial cost and is therefore not immune to economic downturns, as shown by the decline in IT service expenditure in 2009. **Financial services**: the financial and insurance sectors represented 39% of FY09 turnover. Industry turmoil is likely to continue to affect budgets for new software implementation and testing. **Acquisition risks**: management's strategy is to continue to make in-fill acquisitions. While this has been successful in broadening the geographic footprint and developing an off-shoring capacity, the non-organic element of the growth strategy raises the risk profile. **Offshoring**: SQS is addressing the challenge posed by off-shoring through strategic acquisitions and developing organically in South Africa, Egypt and India.

Financials

- While FY09 revenues undershot our forecast, normalised PBT was in line, and normalised EPS beat our forecast due to lower than expected taxes.
- We see 2010 as recovery year, positioning the company for strong growth in 2011.

Exhibit 1: Changes to forecasts.

Note: Figures in €m except per share data (€c)

	EPS			PBT			EBITDA		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2009	19.0	21.1	11	7.0	7.0	0	10.8	12.5	16
2010e	22.6	22.6	0	8.8	8.8	0	12.5	14.3	14
2011e	N/A	28.7	N/A	N/A	11.4	N/A	N/A	17.0	N/A

Source: SQS Software Quality Systems and Edison Investment Research

Company description: Leader in independent testing

SQS is Europe's largest provider of independent software testing and quality management. The vast majority of the group's revenues are derived from consultancy services to a client base that now includes 20 FTSE 100 companies and half the DAX 30. SQS also generates revenues from its training and conference business and the development of specialised software tools. The company was founded 28 years ago in Germany by the current CEO and former COO, and although Germany remains the largest market, the UK has become increasingly important. There are operations in a number of other European markets – including Scandinavia – as well as South Africa and India.

Background: Track record of nearly 30 years

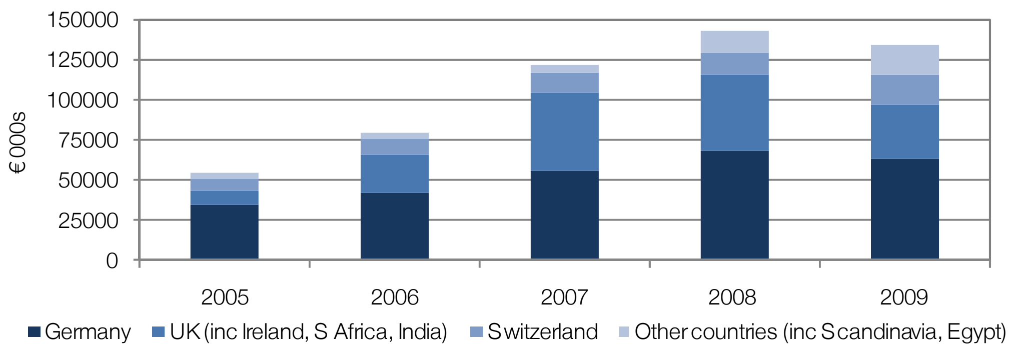
SQS was founded in 1982 in Germany by Rudolf van Megen (current CEO) and Heinz Bons (ex-COO) to introduce systematic and methodical software testing to IT projects with the aim of reducing error rates.

In 2000, the company started its international expansion, founding an Austrian operation and buying two Dutch consulting firms (AQsoft B.V. and AQpro B.V). The company first entered the UK market in 2001 with the acquisition of SIM, and boosted its UK presence with the purchase of Cresta in 2006. In 2002, SQS set up a Swiss subsidiary. In 2005, the company listed on AIM. In 2007, SQS bought insurance specialist Triton (based in Austria). In the same year, the company opened its first off-shore operation in South Africa, followed by an Egyptian operation in 2008. The company's most recent acquisitions, Validate and Verisoft, took them into the Scandinavian and Indian marketplaces respectively.

Group strategy: Expansion by geography and service offering

As described above, SQS has expanded out of its home market of Germany through a combination of organic growth and acquisition. The company reports revenues and profitability by geography – Exhibit 2 demonstrates revenue progression over the last five years.

Exhibit 2: Revenue by geography, 2005-2009



Source: SQS Software Quality Systems

The company generates revenues from three business lines:

1) Professional services for IT: management consultancy, software testing and quality management (95% of FY09 revenues).
2) Software tools, licenses and maintenance (2% of FY09 revenues).
3) Conferences, training and events (3% of FY09 revenues).

Professional service: Three phases

Around 10% of SQS's revenues in 2009 came from **management consultancy** services to banks and insurance companies, where SQS advises clients on business processes, potentially leading to the initiation of IT projects. The bulk of revenues (82% in 2009) come from performing **professional testing and quality management** on projects in the development or implementation phase. A small but growing percentage of business (3% in 2009) comes from **managed testing services** to provide regression testing for upgrades, patches and new releases of software in productive use.

Growing off-shore capabilities

SQS's first move off-shore was to set up a subsidiary in South Africa. This office provides off-shore capability for European clients and on-shore capability for South African clients. SQS opened its Egyptian operation in 2008, based in Cairo. Staff speak a variety of languages and mainly work as off-shore capability for Central European clients. SQS acquired Verisoft, based in Pune, India, in 2008. Staff are predominantly English speaking and serve international clients.

SQS grew the number of off-shore consultants to 310 by the end of 2009, equating to 26.5% of total consultants, up from 258 consultants/22.1% of total at the end of 2008.

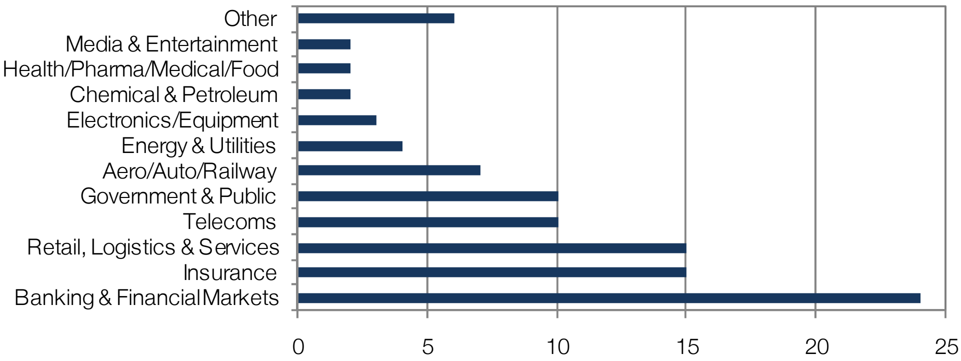
The development of the off-shore businesses allows SQS to offer hybrid on-shore/off-shore contracts to European customers at a lower price. Within the professional services businesses, management consulting is typically provided by European-based consultants. Professional testing and quality management is served by a combination of on-shore and off-shore consultants. Managed testing is predominantly served by off-shore consultants.

Diversified customer base

SQS has historically worked on a consultancy basis with clients, providing testing services as clients design and implement IT projects. The majority of SQS's business comes from existing customers, as they tend to return to SQS for each additional project that they implement. The move into managed services should increase the level of recurring revenues, as contracts are typically signed for three to five years.

In 2009, the company signed 160 new customers (2008: 175). Exhibit 3 shows the end markets served by SQS in 2009. In 2009, the company won new clients in the technology, energy, utility and public sectors. In 2010, the company intends to target companies in higher growth areas such as the utilities, telecom, insurance and public sectors.

Exhibit 3: Revenues by market, 2009 (%)

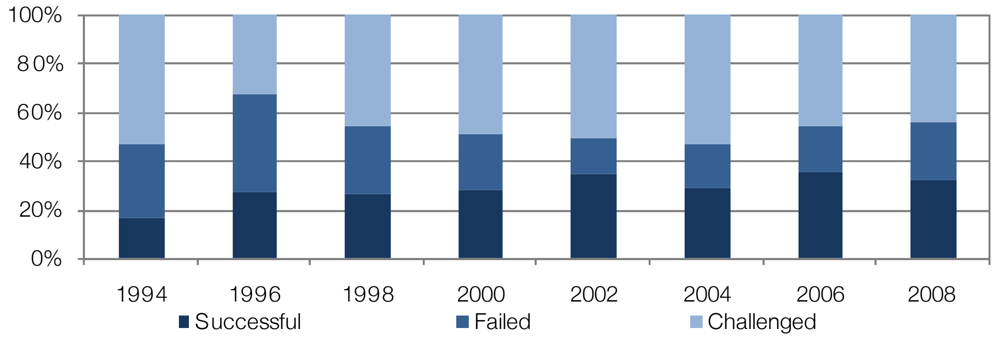


Source: SQS Software Quality Systems

Market overview: Independent software testing

The market for independent software testing has grown rapidly in recent years, driven by the need to reduce the failure rate of IT projects. A global study by the Standish Group on the success rate of IT projects showed that in 2008, 24% of projects failed, 44% were challenged (either late and/or over budget) and only 32% were classed as successful. Exhibit 4 shows that while the rate of success has improved since the study first began in 1994, it has remained relatively stable for the last eight years.

Exhibit 4: Success rates of IT projects



Source: Standish Group

SQS has commissioned its own research into the subject, with a study by PAC in 2008 surveying 1,030 companies in 13 countries. It found:

- 79% think that poor testing has a significant cost impact on the company.
- 68% need to adapt their testing to compliance and regulatory requirements.
- 65% agree software testing should be independent from development.
- 33% see testing as essential investment in the product.
- Only 20% have no problems in the first few months that the product goes live

Market size and growth

SQS recently commissioned research from PAC on the size of the opportunity in the countries that it operates in. PAC found that the market for testing is worth c €22.6bn – around 20% of testing will be contracted externally (c €4.5bn). Around two-thirds of external testing is performed by systems integrators as part of other IT service contracts and the remaining one-third as stand-alone contracts. Pure-play test specialists like SQS fulfil a quarter of the stand-alone contracts worth about €360m. This implies that SQS has c 37% share of the pure play test specialist market, 9% of the standalone test market and 3% share of the external test market.

PAC estimates that the external testing market in SQS-served countries will grow at a CAGR of 5% from 2009 to 2013.

IDC forecasts that global IT services spending will rise 3% in 2010. Within this we would expect software testing to show faster growth, as more companies decide to appoint independent software testers for new projects or outsource ongoing testing work to independent service providers.

Competition: Systems integrators and pure play specialists

SQS competes against a variety of independent software testing companies as well as the in-house testing divisions of systems integrators.

The largest systems integrator test provider is Wipro, generating revenues of €365m from testing in CY09. The next largest systems integrators by test revenues are Infosys, SOGETI, Cognizant and TCS, all generating revenues above or at a similar level to SQS. SQS is the largest specialist testing company – we estimate the next largest company is Applabs, generating revenues of c €70m in FY09. Applabs is headquartered in India but has operations in Europe (having acquired British testing company, IS Integration, in 2006). We estimate that no other specialist testing company generated revenues in excess of €20m in 2009.

Growth strategy: Diversification into managed testing

We estimate that SQS's revenue growth will come from the following areas:

- The continued trend towards independent software testing (see above).
- The growth of the managed services business.
- Further development of the off-shore businesses.
- Potential expansion into other geographies, most likely through acquisition.

Managed services

SQS has expanded its business into the managed testing market. Many clients have in-house IT staff dedicated to testing software and software updates before roll-out firm-wide. SQS is able to support this function, reducing the number of in-house staff required. SQS charges for this service on a service level rather than a day-rate basis and signs up customers to longer-term contracts, which help improve visibility for the group. Another advantage of this type of business is that it offers SQS an insight into the customer's plans for future IT projects, helping position SQS to win project-based work earlier in the process.

In 2009, the company won 15 managed services contracts, generating 3% of group revenues (0% in 2008). SQS would like to grow this to nearer 50%. As much of the work does not need to take place on customer premises, SQS is able to use its off-shore staff to undertake most of the work. Year-to-date, SQS has signed three more significant contracts with two banks and a global insurer.

Geographical expansion

SQS currently operates in Germany, Austria, Switzerland, the Netherlands, the UK, Ireland and Scandinavia. Off-shore operations in India, South Africa and Egypt serve mainly European clients, although there is some on-shore business in South Africa. The company has a partnership in Spain (which was previously a joint venture) and has an investment in Portugal. It is possible that SQS may make fill-in acquisitions in countries where it already operates as well as consider entry into the French and Italian markets.

Financials

Review of FY09 results

Exhibit 5: Summary of performance, 2008-2009

€m	2008	2009	Change
Turnover	142.9	134.3	(6%)
Gross margin	34.7%	31.7%	(300bps)
EBITDA	17.3	12.5	(28%)
Normalised PBT	13.1	7.0	(47%)
Normalised EPS (€)	0.43	0.21	(51%)
Dividend (c)	11.0	7.0	(36%)
Net (cash)/debt	(4.0)	(1.6)	(61%)

Source: SQS Software Quality Systems

SQS reported a revenue decline of 6% y-o-y versus our forecast of a 1% decline. Utilisation dropped in H109 and drove gross margin down to 29.4%. With improving utilisation in H209 (billable staff utilisation rose from 175 to 181 days h-o-h), gross margin rose to 33.9%, resulting in a drop of 300bp overall y-o-y. The number of consultants remained almost flat y-o-y (1,168 in 2009; 1,169 in 2008) although the mix of on-/off-shore changed from 77.9%/22.1% to 73.5%/26.5%.

Restructuring carried out in the year resulted in a cost reduction of €8.9m versus H208 annualised costs. G&A expenses fell on an absolute basis as a result of the restructuring. Investment in sales and marketing staff to drive new business and sales of managed testing drove sales and marketing expenses up 5.7% y-o-y. R&D expenses benefited from the capitalisation of development costs (amortisation of development costs €2.4m versus capitalised development costs of €3.3m).

Exhibit 6: Revenues by geography

Revenues (€ 000s)	H108	H208	FY08	H109	H209	FY09
Germany	33,941	34,798	68,739	32,403	31,221	63,624
UK	23,905	22,171	46,076	16,128	17,320	33,448
Switzerland	6,879	7,259	14,138	9,929	8,749	18,678
Other	4,142	9,808	13,950	9,039	9,555	18,594
Growth y-o-y						
Germany	29.9%	17.7%	23.4%	(4.5%)	(10.3%)	(7.4%)
UK	6.4%	(15.5%)	(5.4%)	(32.5%)	(21.9%)	(27.4%)
Switzerland	15.6%	10.3%	12.8%	44.3%	20.5%	32.1%
Other	148.0%	301.5%	239.2%	118.2%	(2.6%)	33.3%
Growth h-o-h						
Germany	14.8%	2.5%		(6.9%)	(3.6%)	
UK	(8.9%)	(7.3%)		(27.3%)	7.4%	
Switzerland	4.5%	5.5%		36.8%	(11.9%)	
Other	69.5%	136.8%		(7.8%)	5.7%	

Source: SQS Software Quality Systems

On a geographical basis, the UK market showed the largest annual decline, although in constant currency, the UK would have shown a smaller 18% decline. The UK business has a high proportion of banking clients (both in the UK and Ireland). The segment saw revenues pick up 7% H2 versus H1 although the Irish market remains weak.

Both the Swiss and German markets showed a decline in H2 versus H1, although Swiss revenues grew 32% for the full year. In Germany, the company saw the resumption of suspended projects in H2 but is still experiencing price pressure. The strong full year growth in Switzerland was attributable to the demand for managed service contracts from the wealth management and insurance sectors.

Other (including Scandinavia and Egypt) showed a decline in H109 versus H208 but recovered in H209 to show 6% h-o-h growth. Full year growth for the Other segment was boosted by the inclusion of Validate revenues from July 2008. Dutch markets remain weak, but all other markets are showing signs of recovery. The Egyptian off-shore centre generated a loss of €0.4m in 2009 as it is still in expansion mode and many staff are being trained.

Cash flow and balance sheet

SQS generated €9.1m cash from operations, helped by good working capital management. Debtor days remained at 55 in 2009. Net cash stood at €1.6m at year end.

The company announced a dividend of 7c/6.4p for 2009, compared to 11c/10p in 2008. The payout ratio (based on normalised net income) is 33%, higher than the company target of 30%. The company commented that as second half showed signs of recovery, it was comfortable paying out a slightly higher amount but would revert to the target payout ratio in future.

Outlook

Although the second half saw a pick-up in orders and hence an improvement in utilisation, the company is not expecting pricing to return to pre-recession levels. For FY10, the company expects margins to continue to be depressed, albeit at a higher level than in FY09.

Changes to forecasts

For FY10, we have factored in moderate revenue growth for Germany and Switzerland and stronger growth for the UK and Other geographies. In the UK, this reflects a rebound from very depressed levels. For FY10 margins, we expect flattish margins for Germany and Switzerland but improving margins for the UK and Other.

For FY11, we are forecasting stronger growth and margin improvement across all divisions.

Exhibit 7: Divisional revenues and profitability, FY09-FY11E

€'000s	Revenues			Adj. operating profit			Adj. operating margin		
	FY09	FY10E	FY11E	FY09	FY10E	FY11E	FY09	FY10E	FY11E
Germany	63,624	65,533	71,431	4,147	4,260	5,357	6.5%	6.5%	7.5%
UK	33,448	36,124	39,736	1,427	2,709	3,576	4.3%	7.5%	9.0%
Switzerland	18,678	19,052	20,766	979	991	1,246	5.2%	5.2%	6.0%
Other	18,594	20,267	22,294	996	1,338	1,784	5.4%	6.6%	8.0%
Total	134,344	140,976	154,227	7,549	9,297	11,963	5.6%	6.6%	7.8%
Growth		*4.9%*	*9.4%*		*23.2%*	*28.7%*			

Source: SQS Software Quality Systems and Edison Investment Research

The table below shows the changes to FY10 earnings forecasts and the introduction of FY11 forecasts.

Exhibit 8: Changes to forecasts

Note: Figures in €m except per share data (€c).

	EPS			PBT			EBITDA		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2010e	22.6	22.6	0	8.8	8.8	0	12.5	14.3	14
2011e	N/A	28.7	N/A	N/A	11.4	N/A	N/A	17.0	N/A

Source: Edison Investment Research

Sensitivities

When assessing the potential factors which can affect the investment case, the following sensitivities should be considered:

- Cyclicality: Despite its advantages, and potentially positive impact on ROIs, external testing does represent an initial cost and is therefore not immune to economic downturns, as evidenced by the slowdown in IT service expenditure in 2009.
- Financial services: Despite the increasing spread of industry verticals, the financial and insurance sectors still represented 39% of turnover in 2009. The well documented industry turmoil may affect budgets for new software implementation and testing.
- Acquisition risks: The management's strategy is to continue to make in-fill acquisitions in a fragmented market and this has been extremely successful in broadening the geographic footprint and developing an off-shoring capacity. However, the non organic element of the growth strategy raises the risk profile.
- Off-shoring: SQS is addressing the challenge posed by off-shoring through strategic acquisitions and developing organically in South Africa, Egypt and India.

Valuation

We are forecasting a modest recovery in revenues and margins in FY10 followed by stronger growth in FY11. The stock has rebounded c 60% from its low of 137.5p in August 2009 and is currently trading at 10.5x our FY10 and 8.3x our FY11 forecasts. This is marginally below its peer group – we expect that as confidence in the recovery of SQS's business increases, the stock has the potential to rerate.

Although the dividend has been rebased to reflect the fall in earnings in FY09 there is still some support in a yield of c 3%.

DCF

In terms of intrinsic value, our DCF analysis below highlights the potential which exists given the predicted value of future cash flows. Based on our typically ultra-conservative discount rate of 15%, this reveals an equity value of 278p, some 29% above the current share price. Given that this analysis is based on a starting point that reflects the impact of currently depressed earnings streams, there is also scope for this value to increase moving forward.

Exhibit 9: Discounted cash flow analysis

Discount rate	15%
Growth rate in perpetuity	3%
NPV €m	82.2
Net debt/(cash) 2009 €m	(1.6)
Equity value €m	83.8
Equity value £m	75.9
Equity value (p)	278.4
Upside/(downside)	29%

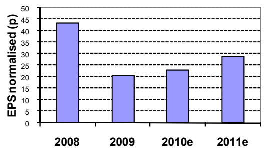
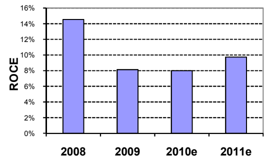
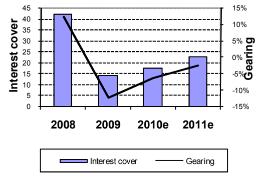
Source: Edison Investment Research

Exhibit 10: Financials

Note: Normalised EPS excludes exceptionals, amortisation of acquired intangibles and share-based payments.

€'000s	2005	2006	2007	2008	2009	2010e	2011e
Year end 31 December							
PROFIT & LOSS							
Revenue	54,737	78,933	121,059	142,903	134,344	140,976	154,227
Cost of Sales	(35,563)	(51,997)	(79,307)	(93,294)	(91,798)	(92,762)	(101,019)
Gross Profit	19,174	26,936	41,752	49,609	42,546	48,214	53,208
EBITDA	6,847	8,507	14,126	17,327	12,493	14,324	16,990
Operating Profit (before GW and except.)	4,486	5,734	10,513	13,462	7,548	9,297	11,963
Amortisation of acquired intangibles	0	0	(241)	(1,140)	(1,557)	(1,557)	(1,557)
Exceptionals	0	(276)	(561)	(1,161)	(432)	(250)	(150)
Other	0	0	0	0	(129)	0	0
Operating Profit	4,486	5,458	9,711	11,160	5,430	7,490	10,256
Net Interest	(773)	(390)	(46)	(319)	(530)	(530)	(530)
Profit Before Tax (norm)	3,713	5,344	10,467	13,143	7,018	8,767	11,433
Profit Before Tax (IFRS)	3,713	5,068	9,665	10,841	5,029	6,960	9,726
Tax	(1,319)	(383)	(2,932)	(4,146)	(1,261)	(2,543)	(3,316)
Profit After Tax (norm)	3,475	4,573	7,535	8,997	5,757	6,225	8,117
Profit After Tax (IFRS)	2,394	4,685	6,733	6,695	3,768	4,418	6,410
Average Number of Shares Outstanding (m)	11.7	16.5	19.1	22.3	26.2	27.5	28.3
EPS - normalised (c)	20.5	27.8	41.5	43.2	21.1	22.6	28.7
EPS - IFRS (c)	20.5	28.4	35.3	30.0	14.4	16.0	22.7
Dividend per share (c)	0.0	0.0	20.0	11.0	7.0	7.0	8.5
Gross Margin (%)	35.0%	34.1%	34.5%	34.7%	31.7%	34.2%	34.5%
EBITDA Margin (%)	12.5%	10.8%	11.7%	12.1%	9.3%	10.2%	11.0%
Operating Margin (before GW and except.) (%)	8.2%	7.3%	8.7%	9.4%	5.6%	6.6%	7.8%
BALANCE SHEET							
Fixed Assets	16,747	36,033	56,598	68,330	62,976	61,892	60,808
Intangible Assets	2,395	3,356	5,999	10,740	10,402	8,818	7,234
Goodwill	11,589	28,313	45,977	52,652	47,513	47,513	47,513
Tangible Assets	2,763	4,364	4,622	4,938	5,061	5,561	6,061
Investment in associates	0	0	0	0	0	0	0
Current Assets	18,857	26,432	35,689	34,650	33,830	38,326	44,116
Stocks	135	314	139	0	0	0	0
Debtors	11,951	23,289	28,173	26,161	24,251	25,500	27,000
Cash	6,465	2,565	7,220	5,753	5,351	8,598	12,888
Current Liabilities	(13,123)	(27,530)	(33,930)	(29,029)	(23,171)	(23,171)	(23,171)
Creditors & other liabilities	(9,347)	(22,200)	(33,224)	(28,023)	(21,515)	(21,515)	(21,515)
Short term borrowings	(3,776)	(5,330)	(706)	(1,006)	(1,656)	(1,656)	(1,656)
Long Term Liabilities	(4,286)	(8,436)	(9,339)	(10,995)	(12,025)	(12,025)	(12,025)
Long term borrowings	(2,971)	(465)	(384)	(732)	(2,112)	(2,112)	(2,112)
Other long term liabilities	(1,315)	(7,971)	(8,955)	(10,263)	(9,913)	(9,913)	(9,913)
Net Assets	18,195	26,499	49,018	62,956	61,610	65,022	69,728
CASH FLOW							
Operating Cash Flow	4,106	2,909	13,540	16,693	9,111	13,075	15,490
Net Interest*	(833)	(492)	(256)	(126)	(603)	(530)	(530)
Tax	(509)	(841)	(1,440)	(3,919)	(1,434)	(1,261)	(2,543)
Capex	(2,961)	(3,199)	(2,930)	(6,024)	(6,273)	(5,500)	(5,500)
Acquisitions/disposals	95	(4,080)	(3,088)	(3,410)	(1,923)	(700)	(700)
Financing	14,120	2,755	3,534	(1,009)	1,478	0	0
Dividends	0	0	0	(4,320)	(2,788)	(1,837)	(1,928)
Net Cash Flow	14,018	(2,948)	9,360	(2,115)	(2,432)	3,247	4,289
Opening net debt/(cash)	14,300	282	3,230	(6,130)	(4,015)	(1,583)	(4,830)
HP finance leases initiated	0	0	0	0	0	0	0
Other	0	0	0	0	0	(0)	(0)
Closing net debt/(cash)	282	3,230	(6,130)	(4,015)	(1,583)	(4,830)	(9,120)

Source: SQS Software Quality Systems and Edison Investment Research

Growth	Profitability	Balance sheet strength	Sensitivities evaluation	
			Litigation/regulatory	○
			Pensions	○
			Currency	◐
			Stock overhang	○
			Interest rates	◐
			Oil/commodity prices	○

Growth metrics	%	Profitability metrics	%	Balance sheet metrics		Company details	
EPS CAGR 07-11e	0.6	ROCE 10e	8.1	Gearing 10e	N/A	Address:	
EPS CAGR 09-11e	21.2	Avg ROCE 07-11e	11.4	Interest cover 10e	N/A	Stollwerckstr. 11, D – 51149 Cologne	
EBITDA CAGR 07-11e	10.3	ROE 10e	9.6	CA/CL 10e	1.7		
EBITDA CAGR 09-11e	-2.0	Gross margin 10e	34.2	Stock turn 10e	N/A	Phone	+49 22 03 91 540
Sales CAGR 07-11e	6.2	Operating margin 10e	6.6	Debtor days 10e	66	Fax	+49 22 0391 5415
Sales CAGR 09-11e	7.1	Gr mgn / Op mgn 10e	5.2	Creditor days 10e	45	www.sqs-group.com	

Principal shareholders	%
Mr van Megen and family	15.5
Mr and Mrs Bons	13.9
Herald Investment Management	7.2
Killik Asset Management	7.1
J.O.Hambro Capital Management	6.3
Insight Investment Management	4.0
Legal & General Investment Management	3.7

Forthcoming announcements/catalysts	Date
AGM	26 May 2010
Interim results	September 2010*
*Note: * = estimated*	

Management team
CEO: Rudolf van Megen
Rudolf van Megen graduated from the University of Cologne with a degree in business administration focusing on informatics, and then completed a number of R&D projects in software testing and efficiency. Joint founder of SQS in 1982 with former COO Heinz Bons.
CFO: Rene Gawron
Rene Gawron joined SQS in 2001 having previously worked for Siemens from 1985-2000. While at Siemens he had various roles including head of business development for mobile telecom networks. Before joining SQS as CFO, he was a member of the management board of a software company called Artificial Life (Deutschland) AG, and an electronics company called Meads Inc.
Member of board: David Cottrell
David Cottrell joined the SQS board in 2008. He joined Cresta (bought by SQS in 2006) as CEO in 2002. He is responsible for setting group sales and marketing policies. He is also CEO of UKIISA region (UK, Ireland, India and South Africa). Before SQS, he held senior management roles with ACT Financial Systems, DST International, Customer Analytics and Advent.