



SMALL-CAPS

RECOMMENDATION

Data#3

DTL:ASX
November 2024

GENERAL ADVICE ONLY - THIS RECOMMENDATION IS GENERAL ADVICE ONLY AND DOES NOT TAKE INTO ACCOUNT YOUR SPECIFIC CIRCUMSTANCES

SMALL-CAPS RECOMMENDATION

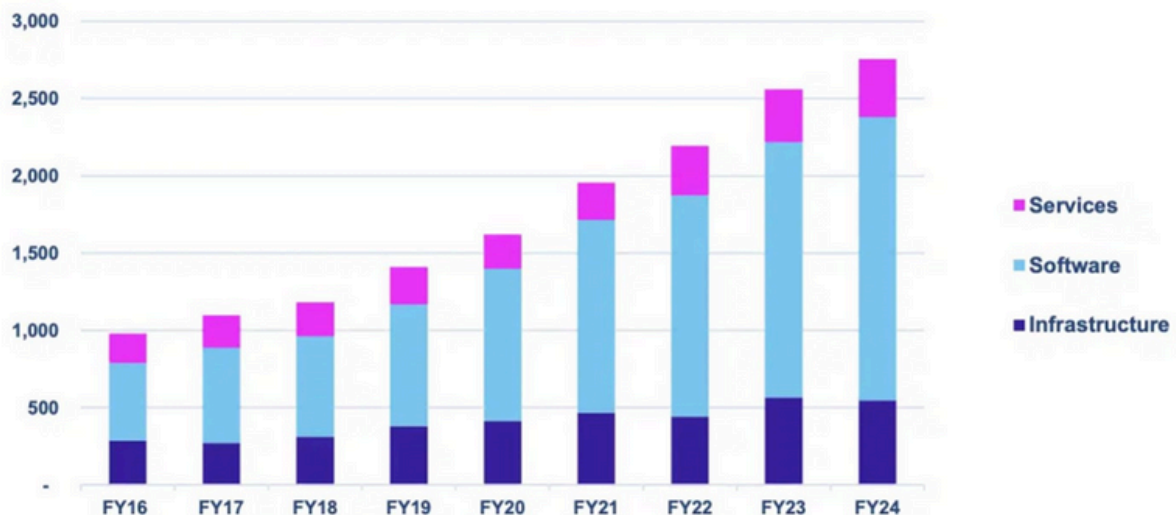
Data#3 DTL:ASX

IT consulting and distribution company Data#3 (ASX: DTL) can trace its beginnings all the way back to a Brisbane garage back in 1977. 50 years later, it has become “one of the world’s largest Microsoft device resellers,” [according to Microsoft](#). That reflects the fact that Data#3 has ridden a multi-decade wave of digital innovation to become one of the best-known Australian IT suppliers to large corporates and government departments.

Data#3 divides its gross sales into software, infrastructure, and services.

As you can see below, software gross sales are now the largest component of gross sales. Reselling software is a lower-margin business, but it has the advantage of being capital-light because Data#3 does not need to tie up capital to store software inventory; it just clips the ticket on the sale.

Gross Sales trend by functional area (\$M)



While Data#3 makes money from a variety of offerings: Software Solutions, Infrastructure Solutions, Consulting, Project Services, People Solutions, Maintenance Services, and Managed Services, the latter two make the highest margins. On top of that, they entail at least somewhat recurring business. Therefore, we could reasonably expect each category of total gross sales to grow over time.

INVESTMENT CONSIDERATIONS

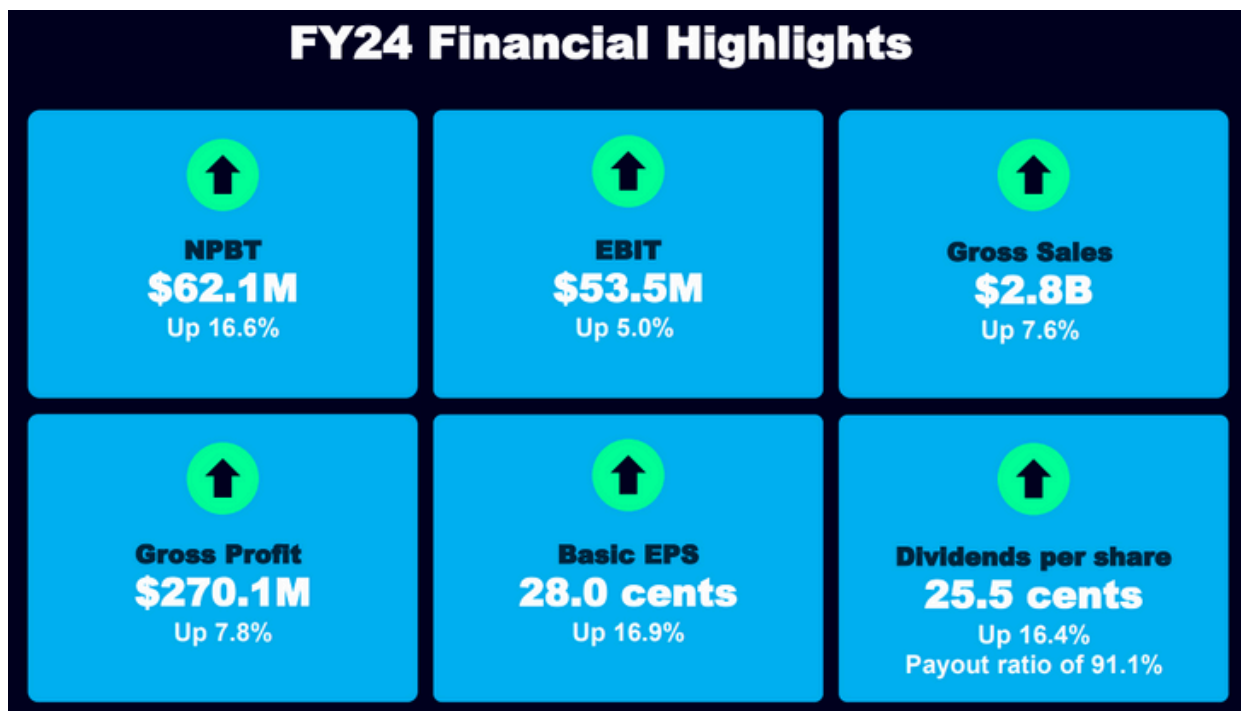
Leadership

Data#3 has recently undergone a leadership transition, with a long-serving Chairman of the Board, CEO and CFO all resigning. The new CEO Brad Colledge was appointed as CEO in 2024 but has worked for Data#3 since 1995. This shows the company has talent beyond the top level. He owns just under \$3m worth of shares.

Some degree of board alignment is provided by long-serving director Mark Esler who owns almost 2.8 million shares, worth over \$21 million. The Chairman claims that Esler is not afraid to hold management to account.

The five person board is rounded out by Leanne Muller, Mark Gray, and Susan Forrester. While none of them own large holdings, the latter two both purchased small parcels above current prices after the FY 2024 result. Overall, Data#3 displays satisfactory though not standout alignment between the board and shareholders.

Financial Performance



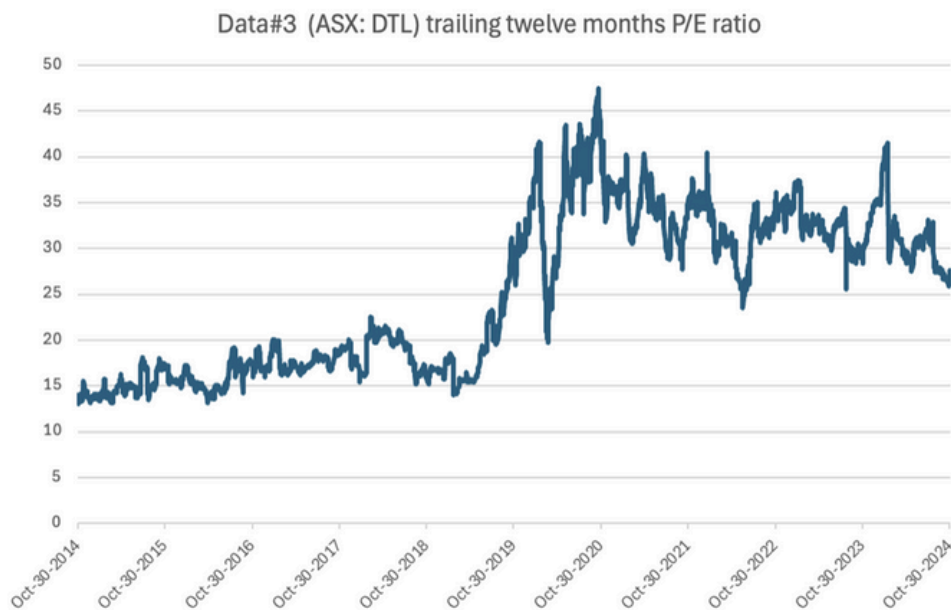
INVESTMENT CONSIDERATIONS

Valuation

Data#3 has given guidance for H1 FY 2025 of \$31m to \$33m profit before tax. Using the midpoint of this range and assuming a 30% tax rate suggests NPAT of about \$22.4 million for the first half. At the AGM, the CEO said that the second half should be stronger, so it would be reasonable to assume at least \$45 million profit for the full year.

At the a share price of \$7.50, Data#3 has a market capitalisation of just under \$1.2b, implying a FY 2025 P/E ratio of around 26.5.

The chart below shows how the trailing twelve months Data#3 P/E ratio has changed over the last 10 years. This suggests that sentiment around the business is within the normal range.



Sociological Factors

Data#3 is already in the ASX 200, so it is unlikely to receive more attention simply by growing in size. It is already well-covered and there is plenty of liquidity for institutions to trade the stock.

Notably, one of the drivers of demand has been the increasing use of artificial intelligence, since Data#3 expects to make money by setting its clients up to use Microsoft Copilot. It is already the Highest selling Microsoft Copilot Licensing partner in Australia. It is possible that narrative speculators could pick up on this exposure to artificial intelligence and drive the stock higher as a result of hype and excitement about AI. However, any gains from this sociological phenomenon might lead to disappointment if overall growth is insufficiently impressive.

RISKS

Risks

Data#3 sells a lot of product to various governments, particularly the federal government and the Queensland government. The former government is up for election next year, and Queensland has just had a change of government. Sometimes, new governments have different priorities with regard to spending, and any reduction in IT budgets for government department has the real potential to hurt Data#3 gross sales.

Data#3 relies on its relationships with vendors like Microsoft and Cisco in order to have product it can sell. Any souring of its key partnerships would certainly hurt the business.



Finally, a recession or macroeconomic strife could see corporates and governments alike hit pause on IT spending. In the short term, that could hurt Data#3, and create unpleasant volatility in the share price. IT spending is at least somewhat cyclical, so there are guaranteed to be some weaker periods over the decades.

WHY HOLD THE COMPANY?

Why hold the Company?

The efficiencies enabled by utilising digital automation create an incentive for governments and corporates to continually invest in better IT systems. While the trends and most popular products do change over time, Data#3 always has the right solution for the day thanks to its relationships with world-leading IT software and hardware vendors. In a sense, it clips the ticket on IT spending.

On top of that, Data#3 benefits from negative working capital, meaning it actually profits from the interest it earns on the cash it holds in the period between when a customer pays Data#3, and Data#3 pays its supplier. As a result, it does not need to raise capital or take on debt in order to grow.

With persistent demand tailwinds, a reasonable valuation, a solid dividend yield and a capital light business model, Data#3 is appropriate for investors looking for long-term growth at a reasonable price.



Conclusion

In summary, Data#3 presents an attractive investment opportunity for those seeking exposure to Australia's growing IT services sector, with a solid track record of growth, strong market position, and promising outlook in high-growth technology areas

Disclaimer



Our Commitment

recommendations, managed and presented by Milton Park Equities Pty Ltd (ABN 33 668 234 562), as a Corporate Authorised Representative of LeMessurier Securities Pty Ltd (ABN 43 111 931 849) (LemSec), holder of Australian Financial Services Licence No. 296877, offers insights and analyses formulated in good faith. Our evaluations and projections are grounded in the known facts at the time of creation and aim to provide a comprehensive view of the anticipated financial landscape in 2024. However, readers should be aware that these projections are estimates and may not fully materialize.

Scope and Application

The insights within MPC Markets are crafted for a broad audience and do not specifically cater to individual investment objectives, financial situations, or needs. Readers should consider the suitability of the advice in relation to their personal circumstances before making any investment decisions.

Research Integrity and Use

The research and content of MPC Markets are intended solely for our readers and should not be copied, distributed, or shared without proper attribution. While we strive to ensure accuracy and relevance, Milton Park Equities cannot guarantee the continuous updating or correction of the information or opinions expressed within the publication.

Disclaimer of Liability

Milton Park Equities, in its capacity as a Corporate Authorised Representative of LemSec, disclaims any responsibility for losses or damages arising from reliance on the opinions, advice, recommendations, or information—whether direct or implied—contained in the MPC Markets Discount Entry Note, notwithstanding any errors, omissions, or instances of negligence.

Analyst Objectivity

All research analysts contributing to the MPC Markets Discount Entry Note affirm that the views expressed represent their personal opinions regarding the subject companies and financial products covered in the publication.

Copyright and Usage Rights

The content of MPC Markets Discount Entry Note is the property of Milton Park Equities Pty Ltd, either through ownership or licensing agreements. Unauthorized reproduction, adaptation, linkage, framing, broadcasting, distribution, or transmission of this material is prohibited without express written permission from Milton Park Equities, except for personal use or as allowed by applicable laws.