

Skyfii Limited

Hits it out of the park in Q2, price target up to A\$ 0.25

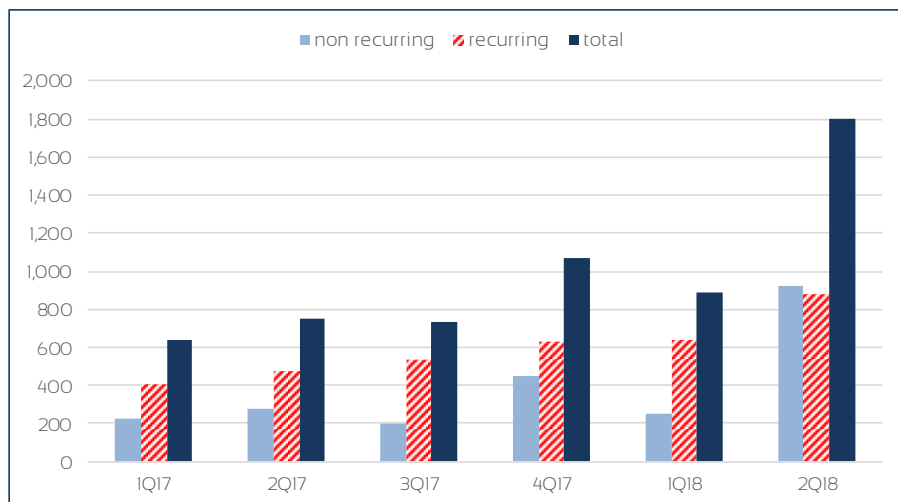
Skyfii (ASX:SKF) announced a strong set of results for 2Q18. Revenues amounted to A\$ 1.79M (+138% y-o-y, +102% q-o-q), driven by strong growth in non-recurring revenues, i.e. one-off provisioning fees charged to bring customer venues onto SKF’s IO platform.

Non-recurring revenues comprised of an estimated 124 new venues coming on stream in the quarter at an estimated average upfront provisioning fee of A\$ 6,600 each. We believe these new venues are predominantly related to the contract wins in Italy (supermarket chain), the UK (premier Quick Serve Restaurant) and the major shopping center group contract win in Europe.

Other non-recurring revenue was derived from Data Consultancy Services (DCS), which contributed A\$ 93k in revenues in Q2, up significantly from ~ A\$ 21k in Q1.

SKF saw its recurring year-on-year revenue growth rate accelerate during the quarter; from 55.5% in 1Q18 to 85.4% in Q2 to total A\$ 879k.

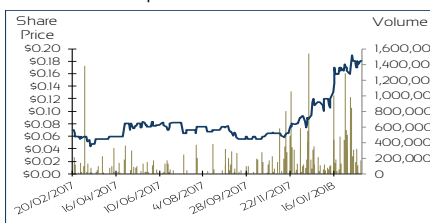
FIGURE 1: DEVELOPMENT OF RECURRING AND NON-RECURRING REVENUE



Source: Skyfii, TMT Analytics

While we expect non-recurring revenues from provisioning to remain lumpy from one quarter to the next, they do serve as a leading indicator for future recurring revenue growth. Hence, we expect a solid uptick in recurring revenues in 2HY18 driven by the firmly higher installed base of in-venue monitoring points and thus subscriptions to the IO platform.

Number of shares (m)	272.6
Number of shares FD (m)	303.9
Market capitalisation (A\$ m)	49.1
Free Float (%)	91%
12 month high/low A\$	0,19/0,044
Average daily volume (tr)	121.7



Skyfii Ltd.

(ASX:SKF)

Information Technology

Australia

Risk: High

Skyfii is an Australia-based, global technology company, which has developed a software platform that captures, analyses and visualizes location-based data within physical spaces. In addition, the platform provides actionable insights to its clients, which solve real business challenges and also provides a marketing platform to allow real time, contextual and targeted engagement with customers within these physical spaces.

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BUY

Current price: A\$ 0.18

Price target: A\$ 0.25

was (A\$ 0.14)

21 February 2018

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Solid revenue outlook

Regarding its revenue outlook, SKF indicated that the value of its FY18 contracted revenue stands at A\$ 4.8M per January 31, i.e. with five months left in the financial year to add to that total. This number is already well above the A\$ 3.2M operational revenues generated during the whole of FY17.

Our forecast for FY18 operational revenues stood at A\$ 5.5M and has been increased to A\$ 7M following SKF's Q2 results (see below).

On the cusp of becoming EBITDA positive

Over the last few quarters, SKF has been very stringent when it comes to costs and has been able to lift its EBITDA to +/- A\$ 300k in 1HY18, from +/- A\$ 1.8M in 1HY17 and +/- A\$ 1.9M in 2HY17. While this substantial improvement was in part driven by the strong non-recurring revenues during the quarter, which were approximately A\$ 600k above the average of the previous five quarters, we believe bootstrapping the business to conserve cash has also made a major contribution to the strong EBITDA improvement. We expect to see more detail around this when SKF releases its full 1HY18 accounts.

The company hasn't given a target date by which it expects the existing business excluding Causely (see below) to be EBITDA break even, but we anticipate SKF to achieve this milestone in the course of FY19 on a quarterly basis.

Expanding into the Banking vertical through contract win with HSBC Australia

In addition to the Shopping Center, Education, Museum, Transportation, Quick Serve Restaurant and Food Retail verticals, SKF has now also expanding into the Banking vertical. The company recently signed a three-year Master Services Agreement with HSBC Australia for the deployment of all three components of the IO Platform in the bank's 35 Australian branches.

We believe this vertical provides a major opportunity for SKF given the nearly 6,000 traditional bank branches in Australia alone. Obviously, the number of bank branches in Europe and the United States are substantially larger and we believe the HSBC win in Australia is likely to serve as an excellent use case for SKF's IO Platform in the Banking vertical.

Causely acquisition provides inroads into more than 1,800 US retail venues

On 5 February, SKF announced the all-scrip based acquisition of US-based marketing services company Causely, which serves 1,850 venues in the US. Causely provides venues, such as gyms, churches, smaller medical practices, restaurants and other retail outlets, with the ability to let customers contribute to a charity by checking into that venue on Facebook.

Causely's customers donate a predetermined amount to a specified charity for each of their customers' check-ins, with a monthly limit based on their subscription level, i.e. US\$ 100, US\$ 140 or US\$ 200 per month.

Consumers are incentivized to check into a venue on Facebook because of the charitable effect of their check-in, while the venues get substantially more Facebook check-ins than they would otherwise, which drives exposure to consumer eyeballs on Facebook.

Clear IO upsell opportunity for SKF

While SKF's marketing services, which are currently being developed, will be mostly data-driven as opposed to Causely's services that are an extension of Facebook marketing, we believe there is substantial opportunity for SKF to upsell the IO platform to Causely's existing customers. Firstly, the customer base is highly comparable where size is concerned. Furthermore, monthly costs of SKF's and Causely's services are comparable, i.e. both are SaaS models. There is likely also an opportunity to cross sell Causely to SKF's current customers.

A\$ 3.5M payment in scrip with a guaranteed minimum net profit of A\$ 2M

SKF has issued 25M shares at A\$ 0.14 (A\$ 3.5M) as payment for the acquisition. Part of the agreement with the Causely vendors is a minimum guaranteed net profit to SKF of US\$ 1.625M (A\$ 2M at an 0.80 exchange rate) in the first three years combined, or A\$ 0.68M per year.

In other words, SKF is paying -1.75x earnings for this acquisition, which we believe is a bargain given the substantial cross sell opportunities.

Furthermore, assuming a conservative average monthly revenue per venue of A\$ 90, Causely's 1,850 venues translate into A\$ 2M in annual revenues. Given the minimum net profit guarantee of A\$ 680k per year, Causely will generate net profit margins of around 34% for SKF, which we believe is very attractive, especially given the near-zero Capex that is required on the part of Causely.

SKF agreed to limit the vendors' downside risk to their new SKF shareholding by guaranteeing an additional 11M SKF shares in case the stock trades below A\$ 0.14 (30-day VWAP) in the period 30 July through 29 August 2018.

Contributing to the top line immediately

We expect the Causely acquisition to start contributing to the top line per 1 February and to bring in around A\$ 300k in 3Q18. For 4Q18 (June quarter) we expect Causely to contribute approximately A\$ 500k to SKF's top line. Our FY19 revenue estimate for Causely is A\$ 2.2M.

Lifting price target from A\$ 0.14 to A\$ 0.25 per share

In our initiation report in May 2017, we used a 15% WACC in our DCF model, which yielded a value of A\$ 0.18 per SKF share. Compared to May 2017 two key things have changed:

1. SKF is in the process of exceeding our initial top line projections by a wide margin. Our initial revenue projection for FY18 stood at A\$ 6.3M (including A\$ 0.8M in tax and R&D grants). Following the company's recent earnings call, we have increased our top line forecast to A\$ 7.7M (of which A\$ 0.8M in grants).
2. Furthermore, our EBITDA projection for FY18 has improved from -/- A\$ 4M to -/- A\$ 0.8M while the company was cash neutral in Q2 (December). The Causely acquisition will bring on some additional costs onto the P&L (4 FTE), but we believe SKF is properly capitalised at A\$ 2.75M to get to EBITDA positive territory. In turn, this has clearly improved SKF's risk profile, which provides room to lower our discount rate.

The model-generated (theoretical) WACC for SKF amounts to 8.6%. However, we feel this is still a bit too low for SKF, despite the substantial improvements in the company's risk profile. We believe a discount rate of 12% (down from 15%) is more reflective of the company's current position. This yields a value of A\$ 0.26 per share.

FIGURE 2: DISCOUNTED CASH FLOW SENSITIVITY ANALYSIS

8.6%	0.40
10%	0.33
11%	0.29
12%	0.26
13%	0.23
14%	0.21
15%	0.19

Source: TMT Analytics

Peer group suggests upside to A\$ 0.24

Looking at the FY19 valuation multiples for SKF's data analytics peer group, we can see a clear undervaluation for SKF. The peer group averages suggest a target value per SKF share of A\$ 0.24 (EV/Revenues) and A\$ 0.23 (EV/EBITDA) respectively.

FIGURE 3: PEER GROUP VALUATION

Company	Code	EV/Revenues FY19	EV/EBITDA FY19
Catapult Sports	CAT	2.7	20.7
Tableau	DATA	5.2	62.7
Splunk	SPLK	7.8	57.7
Alliance Data Systems	ADS	3.8	14.3
Average valuation		4.9	38.9
Skyfii	SKF	3.6	30.0

Source: TMT Analytics, S&P Capital IQ

While most of these peers are obviously substantially larger than SKF, and therefore less risky, we would argue that SKF's expected superior revenue growth profile in the next several years offsets this higher risk. On balance, we believe SKF should be valued at par with its peer group.

Reiterating our BUY rating

We increase our 12-month price target for SKF from A\$ 0.14 to A\$ 0.25 per share, based on the average of our DCF and peer group valuation. This implies an approximate A\$ 68M market capitalisation.

Given this strong share price upside of nearly 40%, we reiterate our Buy rating for SKF.

Skyfii Limited (A\$) FY-end June

Profit & Loss account	2017A	2018E	2019E	2020E
Revenues	4.1	7.7	13.1	18.8
EBITDA	-3.8	-0.8	1.6	6.2
<i>EBITDA %</i>	<i>-92.0%</i>	<i>-10.7%</i>	<i>11.9%</i>	<i>32.9%</i>
Depreciation & Amortisation	-1.1	-1.0	-1.2	-1.1
EBIT	-4.9	-1.9	0.4	5.1
<i>EBIT %</i>	<i>-119.9%</i>	<i>-24.2%</i>	<i>3.1%</i>	<i>27.3%</i>
Interest income & expense net	0.0	0.0	0.0	0.0
Other items	0.0	0.0	0.0	0.0
Profit before Tax	-4.9	-1.8	0.4	5.2
Taxes	0.0	0.0	-0.5	-1.8
Net earnings	-4.9	-1.8	0.0	3.3
Ordinary shares outstanding	211	273	273	273
Fully diluted # shares	214	304	304	304
Earnings per share	-0.023	-0.007	0.000	0.012
Earnings per share fully diluted	-0.023	-0.006	0.000	0.011

Cash Flow Statement	2017A	2018E	2019E	2020E
Net income P&L	-4.9	-1.8	0.0	3.3
Depreciation & amortisation	1.1	1.0	1.2	1.1
Impairments	0.0	0.0	0.0	0.0
Change in working capital	0.9	1.0	0.3	0.8
Other items	0.5	0.0	0.0	0.0
Cash flow from operations	-2.4	0.2	1.4	5.2
Net cash flow from investments	-1.7	-3.5	-0.3	-0.5
Dividend paid	0.0	0.0	0.0	0.0
Change in equity	3.7	3.5	0.0	0.0
Change in debt	0.0	0.0	0.0	0.0
Other items	0.0	-1.2	0.0	0.0
Cash flow from financing	3.7	2.3	0.0	0.0
Net cash flow	-0.4	-1.0	1.1	4.7

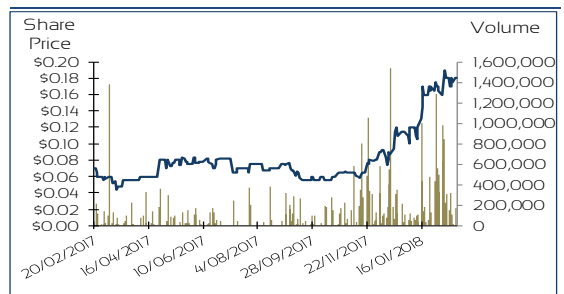
Balance Sheet	2017A	2018E	2019E	2020E
Current assets				
Cash and marketable securities	2.3	1.3	2.4	7.1
Accounts receivable	2.2	1.3	2.0	2.6
Inventories	0.0	0.0	0.0	0.0
Other current assets	0.1	0.3	0.5	0.3
Total current assets	4.7	2.8	4.9	10.0
Fixed assets				
Net property, plant & equipment	0.2	0.1	0.1	0.0
Goodwill	0.0	0.0	0.0	0.0
Other intangible assets	3.3	5.8	5.0	4.5
Other assets	0.0	0.0	0.0	0.0
Total fixed assets	3.5	5.9	5.1	4.5
Total assets	8.1	8.8	9.9	14.5
Current liabilities				
Short-term debt	0.0	0.0	0.0	0.0
Accounts payable	0.7	0.8	0.9	1.6
Dividends payable	0.0	0.0	0.0	0.0
Other current liabilities	0.2	0.8	0.8	1.3
Total current liabilities	1.6	1.7	2.9	4.2
Long-term debt	0.0	0.0	0.0	0.0
Total provisions	0.2	0.2	0.2	0.2
Total group equity	6.4	6.9	6.8	10.2
Total liabilities and equity	8.1	8.8	9.9	14.5

Valuation	2017A	2018E	2019E	2020E
Relative valuation				
P/E (reported)	N/M	N/M	N/M	14.8
P/B	6.0	7.2	7.2	4.8
P/CF	N/A	256.8	34.1	9.4
Price to sales	9.3	6.4	3.7	2.6
EV / sales	11.5	6.2	3.6	2.2
EV / EBITDA	N/A	N/A	30.0	6.8
Dividend yield	0.0	0.0	0.0	0.0
EV / EBIT	N/A	N/A	116.1	8.2
Discounted Cash Flow				
<i>Assumptions</i>				
Long term interest rate				2.5%
Risk premium				4.3%
Marginal tax rate				30.0%
Long term growth				3.0%
Leveraged Beta				1.39
Implied WACC				8.6%
TMT Analytics applied WACC				12%
DCF fair value range per share				A\$ 0.26

Profitability ratios	2017A	2018E	2019E	2020E
Return on Equity	-77%	-26%	0%	33%
Return on Assets	-60%	-21%	0%	23%
Return on Invested Capital	-67%	-23%	0%	58%
EBITDA margins	-92.0%	-10.7%	11.9%	32.9%
EBIT margins	-119.9%	-24.2%	3.1%	27.3%
Net margins	-120.1%	-23.6%	-0.2%	17.7%

Financial Strength	2017A	2018E	2019E	2020E
Net debt (cash)	-2.3	-1.3	-2.4	-7.1
Net debt / Equity	-0.4	-0.2	-0.4	-0.7
Net debt / EBITDA	0.6	1.6	-1.6	-1.2
Interest coverage	N/M	N/M	N/M	N/M

Capital Structure	
Ordinary shares	273
ESP shares	26
Options and warrants (m)	5
Fully diluted	304
Market capitalisation (A\$ m)	49.1
Market cap. fully diluted (A\$ m)	54.7
Free float %	91%
12 month high/low A\$	0.19/0.044
Average daily volume (tr)	121.7



Source: Factset, TMT Analytics

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