TMT ANALYTICS

Skyfii Limited

EBITDA break even in June quarter...more room to invest in growth now

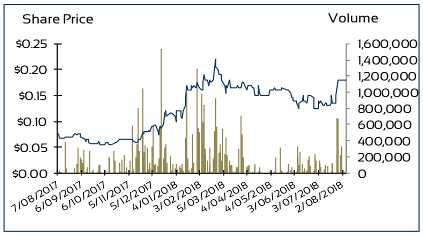
In its results announcement for 4Q18 (June quarter) on 25 July, Skyfii (ASX:SKF) reported its first ever break even result at the EBITDA level. The company has been very cost-conscious in the last two years, almost to the point of being bootstrapped, to avoid raising additional capital and prove the business model can operate profitably. While many investors prefer to see companies reach EBITDA break even as soon as possible, we believe highly leverageable businesses, such as SKF's, are likely to see their growth inhibited as a result of a very strong focus on costs.

In other words, now that SKF has reached the EBITDA break even level, and can operate cash neutral at the very least, we hope to see the focus shift more towards additional topline growth. We discussed this topic with SKF CEO Wayne Arthur in the interview below.

Click below to view our interview with SKF CEO Wayne Arthur

Even though SKF has been very cost-conscious in the last two years, the current cost-base should support another 25% to 30% of revenue growth. Recurring revenue growth should pretty much take care of itself as it is subscription-based. Beyond that 25% growth, we expect the company will need to make additional FTE investments, e.g. in sales and support staff. In other words, in addition to a growing network of channel partners who provide reach and revenue growth at a relatively low cost, given our revenue growth projections for FY19, we expect SKF will be expanding its front-office capabilities shortly.

Number of shares (m)	273.3
Number of shares FD (m)	306.3
Market capitalisation (A$ m)	49.2
Free Float (%)	91%
12 month high/low A$	0,205/0,044
Average daily volume (k)	153.0



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Flash Note

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

7 August 2018

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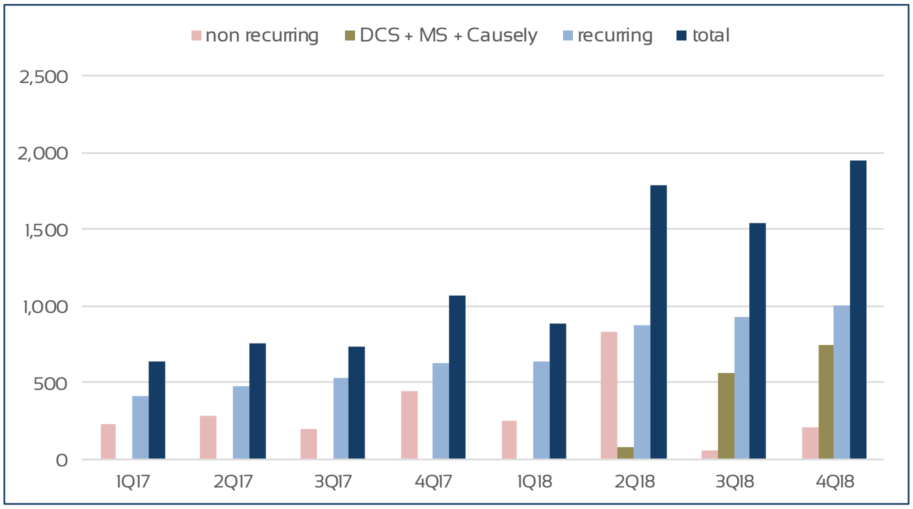
Recurring revenue growth consistently above 50% in FY18

Revenues in 4Q18 amounted to A$ 1.95M, bringing the total for FY18 to A$ 6.17M, an increase of 92% y-o-y. While this is a very impressive growth rate in itself, we are even more encouraged by the y-o-y growth rate of quarterly recurring revenues from SKF's I/O platform. This growth has been consistently above 50% y-o-y in each quarter in FY18, actually reaching 85.4% in 2Q18. We estimate these recurring revenues to be SKF's highest margin business bedded down in long term contracts.

FIGURE 1: UNINTERRUPTED RECURRING REVENUE GROWTH IN LAST 8 QUARTERS

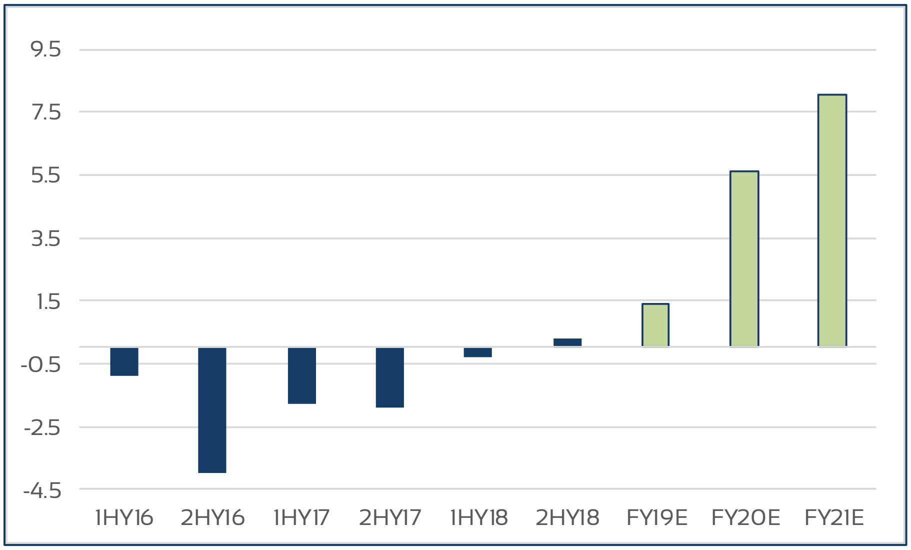


Source: TMT Analytics, SKF

EBITDA positive for the first time ...

During 4Q18 SKF achieved a positive EBITDA result for the first time since its inception (see Figure 2). The company generated A$ 0.3M in 2HY18 EBITDA following -/- A$ 0.3M in 1HY18 and -/- A$ 1.9M in 2HY17. This is clearly better than our -/- A$ 0.8M estimate for FY18.

FIGURE 2: DEVELOPMENT OF EBITDA



Source: TMT Analytics, SKF

… leaves more room to invest in growth

Going forward, we expect SKF to run the company on an EBITDA-positive basis, while investing "excess" EBITDA, say above A$ 300k-500k, back into the business. In other words, we expect accelerated investment in revenue growth now that the company no longer has to prove to the market it can operate cash neutral.

We expect this minimum EBITDA level to be achieved on the back of the company's high level of recurring revenues (55.8% of total revenues in FY18). Recurring revenues are subscription-based, typically bedded down in long term contracts and are highly automated. In other words, SKF has good visibility of its recurring revenues and indicated that the current annualized recurring revenue run rate is A$ 1M per quarter.

> *In addition to a backlog of A$ 1.9M in Non-recurring and Services revenues, this already brings the total booked revenues for FY19 to A$ 5.9M at the start of this financial year, i.e. close to the A$ 6.17M SKF recorded for the whole of FY18.*

Substantial contract wins and expansions in 4Q18

During the last quarter, SKF won significant new business and expanded several existing contracts, including Precision Group (3-year contract for 5 shopping malls), Lewis Land Group (3-year contract for 2 shopping malls), Versace (initial 12-month contract for 45 retail outlets), Nuffield Health (contract extension to 142 venues), an unnamed leading Italian service station (210 venues), a smart city solution for the city of Covington, Kentucky (USA) and Nando's (2-year contract for 120 venues initially and an option to add 100 franchisee-owned restaurants). Post-closing of 4Q18, Nando's has extended its contract with SKF to include 400 additional restaurants.

We believe that, on the back of such contract wins and expansions, SKF will be able to experience multiple years of very strong revenue growth (Figure 3) and improvements in operating results.

FIGURE 3: SUMMARY OF P&L ACCOUNT

A$ M	2016A	2017A	2018F	2019F	2020F
Revenues	3.3	4.1	6.2	10.4	15.6
EBITDA	-1.9	-3.8	0.0	1.3	5.2
EBITDA margins	-58%	-92%	0%	13%	34%
NPAT	-5.4	-4.9	-1.0	-0.2	2.7
EPS fully diluted (c)	-0.04	-0.02	-0.003	-0.001	0.01

Source: TMT Analytics

Services revenues starting to contribute in a meaningful way

In addition to revenues from the I/O platform growing fast, we can see Services revenues starting to become increasingly meaningful. Services revenues consist of Data Consultancy Services (DCS), Marketing Services and revenues from recently acquired Causely and contributed A$ 746k to revenues in 4Q18, up from A$ 80k and A$ 561k in the two preceding quarters respectively.

As SKF's installed base of venues using the I/O platform grows, we can see increasing opportunities for the company to sell its Marketing Services on the back of data generated through the I/O platform. Similarly, as SKF further integrates Causely and expands cross sell, the increasing amount of visitor data generated through Causely's more than 1,800 customer venues should also enable SKF to increase revenues from Marketing Services going forward.

Lastly, we expect DCS projects to increase in number and in size as SKF's client base grows, driving revenues from consultancy services.

Reiterating our BUY rating and A$ 0.25 price target

Based on SKF's solid performance in 4Q18 and the company's milestone of reaching EBITDA break even, we expect to see a growth acceleration in FY19. Additionally, we may see bolt-on acquisitions that would expand the company's customer base in Europe and the US in particular.

SKF is making clear headway with its strategic plan that should see the company becoming a dominant player in certain verticals, e.g. Australian shopping Malls, while expanding into others, such as QSR (Quick Serve Restaurants).

In our view, the way the company has been able to bootstrap over the last twelve months, while maintaining strong top line growth, is testament to strong management which has flawlessly executed on its plans.

For these reasons, we reiterate our 12-month price target of A$ 0.25 per share as well as our Buy rating for SKF.

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