EDISON

migme

H116 results

Funded until cash positive in FY17

Software & comp services

migme (MIG) is a global social media company employing a freemium model to drive user engagement. It is focused on the emerging markets of Indonesia, the Philippines and India. At 30 June 2016 monthly active users (MAUs) totalled 43 million, an increase of 34% in the last year (32 million in December 2015) and number of artists and verified users increased to 2,900 up 368% since 31 December 2015). On 19 August 2016 MIG raised A$10.2m from an issue of shares at A$0.40/share.

Year end	Revenue (A$m)	PBT* (A$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/15	12.3*	(21.0)	(7.9)	0.0	N/A	N/A
12/16e	46.0	(16.5)	(3.6)	0.0	N/A	N/A
12/17e	103.9	9.9	2.1	0.0	11.4	N/A
12/18e	171.7	37.7	8.0	0.0	3.0	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments. *includes other income

Where to from here?

MIG has successfully built a user base of 43 million, signed some 2,900 artists onto the platform and generated revenue for the last six months of A$14.9m. In the last six months costs grew by A$11.3m compared with revenue growth of A$5.7m and MIG continued to make gross operating losses. The company has incurred A$27.8m operating cash losses in the last 18 months to 30 June 2016. These losses have been funded by equity raises, including funds raised at IPO of A$44m. We understand that MIG expects to reduce the operating cash flow deficits and become cash flow positive in 2017, which is in line with our forecast. The June 2016 quarterly net cash outflows were A$5.1m. Cash on hand at 30 June 2016 was A$4.7m and the August 2016 capital raise brought in another A$10.2m, which could see the company through to profitability.

Valuation: Market continues to adopt a ‘wait and see’ approach

In our view, MIG’s current share price does not reflect the success it has achieved to date in building both MAU and revenue. We believe the market is waiting for more proof that it is possible to increase monetisation of the user base via MIG’s freemium model strategy. MIG has not yet produced positive gross margin and there is therefore concern about the viability of the business model, including the cost of customer acquisition and the revenue share required to attract and retain artists. As MIG provides proof that there is a clear path to profitability, the gap should begin to close between the share price and our DCF valuation of A$1.78/share (WACC of 13.1%, terminal growth rate of 2% and 54% of DCF accounted for by the terminal value.)

7 September 2016

Price	**A$0.24**
Market cap	**A$76m**

US$1.00/A$0.75

Net cash (A$m) post-capital raise of A$10.2m in August 2016	12.9
Shares in issue	316m
Free float	45%
Code	MIGT
Primary exchange	ASX
Secondary exchange	Frankfurt

Share price performance

%	1m	3m	12m
Abs	(48.9)	(54.3)	(78.4)
Rel (local)	(48.2)	(54.9)	(80.1)
52-week high/low		A$1.15	A$0.24

Business description

migme is a social entertainment platform targeting the world’s next wave of internet users, the 3.5 billion people in emerging markets. The service offers free chat, content and blogging services to acquire users. Users buy virtual goods and engage in gaming and e-commerce.

Next events

Quarterly results	October 2016

Analysts

Moira Daw	+61 (0)2 9258 1161
Bridie Barrett	+44 (0)20 3077 5700

tech@edisongroup.com

Edison profile page

migme is a research client of Edison Investment Research Limited

H116 results

Highlights from the H116 results included:

- revenue of A$14.9m, which was A$5.7m (63%) more than revenue for the preceding six months;
- half-on-half MAU growth of 34% in the last six months to 43 million (from 32 million);
- net operating cash outflows of A$10.7m compared with net operating cash outflows of A$7.5m for the six months to 30 June 2015; and
- net loss after tax of A$13.6m compared with net loss after tax of A$8.8m for H115.

Exhibit 1: H116 results

A$m	Total 18 months	6m to 30-Jun-16	6m to 31-Dec-15	6m to 30-Jun-15
Revenue	27.2	14.9	9.3	3.0
COGS	(34.1)	(21.1)	(6.3)	(6.8)
Gross profit	(6.9)	(6.1)	3.0	(3.8)
Other income	0.1	0.0		0.0
R&D	(3.6)	(1.8)		(1.7)
Administration	(7.7)	(4.6)		(3.1)
Other expenses	(11.4)	(0.6)	(10.6)	(0.2)
EBIT	(29.6)	(13.2)	(7.6)	(8.8)
Interest	(0.5)	(0.4)	(0.1)	0.0
Loss before tax	(30.1)	(13.6)	(7.6)	(8.8)
Income tax expense	4.9	(0.0)	4.9	(0.0)
Net loss	(25.1)	(13.6)	(2.7)	(8.8)
Operating cash flow	(27.8)	(10.7)	(9.6)	(7.5)
Investing cash flows	(0.9)	(1.3)	0.1	0.3
Financing cash flows	24.4	8.3	9.6	6.6
Cash on hand	4.7	4.7	5.5	5.4
No of MAU (period end)	43.0	43.0	32.0	19.0
MAU inc in six months		34%	68%	90%
Revenue increase in six-month periods		61%	206%	237%
Exp increase in six-month periods		67%	42%	91%
Revenue increase in six months (A$m)		5.7	6.2	2.2
Exp increase in six months (A$m)		11.3	5.0	5.6
Total costs	(56.8)	(28.2)	(16.8)	(11.9)

Source: migme accounts

Capital raises

The table below shows capital raises since listing. The average issue price has been A$0.43 per share. The August 2016 capital raise of A$10.2m included support from Meitu (A$2m) and A$4.5m from strategic investors including FIH Mobile (Foxconn), PT Media Nusantar Tbk and Malcolm Steinberg, the proprietor of the LAI group. The balance of A$3.7m was raised from sophisticated investors.

Exhibit 2: Capital raises since IPO

Capital raises	No shares (m)	Per share (A$)	Gross A$m raised
IPO (August 2014)	40.0	0.20	8.0
Apr-15	10.4	0.67	7.0
Nov-15	10.1	1.00	10.1
Mar-16	11.7	0.60	7.0
Jun-16	5.0	0.40	2.0
Aug-16	25.6	0.40	8.2
Total	102.8	0.43	44.3
Convertible note (Dec 15)	3.2	1.10	3.5

Source: migme data

Forecast changes

We have not changed our forecasts of revenue and costs. The only change to our forecasts has been the inclusion of the August 2016 capital raise of $10.2m (25.6m shares at A$0.40/share)

Outlook

Management has stated that it will concentrate on deepening user engagement by adding more games and apps to the platform. The focus will turn to reducing operating cash outflows and improving operating margins, while continuing to grow user numbers and the rate of monetisation. Management now expects to reach cash flow-positive operations in 2017.

Valuation: At odds with comparative pricing

The current share price of A$0.24 is 40% less than A$0.40 price of the capital raise and, in our view, the current market valuation for MIG is at odds with the price that the market has paid for comparable companies at a similar stage in their life cycle.

At the same early stage in their life cycle the comparable group grew revenues by an average of 41% (range 25% to 199%) compared with MIG's revenue growth rate of 975% (using Q414 compared with Q415) and 273% using FY15 compared with FY16e. In terms of MAUs, the comparable group increased MAUs by an average of 28% (range minus 21% to 199%) compared with a 220% increase in MIG's MAUs in FY15.

Like the best in class in its comparable group, we suggest that MIG has the building blocks in place for success, including a full suite of products and a payments platform which, in our view, should enable it to convert users attracted to its platform into monetising users via the freemium model. It is operating in markets where there is competition from global players such as Facebook, but has achieved notable early success by capturing 43 million MAUs, which is ~16% of active social media users in its target markets (estimated to be 267 million users).

We have identified Tencent and Momo as the companies that have a business model closely allied with MIG's business model (see our note Success to date undervalued by market published on 15 April 2016). Using the pricing applied by the market to these companies at a similar stage in their life cycle results in a valuation range for MIG of A$1.41 to A$2.29 per share if we use EV/revenue multiples. If we use EV/MAU, the valuation range is A$2.67 to A$2.92 per share for MIG. However, we believe that some caution should be exercised because MAU does not take into account monetisation rates, spend per user or changes in the time value of money. For example, the amount spent per user by Tencent in 2005 (as the second year of operations in the comparative table) was US$0.88, compared with Momo (2015) at US$0.94, YY.com (2012) at US$3.27 and Renren (2012) at US$0.90.

Exhibit 3: MIG pricing using comparative company EV/revenue and EV/AU multiples (Year 2 of operations)

	MIG	Tencent	Momo	YY.com	Renren
	2016e	2005	2015	2012	2012
Operating metrics					
Revenue growth	273.0%	25.0%	199.0%	159.1%	43.0%
Revenue (US$m)	34.9	176.8	134	131.6	159.5
MAU (m)	69	201.9	70	69	56
Implied EV/revenue multiple (x)	1.4	8.9	14.3	9.8	19.2
Implied EV/MAU multiple (x)	0.9	11.1	12.1	42	15.5
MIG's EV using peer group multiples					
EV (A$m) applying peer EV/revenue (x) to MIG	63	408.5	657.7	449.8	881.3
EV (A$m) applying EV/MAU to MIG	63	765.9	834.9	2,898.0	1,073.2.
MIG share price using peer group EV/revenue	$0.24	$1.42	$2.29	$1.56	$3.07
MIG share price using peer group EV/MAU	$0.24	$2.66	$2.90	$10.08	$3.74

Source: Edison Investment Research, Bloomberg. The EV of MIG is calculated as 316m shares x A$0.24 less net cash of A$12.9m after the August 2016 capital raise of A$10.2m. Note: The comparative years are the second year of operation for each of the companies, which is comparable with MIG's second year of operation.

Importantly, in determining these valuation ranges, we have not adjusted for the broader and industry-specific market conditions as well as for investor sentiment, which to some extent will be driven by the supply of opportunities and the capital available. In our view, there is now some evidence of a cooling in market sentiment and more of a focus on the path to profitability rather than top-line growth or growth in the number of MAU.

DCF valuation

Our DCF valuation of A$1.78 per share (previously A$1.93 per share) reflects the additional shares issued in August 2016 following the capital raise of A$10.2m. This valuation should be viewed in the context of the comparable company valuation ranges of A$1.41 to A$2.29 (using EV/revenue multiples of between 8.9x and 14.3x) and A$2.67 to A$2.92 (using EV/MAU of 11.1x to 12.1x). MIG's current price assumes an EV/revenue multiple for FY16e of 1.4x and an EV/MAU of 0.9x.

Exhibit 4: Updated DCF valuation (A$m)

Sum of PV	256.1
Terminal value	1,026.6
Discount factor for TV	0.292
PV of terminal value	299.8
PV of enterprise value	555.9
Net cash (at end FY15)	5.5
Equity value	561.4
Number of shares in issue (m)	316.0
NPV	A$1.78

Source: Edison Investment Research

Sensitivities

Initial signs are encouraging; however, this is an early-stage business competing in a fast-moving market with an established competitor, albeit one using a different business model. MIG is not immune to competition from regional players, and changes in strategy by established ones could have a meaningful impact on its prospects. Approximately 75% of MIG's operating costs of ~A$21m pa (excluding cost of goods sold) are fixed; therefore, any swing in activity levels will have a significant impact on earnings and valuation. We have incorporated in our forecasts an increase in gross margin from the current state, where gross margin is negative, to a gross margin of 35% by

FY18. The improvement in gross margin is driven by a reduction in the proportion of revenue paid to artists who sign on to the migme platform.

Exhibit 5: Financial summary

A$000s	2014	2015	2016e	2017e	2018e
31 Dec	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue	1,953	12,300	45,962	103,925	171,734
Cost of Sales	(605)	(13,043)	(40,398)	(71,001)	(110,730)
Gross Profit	1,347	(744)	5,564	32,924	61,004
EBITDA	(28,597)	(21,021)	(16,320)	9,940	37,173
Operating Profit (before amort. and except.)	(16,017)	(20,930)	(16,363)	9,900	37,135
Intangible Amortisation	0	0	0	0	0
Exceptionals	0	0	0	0	0
Other	0	0	0	0	0
Operating Profit	(16,017)	(20,930)	(16,363)	9,900	37,135
Net Interest	0	(20)	(87)	4	544
Profit Before Tax (norm)	(16,017)	(20,950)	(16,450)	9,904	37,679
Profit Before Tax (FRS 3)	(28,597)	(21,313)	(16,450)	9,904	37,679
Tax	(32)	(3)	4,935	(2,971)	(11,304)
Profit After Tax (norm)	(16,048)	(20,680)	(11,515)	6,933	26,375
Profit After Tax (FRS 3)	(28,629)	(21,043)	(11,515)	6,933	26,375
Average Number of Shares Outstanding (m)	251.6	262.7	316.0	326.7	330.2
EPS - normalised (c)	(6.38)	(7.87)	(3.64)	2.12	7.99
EPS - normalised and fully diluted (c)	(5.95)	(7.33)	(3.43)	2.05	7.79
EPS - (IFRS) (c)	(11.38)	(8.01)	(3.64)	2.12	7.99
Dividend per share (c)	0.0	0.0	0.0	0.0	0.0
Gross Margin (%)	69.0	-6.0	12.1	31.7	35.5
EBITDA Margin (%)	-1464.3	-170.9	-35.5	9.6	21.6
Operating Margin (before GW and except.) (%)	-820.2	-170.2	-35.6	9.5	21.6
BALANCE SHEET					
Fixed Assets	646	1,077	5,971	5,933	5,898
Intangible Assets	0	326	326	326	326
Tangible Assets	502	583	542	504	469
Investments	145	168	5,103	5,103	5,103
Current Assets	6,539	9,419	11,875	21,853	54,014
Stocks	0	100	0	0	0
Debtors	0	0	0	0	0
Cash	5,926	8,658	11,214	21,192	53,353
Other	613	661	661	661	661
Current Liabilities	(1,593)	(2,931)	(4,586)	(6,093)	(9,386)
Creditors	(1,352)	(1,694)	(3,348)	(5,884)	(9,177)
Short term borrowings	0	0	0	0	0
Other current liabilities	(241)	(1,238)	(1,238)	(209)	(209)
Long Term Liabilities	0	(3,178)	(3,178)	0	0
Long term borrowings	0	(3,178)	(3,178)	0	0
Other long term liabilities	0	0	0	0	0
Net Assets	5,593	4,387	10,082	21,693	50,526
CASH FLOW					
Operating Cash Flow	(11,074)	(17,065)	(14,565)	11,448	40,465
Net Interest	0	0	(87)	4	544
Tax	(143)	(10)	0	(2,971)	(11,304)
Capex inc R&D	(506)	(328)	(2)	(2)	(2)
Acquisitions/disposals	9,344	411	0	0	0
Financing	11	16,146	17,210	1,500	2,458
Dividends	0	0	0	0	0
Net Cash Flow	(2,368)	(846)	2,555	9,978	32,161
Opening net debt/(cash)	(2,182)	(5,926)	(5,480)	(8,036)	(21,192)
HP finance leases initiated	0	0	0	0	0
Other/ Conv note converted to equity	(1,376)	400	0	3,178	0
Closing net debt/(cash)	(5,926)	(5,480)	(8,036)	(21,192)	(53,353)

Source: migme, Edison Investment Research. Note: COGS does not include marketing costs and revenue includes ‘other income’. Our forecasts assume that options are converted at their expiry date.

Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
245 Park Avenue, 39th Floor
10167, New York
US

Sydney +61 (0)2 9258 1161
Level 25, Aurora Place
88 Phillip St, Sydney
NSW 2000, Australia

Wellington +64 (0)48 948 555
Level 15, 171 Featherston St
Wellington 6011
New Zealand