EDISON

migme

Quarterly update

Monetisation rates up

Software & comp services

migme (MIG) is a global digital media company focused on emerging markets. By taking a different approach to the more established Facebook, MIG believes its platform will have little competition for its freemium offering. This approach is validated by the rapid growth in user numbers, which have increased from >5m on listing in August 2014 to >19m at 30 June 2015. Monetisation rates continue to build, with Q215 revenues up 95% on Q115 revenues. The number of users and the spend per user are ahead of our forecasts, but monetisation rates are less than expected due to delays in putting payment systems and other infrastructure in place.

Year end	Revenue (A$m)	PBT* (A$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/14	2.0	(0.4)	(1.5)	0.0	N/A	N/A
12/15e	9.0	(12.1)	(3.3)	0.0	N/A	N/A
12/16e	33.2	(1.6)	(0.4)	0.0	N/A	N/A
12/17e	66.0	13.7	3.7	0.0	33.2	N/A

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

Growth in user numbers

MIG continues to demonstrate that it can grow monthly active users (MAUs) and is currently adding users at the rate of 1.3m/month. The number of MAUs at 30 June 2015 is 33% ahead of our forecasts, but the monetisation rate of ~0.2% is less than our forecast of 3%. The spend per monetising customer was A$41.60 in Q115 compared with our forecast of A$2.40. In the same time period the number of audience builders (artists) increased from 150 to 400 and two new territories were added – India and the Philippines. MIG believes it can achieve monetisation rates of 1% in line with the monetisation rates achieved by YY.com, Momo and 9158.com. If the monetisation rate lifts to 1% the number of monthly paying users (MPUs) would increase from the Q115 level of 27,000 to 140,000. MPU numbers were not released for Q215.

Funding – A$5.4m on hand at 30 June 2015

Revenues in Q215 grew by 95% to A$2.2m, while costs grew from A$4.3m in Q115 to A$6.4m in Q215. We expect that the cash burn rate will decrease in line with increases in the number of MPUs.

Valuation: Early stages of commercialisation

Our previous DCF valuation range of bear case A$0.42/share to blue sky case A$1.03/share was based on user number monetisation rates and operating costs. The assumptions used in our previous analysis were based on limited data and as a result we underestimated both user numbers and spend per user, but overestimated the proportion of users spending money on virtual goods/games. We have factored these changes into our model, rebuilt our cases and now have a range from the current share price case of A$1.23/share to a blue sky or bull case of A$2.32/share. The DCF value implied by our forecasts, which are considered a base case, is A$1.75/share.

10 August 2015

Price	**A$1.23**
Market cap	**A$324m**

Net cash (A$m) at 30 June 2015	A$5.4m
Shares in issue	263.2m
Free float	72%
Code	MIG/A117AB
Primary exchange	ASX
Secondary exchange	Frankfurt

Share price performance

%	1m	3m	12m
Abs	13.6	86.6	212.5
Rel (local)	15.5	92.5	214.1
52-week high/low		A$1.30	A$0.30

Business description

MIG is a social entertainment platform targeting the world's next wave of internet users, the 3.5bn people in emerging markets. The service offers free chat, content and blogging services to acquire new users. These users buy virtual goods including gifts, games, avatar items, emoticons and stickers.

Next events

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Quarterly report – Q215

The key messages from the Q215 cash flows report and the operations update are:

- an average of 1.3 million users were added each month in Q215 to a total of >19 million MAUs at 30 June 2015;
- as at the date of the release of the Q215 report (30 July 2015), the number of MAUs had increased to >20 million;
- most of the audience growth came from Indonesia, India and the Philippines;
- India and Philippines are the newest markets. Promotional and marketing programmes and the signing of more artists are expected to see the number of MAUs grow significantly in Q315 and beyond;
- in India MIG has established a partnership with CAA Kwan (celebrity and sports management agency) and has entered into a partnership with Sony Music India;
- in the Philippines four artists have been signed: singer songwriter BP Valenzuela, alternative rock band Save Me Hollywood, TV celebrity Fay Hokulani and blogger Flow Galindez;
- operating costs during Q215 were A$6.4m compared with A$4.4m in Q115; and
- the business is expected to break even in the first half of FY16 as "higher margin services are expected to outweigh market development costs and activities."[1]

Exhibit 1: MIG – key performance indicators

	Listing date	Q314	Q414	Q115	Q215
Monthly active users (MAUs) (m)	>5	>7	>10	>14	>19
Average monthly paying users (MPUs) (000s)		33	33	27	N/P
Number of artists/verified users		>30	>150	>380	>400
Cash receipts from operations (A$000s)		306	565	1,125	2,201
Net operating cash inflows/(outflows) (A$000s)		(1,613)	(3,723)	(3,240)	(4,208)
Net other cash inflows/(outflows) (A$000s)		801	-265	339	6497
Cash on hand (A$m)	11.0	9.7	5.9	3.2	5.4
Monthly increase in MAUs (m)			1.0	1.3	1.7
Quarterly increase in cash receipts (%)			85%	99%	96%
Australian cents per MAU			5.65	8.04	11.58
A$ per MPU			17.1	41.7	N/P

Source: MIG Quarterly Operations Update, 30 July 2015

Forecast changes

We have changed our forecasts to incorporate the current information on users, monetisation rates and operating costs. The company has stated in its Quarterly Operations Update that it expects to reach break-even in the first half of FY16. We have been conservative and still show a small operating loss for FY16 of A$1.0m, followed by a significant uplift in profitability from FY17 onwards as user monetisation and spends continue to build.

Our initial modelling carried out in December 2014 was based on limited data. MIG is operating a new model in new territories and as such we believe there could be unexpected changes in the key variables that drive the business. These include the number of MAUs, the number of MPUs and the amount spent per user. The revenue is lower than we expected because there have been some delays in opening new territories and putting in place payment systems and other infrastructure. The company expects revenue will begin to build rapidly, with operations established in Indonesia, the Philippines and India. It expects the operations to reach break-even sometime in H216 and that

[1] MIG Quarterly Operations Update, 30 July 2015.

by FY17 there will be evidence of the operating leverage inherent in the business model, which is based on driving more paying users through the same infrastructure.

Details of our forecast changes are set out in Exhibit 2 below.

Exhibit 2: MIG – forecast changes

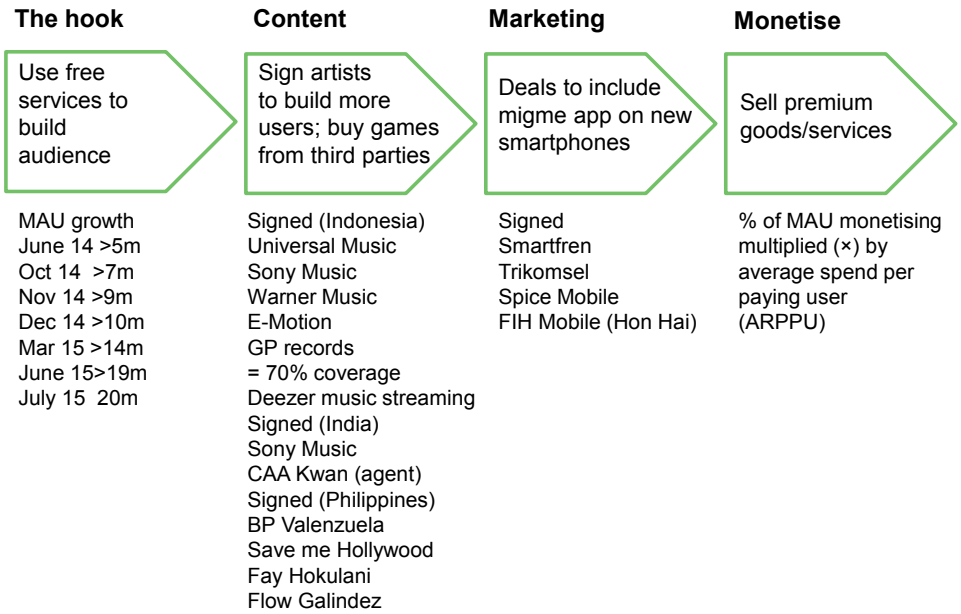
	2015e	2016e	2017e	2018e
Previous forecasts				
Revenue	11,837	35,024	56,498	73,490
Profit before tax	(5,669)	3,835	13,176	20,132
EPS (c)	(1.5)	1.0	3.5	5.4
DPS (c)	-	-	-	-
Current forecasts				
Revenue	8,995	33,176	66,022	110,776
Profit before tax	(12,145)	(1,575)	13,747	34,955
EPS (c)	(3.3)	(0.4)	3.7	9.3
DPS (c)	-	-	-	-
Variance				
Revenue	(24.0%)	(5.3%)	16.9%	50.7%
Profit before tax	114.2%	(141.1%)	4.3%	73.6%
EPS (c)	(1.8)	(1.4)	0.2	3.9
DPS (c)	-	-	-	-

Source: Edison Investment Research

Investment case

MIG's investment case is based on the premise that there is room for more than one social media platform in the emerging markets of Indonesia and India. There is precedent in China, where in large regions two or three exist in parallel. The large and fast-growing mobile markets in Indonesia and India have a high propensity to use social media, and there may be room for a new entrant. MIG's platform look is distinct from Facebook and its business model, which is geared more towards celebrity, games and blogging, could prove appealing to an Asian audience. With its revenue share business model for artists, it offers them a low-risk approach to developing new revenue streams, and initial artist take-up from 30 in September 2014 to >400 in June 2015 is very encouraging. Its addressable market in Indonesia and India is large (294 million smartphone users by 2017 as forecast by www.statista.com) and could increase further should MIG expand into other countries in South Asia, South-East Asia and Africa. The increase in MAUs from over five million in June 2014 to more than 20 million in July 2015, and management's expectation that MAUs will grow by more than one million per month in the short to medium term, provides evidence of the strength of the market and the appeal of migme's product. The content deals with music artists and record companies, plus the sale of smartphones with pre-loaded free migme apps (covering about 50% of the smartphones shipped in Indonesia) should underpin near-term user growth. That said, this is a very early-stage business, pitted against a strong and established competitor in a fast-changing market. If it succeeds, the rewards could be significant, but the risks are considerable.

Exhibit 3: MIG – Business model



Source: Edison Investment Research

Strengths, weaknesses, opportunities, threats

Exhibit 4: MIG – SWOT analysis

Strengths	Opportunities
FIH (Hon Hai) shareholding of 19.9% adds credibility/pre-load possibilities	Continues to add content to platform
50% Indonesian smartphone shipments have migme app pre-loaded	Advertising revenue as MAUs grow
Content deals covering 70% Indonesian music	Expansion into new geographies
Rapid growth in MAUs (adding 1.3m/month in March 2015)	
First mover advantage in Indonesia	
Funding in place - A$5.4m cash after 13 April 2015 placement	
Weaknesses	**Threats**
Small games portfolio	Competition from local players
Key man risk (Steven Goh)	Technology changes
Monetisation unproven in migme app	Privacy issues
Exposure to 'killer' games	Managing growth
Dependent on third parties for content	System failure
Relatively small number of users (20 million at 31 July 2015 vs hundreds of millions on other successful platforms)	

Source: Edison Investment Research

Valuation

MIG has a sizable addressable market in the developing countries of South Asia and South-East Asia. Markets in which MIG has an established market are Indonesia, Nepal, India and the Philippines. These markets have a young demographic and a high propensity to use social media. Given the network effect nature of this industry, rapid scaling is essential which means that MAUs will be a key metric for measuring early success. In July 2015 users reached 20 million from a base of >5m when the company listed in August 2014. We expect user numbers to continue to build at increasing rates as the company enters new markets and signs more audience builders. The increase in revenue was below our forecasts due to delays in setting up payment systems and in entering new markets and signing artists. However, the increase of 95% in Q215 compared with Q115 provides some proof of concept and increases our confidence in the likelihood of success. We acknowledge that it is still early days and therefore put our valuation in a range from the current share price of A$1.23/share to our bull/blue sky case of A$2.32/share. These valuations are

contingent on the timing and the quantum of additional monetising users and the amount spent per user.

We have prepared three valuation cases:

- implied in share price;
- financial forecasts case, which is equivalent to a base case; and
- bull or blue sky case.

We have dropped our bear case valuation which had included difficulties in proving the MIG concept. User numbers of 20 million now give us confidence in the concept and set MIG some of the way along the path followed by YY.com (US.YY), which now has 105 million users, revenue of US$745m and a market capitalisation of ~US$4.6bn. YY.com operates in China, which does not allow Facebook, Twitter or Instagram, and it will therefore be difficult for MIG to achieve the same success in markets where there is competition from well-established global brands.

Exhibit 5: DCF – valuation parameters

Base case (A$000s)	2015e	2016e	2017e	2022e	DCF
No of users at period end (m)	30	52	82	262	$1.75
% of users monetising	1.0%	1.8%	2.0%	2.0%	
Smartphones India, Indonesia (m)	254.9	276.7	294.8	N/P	
% of smartphone users	11.8%	18.8%	27.8%	N/P	
$ spent month/user (A$)	6.34	7.43	8.19	11.21	
Revenue	8,995	33,176	66,022	290,114	
EBITDA	(12,108)	(1,540)	13,779	89,146	
Net cash/(debt)	350	805	13,694	249,752	
Implied in current share price					
No of users at period end (m)	30	46	72	243	$1.23
% of users monetising	1.0%	1.8%	2.0%	2.0%	
Smartphones India, Indonesia (m)	254.9	276.7	294.8	N/P	
% of smartphone users	11.8%	16.6%	24.4%	N/P	
$ spent month/user (A$)	6.30	7.17	7.68	9.22	
Revenue	8,914	29,500	54,037	223,600	
EBITDA	(16,017)	(12,148)	(3,378)	65,446	
Net cash/(debt)	302	(1,050)	6,826	179,063	
Bull/blue sky					
No of users at period end (m)	30	58	92	281	$2.32
% of users monetising	1.0%	1.8%	2.0%	2.0%	
Smartphones India, Indonesia (m)	254.9	276.7	294.8	N/P	
% of smartphone users	11.8%	21.0%	31.2%	N/P	
$ spent month/user (A$)	6.41	7.78	8.86	13.23	
Revenue	9,102	37,532	80,556	365,044	
EBITDA	(16,017)	(12,054)	637	116,158	
Net cash/(debt)	414	2,961	21,940	330,833	

Source: Edison Investment Research

Exhibit 6: Financial summary

A$000s	2014	2015e	2016e	2017e	2018e	2019e
31 Dec	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	1,953	8,995	33,176	66,022	110,776	164,937
Cost of Sales	(1,356)	(4,497)	(16,588)	(33,011)	(55,388)	(82,468)
Gross Profit	596	4,497	16,588	33,011	55,388	82,468
EBITDA	(28,597)	(12,108)	(1,540)	13,779	34,984	60,822
Operating Profit (before amort. and except.)	(434)	(12,145)	(1,575)	13,747	34,955	60,794
Intangible Amortisation	0	0	0	0	0	0
Exceptionals	0	0	0	0	0	0
Other	0	0	0	0	0	0
Operating Profit	(434)	(12,145)	(1,575)	13,747	34,955	60,794
Net Interest	0	0	0	0	0	0
Profit Before Tax (norm)	(434)	(12,145)	(1,575)	13,747	34,955	60,794
Profit Before Tax (FRS 3)	(708)	(12,145)	(1,575)	13,747	34,955	60,794
Tax	(32)	3,643	472	(4,124)	(10,486)	(18,238)
Profit After Tax (norm)	(28,629)	(8,501)	(1,102)	9,623	24,468	42,556
Profit After Tax (FRS 3)	(740)	(8,501)	(1,102)	9,623	24,468	42,556
Average Number of Shares Outstanding (m)	251.6	260.3	263.2	263.2	263.2	263.2
EPS - normalised (c)	(11.4)	(3.3)	(0.4)	3.7	9.3	16.2
EPS - normalised and fully diluted (c)	(1.5)	(3.3)	(0.4)	3.7	9.3	16.2
EPS - (IFRS) (c)	(0.3)	(3.3)	(0.4)	3.7	9.3	16.2
Dividend per share (c)	0.0	0.0	0.0	0.0	0.0	0.0
Gross Margin (%)	30.5	50.0	50.0	50.0	50.0	50.0
EBITDA Margin (%)	-1464.3	-134.6	-4.6	20.9	31.6	36.9
Operating Margin (before GW and except.) (%)	-22.2	-135.0	-4.7	20.8	31.6	36.9
BALANCE SHEET						
Fixed Assets	646	145	3,788	4,646	4,646	4,646
Intangible Assets	0	0	0	0	0	0
Tangible Assets	502	0	0	0	0	0
Investments	145	145	3,788	4,646	4,646	4,646
Current Assets	6,551	1,580	3,660	18,757	50,671	102,231
Stocks	0	0	0	0	0	0
Debtors	0	605	2,230	4,438	7,446	11,087
Cash	5,926	350	805	13,694	42,600	90,519
Other	625	625	625	625	625	625
Current Liabilities	(1,423)	(1,491)	(5,499)	(10,943)	(18,361)	(27,338)
Creditors	(1,423)	(1,491)	(5,499)	(10,943)	(18,361)	(27,338)
Short term borrowings	0	0	0	0	0	0
Long Term Liabilities	(253)	(253)	(253)	(253)	(253)	(253)
Long term borrowings	0	0	0	0	0	0
Other long term liabilities	(253)	(253)	(253)	(253)	(253)	(253)
Net Assets	5,521	(19)	1,696	12,207	36,704	79,286
CASH FLOW						
Operating Cash Flow	(11,074)	(12,573)	842	17,015	39,394	66,158
Net Interest	0	0	0	0	0	0
Tax	(143)	0	(386)	(4,124)	(10,486)	(18,238)
Capex inc R&D	(506)	(3)	(2)	(2)	(1)	(1)
Acquisitions/disposals	9,344	0	0	0	0	0
Financing	11	7,000	0	0	0	0
Dividends	0	0	0	0	0	0
Net Cash Flow	(2,368)	(5,576)	455	12,889	28,906	47,919
Opening net debt/(cash)	(2,182)	(5,926)	(350)	(805)	(13,694)	(42,600)
HP finance leases initiated	0	0	0	0	0	0
Other	(1,376)				0	0
Closing net debt/(cash)	(5,926)	(350)	(805)	(13,694)	(42,600)	(90,519)

Source: migme accounts, Edison Investment Research

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