EDISON

eServGlobal

Trading update

Material progress for HomeSend

Software & comp services

eServGlobal has been on a long journey to restructure its core business; we believe it is now nearing the end of this process. The cost base has been resized to match the revenue base case and the recent fund-raising has removed funding concerns. Its HomeSend joint venture has expanded its addressable market to serve the cross-border banking payments market, with joint venture partner Mastercard signing up 10 banks to use the service so far. This has the potential to add material revenues and grow the value of the joint venture.

Year end	Revenue (A$m)	EBITDA* (A$m)	EPS* (A$)	DPS (A$)	P/E (x)	EV/EBITDA (x)
10/15	25.9	(10.4)	(5.41)	0.0	N/A	N/A
10/16	21.6	(7.0)	(3.88)	0.0	N/A	N/A
10/17e	12.9	(8.2)	(2.18)	0.0	N/A	N/A
12/17e**	15.2	(7.6)	(2.16)	0.0	N/A	N/A

Note: *EBITDA and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **14-month period to 31 December 2017.

HomeSend – exploiting the banking opportunity

Mastercard has been actively marketing its Mastercard Send Cross-Border service (powered by HomeSend) to many of its banking customers, and so far 10 have signed up. As these banks shift their cross-border payments over to the service, eServGlobal estimates that annual transaction volumes could reach $3-5bn over the next few years, adding incremental revenues to HomeSend's existing peer-to-peer, remittance-based revenues and accelerating the JV's path to profitability.

Core business – adjusting the cost base

eServGlobal has revised down its revenue guidance for 2017, from €15-19m to €9.7-11m for the 14 months to December 2017 (FY17). It also noted that it should be EBITDA break-even for Q417. We have revised our forecasts for the 12 months to 31 October and FY17 to reflect the mid-range of lowered revenue guidance. This results in a cut to FY17 revenues of 32% and the EBITDA loss for widening by 59% from A$4.8m to A$7.6m. The company estimates that it has reduced the cost base such that EBITDA break-even should be achievable in FY18 at revenues of €12m/A$18m. We have updated our forecasts to reflect the institutional placing of 229m shares (assumed net proceeds of A$33m) and will update for the retail offering when the outcome is known.

Valuation: Starting to reflect larger JV opportunity

Since the recent HomeSend update and the fundraising, the share price has gained 40% as we believe the market is now starting to factor the banking opportunity into the valuation of eServGlobal's stake in HomeSend, and funding concerns have been removed. Evidence of progress in the banking sector for HomeSend (new agreements as well as recently signed banks transitioning volumes to the platform) and pipeline conversion in the core business could support further upside to the share price. Conversely, weaker performance in the core business or slower execution for HomeSend could weigh on the share price.

30 October 2017

Price	**10.88p**
Market cap	**£95m**
	A$1.7:€1.13:£1
Net debt (A$m) at end H117	10.6
Shares in issue	869.2m
Free float	96%
Code	ESG
Primary exchange	AIM
Secondary exchange	ASX

Share price performance

%	1m	3m	12m
Abs	47.9	64.0	84.1
Rel (local)	44.0	62.4	69.1
52-week high/low		12.4p	4.9p

Business description

eServGlobal develops mobile software solutions to support mobile financial services, with a focus on emerging markets. It also has a 35% share in the HomeSend international remittances hub, alongside Mastercard and BICS.

Next events

Results to 31 October	December 2017

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Edison profile page

eServGlobal is a research client of Edison Investment Research Limited

HomeSend update – growing the addressable market

On 2 October, the company released an update on the HomeSend joint venture. Mastercard has confirmed that it has signed up 10 banks for its Mastercard Send Cross-Border service, which is powered by HomeSend. We have already written about HomeSend's experience with KEB Hana (Restructuring ongoing). Mastercard has since named Standard Chartered Bank and Atlas Mara as having signed up to the service.

The company estimates that annual transaction volumes from these agreements could reach $3-5bn in the next couple of years (ie average volume per bank of $300-500m per annum). We estimate that the HomeSend JV would charge commission of c 2.5% of the transaction value, retaining c 20% as gross margin. This would generate annual revenues of $75-125m and gross profit of $15-25m for the JV. This compares to HomeSend's reported revenues of €4.2m/$4.6m and reported gross margin of €1.2m/$1.3m in CY16. To date, HomeSend has generated the majority of its revenues from cross-border, peer-to-peer remittances. Entry into the much larger cross-border banking payments market presents a significant opportunity for the joint venture to grow revenues; with a relatively fixed cost base, the joint venture has high operational leverage.

Core business update – still tough going

On 10 October, the company confirmed that revenues for the 14-month period to 31 December are likely to be lower than the range expected at H117 results in June. It now expects revenues of €9.7-11m, down from €15-19m. This implies a revenue range of €5.6-6.9m for the eight months to 31 December 2017, compared to the €4.1m reported in H117. It expects to receive orders worth €11-15m over the 14-month period, providing a growing backlog going into FY18. Management expects to achieve EBITDA break-even in the last quarter of CY17 and expects to be able to achieve EBITDA break-even at revenues of €12m in FY18.

The company has been working hard to reduce the cost base to reflect the revenue base case. The sales team has been reorganised, and the agent footprint reduced, with an increased focus on direct sales. Partners will still be used, but these are likely to be well-established multi-national organisations. To improve profitability, the business is promoting its software in a virtualised format, reducing the volume of low margin hardware sales.

The company believes that the €12m break-even revenue figure could be achieved from the existing customer base, from the combination of €2m in deferred revenues, €5m in recurring revenues (eg maintenance revenues, subscription licences) and a further €5m in changes and upgrades to licences. The enhanced focus on existing customers may result in a lower volume of new customer sales than the company has previously reported, but should result in higher quality and therefore more profitable orders.

The company is seeing a good level of interest in its mobile financial services recharge platform and expects this to be the main driver of new business in the coming year.

Fundraising removes cash concerns

On 20 October, eServGlobal announced a fundraising to raise gross proceeds of up to £24.0m. This is structured as two separate placings: institutional and retail.

The institutional placing consists of 228.979m shares at 9p/A$0.15 for gross proceeds of £20.6m. The price represents a 10% discount to the closing mid-market price on AIM of 10p as at 19 October. The shares have all been placed and were admitted to trading on AIM or the ASX today.

The retail placing consists of 37.688m shares also priced at 9p/A$0.15 for gross proceeds of £3.4m. The shares are offered in the ratio of one share per three held. Retail investors have until 10 November to decide whether to take up the offering. Those shares not taken up by retail investors will be offered to institutional shareholders, and we understand that these will all be taken up.

The company plans to use the proceeds as follows:

- £11m to repay outstanding debt. We estimate that at the end of October, eServGlobal would have had gross debt of A$18.3m/£11m outstanding (including accrued interest), all owing to its largest shareholder, Lombard Odier. This was accruing interest at 1% per month.
- £8.5m to fund the HomeSend JV. Management expects HomeSend to make a funding call to support short-term trading until the JV reaches profitability. In order to maintain its 35% stake, we expect eServGlobal to participate. The precise amount of the cash call is not known, but the company expects the £8.5m allocation to cover this plus any future funding requirements.
- £2.5m to cover the final restructuring of the core business.
- £2m working capital, including the payment of £1.2m transaction fees.

Changes to forecasts

We have revised our forecasts to reflect the middle of the lower revenue guidance range for 2017.

We have included the institutional fund-raising, and have allocated £1.03m of the £1.2m transaction fees to this tranche. We will update forecasts for the retail offering once the outcome is known.

We have not yet factored in the cash call for HomeSend as this has not been formally announced. Even if the full £8.5m/A$14.3m were required, this would still leave the company with a cash balance of A$2.8m as at the end of CY17 before the addition of likely net proceeds from the retail offering of £3.2m/A$5.4m.

Exhibit 1: Changes to forecasts

A$'000	12 months to end Oct 17		Change	y-o-y	14 months to end CY17		Change
	Old	New			Old	New	
Revenues	18,163	12,890	(29.0%)	(40.3%)	22,264	15,233	(31.6%)
Gross profit	5,081	2,971	(41.5%)	(51.2%)	6,721	3,909	(41.8%)
Gross margin	*28.0%*	*23.1%*	*(4.9%)*	*(5.2%)*	*30.2%*	*25.7%*	*(4.5%)*
Normalised EBITDA	(6,071)	(8,181)	34.7%	17.2%	(4,769)	(7,582)	59.0%
Normalised EBITDA margin	*(33.4%)*	*(63.5%)*	*(30.0%)*	*(31.1%)*	*(21.4%)*	*(49.8%)*	*(28.3%)*
Normalised EBIT	(9,461)	(11,571)	22.3%	(15.3%)	(8,724)	(11,537)	32.2%
Normalised EBIT margin	*(52.1%)*	*(89.8%)*	*(37.7%)*	*(43.2%)*	*(39.2%)*	*(75.7%)*	*(36.5%)*
Reported EBIT	(13,621)	(15,731)	15.5%	(67.5%)	(12,918)	(15,730)	21.8%
Normalised PBT	(15,830)	(17,225)	8.8%	1.8%	(16,334)	(17,846)	9.3%
Reported PBT	(19,990)	(21,385)	7.0%	(1.1%)	(20,528)	(22,040)	7.4%
Normalised net income	(12,864)	(13,980)	8.7%	1.7%	(13,301)	(14,510)	9.1%
Reported net income	(20,290)	(21,685)	6.9%	1.2%	(20,861)	(22,373)	7.2%
Normalised EPS	(2.01)	(2.18)	8.7%	43.7%	(2.08)	(2.16)	3.8%
Net debt/(cash)	9,912	(17,175)	(273.3%)	(820.4%)	9,542	(17,074)	(278.9%)

Source: Edison Investment Research

Exhibit 2: Financial summary

A$'000s	2012	2013	2014	2015	2016	2017e	2017e*
Year end 31 October	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue	28,070	31,003	31,261	25,866	21,577	12,890	15,233
Cost of Sales	(12,267)	(11,789)	(13,359)	(20,608)	(15,490)	(9,918)	(11,325)
Gross Profit	15,803	19,214	17,902	5,258	6,087	2,971	3,909
EBITDA	(1,936)	1,683	2,571	(10,449)	(6,982)	(8,181)	(7,582)
Operating Profit (before amort acq intang, SBP and except.)	(7,277)	(660)	1,987	(12,469)	(10,039)	(11,571)	(11,537)
Amortisation of acquired intangibles	0	0	0	0	0	0	0
Exceptionals	(6,485)	5,997	28,735	(12,539)	(3,533)	(3,971)	(3,971)
Share-based payments	(624)	(456)	(438)	(54)	(75)	(189)	(222)
Operating Profit	(14,386)	4,881	30,284	(25,062)	(13,647)	(15,731)	(15,730)
Income from associate	0	0	(2,275)	(3,831)	(4,638)	(3,883)	(4,538)
Net Interest	(1,016)	(386)	(254)	(1,356)	(2,861)	(1,772)	(1,772)
Profit Before Tax (norm)	(8,293)	(1,046)	(542)	(17,656)	(17,538)	(17,225)	(17,846)
Profit Before Tax (FRS 3)	(15,402)	4,495	27,755	(30,249)	(21,146)	(21,385)	(22,040)
Tax	(187)	5,879	(13,515)	(2,125)	(596)	(100)	(100)
Profit After Tax (norm)	(5,805)	(732)	(379)	(14,125)	(14,030)	(13,780)	(14,277)
Profit After Tax (FRS3)	(15,589)	10,374	14,240	(32,374)	(21,742)	(21,485)	(22,140)
Average Number of Shares Outstanding (m)	196.8	241.1	253.1	264.0	366.6	640.2	672.9
EPS - normalised (c)	(3.01)	(0.36)	(0.20)	(5.41)	(3.88)	(2.18)	(2.16)
EPS - FRS 3 (c)	(7.98)	4.25	5.57	(12.33)	(5.98)	(3.39)	(3.32)
DPS (c)	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Gross Margin (%)	56.3%	62.0%	57.3%	20.3%	28.2%	23.1%	25.7%
EBITDA Margin (%)	(6.9%)	5.4%	8.2%	(40.4%)	(32.4%)	(63.5%)	(49.8%)
Operating Margin (before am and except.) (%)	(25.9%)	(2.1%)	6.4%	(48.2%)	(46.5%)	(89.8%)	(75.7%)
BALANCE SHEET							
Fixed Assets	16,303	14,330	43,431	42,928	33,274	27,590	26,635
Intangible Assets	9,386	3,523	9,011	6,939	5,598	3,797	3,497
Tangible Assets	912	482	3	84	32	32	32
Other Fixed Assets	6,005	10,325	34,417	35,905	27,644	23,761	23,106
Current Assets	18,136	38,855	30,761	34,895	28,240	28,658	30,483
Stock	158	74	173	66	72	72	72
Debtors	14,094	21,846	26,811	24,403	17,976	10,594	12,521
Cash	3,794	4,909	3,679	4,976	9,375	17,175	17,074
Other	90	12,026	98	5,450	817	817	817
Current Liabilities	(12,934)	(15,082)	(18,033)	(25,520)	(14,469)	(8,256)	(9,797)
Creditors	(11,665)	(11,932)	(13,010)	(22,285)	(14,189)	(7,976)	(9,517)
Taxation & social security	(69)	(150)	(2,023)	(235)	(280)	(280)	(280)
Short term borrowings	(1,200)	(3,000)	(3,000)	(3,000)	0	0	0
Long Term Liabilities	(6,431)	(749)	(865)	(19,532)	(12,649)	(890)	(890)
Long term borrowings	(6,000)	0	0	(16,531)	(11,759)	0	0
Other long term liabilities	(431)	(749)	(865)	(3,001)	(890)	(890)	(890)
Net Assets	14,989	37,154	55,070	32,359	33,823	46,750	46,045
CASH FLOW							
Operating Cash Flow	(11,901)	(7,207)	(5,810)	(12,130)	(10,712)	(10,983)	(10,769)
Net Interest	(974)	(580)	(271)	(423)	(175)	(148)	(148)
Tax	(7,813)	(1,088)	2,018	(3,148)	(1,159)	(300)	(350)
Capex	(1,966)	(1,950)	(6,403)	(2,921)	(1,583)	(1,590)	(1,855)
Acquisitions/disposals	23,307	0	5,418	0	5,133	0	0
Financing	(77)	16,140	3,964	4,365	15,929	33,001	33,001
Dividends	(111)	0	(146)	0	0	(421)	(421)
Net Cash Flow	465	5,315	(1,230)	(14,257)	7,433	19,559	19,458
Opening net debt/(cash)	3,871	3,406	(1,909)	(679)	14,555	2,384	2,384
HP finance leases initiated	0	0	0	0	48	0	0
Other	0	0	0	977	(4,690)	0	0
Closing net debt/(cash)	3,406	(1,909)	(679)	14,555	2,384	(17,175)	(17,074)

Source: eServGlobal, Edison Investment Research. Note: *14-month period ending 31 December.

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