

# Fusionex International

Another GIANT step forward

FY16 results - forecast change

Software & comp services

**FY16 results were ahead of forecast and sales momentum remained strong in the first four months of FY17. The next iteration of the platform, GIANT 2017 marks a step-change in usability and functionality and with a growing network of sales partners, this should underpin sustained revenue growth. This progress is not reflected in Fusionex's EV/EBITDA rating which despite its higher margins, is the lowest in its peer group at 13x FY17e.**

Year end	Revenue (MYRm)	Revenue (£m)	EBITDA (£m)	PBT* (MYRm)	EPS* (sen)	DPS (p)	EV/ Sales (x)	EV/ EBITDA (x)
09/15a	77.0	14.0	33.2	26.3	53.3	2.1	3.4	8.0
09/16a	94.6	17.2	15.1	4.6	3.0	2.6	2.8	17.6
09/17e	127.1	23.0	20.3	1.2	2.0	0.0	2.1	13.1
09/18e	170.0	30.7	35.3	8.2	13.9	0.0	1.6	7.5

Note: \*PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

## Results ahead of forecast; GIANT momentum strong

FY16 revenues increased 23% to MYR94.6m (6% ahead of our forecast) and EBITDA of MYR15.1m was more than double our forecast (from a compressed level), returning the group to a small net profit position. Sales of GIANT accelerated during Q4 to 115 customers (ahead of 90 targeted). The second iteration of the platform, which was configured for the SME market, is supporting ongoing strong momentum with 48 customers added in the first four months of the year and the pipeline is underpinned by a further 20 customers that are trialling GIANT 2017. Due to launch in the coming weeks, it offers a step-change in usability and functionality, adding natural language processing capabilities, additional drag and drop capabilities and third-party data sources, as well as an impressive array of analytics and algorithm-based forecasting tools which incorporate elements of machine learning.

## Upgrade FY17 EBITDA, back to profitability

The majority of new customers are joining on a subscription basis; while this improves visibility, it does reduce our near-term revenue forecasts. However, the pace of increase in marketing and sales has been moderated with the focus remaining on AsiaPac for now. We upgrade our FY17 EBITDA forecast by 108% and now expect the group to move back into profitability at the net level this year.

## Valuation: Current price assumes little for GIANT

On 13.1x FY17e EV/EBITDA Fusionex trades at the low end of its big data/analytics peer group, despite similar revenue growth and higher margins. We believe there is considerable upside potential in the shares; the group's transition is largely complete and GIANT is now the majority of group revenues, momentum is strong and GIANT 2017 offers an impressive step-change in functionality which should expand the already large addressable market further. Our reverse DCF also suggests that the shares are pricing in little medium-term success from GIANT.

4 April 2017

**Price** **132.00p**

**Market cap** **£62m**

GBP: MYR 5.53

Net cash (MYRm) at end September 2016 75

Shares in issue 47.3m

Free float 53%

Code FXI

Primary exchange AIM

Secondary exchange N/A

### Share price performance



% 1m 3m 12m

Abs (11.7) (13.4) (26.1)

Rel (local) (10.9) (15.2) (37.1)

52-week high/low 207.0p 127.5p

### Business description

Fusionex International's main product is GIANT, a big data analytics solution. Headquartered in Malaysia, Fusionex also has offices in five other Asian markets, the UK and the US. It sells its product through both direct and indirect channels to an international client base including Intel, DHL, Las Vegas Sands Corp and GroupM.

### Next events

H117 results May 2017

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## FY16 results highlights

Fusionex's FY16 preliminary results to 30 September 2016 were reported ahead of forecasts at the revenue (6% beat), gross profit (11% beat) and EBITDA levels (approximately double our forecast although from a compressed level) and the outlook for the current year remains strong.

### Exhibit 1: Summary results

Year end 30 September MYR000s	2015	2016 Edison forecast	2016 reported	Difference to forecast (%)	yoy % change
Revenue	77,044	89,500	94,624	6%	23%
Gross profit	58,853	66,480	74,044	11%	26%
Gross profit margin	76%	74%	78%		
EBITDA	33,195	7,085	15,063	113%	-55%
Operating profit (before except.)	26,376	(5,910)	4,614	-	-83%
Exceptionals	2,037	0	0		
Operating profit	28,412	(5,910)	4,614	-	-84%
Net Interest	(41)	(8)	(63)	687%	52%
Profit Before Tax (norm)	26,334	(5,918)	4,551	-	-83%
Profit Before Tax (FRS 3)	28,371	(5,918)	4,551	-	
Tax	(3,424)	710	(3,143)	-	-8%
Profit After Tax (norm)	22,910	(5,208)	1,409	-	-94%
EPS - normalised and fully diluted (sen)	53.3	(11.1)	3.0	-	-94%

Source: Fusionex report and accounts

Revenues increased 23% to MYR94.6m underpinned by the growth of the GIANT customer base in focus regions of Asia Pacific (+24%) and the USA (+48%), although Europe declined (-9%).

While the product/service mix was broadly the same as last year (89%/11%), gross margins increased 200bps to 78%, well ahead of our forecast of 74%. This increase was despite a higher amortisation charge (MYR7.7m – 9% sales) being included. Excluding amortisation, the underlying gross margin increased to 86% from 82%. Typically, gross margins on SaaS sales are lower than for licence sales (reflecting the cloud hosting costs). However, we understand that for Fusionex's subscription service, a number of clients opt to continue to use their own hosting services as permitted by Fusionex and, as it reflects much of its own hosting costs in operating expenses, the gross margin differential between subscription services and licence sales is less marked than usual. In addition, Fusionex has benefited from scale economies in the fees it pays to its own third party software providers. The higher revenue and gross margin combination meant that EBITDA was significantly ahead of our MYR3m estimate at MYR15.1m (16% margin), although still down on FY15 (MYR33m) due to the increased investment in marketing, infrastructure (cloud storage to support expansion), product development and geographic reach in order to accelerate the commercialisation of GIANT.

Fusionex continues to benefit from the tax exemption that goes with its Multimedia Super Corridor (MSC) status in Malaysia. However, a proportion of the cost base is disallowable for tax purposes; consequently, and off a fairly low base of profitability, this converted to an effective tax rate for the year of 69%. Despite this, the group returned to a small net profit position of MYR1.4m. An interim dividend of RM0.138/share (2.1p, up 20%) was paid and again, we assume that there will be no final dividend (as per last year).

In FY15, cash conversion was affected by the timing of a number of large sales just prior to the year-end (now fully recouped). In FY16, following a tightening of the payment terms and conditions offered to customers, cash conversion improved considerably to 114% of EBITDA (payables turnover decreased from 135 days to 78 days). Of the FY16 year-end receivables balance of MYR20m, 85% has now been collected. Net of working capital improvements, MYR26m of R&D expenditure, MYR18m of capex (investment in computers, servers and other equipment for the R&D team), and the £14m (MYR88m) share placing, year-end cash of MYR94.2m was reported.

## Operational update

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2016 was a year of investment by the company to drive the adoption of its big data analytics platform, GIANT. Operating expenses increased by 82% and capitalised R&D spend by 60% as the company stepped up its investment in marketing, expanded its sales capabilities with an emphasis on indirect channels, opened an office in the Philippines and acquired the necessary capacity to support the anticipated growth.

### **GIANT customer wins ahead of plan: Momentum continues post year end**

Increased investment into sales and marketing converted into an acceleration in the addition of new customers to GIANT with a further 79 customers signed, taking the total to 115 by the year end, ahead of management's target of 90. Growth accelerated post the launch in CTP mode of the second version of the platform over the summer. This was the first step in extending the big data analytics platform to the wider SME market, which is reflected in the year-end customer mix with 66 of the 115 GIANT customers SMEs (up from 11 at September 2015).

Fusionex has customers across a wide range of industries: retail (AEON, Carrefour, Chanel), hospitality (Starwood, Resorts World), media (eg Kantar, Group M), brands (eg PRADA), airline (American Airlines, Delta, KLM), financial services (RBS, OCBC Bank) and manufacturing sectors (Intel).

While growth is focused on the SME segment, during FY16 several multi-million dollar client wins were also announced including: The Bursa Malaysia Berhad (Kuala Lumpur Stock Exchange) where GIANT will enable it to keep track of stock and price movements; an Asian integrated resort to optimise a marketing strategy (Okada Group, Japan); a global media conglomerate; and an Asian bank where GIANT will upgrade a previously manual data management system to automate data collection across a range of sources, customer portfolio analysis, risk management and planning.

### **Development: GIANT 2017 'Humanising Big Data analytics'**

Fusionex invested MYR26.4m (28% revenues) in product development during FY16 (+60% y-o-y) and the company is on schedule to launch version three, GIANT 2017, in the coming weeks. GIANT 2017 offers a step-change in functionality and usability with a highly intuitive dashboard which enables a wide range of employees across an organisation to engage with the platform.

Key new features include the introduction of natural language processing (NLP), with the ability to use a search bar function to ask GIANT intuitive questions such as 'year to date sales, females, Blackpool'. The user interface also has added visualisation tools and more intuitive drag and drop capabilities. In addition, it gives the option to integrate with more third-party data sources, both structured (eg GDP statistics), semi structured (weather) or unstructured (eg public social media posts), which can enhance a company's ability to use the platform for algorithm-based forecasting, incorporating elements of machine learning; eg to analyse historical occupancy rates in relation to the weather or a social media campaign and to predict customer behaviours based on these trends.

Management believes it is several years ahead of its competitors' Business Intelligence solutions (Oracle, SAP, IBM). The simulated demonstration of the platform given at the results presentation was impressive in terms of the breadth of data that can be captured, speed, visualisation tools, forecasting capabilities (we particularly like the 'forecasting reliability' function based on data volume, timeframe and source) and the NLP search bar which can be used in more than ten different languages.

## Cloudera partnership – GIANT 2017 launch on track

The majority of sales are made on a direct basis (working in tandem with Dell, HP, Accenture, Microsoft, IBM and EMC). In order to cost-effectively scale the business, management is focused on increasing sales via channel partners and has announced relationships with Avnet, Mesiniaga Berhad and VADS. The proportion of indirect sales (approximately 30%) has not increased over the last year. However, in December 2016 Fusionex announced the extension of its strategic partnership with Cloudera (the world's largest Hadoop big data management company), which involves the deepening of their existing relationship with a joint go-to-market strategy. Cloudera's integration of GIANT 2017 (also known as VISION) has 20 customers in CTP mode (Community Technology Preview – equivalent to beta test) and the company expects all of these customers to convert on launch.

## Transitioning to subscription-based model

The majority of new SME clients signed on a SaaS basis and MYR35m (37%) of sales are now subscription based (22% in FY15). This means that together with maintenance and services, approximately 60% of revenues are recurring in nature.

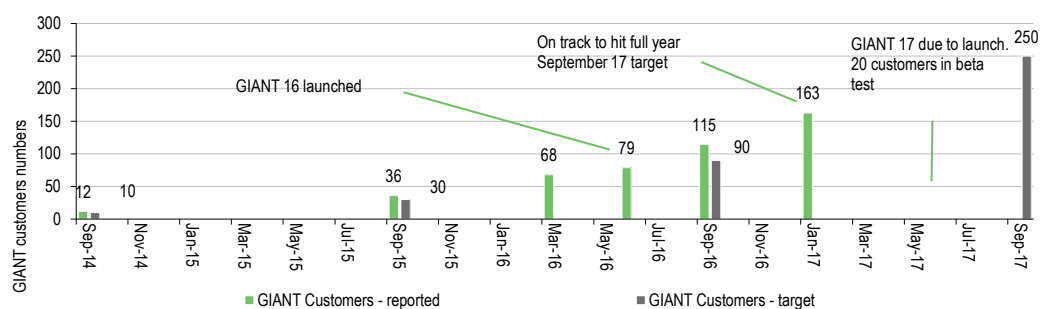
## Outlook: Target to more than double number of GIANT customers in FY17

The increase in marketing spend and product investment during FY16 has paid dividends with the pace of new customer additions increasing from two a month during FY15 to 12 a month in Q416.

Management is targeting 250 GIANT customers by the year end, more than double that reported at the end of FY16. The current momentum puts the company comfortably on track to achieve this with 48 new customers added in the first four months of FY17 (an average of 12 a month). This does not include the 20 GIANT 17 customers that are currently in CTP mode, which are expected to convert.

Since reporting its FY16 results, Fusionex has announced another multi-million dollar contract win with an Asian based insurance company to transform its business processes over a five-year period.

**Exhibit 2: GIANT customers – momentum continues with 250 targeted by end FY17**



Source: Fusionex/ Edison

## Forecasts

We have reduced our revenue forecast to reflect the pace of uptake of the SaaS offer. However, we have increased our margin assumption considerably following the FY16 beat and a significant reduction to our forecast increase in operating expenses in FY17. Overall, the changes result in a more than doubling of our EBITDA forecast in FY17 and brings forward to the current year our expectation of profitability at the operating and net profit levels.

**Exhibit 3: Summary forecast changes**

MYR'000s	FY16 reported	FY17 old	FY17 new	% change	FY18 old	FY18 new	% change
Revenues	94,624	133,719	127,099	-5%	190,831	170,038	-11%
Revenue growth (%)		41%	34%		43%	34%	
Gross profit	74,044	100,077	94,810	-5%	144,054	125,264	-13%
Gross margin (%)	78%	75%	75%		75%	74%	
EBITDA	15,063	9,733	20,281	108%	30,248	35,302	17%
EBITDA margin (%)	16%	7%	16%		16%	21%	
Operating profit	4,614	(6,767)	1,281		10,248	8,302	-19%
PBT	4,551	(6,775)	1,184		10,240	8,209	-20%
EPS - normalised (sen)	3.0	-12.6	2.0		19.1	13.9	-27%

Source: Edison Investment Research

Management has a good track record of hitting targeted customers numbers (having done so every year since launch in 2013 – Exhibit 2) and based on current momentum, we believe that the group is on track to hit or exceeded targets once again this year. However, the transition to SaaS is progressing more rapidly than we had forecast, with the vast majority of SME customers contracting on a subscription basis as well as a significant share of new Enterprise customers (we estimate 50%). While this does not impact the economics over the life of an average contract, licence revenues are recognised up front, which affects the phasing of revenues. With a greater share of SME customers signing up we also trim our ARPU assumption. Consequently, we reduce our revenue forecasts in FY17 by 5% and FY18 by 11%.

We assume the underlying gross margin is flat, with a proportionately lower share of revenues from services offsetting the gross margin impact from a transition towards subscription services. However, net of our raised assumption for amortisation of development costs, we forecast a reduction in the reported gross margin.

Planned investment in marketing and sales has been moderated and we have reduced our forecast rate of growth in operating expenses to 30% (from 45%) in FY17 (we leave FY18 unchanged at 25%). Management is experiencing considerable traction in the Asia Pacific region, where it also enjoys a lower cost base and resources are being focused here for now.

The net effect of our changes is to increase our EBITDA margin forecast from 7% in FY17 to 16% and from 16% in FY18 to 21% and to increase our EBITDA forecasts considerably in both FY17 (more than doubling from a low base) and FY18 (+17%). We now expect the group to be profitable at the operating and net profit levels in FY17. However, in FY18 the impact of our increased amortisation charge means an overall reduction to our forecast PBT of 20%.

## Valuation and investment case

The current share price (implied by our reverse DCF) is assuming very little medium-term growth from GIANT. We estimate that it discounts our FY17 and FY18 forecasts followed by approximately 7% revenue growth for the following five years with EBITDA margins peaking at 30%, a sharp slow down to the current pace of growth.

Similarly, when compared to peers, Fusionex's valuation looks out of line. We forecast revenues to grow at broadly the same rate as its peers to FY18 (c 34%), yet Fusionex is considerably more profitable (based on EBITDA margins). Despite this, its FY17 EV/Sales rating is mid of its peers and its EV/EBITDA rating is one of the lowest in its peer group of big data/analytics companies.

We believe that there is considerable upside potential to the current share price; GIANT is early in its sales cycle and is showing good momentum in a large and growing addressable market. Investors should consider:

**Group's transition now largely complete** The last year has been one of transition for Fusionex. The company sacrificed near-term margins to support a more ambitious product and growth strategy for GIANT, while de-emphasising its legacy Business Intelligence and Core Transaction Engine products. At the same time it has been encouraging customers to take up its subscription offering which has the effect of flattening growth in the near term. Despite these drags on revenue, it has continued to grow strongly and with approximately 85% of revenues now from GIANT the transition is largely complete.

**Visibility on GIANT's prospects has improved and is showing good momentum** The launch of the second version of GIANT last year has already led to a significant uptick in sales. The average of two client wins per month at the start of the year increased to 12 per month in Q416 and Q117 and via its partnership with Cloudera, there is a good pipeline of customers for GIANT 17. 37% of revenues are subscription based and together with maintenance contracts approximately 60% of revenues are now recurring.

**Well positioned in a large and growing addressable market** IDC forecasts a CAGR of 48% in the big data technology and services market to \$187bn by 2020. Fusionex is competing against the traditional global Business Intelligence groups including SAP, IBM, Teradata, and Oracle. While significantly smaller than its main competitors, with its intuitive interface and aggressively priced product (three to four times cheaper than the equivalent products) it is well positioned to gain share, particularly in the SME segment. Its relationships with Microsoft, Cloudera, IBM, HP etc are testament to its technology.

**Asian exposure** 80% of revenues are derived within Asia Pacific (mainly Malaysia, the Philippines and Thailand) giving quality exposure to these emerging economies.

**Already profitable, well funded.** While margins remain compressed compared to the 45% delivered in FY15, the group remains profitable despite the increase investment – unlike many other big data companies and with an operationally-gearred model, we expect to see a rapid rebuild in operating margins over the forecast period.

**Well funded** The group reported MYR94m of cash (MYR75m net of mortgage debt) in FY16, which we forecast to be ample to fund the group's current investment phase.

**Sensitivities** The mix of customers between SME/Enterprise and the pace of transition to subscription model differ from our assumptions. Also, as the company scales, there is a trade off between revenue growth and margins and we do not consider the group's exact margin structure to be set in stone. Currency is also a consideration given the majority of revenues are derived in dollars, reported in MYR and the group's sterling listing.

**Exhibit 4: Summary peer valuation**

Name	Price	Market Cap	Sales growth, %		EBITDA margin, %		EV/Sales, x		EV/EBITDA, x		EV/EBIT, x		P/E, x	
			1FY	2FY	1FY	2FY	1FY	2FY	1FY	2FY	1FY	2FY	1FY	2FY
<b>FUSIONEX</b>	<b>130p</b>	<b>£61.5</b>	<b>34</b>	<b>34</b>	<b>16</b>	<b>21</b>	<b>2.1</b>	<b>1.6</b>	<b>13.1</b>	<b>7.5</b>	<b>207.2</b>	<b>32.0</b>	<b>359</b>	<b>51.8</b>
Hortonworks	9.4	\$589	95	27	(1)	29	2.1	1.7	neg	5.8	Na	na	neg	neg
Splunk	60.5	\$8,205	78	26	12	13	6.0	4.7	51.4	35.7	75.9	49.4	102.5	68.7
Tableau	48.1	\$3,755	7	8	6	9	3.2	3.0	51.6	33.9	1,109.3	3.5	neg	327.3
Datawatch	8.2	\$98	13	11	(3)	(5)	2.1	1.9	neg	neg	na	na	neg	neg
GB Group	293.0	£395	21	17	21	21	4.5	3.8	21.6	18.3	24.6	20.5	30.6	293.0
CA inc	32.0	\$13,379	(1)	0	37	37	3.1	3.1	8.6	8.6	8.6	8.4	13.3	13.1
Wandisco	391.5	£145	36	44	(32)	1	11.7	8.1	neg	386.8	neg	neg	neg	neg
Attunity	7.4	£125	15	na	11	na	1.8	na	17.2	na	32.4	na	45.2	na

Source: Bloomberg, Edison Investment Research. Priced at 02 April 2017



**Exhibit 5: Financial summary**

Year end 30 September	MYR '000s	2014	2015	2016	2017e	2018e
		IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>						
Revenue		57,106	77,044	94,624	127,099	170,038
Cost of Sales		(12,793)	(18,191)	(20,580)	(32,289)	(44,774)
Gross Profit		44,312	58,853	74,044	94,810	125,264
EBITDA		25,816	33,195	15,063	20,281	35,302
Operating Profit (before amort. and except.)		21,797	26,376	4,614	1,281	8,302
Intangible Amortisation		0	0	0	0	0
Exceptionals		1,365	2,037	0	0	0
Other		0	0	0	0	0
Operating Profit		23,162	28,412	4,614	1,281	8,302
Net Interest		(381)	(41)	(63)	(97)	(93)
Profit Before Tax (norm)		21,415	26,334	4,551	1,184	8,209
Profit Before Tax (FRS 3)		22,780	28,371	4,551	1,184	8,209
Tax		(3,320)	(3,424)	(3,143)	(237)	(1,642)
Profit After Tax (norm)		18,095	22,910	1,409	947	6,567
Profit After Tax (FRS 3)		19,460	24,947	1,409	947	6,567
Average Number of Shares Outstanding (m)		43.0	43.0	47.1	47.3	47.3
EPS - normalised (sen)		42.1	53.3	3.0	2.0	13.9
EPS - normalised and fully diluted (sen)		42.1	53.3	3.0	2.0	13.9
EPS - (IFRS) (sen)		45.3	58.0	3.0	2.0	13.9
Dividend per share (p)		2.0	2.1	2.5	0.0	0.0
Dividend per share RM			0.12	0.14	0.00	0.00
Gross Margin (%)		77.6	76.4	78.3	74.6	73.7
EBITDA Margin (%)		45.2	43.1	15.9	16.0	20.8
Operating Margin (before GW and except.) (%)		38.2	34.2	4.9	1.0	4.9
<b>BALANCE SHEET</b>						
Fixed Assets		57,761	73,605	107,417	126,417	144,417
Intangible Assets		22,125	34,742	53,363	67,363	82,363
Tangible Assets		35,194	38,031	53,313	58,313	61,313
Investments		442	831	741	741	741
Current Assets		79,467	94,140	124,996	109,526	100,996
Stocks		0	0	0	0	0
Debtors		12,312	36,412	30,813	36,806	44,697
Cash		64,021	57,728	94,184	72,720	56,298
Other		3,134	0	0	0	0
Current Liabilities		(12,190)	(13,408)	(10,893)	(15,597)	(21,050)
Creditors		(8,856)	(12,588)	(10,028)	(14,732)	(20,185)
Short term borrowings		(3,334)	(819)	(865)	(865)	(865)
Long Term Liabilities		(23,645)	(25,664)	(27,317)	(26,467)	(25,617)
Long term borrowings		(20,224)	(19,446)	(18,585)	(17,735)	(16,885)
Other long term liabilities		(3,421)	(6,218)	(8,732)	(8,732)	(8,732)
Net Assets		101,393	128,672	194,204	193,880	198,746
<b>CASH FLOW</b>						
Operating Cash Flow		25,869	13,071	19,086	17,720	31,163
Net Interest		(239)	227	294	(97)	(93)
Tax		(1,115)	(1,651)	(1,881)	(237)	(1,642)
Capex		(14,132)	(16,105)	(44,494)	(38,000)	(45,000)
Acquisitions/disposals		0	0	0	0	0
Financing		0	0	88,038	0	0
Dividends		(4,795)	(4,961)	(5,943)	0	0
Net Cash Flow		5,588	(9,419)	55,100	(20,614)	(15,572)
Opening net debt/(cash)		(34,646)	(40,463)	(37,462)	(74,734)	(54,120)
HP finance leases initiated		0	0	0	0	0
Other		229	6,418	(17,829)	0	0
Closing net debt/(cash)		(40,463)	(37,462)	(74,734)	(54,120)	(38,549)

Source: Historics – Fusionex, Forecasts – Edison Investment Research



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