

Facilitate Digital Ltd

Big potential opportunity?

Stock Code: FAC
 Last Sale: \$0.06
 Market Cap (fd): \$9.9m
 Risk Level: High

24 Jun 2010

EVENT

- Select Equities has completed a Facilitate Digital Ltd (FAC) Stock Research note.

KEY HIGHLIGHTS

- FAC is a developer and distributor of highly specialised software tools targeted at media buying agencies worldwide.
- In 2005 the company launched their most promising product Symphony (see below for product details). Since its launch, Symphony has progressively gained traction, resulting in several significant client wins over the 18 months to Jun-10, including GroupM Asia (a regional subsidiary of global media agency GroupM).
- Select Equities is of the view that Symphony delivers a compelling value proposition to media buying agencies by automating a previously labour intensive and time consuming process. Select Equities feels that FAC has a significant opportunity, should it be able to capitalise on its first mover advantage and lock in a number of major global media agency clients. FAC is in open dialogue with some of these companies and we feel that signing a contract with one of them is likely to be catalyst to securing other major deals.
- FAC is managed by an experienced board and executive team, with an extensive background within digital media and media buying industries.
- In FY09 FAC reported Total Revenue, Operating EBITDA and NPAT of \$6.4m (+82.0%), \$0.6m (+131.5%) and -\$2.2m respectively. The business has progressively moved towards profitability, with 1H10 Total Revenue and NPAT of \$3.7m (+137%) and -\$0.1m respectively. FAC management is confident that they will generate positive NPAT between \$0.5m to \$1m in FY11e.
- FAC completed a rights issue in May-10 raising an additional \$0.75m and has advised that the current Operating Plan requires no additional capital.
- The company has no-debt, pays no dividend and reported a 1H10 cash position of \$1.2m.

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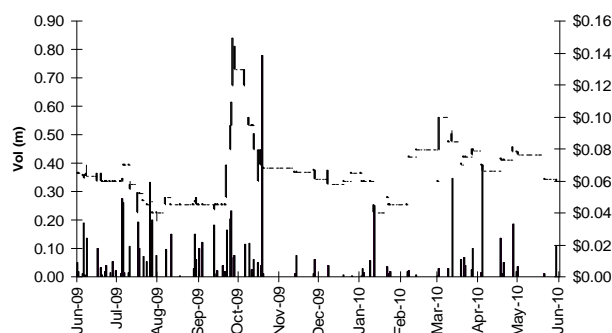
SELECT EQUITIES FORECASTS & RECOMMENDATION

- Select Equities is of the view that FAC is likely to reach profitability off the back of its recent contract wins. We have based our forecast for FY10e and FY11e on the assumption that these contracts generate revenues of up to \$2m over FY11e.
- We are of the view that the Symphony software offers a compelling value proposition fulfilling a core client need. As such we think FAC has good odds at winning a major global agency contract offering significant earnings upside (see our Bull Case Scenario Analysis section over the page for details). Given the high degree of risk inherent in the stock, we rate the stock as a SPECULATIVE BUY.

June Year End	FY09A	1H10A	FY10E	FY11E
NPAT (pre-abs. & OEI)	-2.2	-0.1	-0.2	0.5
Op EBITDA (\$m)	0.6	0.6	1.4	2.5
Op EBIT (\$m)	-0.7	-0.2	-0.5	0.5
EPS (¢)	-1.9	-0.1	-0.1	0.3
DPS (¢)	0.0	0.0	0.0	0.0
PER (x)	-3.2	-43.0	-43.0	20.5
PER Rel All Ords (%)	-23%	-319%	-319%	152%
Ent. Value/EBITDA (x)	14.9	6.2	6.2	3.5
Ent. Value/EBIT (x)	-11.8	-18.0	-18.0	17.8
Yield (%)	0.0%	0.0%	0.0%	0.0%
Diluted Shares (m)				167.6
Avg. Mthly Volume (m)				0.6
Diluted Mkt Cap (\$m)				9.9
Net Cash (\$m)				1.1
Enterprise Value (\$m)				8.8

Source: Company Reports and Select Equities Research

FAC 12-Month Price Vol Chart



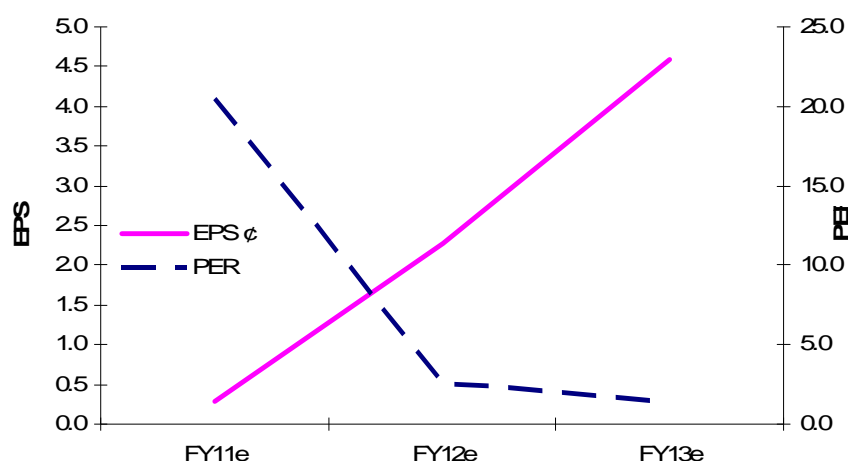
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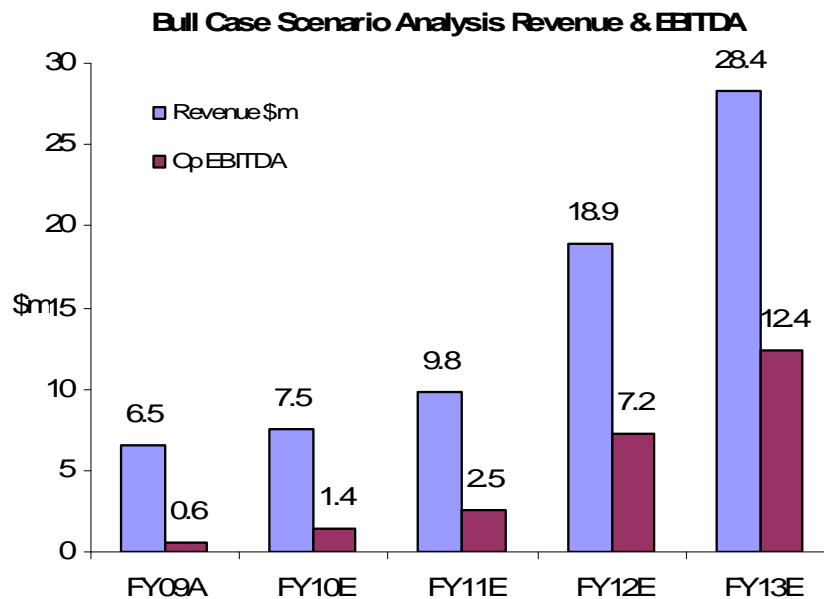
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**BULL CASE
SCENARIO
ANALYSIS**

- FAC target clients include the major global media agencies listed in the Industry Comment section of this report. Below we present a bull case scenario analysis assuming that FAC signs contracts with 3 of the six major global media agencies.
- Select Equities assumes that should FAC be successful in rolling out with one of the global agencies it could generate additional revenue of \$1-2m in the USA and \$2-4m in Europe per annum, with additional upside should further modules or customisation be required.
- In our bull case scenario we assume that FAC sign two major contracts in FY11e and a third in FY12e. All three roll-outs are both in the US and Europe and we assume the high end of the contract dollar value.
- FAC advised that they feel confident that their current infrastructure is capable of supporting major rollouts of its service offering should they land a contract with one or more of the major global media agencies.
- Additional costs are likely to arise with some additional customer support functions. However, we expect significant operating leverage and around 50% EBITDA margin on the incremental revenue.

June Year End	FY09A	FY10E	FY11E	FY12E	FY13E
Revenue \$m	6.5	7.5	9.8	18.9	28.4
Gwth %	82.0%	16.4%	29.8%	94.1%	49.8%
Op EBITDA	0.6	1.4	2.5	7.2	12.4
Op EBIT	-0.7	-0.5	0.5	5.1	10.2
NPAT	-9.2	-0.2	0.5	3.8	7.7
Gwth %	79.5%	-89.7%	310%	689%	101%
EPS ¢	-1.9	-0.1	0.3	2.3	4.6
PER (x)	-3.2	-43.0	20.5	2.6	1.3
Ent. Value/EBITDA (x)	14.9	6.2	3.5	1.2	0.7
Ent. Value/EBIT (x)	-11.8	-18.0	17.8	1.7	0.9

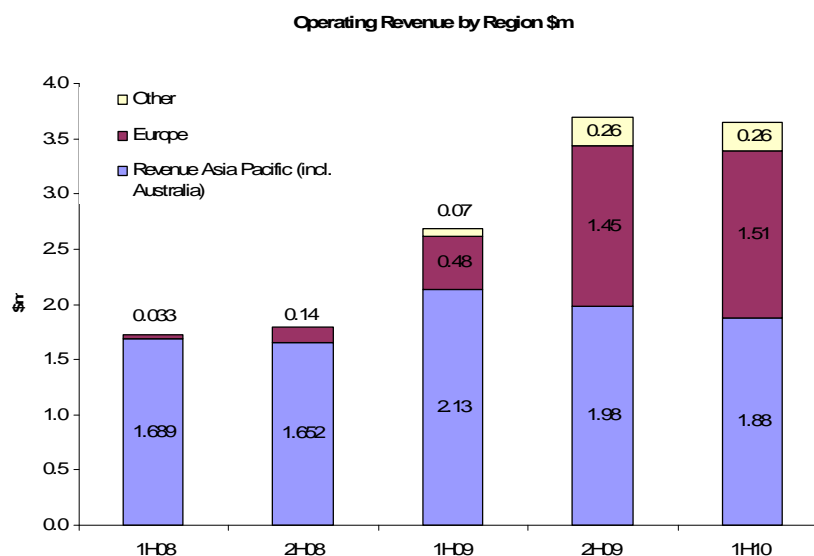
Bull Case Scenario PER vs EPS FY11E to FY13E


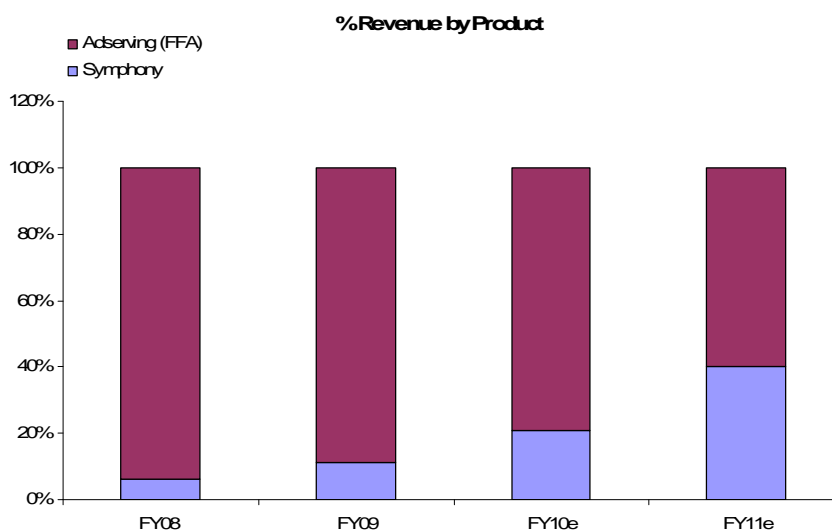


Source: Company Reporting and Select Equities Research

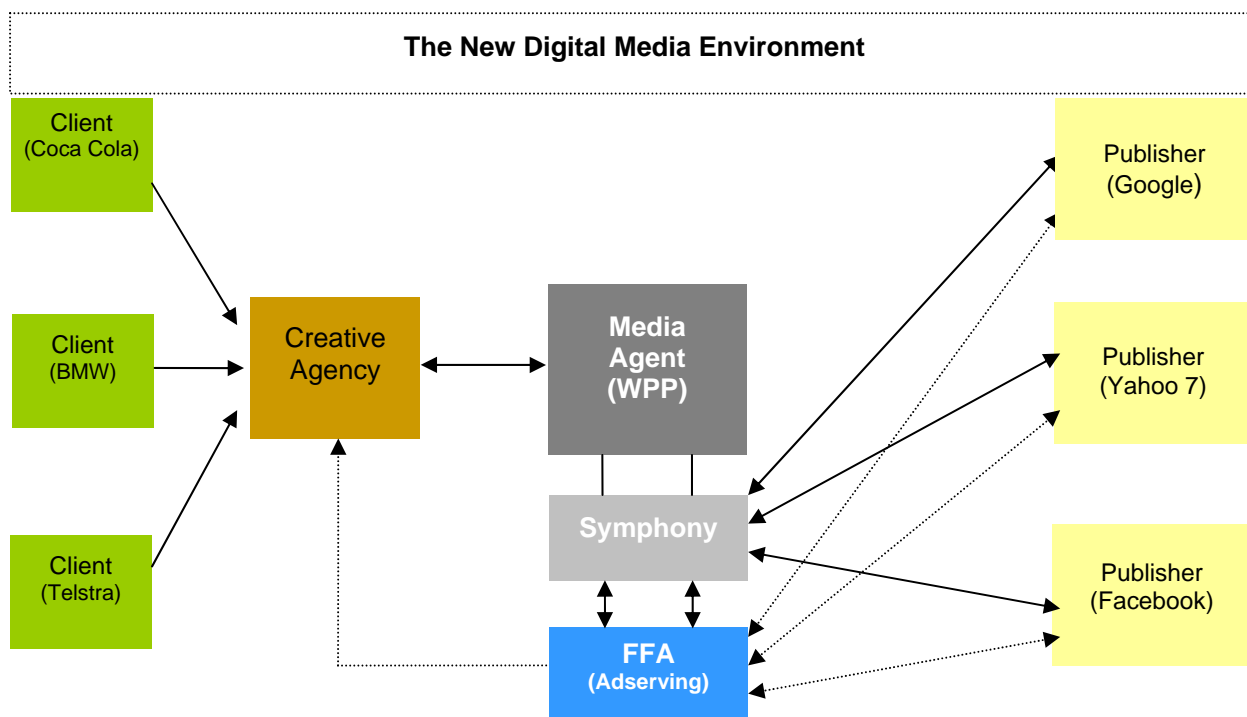
BUSINESS OVERVIEW

- FAC specialises in the development and distribution of digital media campaign management and implementation software. The software is intended to simplify and help manage the highly complex process of digital media buying and campaign execution, see below for key product details and functionality.
- Established in 1999, FAC is based in Sydney with international offices in Asia, US and Europe. Since inception, FAC has constructed two key products Symphony and Facilitate for Agencies (FFA), with the first version of Symphony, making its debut in 2005.
- The company markets its product suite primarily to media agencies and creative agencies around the world. In FY09 FAC generated revenue of \$6.5m, with approximately 53% generated in Australia. The proportion of international revenue has been rising over the last two years as FAC increased its focus on European and American markets.
- FAC's ultimate goal is to target the major global media agencies directly, with the objective of landing global contracts for the roll-out of its software offering.





Source: Company Report and Select Equities Research



Source: Select Equities Research

KEY PRODUCTS & VALUE PROPOSITION

- **Increased efficiency**

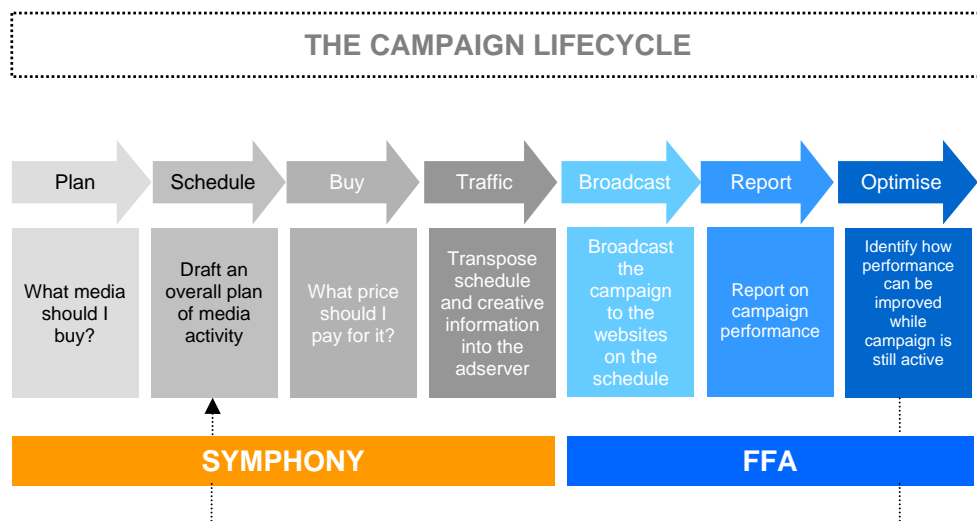
SYMPHONY

- Symphony is the cornerstone of FAC's current growth strategy. The software is essentially a workflow tool that automates the complicated, labour intensive, inefficient and error prone digital media buying process that media agencies engage in on behalf of their advertising clients, see the Campaign Lifecycle diagram over the page.
- The key value proposition for the product stems from the complexity of the digital media buying process compared to traditional media buying. The complexity arises from the multitude of web-content publishers e.g. Google or Yahoo7, each with a variety of websites, with each website supporting a variety of advertising formats e.g. banners, drop down ads, sponsored links etc. As each layer multiplies, you end up with very large permutations of relatively small media purchasing options which have to be processed manually (data entry, faxes and spreadsheets) at

- **Enhanced capabilities**
 - **Independence**
 - **Enhanced bargaining power**
- almost every step of the media buying process. This complexity results in media agencies simplifying strategies and in the process potentially foregoing the full spectrum of audience segmentation and targeting available (a key advantage of digital media advertising over traditional mass media) in order to meet often tough deadlines. Through its automated and integrated processes Symphony speeds up the process and reduces errors, adding efficiencies in the order of 25% to 40%.
- Once the complexity is removed agencies are able to maximise their value by implementing more effective campaigns.
 - Media agencies also face the problem of decentralised market intelligence, as their investment history accumulates with individuals rather than being pooled and shared across the organisation. This, coupled with the complexity of the current regime, places negotiating power into the hands of publishers, as market transparency and efficient pricing is hindered by the inherent process complexities. Symphony - through its record keeping, centralised databases and integrated analysis tools - puts more negotiating power into the hands of the media agency.
 - The software integrates with any ad-serving software, billing system and is provided as an international platform in multiple languages.
 - The product was first to market in 2005 and FAC maintains that it is the most advanced and comprehensive product of its kind in the global market. Competing products developed by DoubleClick and Donovan Data Systems reportedly offer lower levels of functionality and the vendors are subject to various conflicts of interest.

REVENUE MODEL

- FAC charges for initial consultation, implementation and training, with a model similar to other business software providers e.g. SAP. After the initial stage the client is billed on either a per seat basis or, a variable fee based on transaction volume. Significant discretion exists, and pricing is negotiated on a deal by deal basis.



Source: Company Reports

FACILITATE FOR AGENCIES

- Facilitate for Agencies is ad-serving software similar to other products like DoubleClick or Atlas. Its main functionality is to publish ad content to websites on behalf of agencies and/or track its performance. The product generates revenue on a transaction basis, billing based on impressions and click volumes. The ad-serving capability is similar to that of other major ad-serving providers e.g. DoubleClick. However, DoubleClick is owned by Google (one of the largest publishers), hence FAC's independence may be viewed as a competitive advantage.

- FAC sees Facilitate for Agencies as a complementary product for its core offering, Symphony.

INDUSTRY COMMENT

- According to the IAB the digital media market is worth USD 60-70B and growing rapidly. Media agencies have a history of investing 2-5c in every media dollar on tools and executional technology (including a broad range of tools & technologies, not just adserving and workflow software).
- A substantial percentage of global advertising spend is concentrated in the USA and Europe, broadly reflecting the levels of internet penetration and technological proliferation.
- The global digital media buying market is reasonably concentrated. Select Equities estimates that c80% of total global digital advertising spend is facilitated by the 6 major global media agency holding companies, see table below.

Company	Revenue	Employees	Key Subsidiaries
WPP Group plc	£8.7b	138,000	GroupM Gray Global Group, Ogilvy & Mather Worldwide, Young & Rubicam, JWT, Hill & Knowlton
Omnicom Group plc	US \$13.4b	68,000	OMD, PhD, AvreaFoster, BBDO Worldwide, Colangelo, DDB Worldwide, Goodby Silverstein & Partners, GSD &M
Interpublic Group of Companies, Inc	US \$6.0b	40,000	Universal McCann, Initiative, Accentmarketing, Campbell Mithun, Campbell-Ewald, Cassidy & Associates, Deutsch Inc, Draftfcb
Publicis Groupe	€4.5b	45,400	Zenith Optimedia, Leo Burnett Worldwide, Razorfish, Digitas, Saatchi Saatchi, Publicis Consultants, Publicis Worldwide, Phonevalley
Aegis	LSE listed		Carat, Isobar, Synovate
Havas Group	€1.4bn	16,000	Euro RSCG, MPG, Arena Media

Source: Company Reports

KEY COMPETITORS

- Select Equities has identified Donovan Data Systems and DoubleClick as major competitors providing software services to digital media agencies. These companies can be considered incumbents with existing client relationships and are much larger compared to FAC.
- Both companies offer a software solution that claims to provide an integrated workflow solution similar to that of Symphony, we discuss each of these in turn below :
 - Donovan Data Systems has been providing media and advertising agencies with financial management software since the 1960's. It has an annual development expenditure of US \$25m. Donovan's digital workflow product, iDesk, is described as providing similar functionality to Symphony. However, FAC advised that iDesk was developed as a set of workflow tools to augment Donovan's billing module, and the workflow tools are fairly rudimentary by comparison. Furthermore, Symphony integrates with multiple finance systems, whereas iDesk is only built to integrate with Donovan's own finance system.
 - DoubleClick is owned by Google, a major digital media publisher. Double Click has a solution, MediaVisor, which emulates Symphony. MediaVisor was developed off the back of DoubleClick's adserver and its capabilities focus around the traffic step in the campaign lifecycle (loading the digital strategy into the adserver). MediaVisor is only compatible with DoubleClick's adserver, whereas Symphony is compatible with multiple adservers.
- FAC advised that while both product vendors claim they have a solution for simplifying the media agency workflow process, they both have inherent conflicts and run a distant second to Symphony with respect to functionality.

BARRIERS TO ENTRY

- Incumbent relationships – While software revenues are sticky, the current market is largely greenfields with little in the way of incumbent workflow software to be displaced. However, as the technology matures this will become a major obstacle.
- Reputation and technological feasibility – the majority of the market is dominated by major firms who will require large roll outs. Media agencies are global in scale, hence the workflow solution must be scalable and transferable between a variety of jurisdiction and languages, and integrate with other business systems.

RISK FACTORS

- Competition – While the current market seems to offer a potential greenfields opportunity, the company faces the risk that a competitor or major software provider beats them to the punch and locks the major global media agencies into long-term contracts.
- Execution risk – Rolling out with major global companies may prove problematic, particularly if several contracts are being implemented at once. Further issues might arise following implementation, should FAC be unable to fulfil its service level agreements.
- Cash flow and capital raisings – the business has yet to generate a positive free cash flow, as such it is a net cash consumer. Should it be unable to start generating positive cash flow over the next 18 months, additional capital raisings may be required.
- Technology risk
- FAC cost base is largely based in Australia, while its strategy is focussed on international markets. This will expose the company to a degree of FX risk.
- Dilution risk – because the board is largely controlled by insiders, option based remuneration could lead to substantial dilution of shareholders.

BOARD & MANAGEMENT

- Mr Stuart Simson (Independent Chairman) joined the board on 9-Jul-09. Mr Simson has 40 years of experience in media and marketing. He currently serves on the board of Parts All Over Pty Ltd and has previously served as Chairman of emitch Ltd. He owns 1,370,436 shares.
- Mr Geoff Dixon (Non-executive Director) joined the board on 9-Jul-09. He is former Managing Director and CEO of Qantas Airways Ltd and has wide board level experience in the media, general business and philanthropic sectors. He currently serves of the boards of Crown Ltd and Consolidated Media Holdings Ltd. He owns 2,769,559 shares.
- Mr Charles Sweeney (Non-executive Director) co-founded facilitate digital with Mr Ben Dixon. Mr Sweeney works as a corporate lawyer specialising in mergers and acquisitions. He owns 7,996,095 shares and 5,249,105 options.
- Mr Ian Lowe (Director and Chief Executive Officer) joined FAC in 2002. He has 23 years of media and marketing experience across a number of organisations including George Patterson Bates, Thompson Media and PMP Ltd. He was Managing Director of Red Sheriff and CEO of Traffion Pty Ltd. Ian holds 6,958,823 shares and 3,724,401 options.
- Mr Ben Dixon (Chief Operating Officer) co-founded FAC with Charles Sweeney. He has 18 years experience in advertising and media buying. Ben holds 16,686,903 shares and 9,802,097 options.

APPENDIX I: KEY PRODUCTS
SYMPHONY

Function	Value to Client	Revenue Model	Target Clients
Planning & Buying Platform	<ol style="list-style-type: none"> Streamlines otherwise manual workflow, with potential for 25-45% efficiency gains. Aggregation of buying history to inform the buying process 	Fixed & Variable: <ol style="list-style-type: none"> Upfront fee to engage Pre-implementation consulting fee Per seat fee: fixed per seat, monthly recurring 	Media Buying Agencies

Major Competitors	FAC Differentiation	Integrated Offering
Double Click Donovan Data Systems	<ol style="list-style-type: none"> More mature product, richer functional capabilities (first released in 2005, first to market). Vendor agnostic (integrates with all finance systems and adservers) Implemented under a research and consulting model (e.g. SAP) Independent provider (i.e. Investment data remains within the agency) 	Symphony pulls data from Facilitate's aderving platform into key areas such as trafficking, finance and reporting Bundling provides price and revenue model flexibility

FACILITATE FOR AGENCIES

Function	Value to Client	Revenue Model	Target Clients
Publishing and tracking of online display, search and rich media campaigns.	<ol style="list-style-type: none"> Reporting to assess campaign performance (real time) Tools to optimise campaign performance Aggregation of campaign performance data to inform the planning process 	Variable – revenue generated for every ad impression and/or click	Publishers Creative agencies

Major Competitors	FAC Differentiation	Integrated Offering
Double Click Atlas EyeBlaster	<ol style="list-style-type: none"> Independent provider (i.e. no conflict of interest as a media owned technology) More efficient workflow (i.e. campaign set up and admin takes 30% less time) Unique capabilities in the fast growing performance media segment 	Facilitate advertising is fully integrated into the Symphony workflow Bundling provides price and revenue model flexibility

APPENDIX II: Client Testimonial - Zenith Optimedia

Description: Zenith Optimedia is a part of the global Pubicis Goupe. It offers a wide range of services, from the development of communications strategy, through executional planning, negotiation and implementation.

Select Equities spoke with a representative of Zenith Optimedia, a client of FAC, who provided the following feedback.

Key Points:

- Zenith Optimedia user feedback assisted FAC to develop the Symphony product, it therefore may have a biased opinion on how good they think it is.
- Zenith commented that Symphony automates a previously manual process, allows them to remove human resources and human error as well as reducing financial administration.
- They are of the view that that Symphony is a groundbreaking product.
- They see Symphony as a fundamental tool to manage the shift to online advertising. Approximately, 90% of Zenith's clients use it, and Zenith plan to continue to use the software. Zenith feel that there is no comparable product out there at this stage.

Facilitate Digital Holdings Ltd

Select Equities Research

Small Caps

Code	FAC	June Year End	FY09A	1H10A	FY10E	FY11E
Last sale (\$)	(23-Jun-10)	0.06				
# Shares (m)	130.5					
# Options	37.1					
Mkt Cap (\$m)	9.9					
Cash	1.2					
Net Cash	1.1					
Enterprise Value	8.8					
June Year End	FY09A	1H10A	FY10E	FY11E		
Financial Position (\$m)						
Cash	1.4	1.2	1.9	2.6		
Trade Debtors	1.4	1.5	1.6	2.1		
Other Current Assets	0.0	0.0	0.0	0.0		
Prop.,Plant&Equip. (net)	0.2	0.2	0.2	0.2		
Deferred Tax Assets	0.0	0.0	0.0	0.0		
Investments	0.0	0.0	0.0	0.0		
Intangibles	3.0	3.2	3.3	3.4		
Other	0.5	0.5	0.5	0.5		
Total Assets	6.5	6.5	7.5	8.9		
Trade Creditors	1.8	2.0	2.1	2.7		
Current Tax Liabilities	0.2	0.1	0.2	0.2		
Debt	0.1	0.1	0.1	0.1		
Provisions	0.5	0.4	0.5	0.6		
Trade & Other Payables	0.0	0.0	0.0	0.0		
Other Non-Current	0.0	0.0	0.0	0.0		
Total Liabilities	2.5	2.6	2.8	3.6		
Net Assets	4.0	3.9	4.7	5.3		
Issued Capital	13.3	13.3	14.1	14.1		
FX Reserve	-0.1	0.0	-0.1	-0.1		
Reserves	0.3	0.1	0.4	0.5		
Retained Earnings	-9.4	-9.5	-9.7	-9.2		
Total Equity	4.1	3.9	4.8	5.4		
Cash Flows (\$m)						
Net Receipts	0.6	0.7	1.7	2.9		
Net Interest	0.0	0.0	0.1	0.1		
Tax Paid	0.0	0.0	0.1	-0.2		
Operating Cash Flow	0.5	0.7	1.9	2.9		
Development Spend	-1.9	-0.9	-2.0	-2.0		
Capex & Acquisitions	-0.1	0.0	-0.2	-0.2		
Asset Sales & Divest	0.0	0.0	0.0	0.0		
Investing Cash Flow	-1.9	-0.9	-2.2	-2.2		
Change in Equity (net)	0.9	0.0	0.8	0.0		
Change in Debt (net)	0.2	0.0	0.0	0.0		
Dividends	0.0	0.0	0.0	0.0		
Financing Cash Flow	1.2	0.0	0.7	0.0		
Net Inc/Dec Cash	-0.2	-0.2	0.4	0.7		
Cash at Beginning of Yr	1.6	1.4	1.4	1.9		
Cash at End of Year	1.4	1.2	1.9	2.6		
Substantial Shareholders (16 Sep 2009)						
				No. (m)		%
Ian Lowe and Ben Dixon				13.9		11.5%
Eye Wonder Inc				12.9		10.7%
Tarbate Pty Ltd				8.7		7.2%
Dunsmore Nominees Pty Ltd				7.9		6.5%
Michael Lane				7.5		6.2%
Interim Results (\$m)	2H08	1H09	2H09	1H10		
Sales	1.9	2.7	3.7	3.6		
Op EBITDA	-0.9	-0.2	0.8	0.6		
D & A	-0.6	-0.5	-0.8	-0.8		
Op EBIT	-1.6	-0.8	0.0	-0.2		
PBT	-1.5	-0.7	0.0	-0.2		
NPAT (pre-abs. & OEI)	-0.1	-2.1	-0.1	-0.1		
Abnormals	1.1	-7.0	0.0	0.0		
NPAT (pre-oei)	1.0	-9.1	-0.1	-0.1		
OEI	0.0	0.0	0.0	0.0		
Reported NPAT	1.0	-9.1	-0.1	-0.1		

Source: Company Reports and Select Equities Research

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