

1H17 RESULT, RAMP UP TO COMMENCE IN 4Q17

Revenue Generation Commences, but XM completion is the Key

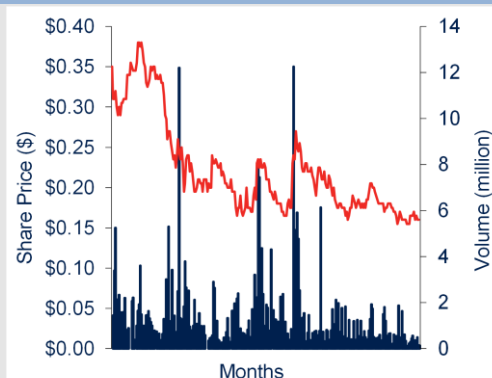
- Following the completion of the XM integration process, ISX now has an automated platform that converges payment transactions with identity verification, and is uniquely placed to provide such services that meet ever tighter regulatory conditions. Cyprus has fully implemented the EU 4th Anti Money Laundering Directive (AMLD) which is a key jurisdiction for FX and Gaming operators. The UK is expected to follow by June. While there are other jurisdictions that need to implement the regulations, these two regulators are key to enabling ISX's full commercial service to be deployed. At the commercial level, a leading FX broker is closing in on a "go live" date for commencing transaction flow. The last aspects of integration are now occurring and it is possible that transactions will commence in the next few weeks. XM is a leader in the retail online FX industry turning over cUS\$12bn / day. We understand that other major customer prospects are waiting to see XM commence operations with ISX before moving forward themselves. XM is key to commercialising the ISX identity and payment processing platform and making ISX profitable. We see this event as a milestone and believe that it should be a catalyst for share price appreciation. **BUY**
- ISX noted that it is now in a position to convert opportunities with customer prospects through finalising integration with several customers that have signed agreements with ISX in the last few months. These customers typically range in size from c5% to c20% of XM, which would make them each material in their own right. ISX is suggesting that they could "go live" progressively from early 4QFY17. Two other large customers; Leverate and FXNet should commence integration in April and could be operational before the end of FY17.
- ISX has actually commenced revenue generation with a couple of small clients late in 1H17. We understand the current revenue run rate is growing significantly month-on-month and these customers are able to expose ISX to a wider customer base across new jurisdictions as the user experience requires.
- It is not yet clear whether ISX will meet our revenue forecast for FY17 as the service offering remains at the embryonic level. However, we are moving closer to ISX being ready to generate strong sales and earnings momentum for FY18.

Year End June 30	2015A	2016A	2017F	2018F	2019F
Reported NPAT (\$m)	(9.6)	(9.2)	0.3	9.1	21.5
Recurrent NPAT (\$m)	(1.9)	(4.4)	0.3	9.1	21.5
Recurrent EPS (cents)	(0.6)	(0.7)	0.0	0.9	2.1
EPS Growth (%)	na	na	na	2,436.5	135.5
PER (x)	(27.0)	(21.9)	445.1	17.5	7.5
PEG	na	na	na	0.0	0.1
EBITDA (\$m)	(1.5)	(4.3)	0.3	13.0	30.5
EV/EBITDA (x)	(34.4)	(22.4)	490.1	12.4	5.3
Free Cashflow	0.9	(3.7)	(0.4)	6.1	17.0
FCFPS (cents)	0.3	(0.6)	(0.1)	0.6	1.7
PFCF (x)	54.8	(25.6)	(315.4)	26.5	9.4
DPS (cents)	0.0	0.0	0.0	0.4	1.1
Yield (%)	0.0	0.0	0.0	2.8	7.0
Franking (%)	0.0	100.0	100.0	100.0	100.0

1 March 2017		
12mth Rating		BUY
Price	A\$	0.17
Target Price	A\$	0.50
12mth Total Return	%	194.1
RIC: ISX.AX		BBG: ISX AU
Shares o/s	m	290.2
Free Float	%	67.0
Market Cap.	A\$m	49.3
Net Debt (Cash)	A\$m	-2.3
Net Debt/Equity	%	-65.3
3mth Av. D. T'over	A\$m	0.11
52wk High/Low	A\$	0.275 / 0.145
2yr adj. beta		0.26
Valuation:		
Methodology		DCF
Value per share	A\$	0.50

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12 Month Share Price Performance



Performance %	1mth	3mth	12mth
Absolute	13.3	3.0	-32.0
Rel. S&P/ASX 300	13.3	-1.8	-49.4

MARKET UPDATE

XM

The integration with XM is almost complete. Although it has taken a long time from announcement (July 2016) to live transaction flow, XM's trading turnover is cUS\$12bn / day and thus getting the operating infrastructure to service this client 100% correct is critical to ISX's future.

XM has required ISX to make additions to its platform, including integrations with Asian payment facilitators, external data sources and the MT4 / MT% trading platforms. This has now been completed and XM is currently planning its operational "cutover" process to the ISX platform. This involves changes to back office, operations, payment facilitation across multiple regions, transaction processing and compliance functions, impacting XM customers, operations and personnel directly. These elements are important to ensure there are no customer outages. Even an outage of a few minutes can be highly disruptive with a high frequency trading business.

XM does appear to be in the final stages of readiness to "go live", and this is now expected within weeks. When this occurs, it will be a milestone event for ISX, as XM is capable of making ISX profitable on an annual basis, given the current annual cost base of c\$4.8m. In our initiation report we conveyed our view of potential revenue generation from the XM transaction flows that we repeat below. Note, that in our model, we assume the transaction value of c75% of actual turnover.

Figure 1: XM Financial Model - Estimated

XM	
Backlog KYC	
Existing Customers to Verify	500,000
Average Verifications per Person per annum	1.0
Price per Verification - EUR cents	2.0
Verification Revenue - EUR dollars	1,000,000
AUD / EUR rate	0.70
Verification Revenue - AUD	1,428,571
New KYC	
New Customers per week	5,000
Customers per year	260,000
Average Verifications per person	1.0
Price per Verification - EUR	4.5
Verification Revenue - EUR	1,170,000
AUD / EUR rate	0.70
Verification Revenue - AUD	1,671,429
Processing - Not Acquiring	
Transactions per Customer per year	12
Total Transaction per annum	9,120,000
Fee per Transaction - EUR	0.08
Transaction Processing Revenue - Not Acquiring	729,600
AUD / EUR	0.70
Transaction Processing Revenue - Not Acquiring	1,042,286
Settlement	
Number of Transactions per year	9,120,000
Average Price per Transaction - EUR	1000
Transaction Value per year - EUR	9,120,000,000
Net Fee to ISX	0.50%
Settlement Revenue @ 100% of Transactions - EUR	45,600,000
AUD / EUR	0.70
Settlement Revenue @ 100% of Transactions - AUD	65,142,857
% of Settlement Volume Allocated to ISX	5.0%
Settlement Revenue to ISX - AUD	3,257,143
Total ISX Revenue from XM - AUD	7,399,429

Source: Patersons Securities Ltd

Other Merchants

ISX has pleasingly recognised that it has limited resources and cannot keep focusing on expanding the platform or seeking new customers. At present it needs to convert the existing group of customers from “sign up” into live transacting customers that generate revenues. This is particularly so as ISX has only c\$6.4m in cash.

ISX has highlighted the next four of its customers that are actively engaged in finalising integrations. These customers (Valutrades, Marketsworld, IronFX, and Calforex) represent from c5% to c20% the size of XM. While much smaller than XM, they are each meaningful in size in their own right and each have substantial revenue generating potential for ISX.

The XM integration process has meant that all future customers should be integrated far more smoothly and quickly, although this is still to be proven. We understand that the integration process, standards and features have been set by the XM process and future integrations should be conducted in an “off the shelf” manner. Our current expectations are that this group of customers could “go live” in 4Q17.

Beyond this group, Leverate and FXNet, which are understood to be c15% and c30% the size of XM, are expected to begin the integration process in April 2017 and should also “go live” later in 4Q17.

Payment Facilitation

ISX note that testing of the platform to be used for the NAB partnering arrangement is under final testing and could be ready for ISX to sell services into by April. We would expect small customers to sign up at first to provide real life proof of the identity and transaction mechanisms before larger customers could be attracted.

ISX noted that a range of international acquiring partners to enable payment facilitation have now been integrated and are transaction ready. We expect this to attract merchants who have relationships with these acquiring partners, and who need the network connections to be correctly established before engaging with ISX. The XM process has resulted in producing a substantial network of infrastructure modules and connections to the most popular acquirers used across the FX industry sector.

Regulatory Environment

ISX acknowledged that its business model relies on regulatory certainty and it can be interpreted that ISX has chosen to move ahead of the curve in anticipation of certain regulatory events occurring.

While the EU parliament approved the 4th Anti Money Laundering Directive (AMLD) in early 2016, implementation requires a national phase of transitioning the EU law into local regulations (transposition) in member states. ISX note that full commercial release of the platform relies upon finalised regulatory requirements.

The UK’s Treasury confirmed in November 2016 that the 4th AMLD would be transposed into UK law, despite Brexit. The Joint Money Laundering Steering Group (JMLSG) guidance previously released remains valid and we expect this to be converted into local regulation by the end of June.

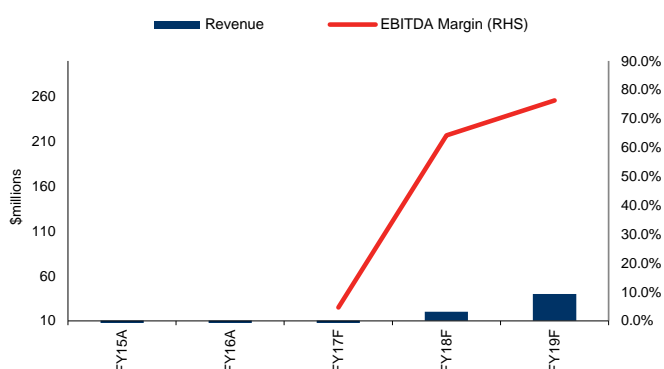
We note that the Cypriot regulator has already confirmed transposition, which is important as many customer prospects are domiciled in Cyprus.

The Cyprus and UK positions have formed the basis for ISX to complete its platform and the requisite logic displays and reporting were completed in early February 2017. The various modules developed by ISX to meet compliance of these regulations will provide the basis for delivering solutions to other Financial Action Task Force (FATF) jurisdictions.

ISX is uniquely placed as the only provider of a Payidentity style service that automates convergence of payment transactions with identity verification, and has completed this process as per its expectations.

iSignthis (ISX)	\$0.17			
Cash Flow (\$m)	2016A	2017F	2018F	2019F
Adj. Operating Cashflow	-3.9	0.9	7.2	18.6
Capex	-0.1	-1.0	-1.0	-1.0
Capitalised R&D	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0
Acquisitions	0.0	0.0	0.0	0.0
Earn-out Payments	0.0	0.0	0.0	0.0
Investing Cashflow	-0.1	-1.1	-1.1	-1.1
Equity Raised	10.7	0.0	0.0	0.0
Increase (Repay) Debt	0.0	0.0	0.0	0.0
Distributions Paid	0.0	0.0	-1.4	-7.8
Other	0.0	0.0	0.0	0.0
Financing Cashflow	10.7	0.0	-1.4	-7.8
Change in Cash Held	6.8	-0.2	4.7	9.7
Closing Cash Balance	9.0	8.8	13.5	23.2

Revenue & Margins



Valuation	2017F	FY18F	FY19F
DCF			
Beta			2.0x
WACC			18.0%
DCF per share			\$0.50
Capitalisation of future earnings	2017F	2018F	2019F
EBITDA	0.3	13.0	30.5
EV / EBITDA multiple	15.0x	15.0x	15.0x
Enterprise value	4.0	194.6	457.7
Net cash / (debt)	8.8	13.5	23.2
Equity value	12.8	208.0	480.9
Equity value per share	\$0.02	\$0.21	\$0.48

Directors & substantial shareholders

Name	Position
Timothy Joseph Hart	Independent Chairman
Nickolas John Karantzis	Managing Director
Barnaby Ian Robert Egerton-Warburton	Independent Non Exec Director
Scott William Minehane	Independent Non Exec Director

Shareholder	No. shares	%
iSignthis Ltd	311.7	50.1
Deutsche Bank	31.9	5.1
Total substantial	343.6	55.2

Profit & Loss (\$m)	2016A	2017F	FY18F	FY19F
Sales Revenue	0.4	5.7	20.2	40.0
COGS	0.0	-0.3	-1.0	-2.0
Gross Profit	0.4	5.4	19.2	38.0
Operating Expenses	-4.7	-5.2	-6.2	-7.5
Associates	0.0	0.0	0.0	0.0
EBITDA	-4.3	0.3	13.0	30.5
Depn & Amort	-0.1	-0.2	-0.3	-0.3
EBIT	-4.4	0.1	12.7	30.2
Net Interest	0.0	0.3	0.4	0.5
PBT	-4.4	0.4	13.0	30.7
Tax expense	0.0	-0.1	-3.9	-9.2
NPAT (Underlying)	-4.4	0.3	9.1	21.5
Adjustment	-4.9	0.0	0.0	0.0
Statutory NPAT	-9.2	0.3	9.1	21.5
NPAT (Adjusted)	-4.4	0.3	9.1	21.5

Segment Revenue (\$m)	2017F	FY18F	FY19F
Average User No. (m)	1.5	2.8	3.8
Average Transactions Processed (m)	3.0	13.0	25.8

Verification Catch-Up Revenue	2.4	1.8	1.8
Verification Annuity Revenue	1.6	12.1	19.3
Transaction Processing Revenue	1.3	4.6	7.7
Settlement Revenue	0.4	1.8	11.3
Total Revenues	5.7	20.2	40.0

Balance Sheet (\$m)	2016A	2017F	FY18F	FY19F
Cash	9.0	8.8	13.5	23.2
PP&E	0.2	1.1	2.0	2.8
Intangibles	1.2	1.1	1.1	1.0
Other	0.1	2.5	4.1	8.0
Assets	10.4	13.5	20.6	35.0
Payables	0.5	2.5	1.9	2.5
Borrowings	0.0	0.0	0.0	0.0
Other liabilities	0.1	0.1	0.1	0.1
Liabilities	0.7	2.6	2.0	2.6
Shareholders Funds	9.7	11.0	18.7	32.4

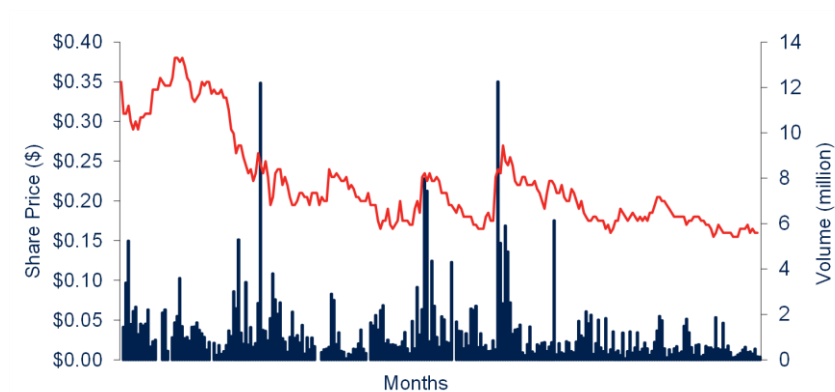
EPS & DPS	2016A	2017F	FY18F	FY19F
EPS (Reported)	-1.5	0.0	0.9	2.1
EPS (Adjusted)	-0.7	0.0	0.9	2.1
EPS growth (%)	23.7	-104.9	2437.1	135.5
DPS	0.0	0.0	0.4	1.1
Payout Ratio (%)	0.0	0.0	49.3	52.4
Dividend Yield (%)	0.0	0.0	2.6	6.6

Ratios	2016A	2017F	FY18F	FY19F
Profitability				
NPAT Growth (%)	133.6	-106.7	3031.4	135.5
Sales Growth (%)	1432.6	1191.4	252.3	97.9
EBITDA Margin (%)	-961.0	4.6	64.2	76.3
ROIC (%)	-555.8	-3.0	168.1	226.6
ROE (%)	-44.9	2.7	48.9	66.4
ROA (%)	-40.9	2.0	62.8	87.2
Tax Rate (%)	0.0	30.0	30.0	30.0

Valuation	2016A	2017F	FY18F	FY19F
Price / Earnings (x)	-23.3	473.5	18.7	7.9
EV / EBITDA (x)	-22.7	609.6	12.1	4.8
Price / FCF (x)	-24.8	-269.7	29.8	10.1
Price / NTA (x)	11.9	14.1	9.7	5.4

Balance Sheet	2016A	2017F	FY18F	FY19F
Net Debt / Equity (%)	-91.9	-80.3	-72.1	-71.4
Net Debt / Assets (%)	-85.9	-65.1	-65.3	-66.2
Interest Cover (x)	-3143.8	-0.2	-36.1	-56.0
NTA (\$/share)	0.0	0.0	0.0	0.0
Shares (m)	621.8	1002.8	1002.8	1002.8

Recommendation History



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