



Dreamscape Networks Limited (DN8.ASX)

Looking to control costs and rebasing expectations

Event:

- 1H18a result; FY18e EBITDA guidance.

Investment Highlights:

- DN8 recently announced 1H18a results**, and while the business recorded solid top line growth for the period (up 30% to \$29.3M on pcp), there were also increased costs for marketing and personnel to set up for its South East Asian expansion (up 27% to \$13.7M on pcp), which compressed margins and profit. Underlying NPAT for the half was \$1.5M, down from \$1.6M in pcp.
- Recent acquisitions (Net Logistics, Vodien, Enetica) accounted for the top line growth**, which was modestly offset by flat conditions in domestic domain and hosting. The company expects the Australian market to remain flat over the next half.
- Looking to control costs in the coming second half:** while DN8 did cycle off a low cost half in 1H17a, the company did need to invest for future growth, allocating increased marketing and personnel spend for its South East Asian expansion, which was in line with budgeted spend, in spite of prima facie cost increase of 27% on pcp.
- Systematic program in place to address costs over 2H18e.** The company has brought forward its office consolidation with a new centralised Singaporean head office, and closure of its offices in Perth and Dubai. The company will also consolidate its data centre functions for Enetica and Quadra to its Sydney facility, as well as duplicated customer care operations for Vodien and Net Logistics into its existing customer care centre in the Philippines. We keenly anticipate progress on this checklist and updates from the company over the coming half.
- The company **guided for FY18e adjusted EBITDA of \$7.2–7.6M**, inferring an improvement over second half trading of \$4–4.4M in 2H18e, compared with adjusted EBITDA in 1H18a of \$3.2M.

Earnings and Valuation:

- We have revised our earnings and now forecast **FY18e NPAT of \$2.5M (previously \$2.6M), and \$3.2M in FY19e (\$4.1M), and EPS of 0.7cps and 0.8cps, respectively (0.7cps and 1.1cps)**, as a result of flat domestic conditions and new cost base for the remainder of FY18e.
- We have decreased our valuation to \$0.265/share (previously \$0.29)** in line with our updated DCF valuation.

Recommendation:

- We maintain our Buy recommendation with a decreased price target of \$0.265 (previously \$0.29), in line with our DCF valuation.** We note the recent price pullback, and remain of the view a near term opportunity exists due to the recent overreaction.
- Catalysts for the share price** include: 1) executing on cost control and acquisitions synergies; 2) increased end user numbers; 3) increased average booking per user (ABPU); 4) continued upsell into higher value products from DN8's significant domain name market share; 5) further acquisitions.

Recommendation		Buy			
Previous		Buy			
Risk		High			
Price Target		\$0.265			
Previous Target		\$ 0.29			
Share Price (A\$)		\$ 0.160			
ASX Code		DN8			
52 week low - high (A\$)		0.135-0.245			
Capital structure					
Shares on Issue (M)		388			
Market Cap (A\$M)		62			
Net Cash/(Debt) (A\$M)		1			
EV (A\$m)		61			
Options, rights (M)		33			
12mth Av Daily Volume ('000)		251			
June end (A\$M)		2017a	2018e	2019e	2020e
Sales		46.4	61.8	67.8	75.0
EBITDA, underlying		4.5	6.6	8.3	11.2
NPAT, underlying		2.1	2.5	3.2	5.1
EPS diluted (cps)		0.63	0.66	0.82	1.31
PER x diluted		25.3	24.3	19.5	12.2
EV/EBITDA x		13.5	9.1	7.3	5.4
Board					
Mr Peter James		Non-Executive Chairman			
Mr Michael Malone		Non-Executive Director			
Mr Evan Cross		Non-Executive Director			
Mr Mark Evans		Managing Director & CEO			
Mr Gavin Gibson		Executive Director & COO			
Major Shareholders					
Bluegeko Holdings		36.4%			
Cloudsafe Holdings		24.3%			
Alvin Chiang		5.5%			
Jervis Wen		5.5%			
Australian Ethical Investment		5.1%			

Share Price Graph



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The analyst does not own DN8 securities.

Foster Stockbroking and associated entities (excluding Cranport Pty Ltd) do not own DN8 securities.

Cranport Pty Ltd owns 3,191,317 DN8 shares.

This report was prepared by Foster Stockbroking.