



## Freelancer Ltd (FLN.ASX)

*Share price fall overdone as fundamentals unchanged*

### Event:

- Review of FLN post 3Q release; Share price decline.

### Investment Highlights:

- FLN's 3Q report showed receipts up 31% YoY, below our expectations of 54% growth.** While no precise breakdown on divisions were provided, we estimate growth in the core Marketplace was 15% YoY and in Escrow.com -12% YoY (proforma basis), both softer than we had forecast.
- The company cited a China domain bubble impact from earlier as inflating previous comparative sales for Escrow.com.** Also some initiatives that FLN is implementing – such as KYC/AML for accounts– may have introduced some friction to growth in short-term. We still see solid prospects for Escrow.com with annual growth to be ca 20% using 3Q receipts as a normalised base.
- For Marketplace the chief reason was the impact of the higher A\$, which we had underestimated.** The tailwind that FLN enjoyed from the gradual weakening of the A\$ since 2013 has now ceased. We estimate constant currency growth was 19% YoY, in-line with historical marketplace growth and suggesting no change to fundamentals.
- We did not see anything materially of concern in the result.** We expect Escrow.com growth, while cycling inflated YoY comps, should exhibit double-digit annualised growth base on 3Q revenues as a baseline. For Marketplace, we expect it will cycle weaker A\$ comps over next 12 months and then normalise. We forecast Marketplace constant currency sales growth of 20% YoY.

### Earnings and valuation:

- We have revised down our earnings forecasts to -\$1.1M and -\$0.7M in FY16e and FY17e (previous \$0.0M and \$0.5M)** based mostly on reducing our sales forecasts, offset slightly by reining in our costs projections.
- Increase in our A\$ forecasts has contributed to sales revision,** while our reduced costs are based on the company providing estimated projections for cash outflows in the current quarter, implying previous rate of costs growth abating.
- Our NPV<sub>10</sub> valuation has decreased to \$1.57/share now and \$1.71/share in 12 months (previously \$1.98 and \$2.19),** due to our reduction in earnings.

### Recommendation:

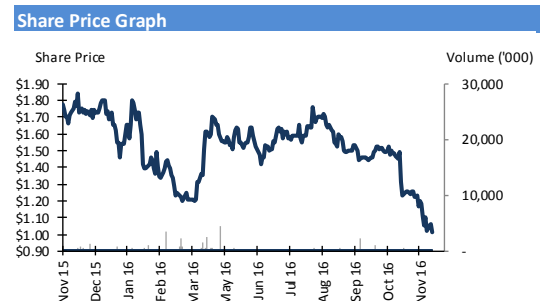
- We maintain our Buy recommendation on FLN, reducing our 12-month price target to \$1.71** (previously \$2.19) in-line with our 12-month forward valuation. The dramatic 48% decline in the shareprice makes our valuation look highly attractive.
- We view the share price fall as mostly overdone as fundamentals are unchanged.** Rather than any material concerns, FLN has simply experienced a softer than anticipated quarter in which still high-double digit growth was achieved in the core business.
- Catalysts for the stock include continuing double-digit growth in Marketplace revenues;** improving Escrow.com revenues; reducing rate of costs growth; improving profitability; and weaker A\$.

<b>Recommendation</b>	<b>Buy</b>
Previous	Buy
<b>12 mth Price Target</b>	<b>\$ 1.71</b>
Previous	\$ 2.19
<b>Share Price (A\$)</b>	<b>1.030</b>
ASX Code	FLN
52 week low - high (A\$)	0.995-1.86
Valuation \$/sh	\$1.57 now, \$1.71 in 12mths
Methodology	DCF
Risk	Med
<b>Capital structure</b>	
Shares on Issue (M)	458.7
<b>Market Cap (A\$m)</b>	<b>472.5</b>
Net Debt/(Cash) (A\$m)	-34.3
<b>EV (A\$m)</b>	<b>438.2</b>
12mth Av Daily Volume ('000)	225.0

Y/e Dec Forecasts	2015a	2016e	2017e	2018e
Revenue A\$m	38.2	52.8	64.6	77.6
Revenue growth	48%	38%	22%	20%
NPAT A\$m	-2.8	-1.1	-0.7	-0.4
EPS c	-0.6	-0.2	-0.2	-0.1
PER x	nm	nm	nm	nm
EV/sales	11.3	8.3	6.7	5.5

Board	
Matt Barrie	Executive Chairman
Darren Williams	Non-Executive Director
Simon Clausen	Non-Executive Director

Substantial shareholders	
Matt Barrie	42%
Simon Clausen	34%



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## Freelancer Ltd (FLN)

Full Year Ended 31 December

Profit and Loss A\$M	2015a	2016e	2017e	2018e
Sales revenue	38.2	52.8	64.6	77.6
Other revenue	0.2	0.1	0.1	0.1
Operating Costs	41.8	54.2	65.2	77.7
<b>EBITDA</b>	<b>-3.4</b>	<b>-1.3</b>	<b>-0.6</b>	<b>-0.2</b>
D&A	0.5	0.7	0.9	1.0
<b>EBIT</b>	<b>-3.9</b>	<b>-2.1</b>	<b>-1.5</b>	<b>-1.2</b>
Net Interest exp / (income)	-0.2	-0.4	-0.7	-0.8
<b>Profit before tax</b>	<b>-3.7</b>	<b>-1.6</b>	<b>-0.7</b>	<b>-0.4</b>
Tax exp / (benefit)	-0.9	-0.5	0.0	0.0
<b>NPAT before minorities</b>	<b>-2.8</b>	<b>-1.1</b>	<b>-0.7</b>	<b>-0.4</b>
Minority interest	0.0	0.0	0.0	0.0
<b>Rep. NPAT</b>	<b>-2.8</b>	<b>-1.1</b>	<b>-0.7</b>	<b>-0.4</b>
Significant items	0.0	0.0	0.0	0.0
<b>NPAT attributable reported</b>	<b>-2.8</b>	<b>-1.1</b>	<b>-0.7</b>	<b>-0.4</b>
<b>EPS diluted (c)</b>	<b>-0.6</b>	<b>-0.2</b>	<b>-0.2</b>	<b>-0.1</b>

Cashflow A\$M	2015a	2016e	2017e	2018e
EBITDA	-3.4	-1.3	-0.6	-0.2
Change in WC	4.9	5.3	5.9	6.7
Tax paid	0.0	0.2	0.0	0.0
Net interest	0.2	0.4	0.7	0.8
Other	-0.2	0.7	0.0	0.0
<b>Operating Cashflow</b>	<b>1.5</b>	<b>5.3</b>	<b>6.0</b>	<b>7.3</b>
Acquisitions	-10.3	-1.0	0.0	0.0
Capex	-1.0	-0.6	-1.0	-1.2
<b>Investing Cashflow</b>	<b>-11.2</b>	<b>-1.7</b>	<b>-1.0</b>	<b>-1.2</b>
Equity raising	20.1	0.3	0.0	0.0
Other	-0.5	0.0	0.0	0.0
<b>Financing Cashflow</b>	<b>19.7</b>	<b>0.3</b>	<b>0.0</b>	<b>0.0</b>
<b>Net Cashflow</b>	<b>9.9</b>	<b>4.0</b>	<b>4.9</b>	<b>6.1</b>

Balance Sheet A\$M	2015a	2016e	2017e	2018e
Cash	32.2	35.6	40.6	46.7
Receivables	3.6	4.1	5.0	6.0
PPE	1.7	1.6	1.7	1.9
Intangibles	23.9	24.9	24.9	24.9
Deferred tax	2.9	2.9	2.9	2.8
Other	1.4	1.3	1.5	1.9
<b>Total Assets</b>	<b>65.6</b>	<b>70.4</b>	<b>76.7</b>	<b>84.2</b>
Accounts payable	31.3	33.2	40.0	47.7
Provisions	1.4	1.3	1.6	1.9
Deferred revenue	0.8	1.1	1.4	1.7
Other	0.0	0.0	0.0	-0.4
<b>Total Liabilities</b>	<b>30.7</b>	<b>35.9</b>	<b>42.9</b>	<b>50.8</b>
Reserves and capital	38.5	39.5	39.5	39.5
Retained earnings	-3.6	-5.0	-5.7	-6.1
<b>Total Equity</b>	<b>34.9</b>	<b>34.5</b>	<b>33.8</b>	<b>33.4</b>

Source: Company; Foster Stockbroking estimates

Financial Metrics	2015a	2016e	2017e	2018e
Sales growth %	48%	38%	22%	20%
EPS growth %	nm	nm	nm	nm
EBITDA margin	-9%	-3%	-1%	0%
EBIT margin	-10%	-4%	-2%	-2%
Gearing (ND/ND+E)	nm	nm	nm	nm
Interest Cover (EBIT/net int)	nm	nm	nm	nm
Average ROE %	-11%	-3%	-2%	-1%
Average ROA %	-15%	-6%	-4%	-4%
Wtd ave shares (M)	440	452	459	459
Wtd ave share diluted (M)	450	459	459	459

Valuation multiples	2015a	2016e	2017e	2018e
P/E x	nm	nm	nm	nm
EV/EBITDA x	nm	nm	nm	nm
EV/EBIT x	nm	nm	nm	nm
EV/sales x	11.2	8.2	6.6	5.5
Dividend yield %	0	0	0	0

Equity Valuation - DCF	Now		12 months time	
	A\$M	A\$/sh	A\$M	A\$/sh
Enterprise value	684.6	1.49	745.3	1.62
Net debt (cash)	-34.9	-0.08	-38.1	-0.08
<b>Equity (NPV)</b>	<b>719.5</b>	<b>1.57</b>	<b>783.4</b>	<b>1.71</b>

Shares on issue	M
Ordinary shares	458.7
Fully Diluted	458.7

Major shareholders	Interest
Matt Barrie	42%
Simon Clausen	34%

Board	
Matt Barrie	CEO & Chairman
Simon Clausen	Non Executive Director
Darren Williams	Non-Executive Director



**3Q REVENUES EXHIBIT SLOWER THAN ANTICIPATED GROWTH**

- Freelancer (FLN) reported cash receipts for the 3QFY16 of \$12.7M, up 31% YoY and below our expectation of \$15.0M, or 54% growth. Although the company did not breakdown the exact revenue split between Marketplace and Escrow.com, it did provide a moving 30-day average graphic from which we derived our own estimates. We arrived at \$11.1M and \$1.7M for Marketplace and Escrow, representing 15% and -12% (proforma) YoY growth. These were both lighter than our forecast \$12.3M and \$2.6M.

**Figure 1: FLN Quarterly Receipts and Growth**

FY end Dec	1Q15a	2Q15a	3Q15a	4Q15a	1Q16a	2Q16a	3Q16a
<b>Receipts (A\$M):</b>							
Marketplace	8.0	8.8	9.7	10.1	10.6	10.3	11.1
Escrow.com	-	-	-	1.8	2.3	3.1	1.7
<b>Total</b>	<b>8.0</b>	<b>8.8</b>	<b>9.7</b>	<b>11.9</b>	<b>12.8</b>	<b>13.3</b>	<b>12.7</b>
<b>Growth YoY (%):</b>							
Marketplace	43%	40%	43%	36%	32%	17%	15%
Escrow.com							-12%*
<b>Total</b>	<b>48%</b>	<b>40%</b>	<b>43%</b>	<b>61%</b>	<b>60%</b>	<b>51%</b>	<b>31%</b>
<b>Constant currency growth :</b>							
Marketplace	29%	21%	18%	19%	24%	13%	19%
Escrow.com							-9%*
<b>total</b>	<b>29%</b>	<b>21%</b>	<b>18%</b>	<b>40%</b>	<b>50%</b>	<b>47%</b>	<b>36%</b>

\*Based on proforma Escrow.com revenue of \$2.2M in 3Q15  
Source: Company; Foster Stockbroking estimates.

Escrow impacted by China bubble.

Marketplace constant currency growth in-line with historical performance.

**Escrow hit by China domain bubble...**

- Revenue from Escrow.com was weaker than we had forecast, mostly due to the bubble in Chinese domain name market in late 2015/early 2016, which the company cited to be non-core, as well as a stronger A\$. We expect the revenue generated by Escrow.com in the 3Q is now more indicative of a base line going forward, the company indicating that its China volumes now reverting back to be in line with long-term trendline.

**....while still being restructured**

- FLN continues to restructure and re-architect Escrow.com. During the quarter the business' headquarters were moved to San Francisco; Engineering, support and other functional staff in Sydney, Vancouver, and Manila were deployed; Re-architecture of the platform included a new website for enhancing user experience; and a tightening of compliance processes post



acquisition in-line with what has been standard in Marketplace. The last likely had a frictional impact on growth.

- Languages and currency continue to be expanded. Two major currencies yet to be introduced are British sterling and the A\$, which require appropriate licensing. We expect these to be added by end 1HCY17 and should provide a fillip to growth.

### **Marketplace impacted by currency turnaround**

- Unlike Escrow, the weakness in the Marketplace seemed purely due to the stronger \$A, which had appreciated 5% YoY. Assuming 80% of Marketplace revenues denominated in US\$ and stripping out currency effects, we estimate constant currency growth was 19% YoY, more in-line with the historical performance of the business (Figure 1).

### **Net cash \$34.3M**

- At the end of September, FLN held \$34.3M cash on balance sheet and no debt.

### **NEW PROJECTS POSTED THE HIGHLIGHT**

- The key highlight of the quarter was posted jobs on Marketplace, which were up 48% YoY to 649k for the Marketplace, the best quarter on record. This follows from the 63% and 46% YoY growth achieved for new jobs posted in the 1Q and 2Q. The leap in growth is due to a various number of improvements the company has implemented that have all contributed to improved user experience, lessened friction, and facilitated posting of projects. Examples include the mobile app which has 1.2M active monthly users, and long-form project posting enabled by predictive questions prompting the poster to more readily fill-in project description and details.
- While marketplace revenues are growing markedly less than projects growth – due to such factors as conversion rate – we expect there is an element of lag on conversion rates lifting. We believe it does highlight the still exceptional demand that can underpin growth of ca. 20% over next few years.
- Liquidity also increased to 73.8% of projects being bid within 60 seconds (up from 70%). Cumulative projects now 10.2M.

### **Local Jobs gathering scale and liquidity**

- Local Jobs continues to build scale for FLN. Jobs have now been posted in 1,000 cities on over 100 countries. Globally average number of bids per project is seven, with 65% receiving bids in first hour and first bid arriving in 15 minutes.

**EARNINGS FORECASTS DOWNGRADED**

- We have downgraded our NPAT forecasts to -\$1.1M and -\$0.7M for FY17e and FY18e, from \$0.0M and \$0.5M previously, mostly due to revision downwards in our sales forecasts, offset slightly by a reduction in our operating costs.

**Pull back in sales growth, increase in A\$ forecast**

- We now expect annual sales growth to be 38%, 22%, and 20% in FY16e, FY17e, and FY18e, vs our previous estimates of 50%, 28%, and 25%. Growth has been revised down both in Marketplace and Escrow, including impact of higher currency headwinds.
- Our new A\$ forecasts are US\$0.75, US\$0.73, and US\$0.73 for FY16e, FY17e, and FY18e vs \$0.70, \$0.68, and \$0.70 previously.

**Figure 2: FLN - Forecast Earnings Changes A\$M**

y/e Jun	FY16e	Old	Chng	FY17e	Old	Chng
<b>Sales revenue</b>	<b>52.8</b>	<b>57.2</b>	<b>-8%</b>	<b>64.6</b>	<b>72.9</b>	<b>-13%</b>
Other revenue	0.1	0.1	0%	0.1	0.1	0%
Operating Costs	54.2	56.8	-5%	65.2	72.2	-11%
<b>EBITDA</b>	<b>-1.3</b>	<b>0.4</b>	<b>nm</b>	<b>-0.6</b>	<b>0.7</b>	<b>nm</b>
D&A	0.7	0.8	-8%	0.9	1.0	-12%
<b>EBIT</b>	<b>-2.1</b>	<b>-0.4</b>	<b>nm</b>	<b>-1.5</b>	<b>-0.3</b>	<b>nm</b>
Net Interest exp / (income)	-0.4	-0.4	0%	-0.7	-0.8	-13%
Profit before tax	-1.6	0.0	nm	-0.7	0.5	nm
Tax exp / (benefit)	-0.5	0.0	nm	0.0	0.0	nm
<b>NPAT</b>	<b>-1.1</b>	<b>0.0</b>	<b>nm</b>	<b>-0.7</b>	<b>0.5</b>	<b>nm</b>

Source: Foster Stockbroking estimates.

**4<sup>th</sup> quarter – we expect 15% YoY receipts growth**

- For the 4th quarter, we forecast receipts of \$13.7M, with Marketplace achieving constant currency growth of 22% YoY and Escrow.com -6% on proforma basis, as it still cycles higher comps. However we forecast it will be a slight lift on the more indicative 3Q number (Figure 3).

**Costs reined in**

- We have also reined in our cost projections. In its quarterly, the company provided estimated cashflows for the 4Q FY16 of \$13.7M. Adjusting for working capital and share-based expenses, we estimate total operating expenses (ex-D&A) to be \$54.2M for the FY16e, vs \$56.8M previously. This implies a modest opex increase in 2H vs 1H of only ca. \$1M, whereas previous cost increase between successive quarters have usually been between \$3M and \$5M.
- We expect marketing, general, and administration costs to grow approximately in-line with sales, while employee costs (mostly associated with engineering and development), less so.



Figure 3: FLN 4Q 16e estimates

FY16 quarters	1Q16a	2Q16a	3Q16a	4Q16e
<b>Receipts (A\$M):</b>				
Marketplace	10.6	10.3	11.1	11.7
Escrow.com	2.3	3.1	1.9	2.0
<b>Total</b>	<b>12.8</b>	<b>13.3</b>	<b>12.7</b>	<b>13.7</b>
<b>Growth YoY (%):</b>				
Marketplace	32%	17%	15%	16%
Escrow.com			-12%*	-11%*
<b>Total</b>	<b>60%</b>	<b>51%</b>	<b>31%</b>	<b>15%</b>
<b>Constant currency growth YoY (%)</b>				
Marketplace	24%	13%	19%	22%
Escrow.com			-9%*	-6%*
<b>Total</b>	<b>50%</b>	<b>47%</b>	<b>36%</b>	<b>21%</b>

\*Proforma growth.

Source: Company; Foster Stockbroking estimates.

**Outlook still positive - focus on fundamentals**

- FLN maintained its bullish outlook for the remainder of FY16, being an “exceptional” year. We do not disagree. While the market and us have tempered back previous highly exceptional sales growth, we still see 20% underlying sales growth over the next few years.
- We do not expect further currency tailwind, with A\$ forecasts flattish (long-term US\$0.75).
- Overall the fundamentals for FLN are intact. If anything we still envisage upside risk especially from the Escrow.com. Growth in this business can markedly improve during FY17e as most of the FLN’s initiatives are completed and begin to filter through sales growth.
- The strong projects growth and the continuing increase in developing world internet penetration developed are other key underlying factors supporting the company’s growth outlook.

**VALUATION REDUCED TO \$1.57 NOW & \$1.71 IN ONE YEAR**

- Our NPV<sub>10</sub> valuation of FLN has reduced to \$1.57/share now and \$1.71/share in 12 months’ time (previously \$1.98 and \$2.19) on the back of the earnings downgrade.

Equity Valuation - DCF	Now		12 mths time	
	A\$M	A\$/sh	A\$M	A\$/sh
Enterprise value	684.6	1.49	745.3	1.62
Net debt (cash)	-34.3	-0.07	-38.1	-0.08
<b>Equity (NPV<sub>10</sub>)</b>	<b>718.9</b>	<b>1.57</b>	<b>783.4</b>	<b>1.71</b>

Source: Foster Stockbroking estimates.

**RECOMMENDATION – MAINTAIN BUY, PT REDUCED TO \$1.71****PT downgraded - but 48% share price fall makes it attractive**

- We maintain our Buy recommendation on FLN, and have reduced our price target to \$1.71/share, based on NPV in 12 months' time. Despite the reduced price target, the share price's dramatic 48% fall post the quarterly release does make FLN shares an attractive Buy, especially in light of the underlying fundamentals being unchanged.



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