

Zip Co (Z1P)

Rating: Buy | Risk: High | Price Target: \$1.60

Ramping It Up With Significantly Bigger Wins Sets The Tone For A Bumper FY19

Key Information

Current Price (\$ps)	0.83
12m Target Price (\$ps)	1.60
52 Week Range (\$ps)	0.58 - 1.30
Target Price Upside (%)	92.8%
TSR (%)	92.8%
Reporting Currency	AUD
Market Cap (\$m)	200.5
Sector	Information Technology
Avg Daily Volume (m)	0.2
ASX 200 Weight (%)	0.02%

Fundamentals

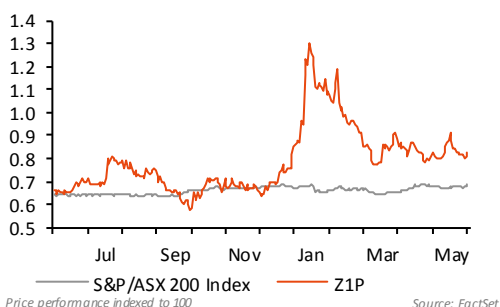
YE 30 Jun (AUD)	FY17A	FY18E	FY19E	FY20E
Sales (\$m)	17.0	35.3	69.2	106.8
NPAT (\$m)	(20.2)	(23.8)	0.8	5.9
EPS (cps)	(6.9)	(7.0)	0.2	1.7
EPS Growth (%)	(91.4%)	(1.4%)	103.3%	657.8%
DPS (cps) (AUD)	0.0	0.0	0.0	0.0
Franking (%)	0%	0%	0%	0%

Ratios

YE 30 Jun	FY17A	FY18E	FY19E	FY20E
P/E (x)	(9.4)	(11.8)	nm	47.5
EV/EBITDA (x)	(8.3)	(12.0)	68.1	19.4
Div Yield (%)	0.0%	0.0%	0.0%	0.0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%

Price Performance

YE 30 Jun	1 Mth	2 Mth	3 Mth	1 Yr
Relative (%)	2.2%	(5.6%)	(5.3%)	22.6%
Absolute (%)	2.5%	(1.8%)	(2.9%)	27.7%
Benchmark (%)	0.3%	3.8%	2.4%	5.1%



Major Shareholders

Larry Diamond (CEO & MD)	21.0%
Westpac Bank	17.1%
Peter Gray (COO & ED)	6.9%

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Event

Z1P has recently announced two significant and large retail merchant wins, each generating well over \$1b turnover each p.a. – Super Retail Group and Officeworks.

Highlights

- **Win #1 with Super Retail Group (ASX: SUL), one of Australia's leading retailers by size** – SUL prints annual revenue in excess of \$2.5b p.a. across five major brands (Supercheap Auto, BCF, Ray's Outdoors, Rebel and MacPac) and ~630 stores nationally and NZ. In-store and online both launch during 1Q19. As a general rule, Shaw and partners expect that if Z1P were to attain only a conservative 10% of this transaction spend, that would equate to over \$20m in transaction volume per month vs. recent 3Q18 monthly quantum of >\$45m.
- **Win #2 with Officeworks (ASX: WES), another significant win** – printing over \$1.5b in turnover annually across 165 stores. In-store rollout commences early 1Q19, followed by online integration at the end of 1Q19.
- **New website streamlines and consolidates the brand into a single destination** (<https://zip.co/>) – with greater transparency about the two key products (Zip Pay <\$1,000 and Zip Money >\$1,000), integration and partner support, in addition to increased clarity around payments and fees.
- **Both wins further highlight Z1P's credibility in securing major merchants with flexible repayment schedules to suit various demographics and those requiring bigger ticket purchases** – weekly, fortnightly or monthly, and you can pay as much as you like as long as you meet your minimum monthly repayments (advised at the time of sign up).
- **To recap the last 3Q18, Z1P announced another set of very strong quarterly numbers in what is a seasonally weaker 3Q** – loan book growth +15% on pcp, number of merchants +16%, customers +19%, transaction volumes +3% (with March hitting \$50m) and, most importantly, revenues +23% to \$11.2m (vs. Shaw's \$10.2m).
- **Key catalyst is cashflow breakeven in FY18 (INCLUDING bad debt write-offs)** – noting that, significantly, in 2Q18 Z1P was effectively already break-even at -\$0.1m.
- **Future ASIC investigation in the space welcomed** – that it, Z1P subjects all credit applicants with identity and credit checks (unlike other players in the market).

Recommendation

BUY. No changes to our numbers. The share price reaction over the past couple of months has been muted. We find this difficult to comprehend given the significant milestones being achieved. The market is not giving Z1P the benefit of the doubt, particularly post cashflow breakeven in FY18, and what should now turn in to a bumper FY19 based on recent milestone wins like Kogan, Tigerair, Super Retail and now Officeworks, with more likely in the near term (noting that implementation takes time). We believe the market will realise this value in time. Moreover, nothing has changed – if anything, there has been more positive news with these aforementioned announcement than ever in Z1P's history. The company is setting itself up for the long haul – and the pieces are slowly, if surely, coming together and the pipeline remains very strong. FY19 (and beyond) should be a cracker for Z1P: with significant upside from the Pocketbook acquisition, lower cost NAB facility (and 17% WBC investment), further monetising the large recent wins / partnerships (i.e. Officeworks, Super Retail, Tigerair, Macquarie Bank, Kogan, eWays, Catch, LUX, Quest, etc.), the push into digital wallets, the (potential) rollout across Westpac, and penetrating NZ to thereby accelerate the company's growth. We believe that Z1P is "best of breed" in this space because the past two years have been focussed on a long term disruption strategy, not the short-term sugar hit of its peers - clearly enunciating a strategy of differentiating itself qualitatively, strategically and visibly vs. what we consider to be its lower quality peers like Openpay, PartPay, FuturePay, Ourpay, Oxipay etc., all offering a homogenous platform with little distinction.

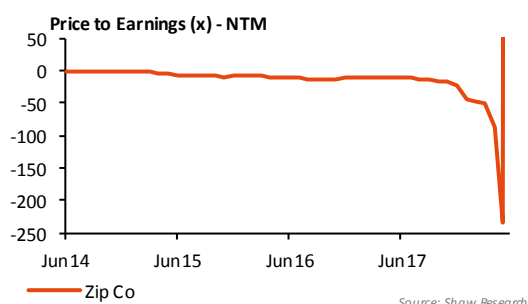
Zip Co Information Technology

FactSet: Z1P-AU / Bloomberg: Z1P AU

Key Items	Data
Recommendation	BUY
Risk	HIGH
Price (\$ps)	0.83
Target Price (\$ps)	1.60
52 Week Range (\$ps)	0.58 - 1.30
Shares on Issue (m)	241.6
Market Cap (\$m)	200.5
Enterprise Value (\$m)	246.0
TSR (%)	92.8%
Valuation NPV	Data
Beta	1.40
Cost of Equity (%)	13.7%
Risk Free Rate (%)	5.3%
Terminal Growth (%)	3.0%
WACC (%)	13.7%

Company Description

Zip Co. Ltd. provides retail finance solutions. It offers point-of-sale credit and digital payment services to consumers and merchants. The company was founded on June 24, 2013 and is headquartered in Sydney, Australia.



Financial Year End: 30 June

Investment Summary (AUD)	FY16A	FY17A	FY18E	FY19E	FY20E
EPS (Reported) (cps)	(3.6)	(6.9)	(7.0)	0.2	1.7
EPS (Underlying) (cps)	(3.6)	(6.9)	(7.0)	0.2	1.7
EPS (Underlying) Growth (%)	82.8%	(91.4%)	(1.4%)	103.3%	657.8%
PE (Underlying) (x)	(17.2)	(9.4)	(11.8)	nm	47.5
EV / EBIT (x)	(15.8)	(7.5)	(10.5)	149.7	23.2
EV / EBITDA (x)	(16.9)	(8.3)	(12.0)	68.1	19.4
DPS (cps) (AUD)	0.0	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	100%	0%	0%	0%	0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Free Cash Flow Yield (%)	(2.2%)	(6.1%)	(1.4%)	0.2%	1.7%
Profit and Loss (AUD) (m)	FY16A	FY17A	FY18E	FY19E	FY20E
Sales	3.2	17.0	35.3	69.2	106.8
Sales Growth (%)	675.7%	436.3%	107.8%	95.9%	54.3%
EBITDA	(8.4)	(19.0)	(20.5)	3.6	10.9
EBITDA Margin (%)	nm	nm	(58.1%)	5.2%	10.3%
Depreciation & Amortisation	(0.6)	(1.9)	(2.9)	(2.0)	(1.8)
EBIT	(9.0)	(20.9)	(23.4)	1.6	9.1
EBIT Margin (%)	nm	nm	(66.3%)	2.4%	8.5%
Net Interest	0.0	0.1	(0.4)	(0.5)	(0.6)
Pretax Profit	(9.0)	(20.7)	(23.8)	1.1	8.5
Tax	0.0	0.6	0.0	(0.3)	(2.5)
Tax Rate (%)	0.0%	(2.7%)	0.0%	(30.0%)	(30.0%)
Minorities	0.0	0.0	0.0	0.0	0.0
NPAT Underlying	(9.0)	(20.2)	(23.8)	0.8	5.9
Significant Items	0.0	0.0	0.0	0.0	0.0
NPAT Reported	(9.0)	(20.2)	(23.8)	0.8	5.9
Cashflow (AUD) (m)	FY16A	FY17A	FY18E	FY19E	FY20E
EBIT	(9.0)	(20.9)	(23.4)	1.6	9.1
Tax Paid	0.0	0.6	0.0	(0.3)	(2.5)
Net Interest	0.0	0.1	(0.4)	(0.5)	(0.6)
Change in Working Capital	(2.4)	11.1	8.6	2.3	3.2
Depreciation & Amortisation	0.6	1.9	2.9	2.0	1.8
Other	9.0	(0.4)	12.4	(2.4)	(3.5)
Operating Cashflow	(1.9)	(7.6)	0.2	2.6	7.5
Capex	(1.4)	(3.3)	(3.9)	(2.1)	(2.9)
Acquisitions and Investments	0.0	(1.9)	0.0	0.0	0.0
Disposal of Fixed Assets/Investments	0.2	0.0	0.0	0.0	0.0
Other	(35.0)	(112.5)	(159.5)	(167.4)	(141.7)
Investing Cashflow	(36.1)	(117.6)	(163.4)	(169.5)	(144.7)
Free Cashflow	(3.2)	(10.9)	(3.8)	0.5	4.5
Equity Raised / Bought Back	15.2	8.2	37.9	37.9	37.9
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Change in Debt	(4.0)	0.0	0.0	0.0	0.0
Other	32.8	129.1	130.8	131.1	131.1
Financing Cashflow	44.0	137.3	168.7	169.0	169.0
Exchange Rate Effect	0.0	0.0	0.0	0.0	0.0
Net Change in Cash	6.1	12.1	5.4	2.1	31.8
Balance Sheet (AUD) (m)	FY16A	FY17A	FY18E	FY19E	FY20E
Cash	7.1	19.2	24.7	26.8	58.6
Accounts Receivable	0.1	0.4	6.3	8.9	12.4
Other Current Assets	0.0	0.0	0.0	0.0	0.0
PPE	0.1	0.5	3.4	3.4	3.4
Goodwill & Intangibles	1.5	10.6	10.5	10.5	10.5
Investments	0.0	0.0	0.0	0.0	0.0
Other Non Current Assets	38.1	143.8	302.0	468.2	608.6
Total Assets	46.9	174.6	346.9	517.7	693.5
Accounts Payable	3.9	2.6	2.7	2.9	3.2
Short Term Debt	0.0	0.0	0.0	0.0	0.0
Long Term Debt	0.0	0.0	0.0	0.0	0.0
Income Taxes Payable	0.0	0.0	0.0	0.0	0.0
Other	31.4	160.3	304.1	425.1	562.2
Total Liabilities	35.4	162.9	306.8	428.1	565.5
Total Shareholder Equity	11.5	11.6	40.1	89.6	128.1
Ratios	FY16A	FY17A	FY18E	FY19E	FY20E
ROE (%)	(158.2%)	(174.4%)	(92.0%)	1.2%	5.5%
ROIC (%)	(77.7%)	(173.7%)	(59.3%)	0.9%	4.6%
Gearing (%)	(159.5%)	253.2%	(159.5%)	(42.6%)	(84.5%)
Net Debt / EBITDA (x)	0.8	1.0	1.2	(7.5)	(5.4)
Price to Book (x)	nm	nm	nm	nm	nm

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Buy	Expected to outperform the overall market
Hold	Expected to perform in line with the overall market
Sell	Expected to underperform the overall market
Not Rated	Shaw has issued a factual note on the company but does not have a recommendation

Risk Rating

High	Higher risk than the overall market – investors should be aware this stock may be speculative
Medium	Risk broadly in line with the overall market
Low	Lower risk than the overall market

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