

23 July 2024

Dropsuite Limited (DSE)**BUY****Share Price: A\$3.40****Record net user growth the key driver in 2Q24****Target Price: A\$3.65**

While DSE's outlook commentary suggests that it will continue to reinvest incremental earnings into future growth, operating momentum has increased, as per the record net seat adds in 2Q24. This bodes well for DSE's future profitability and remains the key pillar for our Buy rating, with our new TP of \$3.65ps reflecting the increase to our ascribed EV/sales ratio to 5.8x.

Positive 2Q24 momentum

- DSE reported a strong 2Q24, with the key driver being record net paid user growth of 112k seats, up from 73k in 1Q24. This reflected a mix of new product upgrades, growth in the partner base, and lower churn rates.
- While DSE's ARPU declined sequentially by 1% in USD terms despite completing the deactivation of a cohort of low ARPU users in prior periods, ARR increased by 8% on 1Q24 and 30% on pcp (in USD terms).

Positive outlook intact

- Although DSE's earnings and cash flow guidance are unchanged, its operating momentum has increased, as evidenced by the 2Q24 growth in both its net seat adds and partners. This bodes well for future profitability.

Negligible change to EPS estimates

- We have strengthened our sales growth assumptions, offset by an allowance for higher reinvestment in opex, as guided. The net effect is no material change to our EPS estimates across our explicit forecast period.
- The key drivers are (i) higher net user growth, reflecting normalisation of churn and record 2Q24 seat adds, (ii) ongoing near-term prioritisation of growth opex ahead of operating leverage, and (iii) a higher AUD/USD.

Reiterate Buy and lift our TP to \$3.65ps (from \$3.20)

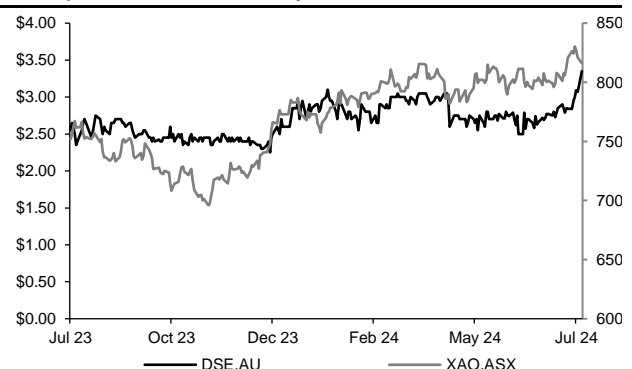
- We believe DSE has the products, business model and capital to exceed system growth (~25% p.a.) within its target market (data back-up and archiving) over the next two years.
- Consistent with DSE's partner-led business model and growth strategy, the key share price catalysts include (i) better-than-expected sales, (ii) a sooner-than-expected normalisation in growth opex, and (iii) strategic M&A.
- Given DSE's ability to leverage its strong balance sheet to supplement what we expect to be a strong multi-year organic growth profile with M&A, we reiterate our Buy rating and lift our TP to \$3.65ps (from \$3.20ps).
- While we continue to use an EV/sales ratio to estimate DSE's fair value, our ascribed ratio has increased to 5.8x (previously 5x). This is in line with N-ABLE, despite the latter exhibiting a more mature growth profile.

Company Data

Shares – ordinary (M)	69.9
Dilution (M)	1.1
Total (fully diluted) (M)	71.0
Market capitalisation (\$M)	237.5
12-month low/high (\$)	2.2 - 3.15
Average monthly turnover (\$M)	7.7
GICS Industry	Software

Financial Summary (fully diluted/normalised)

Year End	December 2022A	2023A	2024F	2025F	2026F
Revenue (A\$m)	20.7	30.6	40.2	52.6	64.7
Costs (A\$m)	19.4	29.5	38.9	50.7	61.6
EBITDA (A\$m)	1.3	1.1	1.3	1.9	3.1
NPAT (A\$m)	1.5	1.6	1.9	2.4	3.6
EPS (¢)	2.1	2.3	2.7	3.3	5.0
EPS Growth (%)	>100.0	7.8	16.0	25.1	49.9
PER (x)	163.8	150.4	128.2	102.5	68.4
FCF (A\$m)	0.9	2.1	1.9	1.6	2.8
FCF per share (cps)	1.2	3.0	2.6	2.2	3.9
Price to FCF (x)	279.5	111.6	128.5	156.1	87.9
EV (A\$m)	217.3	215.0	215.2	216.4	216.8
EV/EBITDA	173.7	194.5	170.2	116.3	69.7
Payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Dividend (¢)	0.0	0.0	0.0	0.0	0.0
Net Yield (%)	0.0	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0	0.0

DSE – performance over one year**Disclosure and Disclaimer**

This report must be read with the disclosure and disclaimer on the final page of this document.

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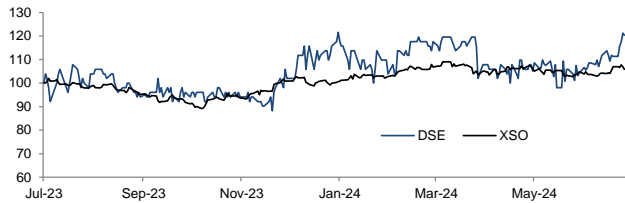
Analysis

Dropsuite Year End December

MARKET DATA

Recommendation		Buy
Price	A\$	3.40
Price target (12-month)	A\$	3.65
52 week high / low	A\$	2.2 - 3.15
Market capitalisation	A\$m	237.5
Shares on issue (basic)	no.	69.9
Performance rights	no.	1.1
Other equity	no.	0.0
Shares on issue (diluted)	no.	71.0

12-MONTH SHARE PRICE PERFORMANCE



INVESTMENT FUNDAMENTALS

	2022A	2023A	2024F	2025F	2026F	
Underlying net profit	\$m	1.5	1.6	1.9	2.4	3.6
Reported net profit	\$m	1.5	1.6	1.9	2.4	3.6
Reported EPS (diluted)	¢	2.1	2.3	2.7	3.3	5.0
Normalised EPS (diluted)	¢	2.1	2.3	2.7	3.3	5.0
....Growth	%	>100.0	7.8	16.0	25.1	49.9
Normalised diluted PER	x	163.8	150.4	128.2	102.5	68.4
Adjusted Op. CF per share	¢	1.3	3.2	2.9	2.4	4.1
Adjusted FCF per share	¢	1.2	3.0	2.6	2.2	3.9
Price to free cash flow per share	x	279.5	111.6	128.5	156.1	87.9
Free cash flow yield	%	0.4	0.9	0.8	0.6	1.1

PROFIT AND LOSS

	2022A	2023A	2024F	2025F	2026F	
Total revenue	\$m	20.7	30.6	40.2	52.6	64.7
EBITDA	\$m	1.3	1.1	1.3	1.9	3.1
Depreciation & amortisation	\$m	0.1	0.2	0.2	0.2	0.2
EBIT	\$m	1.2	0.9	1.1	1.7	2.9
Net interest	\$m	(0.3)	(0.7)	(0.8)	(0.7)	(0.7)
Non-operating income	\$m	0.0	0.0	0.0	0.0	0.0
Pretax Profit	\$m	1.5	1.6	1.9	2.4	3.6
Tax expense	\$m	0.0	0.0	0.0	0.0	0.0
Minorities	\$m	0.0	0.0	0.0	0.0	0.0
Reported NPAT	\$m	1.5	1.6	1.9	2.4	3.6
Significant items	\$m	0.0	0.0	0.0	0.0	0.0
Underlying NPAT	\$m	1.5	1.6	1.9	2.4	3.6

DIVIDENDS

	2022A	2023A	2024F	2025F	2026F
Dividend per share	¢	0.0	0.0	0.0	0.0
Payout ratio	%	0.0	0.0	0.0	0.0
Yield	%	0.0	0.0	0.0	0.0
Franking	%	0.0	0.0	0.0	0.0

ENTERPRISE VALUE

	2022A	2023A	2024F	2025F	2026F	
Enterprise value	\$m	217.3	215.0	215.2	216.4	216.8
EV/EBITDA	x	173.7	194.5	170.2	116.3	69.7
EV/EBIT	x	182.4	244.6	194.4	127.7	73.8
Price to book (NAV)	x	9.7	8.6	8.3	7.7	7.0
Price to NTA	x	9.7	8.6	8.3	7.7	7.0

GROWTH PROFILE

	2022A	2023A	2024F	2025F	2026F	
Operating revenue	%	76.8	48.1	31.2	30.8	23.1
EBITDA	%	>100.0	(11.7)	14.4	47.2	67.3
EBIT	%	>100.0	(26.2)	26.0	53.1	73.3
Operating NPAT	%	>100.0	9.2	17.7	27.1	51.7
Normalised EPS	%	>100.0	7.8	16.0	25.1	49.9
DPS	%	0.0	0.0	0.0	0.0	0.0

KEY RATIOS

	2022A	2023A	2024F	2025F	2026F	
EBITDA margin	%	6.0	3.6	3.1	3.5	4.8
EBIT margin	%	5.8	2.9	2.8	3.2	4.5
Underlying net profit margin	%	7.0	5.2	4.6	4.5	5.6
Return on average equity	%	15.5	17.7	19.2	19.5	19.3
Return on average assets	%	14.0	17.2	18.9	19.5	19.6
Net tangible assets per share	¢	35.1	39.3	41.2	44.0	48.4
Net debt /(cash)	\$m	(22.3)	(24.3)	(26.1)	(27.7)	(30.5)
Interest cover (EBIT / net interest)	x	n/a	n/a	n/a	n/a	n/a
Leverage (net debt / EBITDA)	x	n/a	n/a	n/a	n/a	n/a
Gearing (net debt / net debt plus equity)	%	n/a	n/a	n/a	n/a	n/a

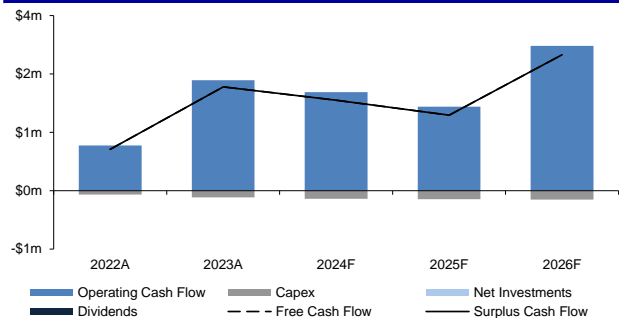
BALANCE SHEET

	2022A	2023A	2024F	2025F	2026F	
Cash	\$m	22.3	24.3	26.1	27.7	30.5
Receivables	\$m	4.1	5.9	7.6	10.0	12.3
Inventory	\$m	0.0	0.0	0.0	0.0	0.0
Other	\$m	0.4	0.7	0.7	0.7	0.7
Current	\$m	26.8	30.8	34.4	38.3	43.4
Prop, plant & equip	\$m	0.1	0.1	0.1	0.2	0.2
Goodwill	\$m	0.0	0.0	0.0	0.0	0.0
Other	\$m	0.1	0.2	0.2	0.4	0.6
Non current	\$m	0.1	0.4	0.4	0.6	0.8
Total assets	\$m	26.9	31.2	34.8	38.9	44.2
Accounts Payable	\$m	2.5	3.2	5.0	6.6	8.1
Borrowings	\$m	0.0	0.0	0.0	0.0	0.0
Other	\$m	0.2	0.5	0.5	0.7	0.9
Total liabilities	\$m	2.7	3.8	5.5	7.3	9.0
Net assets	\$m	24.2	27.4	29.2	31.6	35.2
Equity	\$m	24.2	27.4	29.2	31.6	35.2
Minorities	\$m	0.0	0.0	0.0	0.0	0.0
Shareholder's equity	\$m	24.2	27.4	29.2	31.6	35.2
Shares on issue	m	69.0	69.6	71.0	71.8	72.7

DUPONT ANALYSIS

	2022A	2023A	2024F	2025F	2026F	
Net Profit Margin	%	7.9	9.6	11.4	13.0	14.4
Asset Turnover	x	1.6	1.5	1.3	1.2	1.1
Return on Assets	%	12.3	14.0	15.3	15.8	15.9
Financial Leverage	x	1.3	1.3	1.3	1.2	1.2
Return on Equity	%	15.5	17.7	19.2	19.5	19.3

CASH FLOW SUMMARY



CASH FLOW

	2022A	2023A	2024F	2025F	2026F	
EBITDA	\$m	1.3	1.1	1.3	1.9	3.1
Change in working capital	\$m	(1.4)	(1.0)	0.0	(0.8)	(0.8)
Net interest	\$m	0.2	0.7	0.8	0.7	0.7
Tax paid	\$m	0.0	0.0	0.0	0.0	0.0
Other	\$m	0.9	1.5	0.0	0.0	0.0
Operating cash flow	\$m	0.9	2.3	2.0	1.7	3.0
Capital expenditure	\$m	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)
Acquisitions/divestment/other	\$m	0.0	0.0	0.0	0.0	0.0
Investing cash flow	\$m	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)
Free cash flow	\$m	0.9	2.1	1.9	1.6	2.8
Equity	\$m	0.0	0.0	0.0	0.0	0.0
Increase / (decrease) in borrowings	\$m	0.0	0.0	0.0	0.0	0.0
Dividend/other	\$m	0.0	0.0	0.0	0.0	0.0
Financing cash flow	\$m	0.0	0.0	0.0	0.0	0.0
Net cash flow	\$m	0.9	2.1	1.9	1.6	2.8

Source: Petra Capital



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