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7digital

Media

18 January 2017

EBITDA break-even reached, positive outlook

7digital's FY16 revenues increased 7% y-o-y and EBITDA profitability was reached, as targeted, in Q4. New contract wins in FY16 set the stage for a stronger top-line performance in FY17 and we consider management's reiterated target of operating profitability in FY17 as realistic. For an operationally geared growth company in its first year of profitability, the FY17e EV/EBITDA of c 12x looks attractive.

Trading update: EBITDA profitability reached in Q416

FY16 revenues increased 7% y-o-y to £11.1m (versus consensus £12m) with growth across licensing, content and creative. £1m of annualised cost savings were delivered and 7digital moved into EBITDA profitability in Q4, as targeted. During Q4, £1.6m of contracts were won, including two licensing agreements via its partner Radio Player (in Canada and Peru). Taking into account the H116 wins, this suggests that the total contract value awarded during FY16 should be much healthier than the prior year and provides us with confidence in the direction of the business moving into FY17. Management states that FY17 has started well, reiterating its target for full year operating profitability.

Operational gearing should become evident in FY17

Reaching EBITDA profitability is a key milestone for the group and with 60% of revenues now from high-margin licensing activities, operational gearing effects should ensure a large proportion of future revenue growth is converted to profits. The market for streamed music is developing rapidly (+76% in 2016 in the US according to Nielsen) and as the largest independent global B2B music streaming platform, working with all three major record labels (Universal, Sony and Warner, with the third signing in Q416), and with clients in a number of strategic sectors including mobile, high res, automotive and radio, 7digital has the relationships and platform in place to benefit.

Business transformation complete

Results over the last two years have been held back by the transition from a B2C download model to a B2B licensing model, as well as the closure of two of its larger clients (Blackberry in FY15 and Guvera in FY16). With the transition largely complete, profitability reached and £730k net cash, the valuation, which can now be benchmarked to EBITDA, is more visible. Consensus EBITDA forecasts for FY17 look fairly secure, which implies an FY17e EV/EBITDA of c 12x, unusually low for an operationally geared growth company in its first year of profitability.

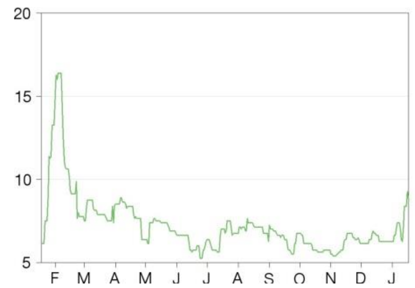
Consensus estimates

Year end	Revenue (£m)	EBITDA (£m)	PBT (£m)	EPS (p)	DPS (p)	P/E (x)	EV/EBITDA (x)
12/14	10.2	(3.1)	(3.8)	(4.3)	0.0	N/A	N/A
12/15	10.4	(2.1)	(2.9)	(2.8)	0.0	N/A	N/A
12/16e	11.1*	(3.1)	(3.9)	(3.4)	0.0	N/A	N/A
12/17e	14.0	0.8	0.1	0.1	0.0	87.5	11.8

Source: 7digital accounts, Bloomberg. Note: *Reported in trading statement.

Price	**8.75p**
Market cap	**£10m**

Share price graph



Share details

Code	7DIG
Listing	AIM
Shares in issue	115.75m

Business description

7digital is a B2B digital music and radio services company. Its platform and access to global music rights enables businesses in the radio, electronics and telecoms industries around the world to offer and commercialise music streaming and radio services. Customers include musical.ly, Onkyo, Panasonic, Astro, Mariposa, Electric Jukebox, eMusic and i.am +.

Bull

- Well positioned in the global music industry's transition to streaming services. Customers in 33 markets.
- Strong pipeline of prospects, high-margin recurring licence revenues growing strongly, EBITDA profitability expected towards the end of this year.
- Debt free.

Bear

- Disruptive business model; large B2C competitors could retaliate.
- The download business, while much lower margin than licensing revenues, is a drag on growth.
- Limited share liquidity.

Analysts

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