WANdisco

Interim results

Progress on all fronts

Software & comp services

WANdisco delivered 73% growth in bookings in H1 while reducing cash costs by $1.4m and moving close to cash flow break even, highlighting the scalability the company has added to the model. The IBM OEM partnership was key to this acceleration but partnerships with other tier one technology companies are also progressing and could provide a further inflection. We have upgraded our FY17 bookings and revenue estimates by 6% and 9%, respectively, and forecast positive cash flows from here. The addition of more tier one strategic partnerships could be a catalyst for further upgrades.

Year end	Revenue ($m)	EBITDA ($m)	PBT* ($m)	EPS* (c)	Net cash ($m)	EV/sales (x)
12/15	11.0	(16.0)	(26.4)	(87.7)	2.6	30.7
12/16	11.4	(7.5)	(16.4)	(46.9)	7.6	29.3
12/17e	17.0	(3.3)	(10.6)	(26.7)	7.1	19.6
12/18e	21.7	(0.7)	(8.3)	(20.6)	10.4	15.3

Note: *PBT and EPS (fully diluted) are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Strong partners key to scalable growth prospects

The IBM partnership moved into a higher gear in H1, delivering $4.2m of revenue, demonstrating the leverage gained from partnerships with tier one technology companies. We believe the strength of WANdisco's partner base highlights the strength of its core replication IP and it has made good progress in developing these relationships over H1. Compliance with Oracle's MAA architecture should be a catalyst for sales via Oracle to expand. WANdisco is integrating its Fusion product with Amazon's Snowball product, for moving massive amounts of data to its public cloud. Partnerships with Google Cloud and Alibaba have potential to progress further. The conversion of one or two of these collaborations into strategic partnerships could lay down a platform for a further acceleration in scalable growth.

Upgrading estimates, expect positive cash generation

We are upgrading our bookings estimates by 6% to $21.7m in FY17 and 4% to $28.0m for FY18. Our FY17 revenues are upgraded by 9%, reflecting the higher bookings and an acceleration in the revenue recognition cycle, due to the increased weighting of royalties and licences coming in via IBM versus annual subscriptions via other channels, while the EBITDA loss estimate reduces to $3.3m from $4.2m. Our FY18 P&L estimates are not significantly changed. We are now forecasting positive cash flows from FY17, with cash building from the $6.9m H117 level.

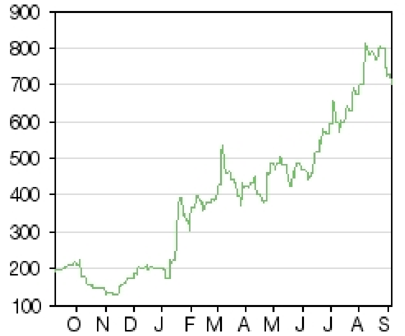
Valuation: Acceleration priced in; partners key

WANdisco's investment case has always been predicated on the potential for it to scale into a significantly larger, highly profitable business. We believe that its progress in H1 has significantly strengthened its credentials. The share price performance has reflected this, and with its FY18e EV/sales rating of 15.3x we believe that the shares discount a further acceleration in growth in excess of our forecasts. Further progress with tier one strategic partners will be the key to moving towards more aggressive growth assumptions.

6 September 2017

Price	**700.50p**
Market cap	**£264m**
	US$1.3/£
Net cash ($m) at 30 June 2017	6.9
Shares in issue	37.7m
Free float	88%
Code	WAND
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(3.7)	49.8	259.2
Rel (local)	(2.4)	52.4	232.3
52-week high/low		812.5p	128.5p

Business description

WANdisco is a distributed computing company. It has developed a suite of solutions based around proprietary replication technology, which solve critical data management challenges prevalent across cloud computing, big data and the ALM software markets.

Next events

Investor day	TBA

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Edison profile page

WANdisco is a research client of Edison Investment Research Limited

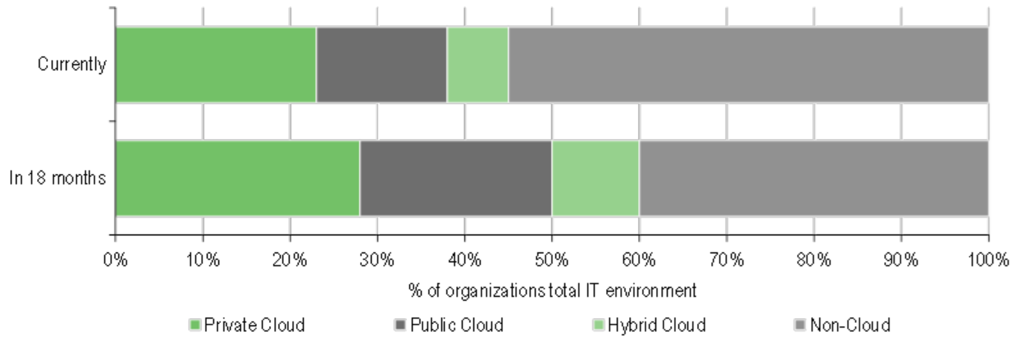
Growth credentials strengthened

WANdisco's investment case has always been predicated on the potential for the company to scale into a highly profitable business of a significantly larger size. We believe that WANdisco's operational and financial progress in H1 has strengthened its credentials.

Operating in the crux of a very large, growing market

In terms of market backdrop, WANdisco operates at the crux of one of the key structural growth trends within the technology landscape today. The rate at which data and computing are moving to cloud platforms continues to gather pace. It is also the technology cycle upon which the development of many others such as big data analytics and AI depend, which strengthens the case for enterprises to move data to the cloud. Market analyst Gartner estimates that cloud computing revenues will grow at a CAGR of 19% from $67bn in 2015 to $162bn in 2020. 451 Research estimates that by 2019, 60% of all IT workloads will run in the cloud, up from 45% today.

Exhibit 1: Share of IT environment by storage type



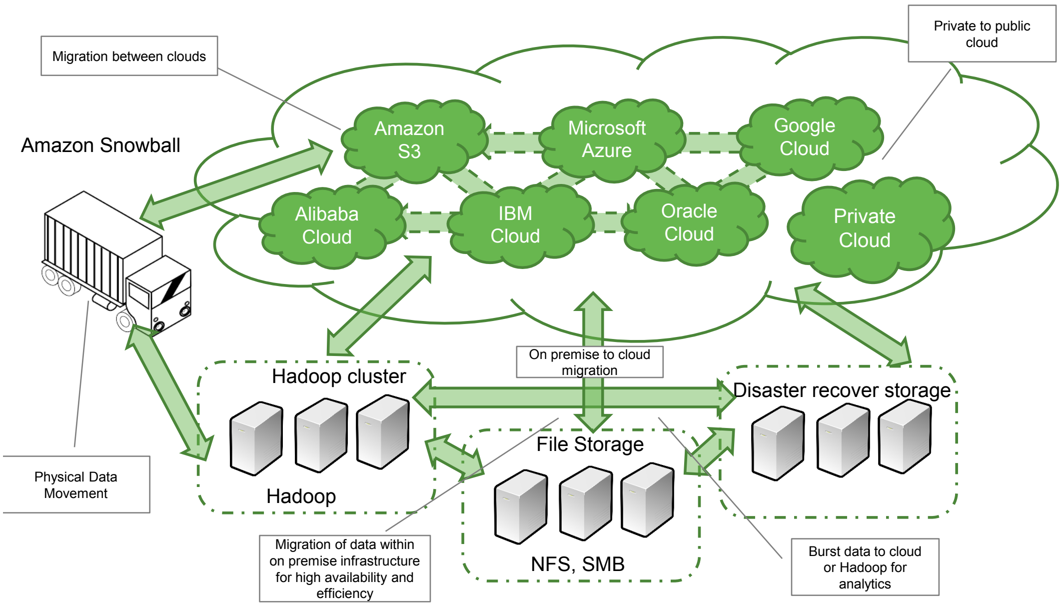
Source: IDG Enterprise: Survey (November 2016) – what percent of your organization's total IT environment (data, applications, infrastructure etc) presently resides in each of the following and will in 18 months?

Enabling the movement of big data

The amount of data being stored across all formats is increasing at a very rapid rate. Companies now need to interrogate, analyse, archive, migrate and protect terabytes, petabytes or exabytes of data, much of which is mission critical. All of these functions require data to be migrated from one place to another, but legacy technologies are increasingly unable to cope, due to the downtime involved in moving large amounts of data, or the inability to maintain consistency between two data sources.

WANdisco's Fusion platform, based around its core DConE replication IP, enables data to be continually synchronised in real time across a wide area network. This enables data to be replicated between data sources without incurring downtime and while ensuring data consistency. The technology can be used to replicate data from one data centre to another, from a data centre to the cloud and back, from one cloud platform to another or to a mobile data centre – such as Amazon's Snowball solution for large-scale cloud migrations.

Exhibit 2: Data can be stored and moved across multiple clouds and locations



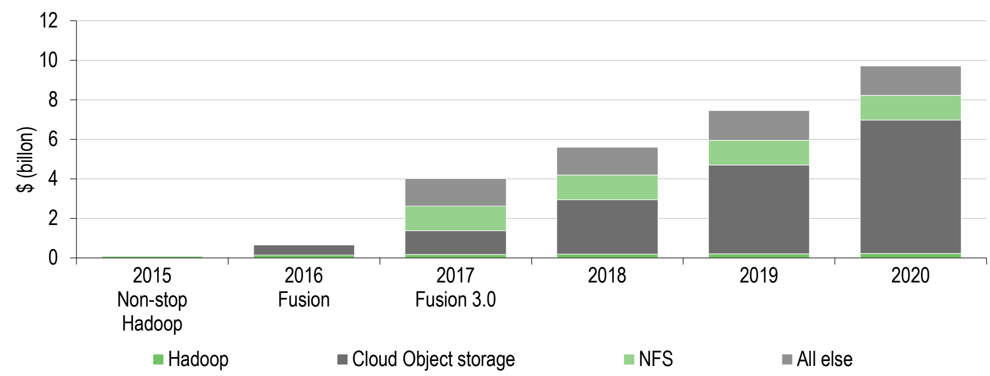
Source: Edison Investment Research

The March launch of Fusion 2.10 extended the platform's ability beyond Hadoop (for big data analytics) and cloud object storage to support Network File System (NFS) servers, extending the company's capability to the mainstream file storage market.

Large and growing addressable market

WANdisco estimates the total addressable market for its technology in cloud deployments to be worth around $1.6bn, growing to circa $7bn by 2020. The addition of NFS capability should extend this by over $1bn. While growth of the NFS market is expected to be marginal, at best, the vast majority of enterprises will continue to store data in multiple locations and across multiple formats. The addition of NFS capability should thus strengthen WANdisco's proposition through giving customers the ability to apply the benefits of Fusion across more of their data infrastructure.

Exhibit 3: Estimated addressable market for WANdisco's product



Source: WANdisco

Credentials with tier one partners and customers strengthened

While the potential for WANdisco's technology has always looked compelling, one can generally get a much better gauge of a company's prospects by looking at who they work with and how much they spend. We believe that WANdisco's credentials have significantly strengthened in this regard over the past six months.

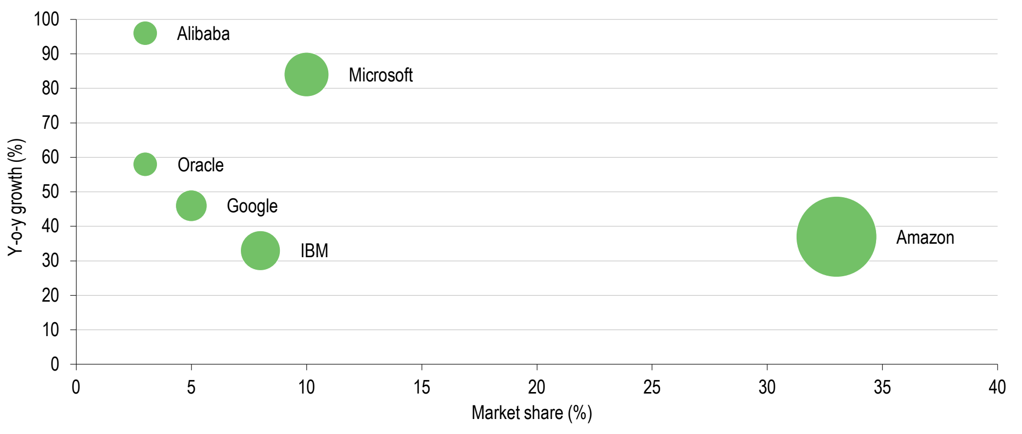
Scale and diversity of deals highlights growth potential

We believe that the broad addressable market for WANdisco's technology is highlighted by the diverse spread of verticals for its last three announced big data deals, which span retail ($2.0m), financial services ($4.1m in April) and automotive manufacture (c $650k in December). Retail and healthcare are both new verticals for the company. We see the scale of these deals as a good indication of both the uniqueness of the company's IP and the return on investment customers are able to generate from deploying it.

Partnerships key to driving scalable growth

WANdisco's roster of partnerships with major technology companies is also impressive. This includes embracing major vendors of enterprise software/hardware that are now moving aggressively into cloud and hybrid solutions, such as IBM, Oracle, Microsoft, HP and Dell, and also the largest pure cloud solution providers, such as Amazon, Google Cloud and Alibaba. Combined, WANdisco estimates that these companies hold over 60% of the total cloud computing market share, with cloud service revenues growing at a healthy double-digit rate.

Exhibit 4: LTM revenue growth and market share of key partners



Source: WANdisco, Edison Investment Research, company reports

The IBM partnership is clearly the most advanced of these relationships. Having initially established the OEM agreement in H116, the collaboration moved up a gear in H117, with a $4.1m contract with a major financial institution brought in via the partnership as well as $1.1m of royalty revenues carried over from 2016. We expect the partnership to generate more leads in H2.

Looking at WANdisco's other partnerships, its relationship with Oracle has already demonstrated its ability to generate $1m+ deals and WANdisco's compliance with Oracle's MAA architecture should be a catalyst for sales via Oracle to expand. WANdisco is also integrating its Fusion product with Amazon's Snowball product, for moving massive amounts of data to its public cloud. We do not have detailed insight into the company's partnerships with Microsoft, Google Cloud and Alibaba, but we believe that these have potential to progress further.

The conversion of one or two of these collaborations into strategic partnerships could lay down a platform for a further acceleration in scalable growth.

Financials

H117 results review

Fusion/IBM drives 73% bookings growth

H1 bookings of $10.2m grew by 73% y-o-y, driven solely by the core Fusion business, where bookings were $7.0m, up 173% from $2.6m last year. Bookings for the Source Code Management business were essentially flat at $3.2m vs $3.3m in H1 last year.

IBM accelerates revenue recognition profile

Revenues grew 71% to $9.7m, which reflects the strong bookings momentum but also a faster revenue recognition cycle. This is due to the upfront contribution of royalties from IBM and a $3.1m perpetual licence (also with IBM) versus the more drawn out profile from the company's subscription model deployed elsewhere. We understand that subscription-based charging remains the company's preferred revenue model, but management will retain a flexible approach to secure large deals, such as the IBM OEM agreement and the large perpetual licence deal, which influenced the H1 numbers.

Scalability of model demonstrated

This improvement in top-line performance was achieved with a substantially reduced cost base, highlighting the scalability that WANdisco has added to its model through its indirect partner-driven model. Total cash costs, including capitalised development costs, were $10.8m down from $14.9m in H1 last year, and as a result EBITDAC (EBITDA treating capitalised R&D as expensed) loss dropped to $2.1m from $9.7m last year. EBITDA was a $0.96m profit from a $5.3m loss last year.

Closing in on cash flow break-even; balance sheet strong

Cash burn in H1 reduced to $600k, down from $5.3m in H1 last year, reflecting the strong bookings progress, the company's positive working capital profile and substantially reduced overheads. Net cash stood at $6.9m, comprising of $9.9m cash and $3.0m debt through an $8m facility ($5m debt, $3m revolving credit) secured with Silicon Valley Bank in June.

Estimates upgraded, scope for more

We are upgrading our bookings estimates by 6% to $21.7m for FY17 and 4% to $28.0m in FY18, respectively. Our FY17 revenues are upgraded by 9%, reflecting the acceleration in the revenue recognition cycle, brought about by the increased weighting of royalties and licences coming in via IBM, while the EBITDA loss estimate reduces to $3.3m from $4.2m. Our FY18 P&L estimates are not significantly changed.

Due to the company's positive working capital model and lower cost base, we are now forecasting positive cash flows from FY17, building from the $6.9m H117 level.

Further strategic partnerships the key catalyst for upside

We believe that these estimates remain cautious, but at this stage we only have a short period of improved trading data, and the company's results can still be highly influenced by the timing of large deals. We believe that the securing of one or more additional strategic partnerships would be the key catalyst for upgrading growth forecasts. Given the company's operationally geared model, any increase in bookings or revenue should translate strongly into cash generation and profit.

Exhibit 5: Estimate changes

$000s	2015	2016	2017e			2018e		
Yea-end 31 December	Actual	Actual	Old	New	% change	Old	New	% change
Bookings Big Data	2,500	7,100	11,000	13,000	18%	16,000	18,500	16%
Bookings SCM	6,500	8,400	9,500	8,700	-8%	11,000	9,500	-14%
Total Bookings	9,000	15,500	20,500	21,700	6%	27,000	28,000	4%
Revenue	10,994	11,379	15,674	17,029	9%	21,616	21,748	1%
Cost of Sales	(749)	(1,349)	(1,784)	(1,784)	0%	(2,349)	(2,349)	0%
Gross Profit	10,245	10,030	13,891	15,246	10%	19,267	19,399	1%
EBITDA	(15,988)	(7,464)	(4,211)	(3,254)	-23%	(644)	(655)	2%
Capitalised development cost	(8,369)	(5,860)	(6,497)	(6,497)	0%	(6,952)	(6,952)	0%
EBITDAC (adjusted for capitalised development)	(24,357)	(13,324)	(10,707)	(9,751)	-9%	(7,595)	(7,607)	0%
Operating Profit (before amort and except)	(25,858)	(16,104)	(13,151)	(10,374)	-21%	(9,884)	(8,075)	-18%
Exceptionals	(614)	(32)	0	0		0	0	
Share based payments	(4,057)	(1,787)	(1,787)	(1,400)	-22%	(1,787)	(1,400)	-22%
Operating Profit	(30,529)	(17,923)	(14,938)	(11,774)	-21%	(11,671)	(9,475)	-19%
Net Interest	(506)	(268)	(268)	(268)	0%	(268)	(268)	0%
Profit Before Tax (norm)	(26,364)	(16,372)	(13,419)	(10,642)	-21%	(10,152)	(8,343)	-18%
EPS - (IFRS) (c)	(103.9)	(27.9)	(39.3)	(36.7)	-6%	(30.5)	(24.8)	-18%
Closing net debt/(cash)	(2,555)	(7,558)	(4,156)	(7,071)	70%	(8,389)	(10,376)	24%

Source: WANdisco data, Edison Investment Research

Successful execution should support continued strong growth and strong margins

Looking to the longer term, we believe that the company's market opportunity and IP underpinned, partnership-driven business model have the potential to support a business of substantially larger scale and very healthy margins. The extent to which margins can scale will hinge upon the breadth of applicability and the defensibility of the company's IP, and as ARM demonstrated with 50%+ operating margins there is no particular cap for companies who get both of these ingredients right. More realistically, we believe that with sustained successful execution, 25-30% operating margins should be achievable.

Valuation: Acceleration demanded – partners key

WANdisco's investment case has always been predicated on the potential for the company to scale into a significantly larger, highly profitable business. We believe that the company's progress in H1 has significantly strengthened its credentials. The share price performance has reflected this, and with WANdisco's FY18e EV/sales rating of 15.3x we believe that the shares discount a further acceleration in growth in excess of our forecasts. We believe that further progress with tier one strategic partners will be the key to moving towards more aggressive growth assumptions. The company's strategic attractiveness should also factor into the valuation equation.

Fundamental valuation highlights the degree of acceleration required

A DCF scenario analysis supports this view, suggesting that a 700.5p share price requires the company to deliver sustained bookings growth of c 40% with EBITDAC (EBITDA + capitalised R&D) margins expanding to above 20%. We believe that the opportunity, IP and business model should support achieving such figures, but it will require strong execution on the indirect model, with strategic partnerships driving rapid, operationally geared growth.

Exhibit 6: DCF sensitivity analysis

		Bookings growth FY18	30%	40%	50%	60%	70%
		Bookings CAGR FY16-25	22%	31%	39%	47%	55%
		Revenues 2020, $'000	35,607	41,965	49,057	56,925	65,615
					Implied share price (p)		
Matured	EBITDAC margin	15%	139	281	517	911	1,562
		20%	185	359	644	1,128	1,900
		25%	229	433	774	1,335	2,246
		30%	271	504	895	1,547	2,580
		35%	310	580	1,023	1,749	2,921

Source: Edison Investment Research. Note: WACC = 10%, reduced from 12.5% previously as the business is approaching cash flow break-even; TGR = 2%. Assumes a progressive nine-year fade in growth rate from 2018.

Growth prospects justify a premium rating to peers

On a relative basis, WANdisco's FY18e EV/sales ratio of 15.3x is a premium to its data infrastructure and cloud software peer group, albeit the range within this peer group is wide (Exhibit 7). WANdisco's FY17 and FY18 forecast growth rates are towards the upper end of this peer group and, equally, we believe there is scope for upside, particularly if other tier one partners are secured.

Exhibit 7: Peer valuations

Name		Ytd perf (%)	Current price (ccy value)	Quoted ccy	Market cap ($m)	EV/ sales 1FY (x)	EV/ sales 2FY (x)	EV/ EBITDA 1FY (x)	EV/ EBITDA 2FY (x)	P/E 1FY (x)	P/E 2FY (x)	Sales growth 1FY (%)	Sales growth 2FY (%)
WANdisco	WAND LN equity	248	720	GBp	271	19.6	15.3	nm	nm	nm	nm	50	28
Infrastructure software													
Nutanix Inc - A	NTNX US equity	(20)	21	US$	3,211	3.7	2.7	(17.9)	(19.1)	(14.6)	(16.1)	73.0	35.5
Servicenow	NOW US equity	44	107	US$	18,206	9.3	7.1	42.2	28.8	91.7	60.4	37.0	30.5
Nice	NICE IT equity	1	26,600	ILs	4,477	3.4	3.1	10.6	10.2	18.7	16.8	32.3	7.2
Hortonworks	HDP US equity	54	13	US$	817	3.1	2.4	(64.4)	12.9	(7.1)	(10.0)	29.8	27.0
Attunity	ATTU US equity	17	7	US$	120	1.8	1.5	20.2	17.2	233.7	28.0	13.0	17.9
Mobileiron	MOBL US equity	21	5	US$	428	1.9	1.7	(25.4)	(85.6)	(24.3)	(64.1)	10.0	11.6
Commvault Systems	CVLT US equity	17	60	US$	2,736	3.2	2.9	21.8	17.9	49.5	41.6	9.0	9.1
Vmware Inc - Class A	VMW US equity	17	92	US$	37,620	4.0	3.8	12.3	11.5	18.5	17.3	8.2	5.2
Citrix Systems	CTXS US equity	11	79	US$	11,957	4.2	4.1	12.7	11.4	17.1	15.5	(17.4)	4.1
High-growth UK software													
Blue Prism Group	PRSM LN equity	95	867	GBp	717	25.5	19.6	(66.4)	(96.6)	(78.8)	(111.1)	115.7	30.5
First Derivatives	FDP LN equity	33	2,821	GBp	941	4.3	3.9	23.6	21.5	44.5	41.4	11.6	11.0
Loopup Group	LOOP LN equity	61	194	GBp	105	4.4	3.4	24.9	13.2	120.1	28.1	43.1	32.0
Sophos Group	SOPH LN equity	79	469	GBp	2,874	5.0	4.3	48.5	36.6	117.1	73.9	19.0	16.9

Source: Edison Investment Research, Bloomberg consensus. Note: Prices as at 5 September 2017.

Exhibit 8: Financial summary

	$000s	2014	2015	2016	2017e	2018e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue		11,218	10,994	11,379	17,029	21,748
Cost of Sales		(2,165)	(749)	(1,349)	(1,784)	(2,349)
Gross Profit		9,053	10,245	10,030	15,246	19,399
EBITDA		(17,874)	(15,988)	(7,464)	(3,254)	(655)
Operating Profit (before amort and except)		(26,424)	(25,858)	(16,104)	(10,374)	(8,075)
Acquired Intangible Amortisation		0	0	0	0	0
Exceptionals		(1,586)	(614)	(32)	0	0
Share based payments		(11,907)	(4,057)	(1,787)	(1,400)	(1,400)
Operating Profit		(39,917)	(30,529)	(17,923)	(11,774)	(9,475)
Net Interest		557	(506)	(268)	(268)	(268)
Profit Before Tax (norm)		(25,867)	(26,364)	(16,372)	(10,642)	(8,343)
Profit Before Tax (FRS 3)		(39,360)	(31,035)	(10,047)	(14,339)	(9,743)
Tax		1,053	1,129	772	522	354
Profit After Tax (norm)		(24,814)	(25,235)	(15,600)	(10,121)	(7,989)
Profit After Tax (FRS 3)		(38,307)	(29,906)	(9,275)	(13,818)	(9,389)
Average Number of Shares Outstanding (m)		24.0	28.8	33.3	37.6	37.8
EPS - normalised (c)		(103.3)	(87.7)	(46.9)	(26.9)	(21.1)
EPS - normalised fully diluted (c)		(103.3)	(87.7)	(46.9)	(26.7)	(20.6)
EPS - (IFRS) (c)		(159.5)	(103.9)	(27.9)	(36.7)	(24.8)
Dividend per share (c)		0.0	0.0	0.0	0.0	0.0
Gross Margin (%)		80.7	93.2	88.1	89.5	89.2
EBITDA Margin (%)		N/A	N/A	N/A	N/A	N/A
Operating Margin (before GW and except.) (%)		N/A	N/A	N/A	N/A	N/A
BALANCE SHEET						
Fixed Assets		10,224	8,813	6,253	5,930	5,761
Intangible Assets		9,814	8,583	5,977	5,574	5,325
Tangible Assets		410	230	276	356	436
Investments		0	0	0	0	0
Current Assets		16,933	9,283	13,703	14,429	20,085
Stocks		0	0	0	0	0
Debtors		14,452	6,728	6,145	7,358	9,709
Cash		2,481	2,555	7,558	7,071	10,376
Other		0	0	0	0	0
Current Liabilities		(8,474)	(6,439)	(9,409)	(11,467)	(12,342)
Creditors & Deferred Income		(8,474)	(6,439)	(9,409)	(11,467)	(12,342)
Short term borrowings		0	0	0	0	0
Long Term Liabilities		(6,067)	(6,060)	(6,980)	(11,557)	(15,201)
Long term borrowings		0	0	0	0	0
Deferred Income		(6,067)	(6,060)	(6,980)	(11,557)	(15,201)
Net Assets		12,616	5,597	3,567	(2,665)	(1,697)
CASH FLOW						
Operating Cash Flow		(13,509)	(18,138)	(2,955)	6,056	10,470
Net Interest		58	59	(161)	(268)	(268)
Tax		(3)	552	690	522	354
Capex (inc capitalised R&D)		(9,515)	(8,464)	(5,924)	(6,797)	(7,252)
Acquisitions/disposals		0	0	0	0	0
Financing (net)		465	26,175	13,523	0	0
Dividends		0	0	0	0	0
Net Cash Flow		(22,504)	184	5,173	(487)	3,305
Opening net debt/(cash)		(25,673)	(2,481)	(2,555)	(7,558)	(7,071)
HP finance leases initiated		0	0	0	0	0
Other		(661)	(43)	(175)	0	0
Closing net debt/(cash)		(2,481)	(2,555)	(7,558)	(7,071)	(10,376)

Source: Edison Investment Research, WANdisco data

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