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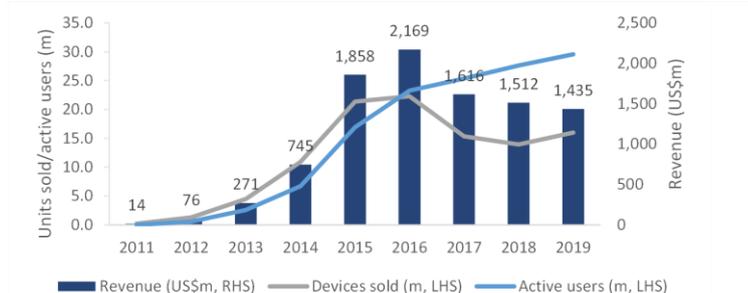
Spacetalk

On the cusp of widespread adoption

We launch coverage of Spacetalk with a Buy recommendation and a fair value of \$0.60 per share, 300% share price upside.

- **Leaders in a nascent market:** Spacetalk make smartwatches for children and seniors paired with software which enables guardians to care for them. In the future most children and seniors will wear a smartwatch. There is a good chance that this watch will be a Spacetalk. Spacetalk currently has an estimated market share >80% of the Australian children’s connected smartwatch category and is a pioneer of the seniors category.
- **A \$17bn addressable market:** Spacetalk has a total addressable market of \$17bn in just countries where the company is present (ANZ and UK) or has firm plans to enter (the US). We estimate that capturing just 1% of the market would give device revenue of \$136m and annually recurring app revenue of \$38m which we believe would justify an equity valuation in excess of \$3 per share.
- **100x revenue is possible:** Over the four years to 2015 Fitbit increased units sales from 0.2m to 21.4m and revenues from US\$14m to US\$1.9bn (Figure 1). Telstra, Australia’s largest telco, announced it will offer Spacetalk for the first time in April 2021. Discussions with other major players are ongoing.
- **Sales growth to accelerate in 2H21:** The company reported revenue growth of 9% YoY in 1H21. We forecast an acceleration to 66% in 3Q21 and 225% in 4Q21 on lower prior year comparables and increased distribution of the new device.
- **Fair value of 60c per share:** Spacetalk trades on EV/Revenue of 0.6x in FY23, an 80% discount to the peer average of 3.2x. Our DCF derived fair value of 60c per share puts it on 2.4x.

Figure 1. Fitbit devices sold, active users (LHS) and revenue (RHS)



Source: Veritas estimates, Company data.

SPA.ASX

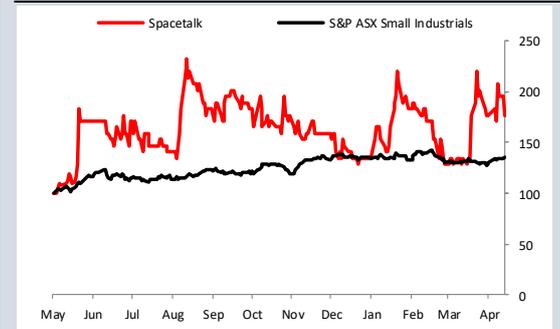
BUY

Wednesday 21 April 2021

Share Price	\$0.15
Price Target	\$0.60
Valuation Method	DCF
Market capitalisation	\$24.8m
Enterprise value	\$25.5m
GICS sector	Consumer Electronics
12 month price range	\$0.08 - \$0.19
Shares in issue	165.3m
Top 20 holders	108.1m
Previous rating	Initiation

Year ended June 30		FY20A	FY21E	FY22E	FY23E	FY24E
Revenue	\$m	10.5	14.7	22.0	41.5	52.7
Growth	%	46.8	40.5	49.6	88.1	27.1
EBITDA	\$m	(2.7)	0.2	(0.1)	2.4	5.6
Margin	%	(25.6)	1.2	(0.3)	5.8	10.5
NPAT	\$m	(4.3)	(2.6)	(4.2)	(1.6)	0.4
EPS	¢ps	(3.0)	(1.6)	(2.2)	(0.8)	0.2
CFPS	¢ps	0.7	(1.3)	(0.8)	0.7	2.3
PER	x	N/A	N/A	N/A	N/A	72.9
Price/Cash Flow	x	22.5	N/A	N/A	22.9	6.4
EV/Revenue	x	2.4	1.7	1.2	0.6	0.5
EV/EBITDA	x	N/A	149.9	N/A	10.6	4.6
EV/EBIT	x	N/A	N/A	N/A	N/A	23.4
EV/Capital	x	4.8	2.8	2.3	1.9	1.9
Gearing (net debt: capital)	%	(57)	8	5	26	14
Fixed charge cover	x	N/A	N/A	N/A	N/A	2
Return on capital	%	N/A	N/A	N/A	N/A	6

Spacetalk vs. Small Industrials Index



Source: Factset, Veritas

SpaceTalk is a global provider of communications solutions for families. The company produce a range of smartwatches for children and seniors and related software. Spacetalk is the leader of these emerging categories in Australia. Management plan to expand the company’s presence globally.

<https://www.spacetalk.com>

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EQUITIES RESEARCH

Spacetalk

Financial Performance (A\$m)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
Revenue	7.1	10.5	14.7	22.0	41.5	52.7
Cost of sales	(1.9)	(3.0)	(6.5)	(10.3)	(20.7)	(26.6)
Gross profit	5.2	7.4	8.2	11.7	20.8	26.1
Operating costs	(5.5)	(7.6)	(8.0)	(11.3)	(17.3)	(19.6)
Share based payments	(3.4)	(2.5)	(0.1)	(0.5)	(1.0)	(1.0)
Normalised EBITDA	(3.6)	(2.7)	0.2	(0.1)	2.4	5.6
Depreciation and amortisation	(2.0)	(2.5)	(2.9)	(3.7)	(4.2)	(4.5)
Normalised EBIT	(5.6)	(5.1)	(2.7)	(3.7)	(1.7)	1.1
Associate income	0.0	0.0	0.0	0.0	0.0	0.0
Net interest	(0.0)	(0.1)	(0.1)	(0.5)	(0.5)	(0.5)
Normalised Pre-tax Profit	(5.6)	(5.3)	(2.8)	(4.2)	(2.2)	0.6
Normalised tax	1.0	1.0	0.2	0.0	0.6	(0.2)
Profit attributable to minorities	0.0	0.0	0.0	0.0	0.0	0.0
Normalised profit to holders	(4.7)	(4.3)	(2.6)	(4.2)	(1.6)	0.4
One off items (post-tax)	0.0	0.0	0.0	0.0	0.0	0.0
Reported profit to holders	(4.7)	(4.3)	(2.6)	(4.2)	(1.6)	0.4

Cash Flow Statement (A\$m)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
Normalised EBITDA	(3.6)	(2.7)	0.2	(0.1)	2.4	5.6
Non cash items	3.4	2.5	0.1	0.5	1.0	1.0
Cash net interest	(0.0)	(0.1)	(0.1)	(0.5)	(0.5)	(0.5)
Cash tax (paid)/received	0.6	1.0	0.0	0.0	0.6	(0.2)
Working capital/other	(0.9)	0.3	(2.3)	(1.4)	(2.2)	(1.0)
Operating Cash Flow	(0.5)	0.9	(2.1)	(1.5)	1.4	4.9
Capex	(2.2)	(3.1)	(4.1)	(4.0)	(4.0)	(3.0)
Free Cash Flow	(2.8)	(2.2)	(6.1)	(5.5)	(2.7)	1.8
Disposals/Acquisitions	0.0	0.0	0.0	0.0	0.0	0.0
Dividends paid	0.0	0.0	0.0	0.0	0.0	0.0
Equity raised/buybacks	0.5	5.2	2.5	6.0	0.0	0.0
Borrowings/(debt repayment)	1.3	(1.3)	3.0	2.0	0.0	(2.0)
Other inc. finance leases	0.0	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Net increase/(decrease) cash	(1.0)	1.5	(0.9)	2.2	(2.9)	(0.4)
Cash at beginning	2.6	1.6	3.2	2.3	4.5	1.6
Cash at end (including bank deposits)	1.6	3.2	2.3	4.5	1.6	1.2

Balance Sheet (A\$m)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
Cash and cash equivalents	1.6	3.2	2.3	4.5	1.6	1.2
Trade and other receivables	0.8	1.0	2.7	4.2	7.7	9.5
Inventories	1.2	1.0	0.7	1.5	2.8	3.6
Other current assets	1.0	1.1	2.6	2.6	2.6	2.6
Current assets	4.7	6.3	8.2	12.8	14.7	16.8
Plant and equipment	0.2	0.2	0.2	0.2	0.2	0.3
Intangible assets	2.8	3.7	5.1	5.7	5.8	4.6
Right of use	0.0	0.1	0.0	0.0	0.0	0.0
Deferred tax assets	0.0	0.5	0.5	0.5	0.5	0.5
Non current assets	3.0	4.5	5.8	6.4	6.5	5.4
Assets	7.7	10.7	14.0	19.2	21.2	22.2
Trade and other payables	1.3	2.1	2.1	3.0	5.7	7.2
Provisions	0.3	0.2	0.4	0.4	0.4	0.4
Borrowings & leases	0.0	0.1	0.0	0.0	0.0	0.0
Income tax liability	0.0	0.0	0.2	0.2	0.2	0.2
Current liabilities	1.6	2.4	2.7	3.6	6.3	7.8
Borrowings	1.3	0.0	3.0	5.0	5.0	3.0
Deferred tax liabilities	0.0	0.0	0.0	0.0	0.0	0.0
Non current liabilities	1.3	0.0	3.0	5.0	5.0	3.0
Total liabilities	2.9	2.4	5.7	8.6	11.3	10.8
Issued shares	10.8	16.1	18.6	25.1	26.1	27.1
Reserve options	3.7	6.2	6.2	6.2	6.2	6.2
Accumulated losses	(9.7)	(14.0)	(16.6)	(20.8)	(22.4)	(22.0)
Total equity	4.8	8.3	8.3	10.6	10.0	11.4

Directors and Key Management Personnel

	Shares	Holding
Mark Fortunatow	17.3m	10.5%
Martin Pretty	0.3m	0.2%
Brandon Gien	0.1m	0.1%

Major Shareholders

	Shares	Holding
Mark Fortunatow	17.3m	10.5%
HSBC Nominees	5.3m	3.2%
Noel Hurd	4.0m	2.4%
UBS Nominees	3.8m	2.3%
Top 20 shareholders	108.1m	65.4%

Source: Company data, Veritas Securities estimates

Share Price: \$0.15 ps

Valuation: \$0.60 ps

Valuation Metrics

	Valuation
Price Target (ps)	\$0.60 303%
Share Price (ps)	\$0.15
FY22E EV/Sales (x)	1.2
Implied FY22 EV/Sales (x)	4.6 294%
Implied FY23 EV/Sales (x)	2.4 109%
Market Capitalisation (A\$m)	24.8
Enterprise Value (A\$m)	25.5
Shares in issue (m)	165.3

Valuation Multiples

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
P/E (x)	N/A	N/A	N/A	N/A	N/A	72.9
Price/Cash Flow (x)	N/A	22.5	N/A	N/A	22.9	6.4
EV/Revenue (x)	3.6	2.4	1.7	1.2	0.6	0.5
EV/EBITDA (x)	N/A	N/A	149.9	N/A	10.6	4.6
EV/EBIT (x)	N/A	N/A	N/A	N/A	N/A	23.4
Equity FCF yield (%)	-11.2	-8.9	-24.7	-22.4	-10.8	7.4
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0	0.0
EV/capital (x)	5.8	4.8	2.8	2.3	1.9	1.9
Price to book value (x)	4.0	2.5	2.9	2.7	3.1	2.7

Per Share Data

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
EPS diluted - adjusted (eps)	(3.69)	(3.03)	(1.58)	(2.24)	(0.78)	0.21
EPS diluted (eps)	(3.69)	(3.03)	(1.58)	(2.24)	(0.78)	0.21
Cash flow per share (eps)	(0.4)	0.7	(1.3)	(0.8)	0.7	2.3
Free cash flow per share (eps)	(2.2)	(1.6)	(3.8)	(2.9)	(1.3)	0.9
Cash (eps)	1.3	2.2	1.4	2.4	0.7	0.6
Net assets (eps)	3.8	5.9	5.1	5.6	4.8	5.5
DPS (eps)	0.0	0.0	0.0	0.0	0.0	0.0
Franking (%)	0.0	0.0	0.0	0.0	0.0	0.0
Shares on issue - avg. basic (m)	121	138	159	185	205	205
Shares on issue - avg. diluted (m)	127	141	162	188	208	208

Segmental Revenue (A\$m)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
App ARR	0.8	1.5	2.7	4.5	8.3	12.1
App revenue	0.4	1.2	2.1	3.6	6.4	10.2
Device revenue	4.2	6.5	10.5	16.7	33.3	40.7
SpaceTalk revenue	4.6	7.7	12.6	20.2	39.7	50.9
MGM schools revenue	2.2	2.7	2.0	1.8	1.8	1.8
Trading revenue	6.8	10.4	14.6	22.0	41.5	52.7
Grants & other income	0.3	0.1	0.1	0.0	0.0	0.0
Revenue	7.1	10.5	14.7	22.0	41.5	52.7

Segmental Revenue Growth (% YoY)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
App ARR growth	N/A	87.5	80.7	65.1	84.6	46.9
App revenue growth	N/A	180.0	77.1	69.1	77.2	60.1
Device revenue growth	836.5	53.8	62.2	58.6	100.0	22.2
Spacetalk revenue growth	931.9	65.4	64.5	60.4	96.0	28.3
MGM schools revenue growth	(1.9)	25.1	(27.8)	(9.1)	0.0	0.0
Trading revenue growth	154.5	52.5	40.2	51.0	88.1	27.1
Revenue growth	160.3	46.8	40.5	49.6	88.1	27.1

Performance Ratios (%)

Year ended June 30	FY19	FY20	FY21E	FY22E	FY23E	FY24E
Gross margin	73.1	70.9	55.9	53.1	50.0	49.6
EBITDA margin	(51.0)	(25.6)	1.2	(0.3)	5.8	10.5
Gross debt inc. leases (\$ m)	1.3	0.1	3.0	5.0	5.0	3.0
Net cash/(debt) (\$ m)	0.4	3.0	(0.8)	(0.5)	(3.5)	(1.9)
Gearing (net debt/(cash): capital)	(8.7)	(57.3)	8.3	4.8	25.7	14.1
Fixed charge cover	N/A	N/A	N/A	N/A	N/A	1.8
Return on capital	N/A	N/A	N/A	N/A	N/A	5.9

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Smartphone watches for children and seniors

In the future, most children and seniors will wear a smartwatch. There is a good chance that the watch will be a Spacetalk. Spacetalk is the leading manufacturer of children’s smartphone watches in Australia with its original Spacetalk Kids (Figure 2) launched in September 2017 and the Spacetalk Adventurer which was launched in December 2020 (Figure 3). The Spacetalk Life, launched in June 2020, is the only smartwatch designed specifically for seniors available at major Australian retailers (Figure 4).

Figure 2: Spacetalk Kids



Source: Company, Veritas research.

Figure 3: Spacetalk Adventurer



Source: Company, Veritas research.

Figure 4: Spacetalk Life



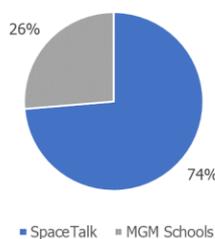
Source: Company, Veritas research.

Spacetalk was co-founded in 2001 by Mark Fortunatow, Executive Chairman and the company’s largest shareholder. It listed on the ASX in 2003 as MGM Wireless Limited. Originally the main product of the company was the MGM Schools SMS service which enables schools to inform parents via text message if their child is missing during rollcall. The company changed its name to Spacetalk in November 2020 in recognition of the increasing importance of the smartwatch business which evolved from the learnings about parent student interactions at school.

The company has two segments: Smartwatches & Apps under the Spacetalk brand and School Messaging Services under the MGM Wireless brand. Smartwatches & Apps comprised 74% of group revenues in FY20 (Figure 5) which we forecast will rise to 97% by FY24.

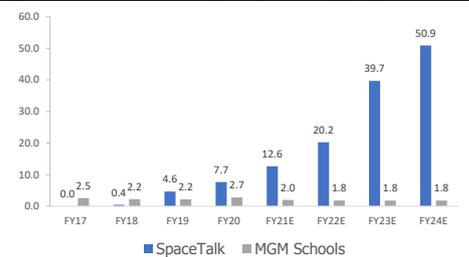
This report focuses on Smartwatches and Apps segment as we expect it to generate all of the revenue and profit growth. The segment has grown from no revenue in FY17 to \$7.1m in 1H21 and we forecast \$50.9m in FY24 (Figure 6).

Figure 5: Revenue by segment in FY20 (%)



Source: Company data.

Figure 6: Revenue by segment (\$m)



Source: Veritas estimates, Company data.

The leading children’s smartphone watch

Our analysis of all children’s smartwatches available at major retailers suggests Spacetalk has the best customer proposition. The original Spacetalk Kids product had the leading market share of SIM enabled watches in FY20 (Figure 7).

The Spacetalk Adventurer, launched in December 2020, extends the lead created by the original Spacetalk Kids device with: double the battery life, superior water resistance, 4G connectivity (Kids was 3G), family group chat and the inclusion of a camera and heart rate monitor for the first time.

Figure 7: The major players in the children’s smartwatch market in Australia

	SpaceTalk Adventurer	SpaceTalk Kids	Moochies	Alcatel Movetime	Garmin Vivofit JR3	Fitbit Ace 3
						
Price (A\$)	349	249	228	197	149	98
Australian market share CY20 est.	N/A	88%	5%	5%	N/A	N/A
SIM enabled	✓	✓	✓	✓	✗	✗
Audio calls	✓	✓	✓	✓	✗	✗
Video calls	✓	✗	✓	✓	✗	✗
SMS	✓	✓	✓	✓	✗	✗
Group chat	✓	✗	✗	✓	✗	✗
4G	✓	✗	✓	✓	✗	✗
GPS enabled	✓	✓	✓	✓	✗	✗
Location accuracy	High	High	Low	Low	N/A	N/A
Gorilla Glass	✓	✓	✗	✗	✗	✗
Step counter	✓	✓	✓	✓	✓	✓
Heart rate monitor	✓	✗	✗	✗	✗	✗
Rewards	✓	✓	✗	✗	✓	✓
Data storage	Local	Local	Local	China	USA	USA
Camera (MP)	5	N/A	2	0.3	N/A	N/A
Battery size (mAh)	750	480	700	370	N/A	N/A
App Store rating (/5)	4.4	4.4	2.5	None	4.5	4.0
App Store Reviews	911	911	120	0	3,000	10,000

Source: Company data, Veritas research. Prices as of 13 April 2021. Market share for SIM enabled watches only.

The features of the Spacetalk Adventurer that make it different from competitors include:

- **Being SIM and GPS enabled:** Spacetalk, Moochies and the Alcatel Movetime are SIM and GPS enabled. The children’s offerings from Garmin and Fitbit are not. A SIM facilitates audio and video calls, SMS and group chat. GPS enables the location of the child to be tracked and also alerts to parents when the child moves out of a ‘safe zone’. The ability to speak with and locate a child is important for a parent’s peace of mind.
- **4G enabled:** One of the primary benefits of the Adventurer is that it is 4G enabled. The Kids was 3G only. This is a big selling point to many mobile network operators that are no longer selling 3G devices.
- **Tracking fitness and allowing parents to issue rewards:** The primary uses of the Garmin and Fitbit children’s fitness trackers are tracking steps and allowing parents to grant rewards to their children for achieving fitness goals or chores. Spacetalk is the only SIM/GPS enabled device to offer the reward functionality.
- **Measuring heart rate:** The Spacetalk Adventurer is the only children’s device to measure heart rate – a feature the Spacetalk Kids does not have. This means it

gives a much better reading of the child's actual exercise and calories burned than the Garmin or Fitbit devices – a step counter alone is not good at measuring exercise intensity.

- **Accurate location detection:** Spacetalk uses a combination of Wi-Fi (powered by Google Maps), mobile phone tower triangulation and GPS to deliver a reliable child location to the parent. Reviews for Alcatel Movetime ([link](#)) and Moochies report inaccurate location tracking. For example a customer review for the Moochies watch reported the child's location as off the coast of Ghana when the child was really in Australia ([link](#)). The lack of GPS on the Fitbit Ace 3 and Garmin Vivofit Junior is a drawback ([link](#)).
- **Gorilla glass:** Durability is extremely important for a children's watch. Spacetalk is the only children's device with Corning Gorilla Glass which is impact and scratch resistant. Gorilla Glass is used on the premium smartphones such as the Samsung S21 and Galaxy Note and premium smartwatches including the Garmin Forerunner and Garmin Fenix.
- **Better battery life:** One of the only consistent criticisms of the Spacetalk Kids in customer reviews was a short battery life. The Adventurer has double the battery life of the Kids and the largest battery of the SIM & GPS enabled watches. Note that the non-SIM/GPS enabled trackers use different batteries which are not directly comparable in terms of the mAh specification. Typically, Fitbit batteries last for around a week without charging, the Garmin Vivofit Jr. battery lasts up to a year before replacement versus the Adventurer which lasts 1.5 days between charges.
- **Leading market share at a higher price point:** Conversations with industry experts suggest that Spacetalk had the leading market share of SIM enabled children's smartwatches in Australia with 88% value share from the older Spacetalk Kids device in CY2020. That this occurred with a less advanced product than the new Adventurer and at a higher price point than competitors demonstrates that the product lives up to the promise of keeping families safe. We estimate that revenues generated by the Garmin Vivofit Junior and Fitbit Ace exceed \$100m annually globally, which points to significant upside for Spacetalk given its superior functionality.
- **A well-regarded app:** The usefulness of a device is largely dependent on its connectivity with the parent's devices via the app. Spacetalk is the only SIM and GPS enabled children's device to have a rating of more than four out of five stars on the Apple App Store with a significant number of reviews. Spacetalk charges \$5.99 per month for up to two devices connected to the app vs. the Moochies app which is free to use. Despite being free the Moochies app is rated 2.5 stars out of 5 with just 120 customer reviews on the Apple App Store.
- **Group chat functionality:** Only the Spacetalk Adventurer and the Alcatel Movetime children's watches have the functionality that the child can chat with multiple family members at the same time. The ability for group chat is a new feature of the Adventurer watch. The Spacetalk app – which was rebuilt in FY20 to enable this functionality – enables families to share locations, photos, videos and comments in a format that is similar to WhatsApp but restricted to people approved by the parents via the Spacetalk app. This functionality should encourage more family members to download the app.

- **The highest resolution camera:** Spacetalk offers the highest resolution camera in the children's device market at 5 megapixels vs. Mochies at 2 megapixels and Alcatel at 0.3 megapixels.
- **Data security:** Spacetalk and Mochies are the only two companies that can guarantee that customer data is stored exclusively in the country where the customer is based. Other competitors can store user data overseas at their discretion, which may mean the data is accessible to foreign entities.

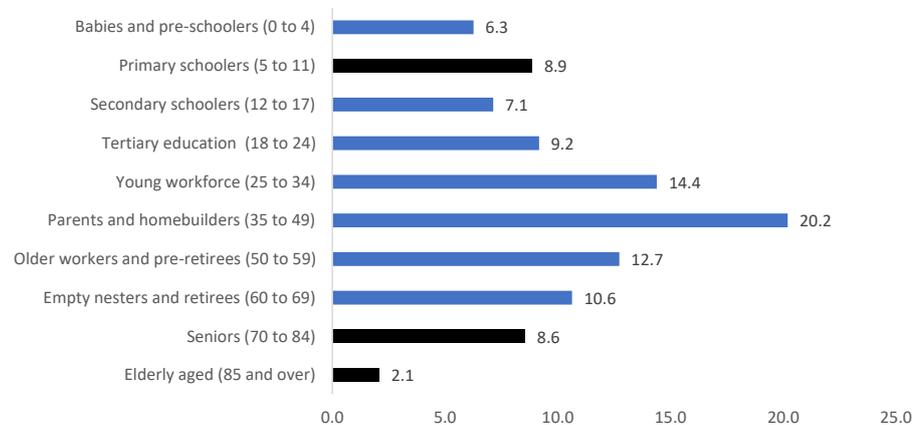
Competitive advantages

We do not see the industry behemoths such as Apple or Samsung as particular threats due to Spacetalk’s competitive strengths which include: a unique focus on families; customer focus; an award-winning design and a position at the top of the customer acquisition funnel for mobile network operators.

Made for families not individuals

Spacetalk designs devices and apps specifically to enhance the relationship between: primary school aged children (9% of the Australian population, Figure 8) and their parents as well as seniors (11% of the population) and their carers. Competitors are primarily focused on the middle of the population distribution.

Figure 8: Australian population by age (% of total) - Spacetalk device audience in black



Source: Informed Decisions, Veritas research.

Putting the needs of the family at the heart of product design is Spacetalk’s primary competitive advantage. Mass market competitors such as Apple and Samsung build smart devices for individuals – with a layer of privacy around each individual. This creates an opportunity for Spacetalk. The role of the parent requires being able to protect children from inappropriate content and contact with undesirable people. Spacetalk is designed specifically to meet these parental needs in a way that mass market smartwatches do not.

Features for parents of the Spacetalk children’s watches include:

- An ability to approve the contacts permitted to communicate with the child via an app downloadable to their smartphone.
- Track their child’s fitness activities.
- Determine their child’s location via GPS.
- No social media.
- Functionality that caters for separated parents, a situation that more than 40% of Australian children live with.

Features for children include:

- The ability to chat with family groups via the Spacetalk app which is similar to WhatsApp except restricted to parent approved contacts.
- Making/taking calls but only from a parent-approved contact list.
- Sharing photos/videos with family groups.
- A 'gorilla glass' OLED display which is impact resistant.
- A 'school time' setting which blocks smartphone features during class times in order to comply with school bans on smart phones.

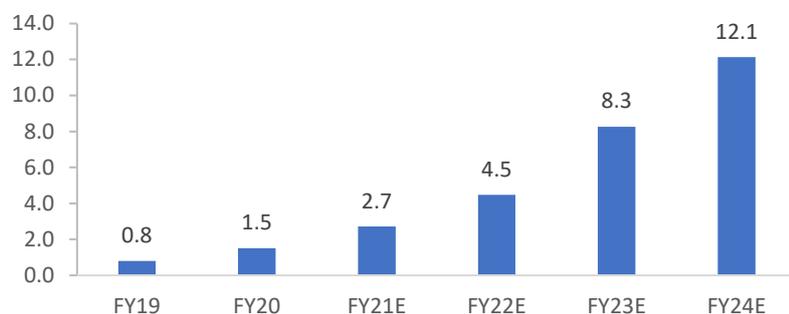
A long association with the education technology sector makes Spacetalk well attuned to the requirements of guardianship. The MGM School division has provided attendance management software to over 6 million parents at more than 5,000 schools in Australia over the past twenty years.

Customer focus

Spacetalk, like Amazon, is a company that is focused on customer experience over the life of the product rather than simply selling a device. Many of Spacetalk’s competitors are distributors of a white labelled, mass produced gadgets – putting their own branding on a generic product that has been designed by a third party. This means many different brands have gone to market with essentially the same device. Such watches come with free apps that usually lack customer support and ultimately do not engender customer loyalty. Spacetalk devices and software has been designed from the ground up to provide a positive environment for families.

The other difference between Spacetalk and many competitors is the recurring revenue it derives from subscription to the app. We forecast annually recurring revenue (ARR) from app subscriptions should rise to \$12m in FY24 from \$1.5m in FY20 (Figure 9). This should give the company more predictable and higher margin earnings. Spacetalk had an estimated 60k active users in 1H21. By way of context Fitbit had 29.6m active users in the year to December 2019.

Figure 9: Spacetalk annually recurring revenue (ARR) from app subscriptions (\$m)



Source: Company data, Veritas estimates.

Award winning product design

Spacetalk’s watches were designed in collaboration with renowned British design consultancy Tangerine. Jonathan Ive – the designer of the iPhone and former chief design officer at Apple – worked at Tangerine on the Apple account prior to being poached by Apple.

Tangerine is responsible for designing devices for Huawei, LG, Samsung and Nikon and the design of the aircraft interiors for numerous airlines including British Airways and Cathay Pacific ([link](#)).

The Spacetalk Adventurer was awarded a Red Dot award for product design according to an ASX release on 6 April 2021. The Red Dot award, based in Germany, is a highly regarded design competition with over 18,000 entries across multiple consumer goods categories. Past winning products include the Apple iPhone and Apple AirPods.

At the top of the customer acquisition funnel

Mobile subscribers are substantial earnings generators for network operators as they typically remain loyal for years. We estimate it costs an Australian telco \$90 to acquire a subscriber on average – measured by the total cost of advertising and promotions divided by the number of new subscribers.

We estimate the acquisition cost for a telco to acquire a Spacetalk customer is less than a third of a regular customer due to the target audience – children aged 6 to 12 – usually not being committed to a competitor. This makes Spacetalk a low-cost way for mobile network operators to gain customers earlier than otherwise – which should mean a higher lifetime value of the customer.

That Telstra – Australia’s largest telecommunications company - will sell the Spacetalk Adventurer is an important validation of this strategy. Telstra is highly selective about the quality of smartwatches it offers stocking only the Apple Watch, Samsung Galaxy Watch and the Fitbit Versa 2 ([link](#)). Spacetalk will join this exclusive club in late April 2021. Furthermore, Telstra will allow existing customers to pay for the SpaceTalk device in instalments which should spur demand.

Parents have been demanding a safe way to communicate with their kids for a long time. Until the Adventurer came along there was not a children’s connected smartwatch which met Telstra’s exacting standards. The comparison of Spacetalk’s features versus the competition (Figure 7) shows why this is the case.

Apple’s Family Setup launch highlights market potential

Apple launched Family Setup for the Apple Watch in September 2020 ([link](#)). This enables children and old people who do not have an iPhone to use an Apple Watch administered by the parents iPhone. Family Setup allows the parent to track the child’s location, approve contacts and has a ‘school time’ setting – features shared with Spacetalk watch. It also allows the parent to approve purchases and app downloads.

We believe the invention of Family Setup validates the size of the Spacetalk opportunity. Apple would not have built the functionality if there was not a material potential market. There are two major limitations of Family Setup:

- **Price:** An Apple Watch costs A\$599 for the Series 6 and \$429 for the SE variant which does not have an always-on retina display, 72% and 23% more expensive than the Spacetalk Adventurer, respectively. Why would someone buy such an expensive device to turn off many of the features?
- **Not designed for families first:** The Apple Watch and most of its apps are designed for adults with their own Apple ID. The overlay of Family Setup is essentially an afterthought. This leaves open the potential that parents may approve apps like TikTok for download without understanding how potentially

harmful they can be. We believe that a core Spacetalk strength is that it designs the device and apps with family safety as the primary objective.

Spacetalk has a sizeable opportunity regardless of the success of Family Setup. Apple first went big into the fitness category a decade ago. This did not prevent Garmin from dominating the fitness watch market because of a laser focus on the specific needs of athletes. We see Spacetalk's focus on children and seniors in the same light.

A \$17bn addressable market

We estimate Spacetalk has a total addressable market of \$17bn in just the markets where the company currently operates or has plans to enter. This includes Australia, New Zealand, UK and the United States for children and Australia and New Zealand for seniors (Figure 10). There are currently no plans to introduce the seniors watch in the US or UK as the company wants to prove viability in Australia first. If this were to happen it would open up an addressable market of approximately twice the size.

The market size comprises of \$13.6bn from device sales and \$3.8bn of annually recurring revenues from app subscriptions. The biggest opportunity is the US market which we estimate is worth \$14bn vs. the ANZ at \$1.7bn.

Spacetalk has a strong position in the ANZ market, a foothold in the UK market and plans to enter the US market in CY21 as we discuss in more detail in the next chapter.

Figure 10: Spacetalk has an estimated total addressable market of \$17bn

Market	Audience	Potential devices (m)	Average app users per device	Paid app users (m)	Device wholesale price (A\$ per unit, post GST/VAT)	Average revenue per user on app (\$ per year, post GST/VAT)	Addressable device revenue (A\$m)	Addressable annually recurring revenue from app (A\$m)	Total revenue (A\$m)
ANZ	Children	2.5	0.9	2.1	200	65	500	139	639
ANZ	Seniors	3.4	0.9	2.9	229	87	770	249	1,019
ANZ	Children + seniors	5.9	0.9	5.0	216	78	1,270	388	1,657
UK	Children	6.5	0.9	5.5	200	65	1,300	361	1,661
US	Children	55.0	0.9	46.8	200	65	11,000	3,055	14,055
Total		67.4	0.9	57.3	201.4	66	13,570	3,804	17,373

Source: Veritas Research.

67 million potential users in the US, UK and ANZ

There are currently 64 million children aged five to twelve years in the US, UK and ANZ and 3 million seniors aged older than 70 in ANZ giving a total addressable market of 67 million potential device owners. The number of possible app users is larger due to the multitude of family members with reason to connect to the child's device.

Customers need to subscribe to the app to get full functionality

Parents or carers need to pay for a monthly in-app subscription in order to communicate with the person they care for via the app, downloaded to their own smart devices. For the children's watch the subscription costs A\$5.99 per month (inc. GST) for up to two connected devices and A\$8.99 per month for use on up to five devices in Australia. For the senior's device the subscription costs A\$7.99 per month, reduced from A\$9.99 per month in April 2021. Only the parent/carer (known as the primary user) needs to pay to use the app. Other relatives or friends can use the app for free.

Spacetalk should benefit from network effects as it gains scale. There is more incentive for relatives and friends to use the app when there are more children with devices. We estimate that the average children's device has 3.5 app users connected to it (including free users). We estimate that every purchased device has 0.85 paid users on average to account for churn.

We estimate the average revenue per paid app user for the children's device to be \$65 per year (12 months at \$5.99, less 10% GST) and the seniors device \$87 per year. Pricing in overseas markets is broadly similar to Australia when adjusted for average exchange rates and accordingly we assume it is identical for the purposes of market sizing.

More than 100x revenue growth is possible

Spacetalk feels like Fitbit in 2011. Fitbit was founded in 2007 but only really began to get traction in 2011. Over the next four years volumes and revenue increased by more than 100x.

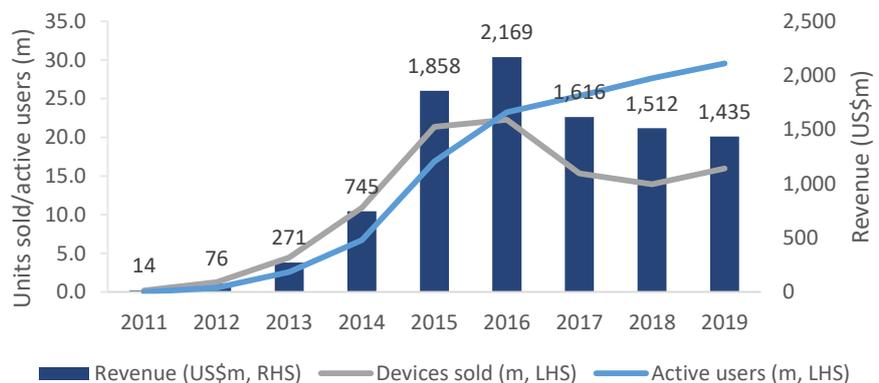
Forecasting revenues for a new product like the Spacetalk Adventurer is difficult. Traditional approaches like applying a constant revenue CAGR do not apply when a category is in its formative stages.

Growth in demand for emergent technologies like Spacetalk typically follows an S-curve ([link](#)): growth is slow at first as early adopters get comfortable with the concept and the manufacturer irons out bugs; growth goes exponential as the concept gains mainstream acceptance and wide distribution; growth plateaus when most customers that need the device already have one or even declines as competition enters the market.

Fitbit first popularised the fitness tracker and so provides a sensible precedent for Spacetalk. Fitbit was founded in 2007 but did not really gain product traction until 2011. Over the following four years the number of units sold increased by more than 100 times: from 208k in 2011 to 21.4m in 2015. Revenue increased by 128x from US\$14m to \$1.9bn over the same period (Figure 11).

We think Spacetalk is in a similar position to Fitbit in 2011. Spacetalk’s first children’s device was launched in September 2017 and is only now (4 years later) on the cusp of mainstream acceptance with companies like Telstra stocking it for the first time. Fitbit was acquired by Google for an equity valuation of US\$2.0bn in January 2021.

Figure 11: Fitbit devices sold (m), active users (m) and revenue (US\$m)



Source: Company data, Veritas Research.

With just 1% penetration Spacetalk could be worth >\$3 per share

If Spacetalk were to get 1% penetration of the children’s market in the US, UK and ANZ as well as 1% of the ANZ seniors market we estimate sales of 670k devices. Applying a 10x multiple to the app revenue and a 1x multiple to device revenue would give a \$515m implied equity valuation or \$3.12 per share (Figure 12). Spacetalk does not disclose devices sold or app users – we estimate the company had roughly 60k active app users in 1H21 of which more than 90% are in ANZ.

Figure 12: Spacetalk revenue and valuation scenarios

Market	Penetration in target market	Devices sold (m)	Paid app users (m)	Device revenue (A\$m)	App ARR (A\$m)	EV/revenue multiple for devices (x)	EV/revenue multiple for ARR (x)	Implied SPA equity valuation (\$m)	Valuation per share (\$)
ANZ	0.5%	0.03	0.02	6	2	1.0	10	25	0.15
	1%	0.06	0.05	13	4	1.0	10	51	0.31
	10%	0.59	0.50	127	39	1.0	10	514	3.11
	20%	1.17	1.00	254	78	1.0	10	1,029	6.22
ANZ, UK, US	0.5%	0.34	0.29	68	19	1.0	10	257	1.56
	1%	0.67	0.57	136	38	1.0	10	515	3.12
	10%	6.74	5.73	1,357	380	1.0	10	5,160	31.22
	20%	13.47	11.45	2,714	761	1.0	10	10,321	62.44

Source: Company data, Veritas Research.

Expanding distribution

Drivers of Spacetalk growth include expanding distribution in Australia, UK and the US as well as the high growth rates of the smartwatch category of wearables. We estimate that Walmart and Best Buy could be a greater than \$80m annual revenue opportunity for the company (6x our FY21 group revenue forecast).

The ability to reach all Australian children will be in place by end of FY21

Increased distribution for the new Spacetalk Adventurer watch during FY21 means the company has the ability to reach all 2.5 million children in Australia aged between 9 and 12 for the first time. The rate of adoption is unknown – but we expect take-up of the second-generation Adventurer watch will be higher than the first, as was the case with later generation Apple iPods and iPhones. First model devices are often the proof of concept, second models overcome the initial shortcomings that only become apparent when the device is put through its paces. Distribution plans for the Adventurer in Australia include:

- **JB Hifi launched in December 2020:** JB Hifi, Australia's preeminent consumer electronics retailer, launched the Spacetalk Adventurer in December 2020. JB Hifi has been a long-term distributor of the Spacetalk Kids. Spacetalk reported higher sales for the Adventurer than the Kids in the first two weeks of it being on sale according to an ASX release on 27 January 2021 ([link](#)).
- **Harvey Norman, Officeworks and Kogan launched in January 2021:** Harvey Norman, Officeworks and Kogan commenced selling the Adventurer in January 2021. JB Hifi, Harvey Norman, Kogan and Officeworks represent at least two thirds of the Australian consumer electronics market by value according to Morningstar estimates ([link](#)).
- **Telstra to launch in late April 2021:** Telstra, Australia's largest telecommunications company with 19 million retail mobile services, will sell the Spacetalk Adventurer across all retail stores and online from late April 2021 for the first time. The watch can be purchased outright or be paid for in instalments as part of the regular Telstra bill. Ability to pay by instalments may lead to much wider adoption as it reduces the initial outlay for the customer.
- **Vodafone and Optus future possibilities:** Vodafone is currently a Spacetalk Kids distributor which suggests it is a likely candidate for distributing the Adventurer. If Telstra gains traction with Spacetalk then we expect Optus will follow suit.

Management plan to replicate the Australian strategy in the UK

Management plans to replicate the Australian launch strategy for the Adventurer in the UK when lockdowns and the school holidays end in September 2021. Existing distributors include Amazon UK, Curry's PC World (part of Dixons Carphone PLC which has a market capitalisation of A\$3bn) and Sky Mobile.

Aside from Amazon UK – which launched the Adventurer in December 2020 - the UK distributors of the Adventurer are yet to be announced. Spacetalk also sells product directly in the country via its local website Spacetalk.co.uk.

The take-up of Spacetalk in the UK has been fairly limited thus far with revenue of \$0.9m reported in 1H21, a decline of 28% YoY. The UK represented 12% of Spacetalk revenue (ex

MGM schools) in 1H21 vs. 20% in FY20. We attribute the poor performance relative to Australia to a lack of advertising, no physical presence in stores and a suboptimal mobile network partner in Sky.

To date the only UK based mobile network operator to distribute Spacetalk is Sky. We think this is holding back Spacetalk due to Sky's low market share of connected mobile subscribers. Roughly 2% of UK mobile subscribers in 2020 used the Sky network according to Statista ([link](#)). Sky has scale in broadband and cable TV – which are not relevant markets for Spacetalk.

Spacetalk was ranged in Curry's PC World online stores in December 2019. Curry's PC World had UK and Ireland revenues of £6.1bn (A\$11bn) in the year to May 2020, making it one of the largest consumer electronics retailers in Great Britain and bigger than JB HiFi with \$8bn revenue in FY20. Our contact with Curry's PC World front line sales staff suggests they have limited knowledge of the Spacetalk product and its capabilities. The fact that the product is not available in physical stores may be a factor in this – this allows customers to test the product before purchase and sales staff to learn about it.

We see the large UK mobile network operators EE/T Mobile, O2 and Vodafone as the most likely partners for Spacetalk for the same reasons that Telstra adopted the product in Australia – a low-cost way to acquire customers at a young age.

Another promising route to market would be the physical stores of Curry's PC World and Carphone Warehouse (another Dixons Carphone subsidiary that focuses on selling mobile handsets and plans for multiple networks). If the company went to market with the same prominent merchandising as JB HiFi it could realistically sell more through Dixons Carphone PLC than in all of Australia currently due to their scale (Australia generated \$6.3m of revenue in 1H21 excluding MGM Schools). Spacetalk onboarded a new UK country head during 1H21 in order to improve execution in the country.

Just two US major retailers could generate >\$80m revenue for Spacetalk

Spacetalk management committed to 'an exciting go to market in the USA planned for CY21' in the 1H21 financial report. With little additional information provided we can only speculate as to what this could look like.

The most likely distribution deals would be with either Best Buy or a Walmart – as these companies are the most highly regarded consumer electronics retailers in the country. Best Buy operates 1,009 stores in the United States and Walmart operates 4,743 stores under the Walmart brand and 599 under the Sam's Club brand in the US alone (there are more stores in Canada, Mexico and other countries).

We estimate that an average store sells 50 Spacetalk units a week. Applying the store-based volume estimate to the total store counts of Best Buy and Walmart in the US gives \$81m revenue of which \$17.6m is recurring (Figure 13).

This analysis suggests that getting ranged in the two most important consumer electronics retailers in the US could increase group revenue by a factor of more than 6x relative to the \$13m we forecast in FY21.

Figure 13: US retailers Best Buy and Walmart could be a >\$80m revenue opportunity

Brand	US stores	Estimated units sold annually per store	Total units sold annually	Paid app users	Wholesale unit price (A\$)	App ARPU (A\$)	Device revenue (A\$m)	App ARR (A\$m)	SpaceTalk annual revenue (\$Am)
Best Buy	1,009	50	50,450	42,883	200	65	10.1	2.8	12.9
Walmart US	4,743	50	237,150	201,578	200	65	47.4	13.2	60.6
Sam's Club US	599	50	29,950	25,458	200	65	6.0	1.7	7.7
Total	6,351	50	317,550	269,918	200	65	63.5	17.6	81.1

Source: Company data, Veritas estimates.

The major hurdle for the company is the time it takes to build a variant for the US market – a different set of antennas is required due to cellular networks operating at different frequencies ([link](#)). The US variant needs to go through the approval process for regulators and the retailers need to test the product. Telstra product testing took 5 months. Accordingly, we view the announcement of any major US retailer as being at least nine months away. The company may announce a soft launch via their own website earlier.

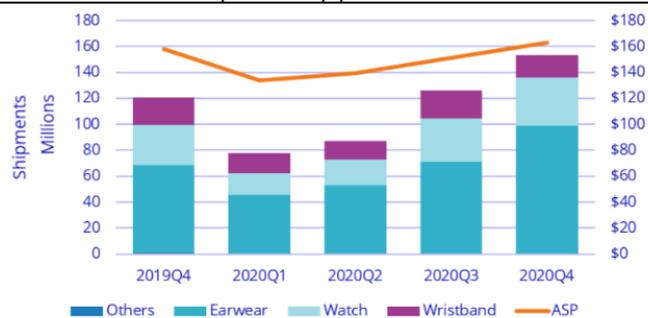
Smartwatches are the fastest growing category of wearables

"Smartwatches are the fastest growing market for wearables globally and the addition of Spacetalk will strengthen Telstra's connected smartwatches offering."

Fiona Hayes, Telstra Retail executive quoted in the Australian on 19 March 2021 ([link](#))

The connected smart wearables market is forecast to grow at 19.5% CAGR to reach 776m units by 2026 according to Researchandmarkets.com ([link](#)). Smart watches are the fastest growing segment of the wearables market, growing by more than 200% from the quarter ending March 2020 to the quarter ending December 2020 according to IDC (Figure 14). COVID lock down measures negatively impacted smartwatch sales because they are predominantly used outside of the home. It follows that demand should increase as lock down measures are eased – a thematic which should boost Spacetalk sales in 2H21.

Figure 14: Worldwide wearables shipments by product



Source: IDC, Veritas Research.

New features should improve engagement over time

At the moment the main functionality for the Spacetalk app is chat – similar to WhatsApp restricted to the Spacetalk universe. In future the company is looking to add entertainment functionality similar to Instagram but also restricted to the Spacetalk universe. Another possible idea is allowing children to access sporting highlights and other safe media.

The company is also exploring the potential for third party apps to be allowed on the Spacetalk platform with likeminded brands. A potential monetisation opportunity is delivering relevant and parent endorsed content to kids.

The aged care opportunity

Spacetalk launched the Spacetalk Life in June 2020 via JB Hifi and its own website. It was the first watch on the market specifically for seniors to be connected to a mobile network.

Features for carers include:

- The ability to request a location and view the location history.
- An ability to communicate with the seniors via SMS, voice messaging or calls (4G enabled).
- Notifications to the carer when the device needs to be charged and when the senior leaves a predefined safe zone.
- Medical history information.
- The ability to manage the contacts for the senior from the application.

Features for seniors include:

- Ability to send an SOS alert to carers using a special button on the watch.
- A software update planned for May 2021 will mean that falls will be automatically detected, and emergency services informed of the fall time and location.
- Water (shower) proof. Competitors fall detection devices typically do not work in the shower.
- Being able to set reminders for calendar appointments and medications.
- A step counter.
- Being able to easily call family and carers via 4G, especially when away from home without a mobile phone.

The company does not separately disclose sales of the Life, so it is difficult to assess how it has performed to date. With the product on the market for only nine months it is fair to assume that management have learned a lot.

On 19 April 2021, the company announced a number of changes to fine tune the Spacetalk Life customer proposition: a new business to business distribution channel, lower pricing and a software upgrade to enable automated fall detection. We expect these changes should spur additional demand by reducing barriers to adoption.

A new distribution channel

Spacetalk announced it will take the Spacetalk Life device to market in Australia via a new channel: business to business to customer (B2B2C). This will entail aged care providers, home care providers, occupational therapists and the National Disability Insurance Scheme (NDIS) providers receiving a referral fee from Spacetalk for recommending the product to patients. The device should be eligible for full government funding at the new price point. Spacetalk has secured its first B2B2C partnership with ACH Group – a leading care organisation with 1,800 staff and 20,000 patients.

Spacetalk's ultimate goal is for the Spacetalk Life device and app to be the 'software as a service' solution at the heart of aged and home care. The ongoing Royal Commission into

aged care recommends increased use of technology to improve care and reduce cost. The Spacetalk Life's relevant functionality and ease of use make it ideally suited to this task.

Lowering prices

Spacetalk also announced that it would be lowering the retail price of the Spacetalk Life to \$399 from \$549 and the cost of the app subscription to \$7.99 from \$9.99 per month. These changes are to make the product fit within the budgets of more carers and to ensure that the full cost of the device and subscription can be covered by NDIS and CHSP funding arrangements. We expect that the volume uplift from the various changes should be greater than the impact of reduced pricing on revenue.

Automated fall detection

One of the foremost items of feedback to Spacetalk following the launch of Spacetalk Life was the need for fall detection. In particular there is an important gap in the market – incumbent fall detection devices are not waterproof so are not effective in the shower which is one of the most common locations for falls.

Spacetalk plan to release a software update in May 2021 which will enable all existing devices to automatically detect falls using the inbuilt gyroscope and then use the GPS, SMS and phone capability to inform carers and emergency services of the occurrence and location of the fall. These features make the product one of the most advanced fall detection devices on the market and will also enable the device to be marketed in a pre-defined product category.

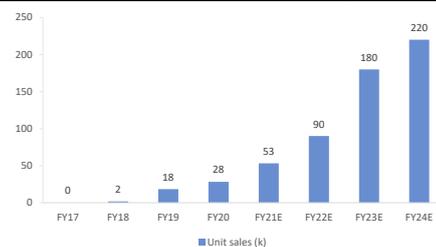
We forecast 50% revenue CAGR to FY24

Increased distribution underpins our forecast that the number of new units sold should rise from 53K in FY21 to 220k in FY24 (Figure 15). We feel that this forecast is conservative in the context that the company previously targeted 90k units sales in FY20 according to the FY19 results announcement on 22 August 2019. Our forecasts do not have this level being hit until FY22.

Management’s prior target was not reached due to the onset of COVID restrictions from March 2020 and a more limited uptake of the product in the UK than expected. Management are likely to adopt a more appropriate rollout strategy in the UK and US which targets in-store distribution at the bigger mobile network operators which include EE, O2 or Vodafone and major retailers rather than relying on Sky which is predominantly a cable TV and broadband provider. We also expect Spacetalk Adventurer to have a greater uptake than the Kids product not least because it is 4G enabled and many network operators now refuse to sell 3G products.

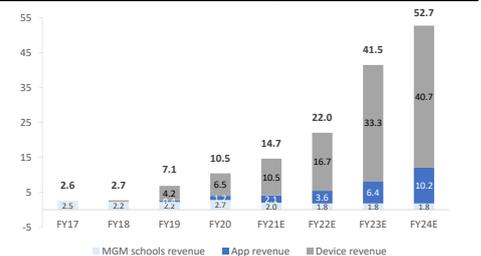
We forecast a wholesale device selling price of \$185 from FY22 onward vs. \$197 in FY21 as the company improves its value proposition. Multiplying unit sales by the average selling price gives device revenue of \$10.5m in FY21 rising to \$40.7m in FY22. We forecast app revenue of \$2.1m in FY21 rising to \$10.2m in FY22 (Figure 16).

Figure 15: Spacetalk unit sales (k)



Source: Company data, Veritas Research.

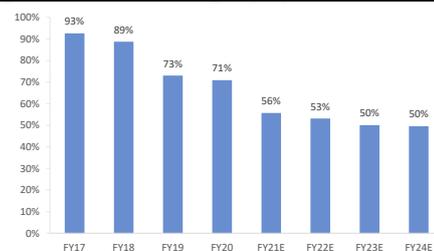
Figure 16: Revenue by segment (\$m)



Source: Company data, Veritas Research.

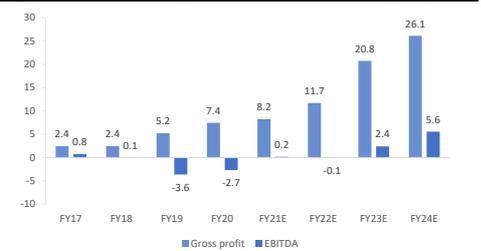
We expect that gross margin should decline to 50% by FY24 (Figure 17) predominantly due to mix. In particular we forecast that app gross margins should be steady at 80%, device gross margins should decline from 44% in FY21 to 40% in FY24 as the company adopts the Xerox model of selling the device more cheaply to grow the ecosystem. We expect the gross margin in MGM schools to be steady at 93%. Investment in sales and marketing means minimal EBITDA in FY21 and FY22. We forecast \$6m of EBITDA by FY24 due to leverage over costs (Figure 18).

Figure 17: Gross margin (%)



Source: Company data, Veritas Research.

Figure 18: Gross profit and EBITDA (\$m)



Source: Company data, Veritas Research.

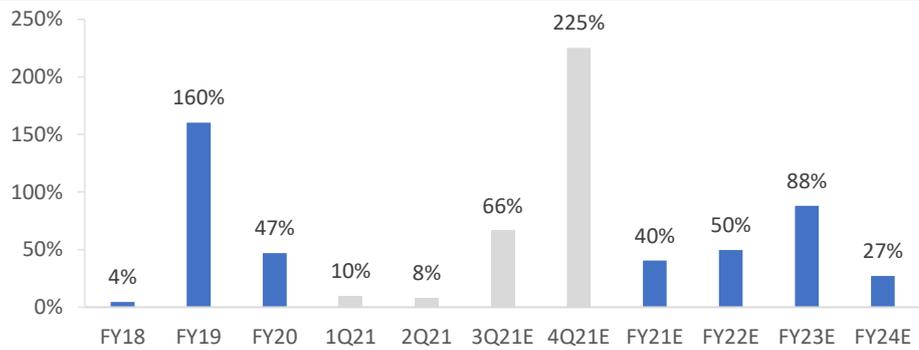
Sales to accelerate in 2H21

We expect 3Q21 and 4Q21 results to show a significant acceleration in revenue growth. Spacetalk reported revenue growth of 9% YoY in 1H21, which looks a bit light in the context of the 160% reported in FY19 and 47% in FY20. Delving more deeply into the detail of the result suggests this is really a function of timing of device sales and COVID impacts. In particular 1H20 (the last full pre-COVID period) was one of the best half year periods in the company’s history making it an incredibly tough comparison.

The comparisons get much easier in the second half of the year because new device shipments dropped in response to COVID. Revenue from device sales was \$5.9m in 1H20, just \$0.6m in 2H20 and \$6.3m in 1H21.

Spacetalk reported group revenue of \$7.6m in 1H20, \$2.9m in 2H20 and \$8.3m in 1H21. We forecast \$6.5m in 2H21 which implies a rapid acceleration in headline growth (Figure 19). Note that we expect the first half to have higher absolute sales than the second due to Christmas falling in the first half.

Figure 19: Spacetalk total revenue growth (% YoY)



Source: Company data, Veritas Research.

Funded for growth

On 19 March 2021 Spacetalk announced an agreement with Pure Asset Management to access a \$5m loan - comprised of a \$3m term loan and a \$2m bridge loan – to finance inventory, geographic expansion and investment in the brand. The \$3m term loan may be settled after 48 months by a warrant for the issuance of 11m shares at \$0.30 per share or can be 50% cash settled at the election of the company to reduce dilution. We forecast the \$2m bridge loan will be drawn in FY22.

The loan terms are relatively competitive for a company at the early stages of its growth opportunity. The term loan has an interest rate of 9.5% and the bridge facility 12.5%. The term loan is also flexible in that it is interest only with a bullet payment in 4 year. The exercise of options attaching to the facility may pay off the loan. The option strike price was a 173% premium to the underlying share price on the announcement of the issuance - indicative of the lenders view of the investment opportunity.

Spacetalk has more receivables and inventory than payables which combined with the forecast revenue growth gives a \$2m drag on operating cash flows per year. The requirement to fund this and capex/R&D of \$3-4m per annum means we forecast the company will raise \$6m in equity in FY22 at the current share price. Alternatives not in our forecasts include another loan, reduced opex/capex or option exercise. Option exercise as a major source of funds is only likely if the share price exceeds \$0.55 per share (i.e. the lowest strike price of outstanding options excluding Pure Asset Management warrants).

Experienced management

Executive chairman Mark Fortunatow has been involved with the company for 20 years and has an accomplished record of entrepreneurship in the technology sector.

Spacetalk co-founder and executive chairman Mark Fortunatow's background is entrepreneurship in marketing, engineering and technology. Prior to Spacetalk he founded three companies of note: Linx Computer Systems, TimeKeeping SA and Netline Technologies. Linx was one of the first multiuser accounting software applications in Australia designed specifically for small business, an early precursor to Xero. TimeKeeping SA was software for workforce management and timesheets which was sold to Kronos Inc in 1996. Netline was a mobile phone application developer that pioneered email access on mobile phones. Mark sold his 45% stake in Netline in January 2001, three and a half years after founding it, to Burdekin Pacific Limited in a deal which valued the enterprise at \$30m. Mark is also largest shareholder of Spacetalk, holding 10.7% of outstanding shares.

Martin Pretty, non-executive director has an extensive career in investments as Managing Director of Equitable Investors and former role as fund manager at Thorney Investment Group.

Martin Pretty has been a non-executive director since May 2020. Martin was previously a fund manager with Thorney Investment Group and held management position at Hub24, Bell Financial Group and IWL Limited. He is currently the managing director of funds management company Equitable Investors and a non-executive director of ASX listed companies Centrepoint Alliance (CAF.ASX, \$36m market capitalisation) and Scout Security Limited (SCT.ASX, \$15m market capitalisation).

Dr Brandon Gien, non-executive director, has an extensive career in industrial design.

Dr Brandon Gien joined the board of Spacetalk as a non-executive at the same time as Martin Pretty. Brandon has 25 years of industrial design experience. He is the founder and CEO of Good Design Australia, Executive Director of the Australian Design Council and Adjunct Professor of Industrial Design at UNSW and former president of the World Design Organisation.

Senior executives include Paul Cooper and Jarred Puro.

Paul Cooper, Director of Operations, previously held senior supply chain positions at Microsoft APAC and Nokia.

Paul Cooper joined the company in May 2017 as General Manager at MGM Wireless, soon becoming Director of Operations. At Spacetalk, Paul has been responsible for the design and manufacturing of the new Spacetalk products. Experience includes prior roles as Director of Supply Chain Operations at Microsoft APAC (2012-2015) and Director of Global Repair Network Management at Nokia (2008-2011).

Jarred Puro, CFO, has worked at Spacetalk for five years.

Jarred Puro became Chief Financial Officer of Spacetalk in 2019, a promotion from finance manager which he commenced in 2016. Prior to Spacetalk Jarred held a number of financial management roles with SA Health and Cobham Aviation Services.

Fair value of 60c per share

Our DCF derived fair value for Spacetalk is 60c per share (Figure 20). The primary assumptions of the DCF include: sales growth fading to 2.0%, a terminal EBITDA margin of 20% which is consistent with management's long term aspiration, terminal capex to depreciation of 1.0x and a WACC of 8%.

Figure 20: DCF valuation for Spacetalk

Year end June	Units	FY22	FY23	FY24	FY25	FY26	FY27	FY28	FY29	FY30	FY31	TV
Revenue	\$m	22.0	41.5	52.7	72.0	79.2	85.5	91.5	97.0	100.8	103.9	105.9
Revenue growth	%	49.6	88.1	27.1	36.5	10.0	8.0	7.0	6.0	4.0	3.0	2.0
EBITDA	\$m	-0.1	2.4	5.6	15.4	15.8	17.1	18.3	19.4	20.2	20.8	21.2
EBITDA margin	%	-0.3	5.8	10.5	21.4	20.0	20.0	20.0	20.0	20.0	20.0	20.0
EBIT	\$m	-3.7	-1.7	1.1	10.3	10.3	11.1	11.9	12.6	13.1	13.5	13.8
Tax rate	%	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5
NOPAT	\$m	-2.7	-1.3	0.8	7.5	7.5	8.1	8.6	9.1	9.5	9.8	10.0
DA	\$m	3.7	4.2	4.5	5.1	5.5	6.0	6.4	6.8	7.1	7.3	7.4
Margin	%	16.6	10.0	8.5	7.0	7.0	7.0	7.0	7.0	7.0	7.0	7.0
Working capital	\$m	-1.4	-2.2	-1.0	-2.2	-1.2	-1.0	-1.0	-0.9	-0.6	-0.5	-0.3
As % of incremental sales	%	-20	-11	-9	-11	-16	-16	-16	-16	-16	-16	-16
Capex	\$m	-4.0	-4.0	-3.0	-4.5	-5.5	-6.0	-6.4	-6.8	-7.1	-7.3	-7.4
Capex/D&A	x	1.1	1.0	0.7	0.9	1.0	1.0	1.0	1.0	1.0	1.0	1.0
FCF	\$m	-4.5	-3.3	1.2	5.8	6.3	7.0	7.7	8.3	8.9	9.3	9.7
Discount factor	%	93%	86%	79%	74%	68%	63%	58%	54%	50%	46%	
NPV of FCF	\$m	-4.2	-2.8	0.9	4.3	4.3	4.4	4.5	4.5	4.4	4.3	

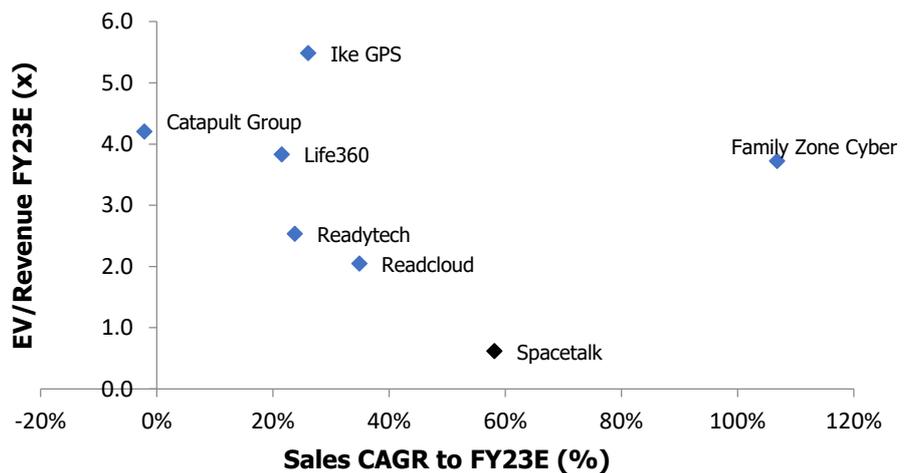
Item	Units	Value	Item	Units	Value
NPV of the forecast period	\$m	24.6	WACC	%	8.0
NPV of terminal value	\$m	74.5	Terminal growth	%	2.0
NPV of cash flows	\$m	99.1	Terminal EBITDA margin	%	20.0
Less net debt	\$m	0.8	Terminal value nominal	\$m	161
Fair value of equity	\$m	99.9	Terminal EV/Revenue	x	1.5
Fair value of equity per share	\$ps	0.60	Terminal EV/EBITDA	x	7.6
Share count	m	165			

Source: Veritas estimates.

Trading at an 80% EV/Revenue discount to peers

Spacetalk has the second highest three-year forecast revenue CAGR of the peer group yet it trades on the lowest EV/Revenue multiple of 0.6x in FY23, an 80% discount to the 3.2x peer average.

Figure 21: EV/Revenue and forecast revenue growth: Spacetalk vs. peers



Source: Bloomberg, Veritas Research.

Our fair value of \$0.60 per share puts Spacetalk on EV/Revenue and EV/EBITDA multiples of 2.4x and 41x respectively in FY23 – both below the averages of peers (Figure 22).

Figure 22: Spacetalk peer valuation

Stock	Code	Price LC	Mkt Cap LC m	EV LC m	EV/Revenue (x)				EV/EBITDA (x)				EBITDA Margin (%)				Sales 3yr CAGR
					FY20	FY21E	FY22E	FY23E	FY20	FY21E	FY22E	FY23E	FY20	FY21E	FY22E	FY23E	
SpaceTalk	SPA-ASX	0.150	24.8	25.5	2.4	1.7	1.2	0.6	N/A	149.9	N/A	10.6	-26%	1%	0%	6%	58%
Life360	360-ASX	5.50	875.0	805.7	6.9	6.3	4.8	3.8	N/A	N/A	N/A	230.2	-28%	-17%	-7%	2%	22%
Family Zone Cyber	FZO-ASX	0.50	193.3	167.9	32.9	13.2	6.3	3.7	N/A	N/A	N/A	23.6	-216%	-98%	-20%	16%	107%
Readcloud	RCL-ASX	0.38	44.4	37.7	5.0	4.0	2.7	2.0	N/A	N/A	15.1	9.0	-17%	0%	18%	23%	35%
Readytech	RDY-ASX	1.98	199.4	191.5	4.8	3.9	2.8	2.5	25.9	10.2	7.3	6.6	19%	38%	38%	39%	24%
Ike GPS	IKE-NZ	0.95	126.0	107.7	11.0	12.1	7.4	5.5	N/A	N/A	N/A	127.4	-38%	-57%	-19%	4%	26%
Catapult Group	CAT-ASX	2.09	418.9	400.9	3.9	5.4	4.8	4.2	93.2	51.7	39.6	25.9	4%	10%	12%	16%	-2%
Peer Average					9.6	6.7	4.3	3.2	59.6	70.6	20.7	61.9	-43%	-17%	3%	15%	38%

Source: Bloomberg, Veritas estimates.

Google acquired Fitbit for a \$1.7bn enterprise value and EV/Revenue multiple of 1.6x in January 2021. It is important to note that the relatively low multiple for a tech company most likely reflects declining sales and profits since 2015.

The Fitbit acquisition highlights the strategic value that a tech platforms place on successful niche wearable manufacturers with a loyal ecosystem of users. We view Spacetalk as a possible acquisition target if it proves itself in the US market.

Spacetalk has the potential to become the dominant smartwatch for children and seniors. It has the leading customer proposition in the category and its original device had the number one market share of children’s connected smartwatches in Australia in CY2020. It launched an improved device – the Adventurer – in December 2020 which is gaining significant traction. We estimate that with just 1% share of the addressable market Spacetalk could be worth more than \$3 per share. We initiate coverage with a Buy recommendation and a fair value of \$0.60 per share, 300% share price upside.

RATING

BUY – anticipated stock return is greater than 10%

SELL – anticipated stock return is less than -10%

HOLD – anticipated stock return is between -10% and +10%

SPECULATIVE – high risk with stock price likely to fluctuate by 50% or more

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