COMPANY RESEARCH

MONITISE PLC

Banking on Success

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Monitise Plc is a client of IS Research Ltd

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Company description

Monitise plc is a leading provider of B2B mobile banking and payments services. The company has built up an impressive eco-system of 240 banks, payment providers, other financial institutions, retailers and mobile network operators, including Visa, Standard Chartered, VocaLink, FIS, HSBC, Lloyds TSB, first direct, Alliance & Leicester, Royal Bank of Scotland, NatWest, Carphone Warehouse, Vodafone, Orange, O2, T-Mobile and Hutchison 3G. The company was founded in 2004 as part of Morse, and spun out and listed on AiM in June 2007.

Table 1: Monitise Fund Raising Activity

Date	Investor/(s)	Price	Amount raised (£m)
Jun-07	Institutional placing	22p	21.4
Jul-08	Standard Chartered, PCCW + institutions	15p	11.8
Jul-09	Visa + institutions	7p	5.1
Jan-10	First Eastern, Visa, Standard Chartered + institutions	13p	7.4
1Q 2010	First Eastern, CPW + institutions (tbc)	13-15p	8.4
Total			54.1

Source: I S Research Ltd, Monitise Plc

Executive management

Alastair Lukies, Co-founder and Chief Executive Officer
Alastair is the driving force behind Monitise, having formed the company whilst it was part of Morse plc. Prior to Monitise, Alastair was a co-founder of epolitix.com, the portal for Westminster, Whitehall and the devolved institutions.

Duncan McIntyre, Chairman and Non-Executive Director
Duncan is a qualified account. He worked for Price Waterhouse for ten years, before joining Morse as Finance Director in 1994 and rising to become Chief Executive Officer and Executive Deputy Chairman.

Tom Spurgeon, Chief Financial Officer and Executive Director
Like Duncan McIntyre, Tom is a Price Waterhouse-trained accountant who joined Morse and became its UK Finance Director. Tom filled that role for five years, before joining Monitise.

Lee Cameron, General Counsel and Executive Director
Lee is a trained lawyer, who oversees Monitise's legal, IP, corporate development, compliance and human resources departments. He was previously General Counsel at Morse plc.

Mike Keyworth, Chief Information Officer
Mike has over 20 years experiencing of managing major projects for financial services companies. He joined Monitise early in 2004 as the Programme Director for MONILINK™, and took up the post of Chief Operating Officer in October 2005.

Darren Sugden, Chief Commercial Officer
Darren joined Monitise in early 2007, having spent 20 years with HSBC. He is responsible for the development of Monitise's business, working closely with banks and operators to deliver Monitise ecosystems in new territories across the globe.

In addition, Monitise has a heavyweight board, including several highly experienced individuals from the telecoms world (David Dey, Colin Tucker and John Brougham) and from finance (Peter Radcliffe and Jan Verplancke) as non-executive directors. The company also has an Advisory Board, comprising John Hardy (ex LINK CEO), Andrew Harrison (Carphone Warehouse CEO), Graeme Hutchinson (ex Virgin Mobile and Barclaycard), Christopher Rodrigues (ex VISA International president and CEO), and Austin Healey (Managing Partner DNA Capital and ex-England rugby player).

Banking on Success

Company basics

RIC	MONI
Share price £	16.5p
Market cap £m	77.8
Net cash £m	16.9
Enterprise value £m	60.9

Monitise's interim results capped a momentous nine months in which the company has moved a huge step forward in becoming a major global mobile money provider. The company has signed important agreements with Visa, First Eastern and Carphone Warehouse, extended its eco-system of financial partners, raised £12.5m of new funding (with £8.4m to come this quarter), and achieved strong customer growth and associated transactions revenues. The UK mobile banking business is within sight of break even, helping prove the concept in a developed market. With sufficient funding in place, we anticipate 2010 being as busy as 2009 for Monitise, with continued growth in UK and US mobile banking, the launch of mobile banking into new territories, particularly Hong Kong, China, Africa and India, and the launch of the new mobile retail payments product with Carphone Warehouse. Our forecasts suggest a 23p valuation, though we believe Monitise's strategic value could be much higher.

Table 2: Estimates and valuation

	Financials					Valuation			
Year end Oct	Rev £m	Adj PBT £m	Adj EPS p	DPS p	Net cash £m	EV/ sales x	EV/ NOPAT x	PER x	Yield
2009 A	2.7	-11.6	-2.3	0.00	10.1	25.4	na	na	0.0%
2010 E	6.4	-12.3	-1.8	0.00	19.7	9.1	na	na	0.0%
2011 E	13.9	-8.8	-1.2	0.00	10.7	4.8	na	na	0.0%
2012 E	25.3	-2.4	-0.3	0.00	7.7	2.8	na	na	0.0%
2013 E	39.6	5.4	0.7	0.00	12.3	1.7	17.2	22.7	0.0%
2014 E	51.6	11.7	1.6	0.00	23.5	1.1	6.6	10.6	0.0%

Source: I S Research Ltd, Monitise Plc, Morningstar

Market Opportunity & Strategy

The global market for mobile money, incorporating bank account management, bill presentation and payment, peer to peer transfers, and electronic payment for goods and services, is likely to be substantial, given 4.5 billion mobile phone users worldwide. The mobile handset is the ideal tool for electronic money, incorporating inherent user ID and security, and being more widely available than the PC, or indeed bank accounts. Monitise itself is proving the model in developed markets like the UK, whilst operations such as M-PESA are proving the developing markets model. Whilst the market is highly competitive, Monitise has established a strong position through offering leading edge solutions on a managed services basis, partnering with major organisations such as Visa, First Eastern and Carphone Warehouse, and promoting an open eco-system of banks, mobile operators, retailers and other financial institutions.

Business model & estimates

Monitise has a B2B strategy, selling its services directly to its eco-system partners (240 at the latest count), and charging per user or per transaction fees. This leverages the brands of the eco-system partners, promotes economies of scale and scope, and minimises Monitise's cost base. Average revenues range from £7 per year for Advanced users, with high functionality smartphone apps, to £3 for Essentials users, with SMS-based functionality, and to pennies for feeder users (account sign ups etc) who will migrate up the value chain. Revenues are now growing fast, with £6.4m forecast this year against £2.7m last year, and with breakeven not until late FY 2012 as the company invests to exploit the multitude of geographic and product opportunities available. We estimate a valuation of 23p per share.

Risk factors

Monitise is faced with considerable risks and uncertainty, including the competitive environment, the potential demand for mobile money services from banks, retailers and end-users, regulatory obstacles, as well as internal risks such as the company's ability to manage rapid growth, remain at the leading edge of mobile money technology, and be able to raise sufficient funds to reach profitability. In our view, though, the risks attached to Monitise, though relatively high, have reduced significantly in the last 12 months, as the company has demonstrated its commercial viability in the UK and raised significant new funding. It is still a relatively high risk, but also high reward, stock.

Market opportunity

4.5 billion and counting

Monitise's ambition is to become a leading provider of mobile banking and payments services (m-money), enabling mobile phones to be used for accessing and managing financial accounts of all types (bank accounts, credit cards etc), for sending money to other parties, and for paying for a wide range of physical and digital goods. As the CGAP (Consultatuve Group to Assist the Poor) notes, the mobile phone is an ideal banking and payments device, being ubiquitous, and containing inherent user ID and security features (the SIM) and native technologies (SMS and USSD) for providing very quick and cost effective data transmission.

There are several broad, inter-twined categories of mobile money:

Mobile banking:

- In developed markets, an alternative means, along side telephone or online banking and bank branches, for account holders to access and manage their accounts (whether current account, credit card, storecard etc), to obtain balances and mini-statements, pay bills, transfer money and so on.
- In developing markets, where banking infrastructure is poor, mobile banking typically involves enabling users with a mobile wallet or bank account to store money and undertake banking transactions, with access provided online via the mobile phone and physically via the mobile operator's distribution channels.

Mobile payments:

- Using the mobile phone as an access device to pay for goods and services using existing on-line digital payments methods (eg PayPal) or bank and credit card accounts
- Paying for content delivered to mobile phones (eg music, ringtones), again using PayPal and equivalents, or specific mobile payments methods (eg PayForIt in the UK).
- Remitting money overseas to friends and family, or making peer to peer (P2P) payments to friends.

Mobile wallet

- The phone uses short distance communications such as Near Field Communications (NFC) or Bluetooth to interact with payment or reader devices, for paying for goods and services in physical (as opposed to online) locations or for peer to peer transfers. Mobile wallets can also contain e-tickets (eg an Oyster travel card).

In all cases, the underlying money account can either be an integral part of the service, or can be a linked existing account such as current account or credit card.

Monitise provides the 'glue' that makes mobile banking and payments possible:

- Providing the underlying technical infrastructure that ensures interconnectivity between banks, retailers, mobile operators and other parties (eg loyalty card providers), typically using a payments network, such as LINK in the UK.
- Developing services, to maximise functionality and user experience, whilst providing banking and other customers with the flexibility to customise and differentiate their own service offerings. These services range from very simple SMS-based alerts through to feature rich smartphone applications

Market Opportunity

- Ensuring that services can be supported on the large majority of handsets, and work on different types of wireless network.

There have been many false dawns about the potential for the mobile phone to become much more than just a device for speaking to another person. Indeed, mobile operators have previously introduced mobile banking service based on WAP, which failed to gain traction due to the well know shortcoming of WAP services (slow, poor user interfaces, expensive data charges etc). In our view, the mobile phone is now proving its potential to become an important tool for banking and payments worldwide, and all of the necessary conditions are at last falling into place (around ten years since the European 3G auctions). The potential prize is vast, given that the mobile phone is the most ubiquitous communications device globally (4.5+ billion subscribers worldwide), far out-stripping fixed lines and PCs. In many developed countries, there are more mobile phones than bank accounts.

The outlook for non-voice mobile services has strengthened significantly over the last 2 years, to Monitise's benefit, with mobile users becoming increasingly comfortable with mobile data services. The main drivers have been the rollout of faster mobile data networks, much lower data pricing by mobile operators, and the revolution in handset design that was stimulated by the Apple iPhone. 2.75G mobile data EDGE networks are now available in 190 countries whilst 3G HSPA networks have been rolled out in 130 countries to date. At the top end, the rapid growth in smartphones and applications ('apps') has made is so much easier for mobile subscribers to access relatively advanced mobile data services. At the bottom end, even the most basic of handsets incorporate SMS, thus supporting basic but still very valuable services such as as balance alerts.

Mobile banking and payments is not just about mobile, however, as there are strong demand drivers from banks, retailers, mobile phone operators:

- Banks in the developed world see mobile banking as a natural extension of telephone and online banking, offering better customer service at a lower cost.
- In developing countries, banks and governments see mobile banking as key to increasing banking penetration, with consequent positive implications for economic growth and wellbeing.
- Mobile network operators view m-banking as a means of generating additional data and transactions revenues and increasing customer loyalty/reducing churn.
- Banks and retailers (both on-line and high street) are generally supportive of new payments methods that increase the probability of a successful transaction taking place, particularly for digital goods, and/or which replace expensive to process cash and cheque payments.

Market forecasts and data

There is a wealth of studies predicting strong take up of mobile banking services, based on a mix of user surveys and bottom up forecasting. Berg Insight (March 2009) forecast growth from 20m users in 2008 to 913m in 2014, or approximately one in six of all mobile phone users globally by that date. Juniper (January 2009) forecast 150m users by 2011 for what they called 'additive banking' (basically providing extra functionality for existing users rather than bringing mobile banking to the un-banked). For the US alone, Javelin forecast 45% take up (99m users) by 2014, with Mastercard (May 2009) predicting 53m users in 2013. These are obviously broad numbers, and there is no differentiation between heavy and occasional users, but they still point to strong take-up of mobile banking.

Market Opportunity

Developed markets

Monitise itself provides an excellent example of take up of mobile banking services in developed markets. Since launching services in 2008, the company witnessed a significant acceleration in take up in 2009. The company reached 0.75m users in August 2009, 1m in October, 1.3m in December (compared with its year end target of 1m), and 1.75m in February 2010. The company says that it is adding 150,000 new customers per month, though we estimate this rate has increased to 220,000 since December 2009.

What do these figures tell us about take up rates? According to the British Bankers' Association, there are 125m bank accounts in the UK (current and savings accounts), 42m people registered for telephone banking and 24m for online banking. Given that Monitise's services are available for banks covering just over half UK bank accounts, and assuming the UK is 75% of the total, it has attracted 1.3m users, or over 10% of the 12m addressable online banking users and over 5% of telephone banking users, which is a fairly impressive take up rate for a new service within 12-18 months of launch. Whilst many new mobile services achieve a high level of registrations, this is not always matched by ongoing usage. In Monitise's case, however, UK subscribers are using the mobile application service an average of 9 times each month, which suggests that mobile banking is becoming an integral part of users' banking interaction.

Developing markets

The provision of mobile banking services in developing markets, particularly to the so-called 'unbanked', is a rich seam. The CGAP and GSMA estimate that there are 1 billion mobile phone subscribers without a bank account currently, rising to 1.7bn by 2012. They forecast 364m low-income, non-banked users of mobile banking services by 2012, generating $7.8bn of banking revenues (approximately $20 pa per user).

M-PESA is the best known and probably most successful mobile banking service focussed on developing countries, in this case Kenya. Operated by Vodafone subsidiary Safaricom, partnering with the Commercial Bank of Africa, it enables users to deposit cash on their account, send money, withdraw cash, pay bills, buy airtime, and manage their account from their mobile phone, interacting with Safaricom's 13,300 agents where necessary. As of September 2009, M-PESA had 8m account holders (out of its 14.5m mobile subscribers) and had reached $3.77bn in cumulative peer to peer payments since inception. The account holder base has doubled in the last year, and now represents 20% of the Kenyan population! In September 2009, the 8m account holders carried out 48m transactions and transferred $302m. Users pay fees of up to 2% for conducting transactions (many are free). Thus, for Safaricom, M-PESA generates additional revenues, and boosts customer loyalty, and Vodafone is now replicating the model in other developing markets, for example Tanazania and Afghanistan.

There are plenty of other examples of successful mobile money services in developing markets. For example, True Money in Thailand is a mobile wallet, with a focus on payments rather than peer to peer transfers, as with M-PESA. According to the GSMA, True has 6m users, processing $900m in payments and 120m transactions a year.

Monitise is partnering with Paynet to provide similar services in Africa, which are described below in the Strategy section.

Competitive Environment

Not surprisingly given its potential, mobile money is being competed for by a large number of players from a variety of backgrounds, which are summarised in the following table. We would classify the broad classes of competitor as follows:

- Banks and other financial institutions themselves, with many choosing to develop their own mobile money applications in-house.
- The specialist banking systems and mobile money software providers such as IBM, Fiserv, mFoundry, m com, and Intelligent Environments.
- Technology-focussed competitors, particularly those in the Near Field Communications area.
- Companies with a background in mobile roaming and billing systems, branching into mobile money, eg Roamware, Earthport and eServGlobal.
- Country-focussed providers, particularly in emerging markets, e.g. M-PESA, True.
- Specialist mobile service providers, such as Monitise, Nokia/Obopay and Firethorn.

Many of these are or will be strong competitors to Monitise, but we would in particular highlight two of the highest profile competitors, Nokia and Qualcomm/Firethorn, which have attracted significant strategic investment.

Nokia Money launched in August 2009, in conjunction with Obopay, a US company in which Nokia invested a reported $70m in March 2009. Nokia Money is a mobile wallet aimed at the unbanked in emerging markets, enabling users to top up their accounts, check balances and make payments. Nokia recently announced the first launch; a trial in Pune, India with Yes Bank. The service is likely to be available only on Nokia handsets initially, and it remains to be seen whether the strength of the Nokia brand will translate into financial services.

Firethorn was founded in 2001 as a mobile banking service provider and was acquired by Qualcomm for a hefty $210m in November 2007. The company provides mobile banking services primarily in the US, mainly serving 2^{nd} tier banks. Qualcomm does not separate out Firethorn's financials, so it is hard to judge the company's performance.

Whilst the competitive landscape is crowded, we would argue that Monitise is the clear market leader in the UK and a strong player in the US, and will be a significant early mover in markets such as India and China. The fact that it has also been selected by major financial players such as Visa and Travelex is testimony to its strong competitive position.

Table 3: Mobile Money Competitive Environment

Background	Players
Mobile wallet	M-PESA, Monitise, Oxigen (India), Nokia Money (Obopay), Blaze Wallet (US)
Banking systems	IBM, Sybase, Fiserv
Remittances	SMART (Philippines), Earthport, eServGlobal
Digital payments	Obopay
Disintermediators	Blaze Wallet (US), Mint.com (US), Firethorn
NFC	Gemalto, Oberthur, Proxima
Software suppliers	mFoundry, Firethorn, m com, Intelligent Environments
Mobile roaming	Roamware, eServGlobal

Source: I S Research Ltd, Monitise Plc

Strategy

Monitise's ambition is to be a major global provider of mobile money services. This ambition looks to be very challenging for the biggest of companies, let alone a UK-based, young business with no well known brand. In practice, the company has a well thought through strategy that plays to its relative strengths and weaknesses, the main elements of which are:

- focus initially on B2B rather than B2C services
- providing an end to end managed service solution
- leveraging existing payments platforms for interconnectivity
- creating an eco-system of financial partners, retailers and mobile operators in each market
- partnering with strong local financial players in each new territory, in a JV structure.

The overall Monitise proposition to potential banking clients is simple: they can buy ready-made, but customisable, mobile money products on a software as a service basis, rather than having to incur the major expense of developing and maintaining their own technology, and will benefit from the ongoing costs of R&D etc being spread across other partners.

Key Strategic Features

B2B

Monitise sells its services primarily on a B2B basis, i.e. selling services that are branded by the client financial institutions and retailers, rather than attempting to establish itself as a B2C brand. This approach is sensible given the huge costs in establishing consumer brands, the importance of trust and branding in financial services, and the fact that Monitise is better off selling white label services to banks rather than trying to compete with their own mobile banking services. The company does have some retail exposure, for example its UK Monilink service is distributed by Carphone Warehouse, T Mobile UK and 3 UK, offering access to Lloyds, HSBC, NatWest, Alliance and Leicester, First Direct and Ulster Bank, but this is effectively just another distribution channel alongside the customer banks' own channels.

Fully managed services

Monitise provides a fully managed, end to end service, that is designed both to lower the cost of service take up by customer financial institutions and retailers, as well as maximise security. Monitise owns the underlying technology for this provision of payments and banking on mobile phones, which was granted UK patent protection in February 2009, and continues to extend the range of functionality and services on offer. Ongoing R&D is also required to ensure that the service will work on most if not all types of handset, no mean feat given that Monitise currently supports 2,700 handset variants. In addition, Monitise needs to keep up to date with developments in mobile operating systems; for example, it announced a Google Android version of the Monitise application in February 2010.

It should also be noted that the Monitise solution has been designed specifically for the mobile phone environment, whereas some of the competitive offerings can be described as 'screen-scraping' – basically taking an online-banking interface and re-purposing for a mobile phone. The latter approach can potentially suffer from issues of security and ease of use.

Strategy

Partnerships

Monitise's approach in each new geographic or product market is to partner with a strong local partner in a JV structure, typically an existing bank (e.g. First Eastern in Asia), payments infrastructure provider (e.g. Vocalink in the UK, and Metavante in the US), or a strong player in the product area (e.g Carphone Warehouse in the new retail mobile money venture). The JV licenses the mobile money technology from Monitise Group, and is responsible for all local sales and marketing, admin and commercial agreements. In the most recent JVs (Asia Pacific and Retail), the partners (First Eastern and Carphone Warehouse) are also injecting equity into Monitise Group to help fund Monitise's share of the JVs.

Table 4: Key Monitise Partnerships/Customers

Partner	Date	Role/details
Visa International	June 09	Monitise is the strategic development partner for Visa's comprehensive suite of mobile services, including payments, mobile money transfer, mobile transaction alerts and mobile marketing. Worth at least $13m to Monitise over 5 years. Visa has invested £4.8m in Monitise
First Eastern (Holdings) Ltd	Dec 09	JV partner for Asia Pacific, particularly Hong Kong and China. Has also subscribed for £5m Monitise shares at 13p plus £2.5m shares at 13p, conditional on completion of the JV, plus warrants for £2.5m at 15p.
Metavante	2007	US mobile money partner, recently taken over by FNIS.
Carphone Warehouse	Dec 09	JV partner for new mobile money initiative for retail. CPW has also subscribed for £2.5m of shares at 15p, conditional on completion of the JV. CPW is also a UK distribution partner for UK Monilink mobile banking.
Travelex	Nov 09	Monitise is developing mobile applications for Travelex's Global Passport foreign exchange card.
Paynet	July 09	Partner for launching mobile money services in East Africa.
ICICI Bank	Mar 09	Partner for mobile money services in India

Source: I S Research Ltd, Monitise Plc

The close relationship between Monitise and its key partners is demonstrated by the company's shareholder profile (post the 1Q2010 funding), with First Eastern, Visa, Standard Chartered and CPW together accounting for 37.1% of Monitise shares.

Table 5: Monitise Key Shareholders (post the planned 1Q2010 equity injections)

Shareholder	Stake
First Eastern	14.0%
Visa	12.8%
UBS	10.4%
Standard Chartered Bank	7.2%
3i Group	4.7%
Duncan McIntyre	3.9%
HKT Media International	3.8%
Carphone Warehouse	3.1%
Rest	40.2%

Source: I S Research Ltd, Monitise Plc

Strategy

Eco-system

Monitise's aim, both in local markets and globally, is to attract as many partners as possible – financial institutions, retailers and mobile operators – in order to generate virtuous network effects and economies of scale, and it now has over 240 partners in the UK and US. Whilst individual banks will be happy to provide their own branded services just to their banking client base, mobile phone operators and retailers will be more likely to want to distribute mobile banking applications if several banks are supported. In addition, the new retail mobile money JV with Carphone Warehouse will, like conventional loyalty cards, have more attraction to consumers, the more retailers are members of the scheme.

Current Status of Geography/Products

Monitise is already well established in the US and particularly the UK. The next 12 months promises to be very eventful for the company, as several new JVs are launched.

The UK

The UK is Monitise's most developed market, and the showcase for the potential of mobile money in a developed market. The UK JV is entitled Monilink, and was set up initially as a JV between Monitise and Vocalink, which operates the UK's ATM network and is a major provider of payments infrastructure. Monitise bought out Vocalink from the JV in August 2009, though Vocalink will continue to receive transaction fees from Monilink.

Monilink's UK customer base comprises Lloyds Bank, HSBC, RBS, Alliance and Leicester, First Direct and Ulster Bank, together accounting for 55% of UK current account customers. In addition to the banks providing their own branded mobile money products, Monilink is distributed as a mobile money product via Carphone Warehouse and the mobile operators, T Mobile UK and 3 UK.

As noted above, we estimate that Monitise has as many as 1.3m mobile banking users in the UK. In our view, Monitise has established a market leading position in the UK, with no clear competitor in sight. Of the other major banking groups not served by Monilink, Barclays has its own internally developed mobile banking service, whilst Santander has yet to launch mobile banking (though one of its subsidiaries - Alliance & Leicester – is a Monilink customer).

The UK is particularly interesting, as it demonstrates the commerciality of mobile money in a developed market. According to Monitise's interim results, the UK subsidiary Monilink contributed revenues of £0.683m and an after tax loss of £1.283m in the period 21st August (ie when Monitise bought out its JV partner) to 31st December 2009. Assuming a 60% gross margin, this suggests an annualised cost base of approximately £5m during this period. We understand, however, that the cost base has been reduced to more like £4m a year. This cost base will be more than covered with 2m UK subscribers, split equally between Advanced users generating £7+ ARPU per year and Essential user generating £3, at a 60% gross margin. Indeed, Monitise has said that it expects the UK operation to reach cashflow breakeven during calendar year 2010.

The US

The US has clearly developed more slowly than the UK for Monitise, though the company notes that it has seen a recent acceleration in take up, aided by the rollout of services to H&R Block, with imminent new services from Visa (see below) likely to further fuel growth.

Strategy

Monitise's partner in the US is Metavante, a provider of banking and payment technologies, which merged with Fidelity National Information Services, a banking transactions processing provider, in October 2009 (the new company is called FIS). FNIS also has its own mobile banking solution, and indeed was ranked 1st by ABI Research in terms of US mobile banking vendor rankings in June 2009, compared with Monitise's 4th position. Monitise's positive statements about the US suggest that the FIS takeover of Metavante has not harmed prospects, and indeed may strengthen them through access to more financial partners.

Hong Kong and China

Monitise is progressing well on a Hong Kong rollout, working in partnership with First Eastern. The formal JV with First Eastern is on track for completion this quarter, with services being rolled out later this year. Hong Kong will serve as a springboard for the much bigger prize of China, with 724 million mobile subscribers at the end of 2009.

India

Following Reserve Bank of India approval, Monitise is in final negotiations with one of its partners ahead of launching in India, with shareholder Standard Chartered expected to be one of the first banking customers. The Indian rollout has taken longer than expected, notably for bureaucratic reasons, but also holds enormous potential, with 394 million subscribers as at January 2010, and an average monthly growth rate of 10 million subscribers over the last year.

East Africa

Monitise has partnered with Paynet, an electronics payments provider with operations in Kenya (supporting M-PESA), Tanzania and Uganda. The JV has been awarded $1.5m in funding from the Africa Enterprise Challenge Fund (AECF).

Visa

Monitise and Visa signed an agreement in June 2009 for Monitise to be its strategic mobile money partner, worth at least $13m to Monitise over five years. Visa has also invested approximately £4.8m in Monitise in two tranches (July 2009 and January 2010), and is currently Monitise's largest shareholder with 14.4%, though will drop below First Eastern if the latter completes its planned investments in Monitise. We understand that details will shortly be announced of the first Visa mobile products. Visa is a potentially very important client for Monitise, with 1.8 billion credit card account holders worldwide, and 42 billion transactions annually.

Retail mobile money

Monitise's latest new product initiative is a JV with Carphone Warehouse to provide mobile money aimed at retailers, initially in the UK, and then Europe and the US. Details will emerge towards the end of the quarter, when the JV is finalised, but the broad aim is to enable consumers to sign up to mobile banking services, buy goods and services from network members, send money to friends/family (including in other countries), and to top up prepaid and loyalty cards and mobile phones, all from a mobile application on their handset. The potential revenue impact will depend on many factors, including the number of member retailers, the range of services offered etc, but with an estimated 16.8m people in the UK using the Nectar card alone (Sainsbury, February 2010), loyalty cards have the potential to attract significant numbers of users. Carphone Warehouse should be a strong partner for Monitise, given its strong retail presence and well known brand.

Business model

Monitise's business model is based on generating transaction fees from its financial and retail partners, plus ongoing licence fees and project work, which though relatively large today will become a much smaller contributor to revenues going forward. For financial services, transaction fees will be paid by the banks themselves to Monitise, with the banks deciding whether or not to charge their customers for mobile banking services, or absorb the cost. We suspect a mixture; there will be customers who are prepared to pay for the utility of mobile banking, but the banks will also have an incentive to provide mobile banking services for free (as they do with online banking) given that it improves customer service and represents a much lower cost of dealing with customers, compared with branch and telephone banking.

Monitise segments the market into three main groups:

- Advanced users – the high end user, downloading a mobile banking application to their smartphone, offering the widest range of mobile banking services (account management, payments, access to m-commerce) and generating a typical ARPU of £7 per year (c60p per month)
- Essentials users –SMS-based services for the low-end/feature phone user, delivering more basic functionality such as user-initiated balance enquiries, alerts (weekly balance, large transactions, impending overdraft etc), and generating typical ARPU of £2 per year (15-20p per month).
- Feeder users – basic services, for example including banking sign up and credit card activation, used to attract customers to mobile banking.

Some customers will be attracted straight away as Advanced users, for example iPhone users downloading the relevant app, whilst others will gradually migrate up from Feeder to Essentials, and possibly on to Advanced, with the upwards migration driven by a mixture of increasing comfort at using mobile banking and users upgrading their handsets to smartphones, which support the more function-rich Advanced applications. According to the interim results statement, Advanced users now account for 25% of all registered users in the UK, implying an average revenue of £3 per year (this is also consistent with Monitise's estimated £5m annual run rate based on the 1.75m registered users).

Average revenues going forward will depend on a variety of factors, including the growth in ARPU per type of user driven by new revenue sources such as the Retail mobile money application, and the mix between Advanced and Essentials. In a market such as the UK, it is hard to see ARPU falling below its current levels, given that overall fees per type of user are likely to trend upwards, whilst the proportion of Advanced users is also likely to increase, driven by the rapid proliferation of smartphones and increasing user familiarity with mobile apps. If anything, the retail mobile money application has the potential to generate more revenue for Monitise than the pure mobile banking application, given that the retail JV will earn commission on all retail spending, money transfers and pre-paid card top ups.

From the perspective of Monitise Group, overall ARPU will also be affected by the mix of countries, as ARPU in developing markets such as India and China is clearly not going to be at a similar level to UK levels. However, lower APRUs will be balanced by much greater subscriber numbers in such heavily populated markets. Our financial forecasts (presented below) assume that ARPUs for the group decline over time, reflecting the impact of the larger, less developed countries in the mix.

Aside from transaction fees, Monitise will also generate licence fee revenues and deployment/integration fees from each of its JVs.

Interim Results Analysis

Monitise's interim results to 30th December 2009 provide a good sign post of the company's current progress, and highlighted just how rapidly revenues are now growing, driven by customer take up of Monitise's services. Whilst the overall revenue figures for the half were only up slightly on the previous half, there was a marked jump in transaction revenues, reflecting the increased customer base. These increased from £0.2m in 1H2009 to £0.3m in 2H2009 and £0.8m in the most recent half. Total revenues for the half were only up marginally because the increase in transaction revenues was almost offset by a more than halving in licence fees from £0.9m to £0.5m. Going forward, the revenue trend should become much clearer, with recurring transaction revenues growing much faster than licence fees. The results also show a slight increase in EBITDA loss and cash outflow, primarily reflecting the increased operating costs as a result of acquiring the other 50% of the UK joint venture in August 2009.

Net cash at the period end stood at £9.5m, but this was subsequently boosted by £7.4m raised in January 2010 from First Eastern, Visa and UBS, and will be further supplemented by the £8.4m expected by the end of this quarter from First Eastern and Carphone Warehouse.

Table 6: Monitise Half Yearly Results (£m)

Year end June	**1H09 A**	**2H09 A**	**1H10 A**
Deployment and integration	0.7	0.4	0.4
Licence fees	0.2	0.9	0.5
Transaction fees	0.2	0.3	0.8
Total Revenue	1.1	1.6	1.7
Revenue growth	181%	41%	57%
Gross margin	0.5	1.0	0.9
Gross margin %	42%	66%	54%
EBITDA	(5.8)	(5.5)	(6.5)
FCF	(5.9)	(5.4)	(6.0)

Source: I S Research Ltd, Monitise Plc

Financial Forecasts

It is difficult to forecast the financial outlook for a company such as Monitise, operating in a nascent but fast growing market segment, with a global addressable market. We have tried, in order to give an indication of the potential scale of the business, but we suspect that if mobile money takes off as some predict, our forecasts could turn out to be woefully short. The company is clearly on a rapid growth trajectory, with a revenue run rate at the interims of £5m per annum, compared with an annualised £3.4m based on the interims, and growth is likely to accelerate given factors such as the impending launch of new JVs, Visa products coming on stream and the availability of the iPhone on Vodafone and Orange helping drive growth in the UK. The forecasts are shown below, and are based on the following major assumptions

- Customer numbers are driven by an assumed 150,000 new users per month per JV in operation – this is the current rate of growth in the UK, though the rate of growth from JVs such as China and India is likely to be much higher.
- We assume a decline in ARPU per customer from £3 a year currently to £1.75, with growth in lower spending markets such as China and India offsetting rising ARPUs in individual markets from new services.
- Licence and deployment fees are assumed at £1m and £0.5m per JV in operation per year.
- The long term gross margin is 60%.
- Monitise corporate overheads grow slightly from the current annualised level of approximately £16m towards £20m, reflecting the costs of supporting new JVs.

We forecast Monitise achieving 2.8m customers by June 2010, thereafter climbing rapidly to reach 56m by June 2014. To put this forecast into context, 56m customers would represent 6.1% of the 914m mobile banking users forecast by Berg at that date, or just over 1% of the world's mobile phone users. If mobile money grows in line with Berg's forecast, a market share of 6.1% for Monitise is certainly achievable given its current strong position and particularly its imminent launch in India and strategic entrée to China through the First Eastern Group.

Table 7: Monitise Revenue Assumptions

Year ended June	FY-10 E	FY-11 E	FY-12 E	FY-13 E	FY-14 E
Active country/product JVs	2	5	7	9	11
Monthly customer adds per JV (m)	0.12	0.13	0.15	0.15	0.15
Customers (end period) - m	2.8	9.6	21.3	36.6	55.5
Customers (average) - m	1.7	6.2	15.4	28.9	46.0
ARPU (£ per year)	2.20	1.78	1.77	1.74	1.74
Usage revenue (£m)	3.4	11.0	27.3	50.2	80.1
Monitise share	77%	70%	65%	60%	50%
Monitise transaction revenue (£m)	2.6	7.7	17.8	30.1	40.1
Licence fee per JV (£m per year)		1.0	1.0	1.0	1.0
Deployment fees per JV (£m per year)		0.5	0.5	0.5	0.5

Source: I S Research Ltd

The resulting revenue forecasts by type are shown below. Usage revenue rise from less than a fifth of revenues in FY2009 to over half of revenues in FY 2011, driven by the rollout in JVs, whilst licence fees continue to rise, but form a declining proportion of revenues. We forecast total revenues to grow from £2.7m in FY09 to £6.4m in the current financial year, and then more than doubling in FY2011 as several new JV start to build momentum, including Hong Kong and possibly China, India, Africa and the retail venture.

Financial forecasts

Table 8: Monitise Revenues (£m)

Year end June	FY-08 A	FY- 09 A	FY-10 E	FY-11 E	FY-12 E	FY-13 E	FY-14 E
Revenue by type							
Deployment and integration	1.0	1.1	1.8	1.8	1.0	1.0	1.0
Growth	0%	10%	64%	-3%	-43%	0%	0%
Licence fees	0.4	1.1	2.0	4.5	6.5	8.5	10.5
Growth	0%	175%	82%	125%	44%	31%	24%
Usage fees	0.1	0.5	2.6	7.7	17.8	30.1	40.1
Growth	0%	400%	414%	200%	131%	70%	33%
Revenue	1.5	2.7	6.4	13.9	25.3	39.6	51.6
Growth	216%	78%	140%	119%	81%	57%	30%

Source: Monitise Plc, I S Research Ltd

Our summary financial forecasts are shown below. We forecast breakeven at EBITDA, net profit and cashflow levels towards the end of FY2012, with the company generating a 24% EBITDA margin by 2014. The £8.4m equity fund raising due in the current quarter should be sufficient for the company to reach cashflow breakeven, though the record shows that there is no shortage of partners willing to invest in Monitise should additional opportunities present themselves.

Table 9: Monitise Summary Financials (£m)

Year ended June	FY-08	FY-09	FY-10	FY-11	FY-12	FY-13	FY-14
	Act	Act	Est	Est	Est	Est	Est
Profit & Loss							
Revenue £m	1.5	2.7	6.4	13.9	25.3	39.6	51.6
Adj EBITDA £m	-12.4	-11.4	-12.0	-8.5	-2.1	5.7	12.0
Adj EBIT £m	-12.8	-11.6	-12.3	-8.8	-2.4	5.4	11.7
Reported PBT	-14.0	-13.1	-13.3	-11.0	-4.7	2.9	9.0
PBT pre exceptionals and AAG	-14.0	-12.8	-13.7	-10.4	-4.1	3.5	9.6
Fully adj PBT	-11.9	-11.0	-12.2	-8.7	-2.3	5.5	11.8
NOPAT	-9.0	-8.1	-8.6	-6.2	-1.7	3.8	8.2
Reported EPS	-5.5	-4.0	-2.8	-2.1	-0.9	0.5	1.7
EPS pre exceptionals and AAG	-3.8	-2.7	-2.0	-1.4	-0.5	0.5	1.3
Fully adj EPS	-3.3	-2.3	-1.8	-1.2	-0.3	0.7	1.6
Dividend per share p	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash flow & Balance sheet							
Operating cash flow	-11.0	-11.4	-11.6	-8.8	-2.9	4.8	11.3
Free Cash flow £m	-10.6	-11.3	-12.0	-9.6	-3.7	4.0	10.5
FCF per share p	-4.2	-3.4	-2.6	-1.8	-0.7	0.7	2.0
Capex	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2
Acquisitions	-0.3	0.0	0.1	0.0	0.0	0.0	0.0
Net cash flow	-10.7	-11.1	-11.3	-8.9	-3.0	4.6	11.2
Shares issued	0.0	11.6	20.8	0.0	0.0	0.0	0.0
Net cash	9.7	10.1	19.7	10.7	7.7	12.3	23.5
Metrics							
Revenue growth	216%	78%	140%	119%	81%	57%	30%
Adj EBITDA growth	129%	-8%	5%	-29%	-75%	-373%	111%
Adj EBIT growth	128%	-9%	6%	-28%	-73%	-329%	116%
Adj PBT growth	112%	-7%	11%	-28%	-74%	-161%	211%
Adj EPS growth	31%	-28%	-22%	-37%	-74%	-185%	175%
Dividend growth	na	na	na	na	na	na	na
Adj EBIT margins	-857%	-437%	-192%	-63%	-9%	14%	23%
Operating cash conversion	89%	100%	97%	103%	138%	83%	94%
Capex/Depreciation	63%	164%	81%	81%	81%	81%	81%

Source: Monitise Plc, I S Research Ltd

Valuation Discussion

Monitise cannot readily be valued on the basis of conventional current year multiples, given that it is generating small (but fast growing) revenues, and is unprofitable. However, as the following table shows, by FY2013/14 the company is trading on multiples that are in line with current multiples of well established peers. For example, according to Megabuyte.com, finance and banking software companies currently trade on 1.5x revenues, 8x EBITDA and 15.9x PE, whilst the Megabuyte universe of 150 or so technology companies trades on 1.4x revenues, 7.6x EBITDA and 14.6x PE. The FY 2014 multiples are, not surprisingly, much lower than FY 2013 multiples for Monitise, reflecting achievement of reasonable levels of profitability.

Table 10: Monitise Valuation metrics

Valuation	FY-10	FY-11	FY-12	FY-13	FY-14
EV/sales	9.1	4.8	2.8	1.7	1.1
EV/EBITDA	-4.9	-7.9	-33.5	11.5	4.5
EV/NOPAT	-6.8	-10.9	-42.2	17.2	6.6
PER	-9.0	-14.3	-54.4	22.7	10.6
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%
FCF yield	-6.4%	-9.1%	-23.8%	22.1%	8.3%

Source: I S Research Ltd, Monitise Plc

We are generally not believers in long term DCF approaches to valuation, given the difficulty in forecasting even 2 years ahead for a company like Monitise, let alone 10 years ahead! However, a reasonable compromise in our view is to apply exit multiples to 2014 forecasts, when the company should be reasonably established, and estimate current year, discounted values. Assuming a discount rate of 15%, the current share price of 16.5p equates to an exit multiple of 10.5x 2014 EBITDA. If Monitise is growing in line with our forecasts, we would expect an exit multiple of more like 15x EBITDA, equivalent to 22.5p per share. This would imply an exit value of £185m in 2014, which is plausible if the market and Monitise develop as we expect.

An alternative approach is to consider Monitise's strategic value, which we believe could be significant. Indeed, the company's strategic value has been amply illustrated by companies such as Visa, Standard Chartered, Carphone Warehouse and First Eastern being willing to invest in Monitise, at premiums to the prevailing share price. The mobile world is littered with significant strategic activity, often involving eye-popping valuations. Some of these are summarised below, and include the two major mobile money deals: Nokia investing $70m in Obopay and Qualcomm buying Firethorn for $210m. The most recent strategic mobile deals included Google paying $750m or 7.5x annual revenues for AdMob, whilst the Qualcomm/Firethorn deal involved $210m being paid for a largely pre-revenue company. In this context, the £185m exit valuation estimated above for 2014 for a strong player in a rapidly growing market does not seem out of place.

This of course raises the question of who would want to buy Monitise? It is unlikely that an existing banking customer would want to, for fear of alienating Monitise's other financial partners. One exception might be Visa, which presumably could more easily co-exist with Monitise's banking customers.

Outside of banking, Nokia has invested heavily to expand beyond its handset and networks manufacturing activities, but of course has already invested in Obopay. This would not preclude buying Monitise if Monitise developed a much stronger market position than Obopay. The other contenders include Google, Apple and Microsoft, who all regard mobile as major growth areas (and a priority area in the case of Google), as well as the major banking technology or software suppliers.

Valuation discussion

Table 11: Example Mobile Strategic Investments

Date	Buyer	Target/sector	Details
Jan 2010	Apple	Quattro, mobile advertising	$275m
Nov 2009	Google	AdMob, mobile advertising	$750m, or 7.5x current revenues
Mar 2009	Nokia	Obopay, mobile banking	Reported $70m for a stake
Nov 2007	Qualcomm	Firethorn, mobile banking	$210m
Nov 2007	Microsoft	Musiwave, music	$46m
Sept 2007	Nokia	Navteq, navigation	Q$8.1bn
July 2007	Nokia	Twango, social networking	$97m
Dec 2005	EA Games	Jamdat, mobile games	$680m

Source: I S Research Ltd

Overall, we believe that a share price of 23p is not out of line with our financial forecasts, but can also see significant value appreciation as the potential of the new JVs becomes more apparent and new JVs are signed. Forthcoming announcements concerning the launch of Visa mobile banking products, as well as the formation of the First Eastern and Carphone Warehouse JVs, will provide further clarity on Monitise's potential, and help underpin our valuation.

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About I S Research

I S Research was founded by Ian Spence in 2007. Ian has been involved in researching and advising companies in the UK technology sector for over 15 years and was voted TechMARK analyst of the year in 2004 and again in 2008 making him the only analyst to win twice and the only independent analyst to be recognised in this way.

The business was founded on Megabuyte. Originally a free blog, our market intelligence service is now available to subscribers only and is now read daily by many of the sector's leading CEOs, investors and advisers.

From this firm foundation we went on to launch our Equity Research service. Our blend of high quality, genuinely independent research combined with intelligent distribution has led to rapid growth for this element of the business.

Our tight customer relationships have also enabled us to provide a range of complementary consulting services including investor relations, transaction support services and peer group analysis.

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