

30 March 2023

X2M Connect Ltd

China contract adds to H2 progress

X2M Connect Ltd (ASX:X2M) has developed and is commercialising a patented proprietary Internet of Things (IoT) solution predominantly focused on the utilities sector across the Asia Pacific region, converting legacy meters into smart meters. The company has announced it has secured \$1.8m in hardware water quality sensor sales in China with three new contracts. The contracts bring the contribution from China to \$3.4m this financial year to date which exceeds the revenue generated from China in FY22. China is a core medium-term driver for X2M but has been impacted in recent halves by lockdowns. These contracts suggest the China growth story is back on track, supplementing the recent success in South Korea. While this announcement is in our numbers, it provides comfort for both near-term and longer-term estimates as units in the field support future recurring subscription fees.

Business model

The X2M business model starts with the sale of a hardware device which enables legacy utility meters or sensors to communicate with an Internet-of-Things (IoT) platform. This sale historically has been at a gross margin between 10% and 25%. A monthly SaaS style platform fee is then charged for each device in the field for the ongoing reading and monitoring of data from the meter, and associated maintenance. The average yearly platform fee across all regions is currently ~A\$3.40 with a gross margin between 60% and 90%. Additional functionality is being developed and deployed to increase this yearly fee over time. The benefits for utility companies include the detection of leaks, a reduction in manual reading, and increased customer insights, while for end customers improved public safety and overall customer service are key benefits. In some regions a licensing-only model is employed where the customer provides all hardware and marketing and X2M the platform services.

China contracts in our numbers, good H2 progress being made

China unit sales have been impacted by lockdowns in recent halves, with most of the new contract wins for X2M in recent times coming from South Korea. The recent \$1.8m China contracts announcement, while in our numbers, is encouraging and places X2M on track for a record China revenue contribution in H2 FY23. More importantly, it increases the number of units in the field that can earn recurring subscription fees into the future. Assuming \$60/unit we estimate ~150k units will be on the ground in China by June 2023. Improving gross margins on China hardware sales promise a positive gross profit contribution.

Valuation of \$0.27/share or \$50m market cap fully diluted

We use a DCF methodology to value X2M given the early stage of market penetration and current loss-making position. Our valuation remains \$0.27/share with the biggest assumptions around device numbers in the field (including China), successful negotiation of related platform fees and success for the Australian Smart Community solution.

Historical earnings and RaaS' estimates (in A\$m unless otherwise stated)

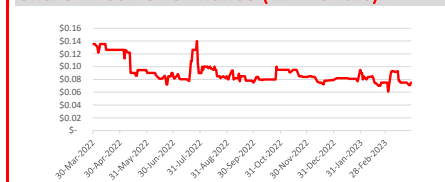
Year end	ARR*	Revenue	EBITDA adj.	NPAT adj.	EPS (adj.) (c)	EV/Revenue (x)
06/21a	0.1	5.7	(5.3)	(6.7)	n.m.	n.m.
06/22a	0.6	10.4	(6.6)	(7.9)	(0.057)	1.0
06/23f	2.0	18.7	(4.8)	(6.7)	(0.033)	0.5
06/24f	4.5	27.8	(1.6)	(3.7)	(0.013)	0.5

Source: Proforma for FY21; Actual FY22; RaaS estimates FY23f and FY24f; *Annual Recurring Revenue; EBITDA, NPAT and EPS adjusted for one-time, non-recurring and non-cash items

Share Details

ASX code	X2M
Share price (29-Mar)	\$0.075
Market capitalisation	\$14.0M
Shares on issue	186.7M
Net cash 31-Dec-2023	\$3.05M
Free float	~60%

Share Price Performance (12 months)



Upside Case

- Market consolidation, particularly in South Korea
- New module/functionality offering higher SaaS fees
- Favourable SaaS pricing deal in China

Downside Case

- Continued SaaS pricing pressures
- Limited uptake of new functionality
- Access to funding

Catalysts

- SaaS revenue follows on from hardware sales
- Evidence of cash-flow breakeven
- Further evidence of take-up of technology

Company Interview

[X2M Connect RaaS 2023 Outlook Interview 16 January 2023](#)

Company Contacts

Mohan Jesudason (CEO)	+61 1800 926 926
Keith Jelley (COO)	+61 1800 926 926
investor.relations@x2mconnect.com	

RaaS Contacts

John Burgess	+61 410 439 723	john.burgess@raasgroup.com
Finola Burke	+61 414 354 712	finola.burke@raasgroup.com

FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

ABN 99 614 783 363

Corporate Authorised Representative, number 1248415

of

BR SECURITIES AUSTRALIA PTY LTD

ABN 92 168 734 530

AFSL 456663



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Contact Details, BR and RaaS

BR Head Office: Suite 5GB, Level 5, 33 Queen Street, Brisbane, QLD, 4000

RaaS, 20 Halls Road Arcadia, NSW 2159

P: +61 414 354712

E: finola.burke@raasgroup.com

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