Q2 2016 Earnings Update – AUGUST 23, 2016

Ackroo Inc. (AKR – TSX-V, $0.235)

Ackroo Inc.	AKR - TSX-V
(Currency is in CAD unless noted otherwise)	
Last Price ($)	$0.235
December 31, 2017 - Target Price ($)	**$0.425**
Return to target	**81%**
52-week high / low ($)	$0.335 / $0.08
Average Daily Volume (90-Day)	54,630

Market Info	
Shares Outstanding (M)	20.9
Warrants (M)	0.3
Options (M)	2.0
Fully Diluted Shares Out (M)	23.2
Market Capitalization ($M)	$4.91
Enterprise Value ($M)	$5.89

Most Recent Quarter	Q2 2016
Revenue ($M)	0.56
Gross Margin (%)	65%
EBITDAS ($M)	($0.09)
Working Capital ($M)	($0.51)
Total Debt ($M)	$0.98

Valuation	
EV/Revenue - FY 15	3,23
EV/Revenue - Annualized H1 16	2,66

FYE: Dec 31	FY 2015	FY 2016E	FY 2017E	FY 2018E
Revenue ($M)	$1.82	$2.40	$3.12	$4.06
Gross Margin	66%	65%	75%	75%
EBITDAS ($M)	($0.76)	($0.24)	$0.34	$0.84

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- On July 29, 2016, Ackroo reported its Q2 2016 results, which confirmed steady progress in the company's financial performance.

- On June 8, 2016, Ackroo signed a strategic partnership with First Data Corporation (NYSE: FDC) to become the preferred third-party provider of gift card and loyalty programs for new SMB accounts in Canada. We believe this partnership has the potential to accelerate organic growth significantly.

- On June 9, 2016, Ackroo closed a private placement of $0.20 shares for gross proceeds of $587,316.

- On August 22, 2016, Ackroo launch a new white-labelled mobile app with Williams Fresh Cafe in 20 locations in Ontario.

- We have updated our forecasts and lowered our price target to $0.425 to account for delays in our investment thesis.

- We expect the FDC partnership and small bolt-on acquisitions to fuel at least 30% annual revenue growth over the next few years.

Q2 2016 Financial Summary

On July 29, 2016, Ackroo reported its Q2 2016 results, which confirmed steady progress in the company's financial performance:

- Total revenue was up 77% year-over-year to $559K from $316K in 2015.
- Subscription and service revenue increased 78% to $487K from $273K last year.
- Net Operating Loss (EBITDAS), excluding foreign exchange gains and losses, was reduced 70% year-over-year to ($87K).
- From discussions with management, we estimate that Ackroo's organic growth was approximately 24%[1] in Q2 2016.

On June 8, 2016, Ackroo signed a strategic partnership with First Data Canada, a division of First Data Corporation (NYSE: FDC), to become the preferred third-party provider of gift card and loyalty programs for new SMB accounts. First Data is a global leader in the payment processing space. They serve over 6M merchant locations in 118 countries, including 4M in the US (42% market share according to Fortune Magazine[2]) and 30,000 in Canada, and are looking to aggressively grow their Canadian customer base. In our opinion, a 12-billion-dollar company choosing Ackroo as a preferred partner further validates Ackroo Anywhere (AKR3) technology platform.

We believe this partnership has the potential to accelerate organic growth significantly. First Data has more than 100 sales reps in Canada, but only two partners for gift card and loyalty. In comparison, Chase Paymentech and Global Payments have sales teams of similar size but send leads to three and five partners respectively.

At this point, it's difficult to estimate what will be the impact of the FDC partnership on organic growth rates but, if July is an early indication, it will clearly be substantial. According to management, Ackroo received more leads in the month of July from First Data than Chase and Global combined. That said, integration of new merchant locations

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[1] Ackroo Q2 2016 reported revenue = $559K
Minus: - DRC acquired recurring revenue = ($150k)
- OTR from acquired DRC locations = 107 * 131$ (average OTR per existing location) * 50% = ($7k)
- D1Mobile revenue = ($10k) – 100% OTR
Ackroo Q2 2016 organic revenue = $392k (+24% over revenue of $316k in Q2 2015)
[2] http://fortune.com/2015/10/21/first-data-ipo/

on AKR3 can take up to 90 days, so investors should wait until Q4 2016 to draw any firm conclusion.

On June 9, 2016, Ackroo closed a private placement of $0.20 shares for gross proceeds of $587,316. Of the amount raised, $330K was used to reduce the Dealer Rewards Canada (DRC) vendor debt to $800K, which will be paid in 24 monthly payments of $36,916 (including 10% interest) starting in January 2017. The restructuring of the DRC vendor debt certainly helped alleviate short term capital needs and CEO Steve Levely deserves a lot of credit for getting this done. However, considering Ackroo is currently burning $20K to $30K per month, shows negative working capital and has limited resources to execute on their strategic plan, we think the company will have to raise growth capital by the end of 2016.

During the quarter, Ackroo developed a white-labelled mobile app for loyalty customers via the acquisition of D1 Mobile's Appetite platform. It was required to move Williams Fresh Cafe on AKR3 and has launched officially in 20 locations in Ontario on August 22, 2016. More interestingly, Ackroo can now upsell a mobile app to all of their current loyalty customers, which represents a $165K annual recurring revenue (ARR) opportunity[3], while increasing their chances to land new merchants.

Moving Williams Fresh Cafe on AKR3 also gave the company the occasion to add a new integrated product partner in Quickservice, a provider of POS systems in the quick-service industry. They service some really big brands like McDonald's, Tim Horton's, Wendy's, A&W, Burger King, Dairy Queen, KFC, Mr. Sub, Pizza Pizza and Petro-Canada, just to name a few. This relationship could yield some interesting opportunities.

Once migration is over, the D1 Mobile acquisition should add close to $100K in annual recurring revenue to Ackroo. When the company acquired D1 Mobile, it was doing roughly $30K in ARR and $70K in one-time revenue (OTR). To convince brands to move to Ackroo, CEO Steve Levely offered to waive monthly recurring revenue (MRR) while they migrate accounts to AKR3. Three brands with approximately 80 locations have accepted to move and the company is in discussions with a fourth. When all is said and done, D1 Mobile should prove to be another highly accretive acquisition for Ackroo.

[3] Annual revenue opportunity = Approx. 550 loyalty locations * 25$ per month * 12 months = $165,000

On August 9, 2016, CEO Steve Levely sent a letter to Ackroo's shareholders[4], outlining the company's financial performance and capital allocation since he took over in May 2014. We strongly advise current or potential shareholders to give it a good read. Ackroo has come a long way under Steve's leadership. As a young CEO of a tiny public money-losing company, odds were surely stacked against him when he accepted the role over two years ago. Looking at the company now and all the work he has accomplished with fairly limited resources to position the company for profitability and growth makes us extremely bullish on Ackroo's future.

Here's an excerpt from Steve's letter to shareholders that we particularly liked: *"As a CEO I have made mistakes, including focusing too much on providing specific guidance early on when there were too many variables at play and closing a significant acquisition prior to having the necessary capital to support that acquisition. The journey has been far from easy; however, we do believe we are leveraging those learnings and are at the doorstep of great success. We are very well positioned with our partners and customers and have a business model that is built for scale. The majority of the strategic pieces of the puzzle are in place and so we are very bullish on what the future holds for the Company and our shareholders."*

[4] http://us10.campaign-archive1.com/?u=912ea449640960f286d6283f6&id=7141a2672f

Forecasts and Outlook

	FY 15	FY 16E	FY 17E	FY 18E
Revenue	1 822 224	2 400 000	3 120 000	4 056 000
(-) COGS	611 898	840 000	780 000	1 014 000
Gross Profit	1 210 326	1 560 000	2 340 000	3 042 000
(-) OPEX	2 066 868	1 900 000	2 100 000	2 300 000
(-) Grants and tax credits*	(100 000)	(100 000)	(100 000)	(100 000)
EBITDAS**	**(756 542)**	**(240 000)**	**340 000**	**842 000**
Key Metrics				
Revenue Growth y/y	37%	32%	30%	30%
Gross Margin	66%	65%	75%	75%
EBITDAS Margin	-42%	-10%	11%	21%
Shares Outstanding	**21 087 000**			
10% Option Pool + Warrants	2 408 700			
FD Shares Out	**23 495 700**			**29 369 625**
			Dilution	*25%*
Hurdle Rate	30%			
Price Target 2018 @ 4x EV/Revenue	0,55 $			
Price Target December 31, 2017	**0,425 $**			

* Grants and tax credits exclude a $100K provision for potential reversal of previous years SRED in FY 15
** EBITDAS excluding foreign exchange gains & losses

We have updated our forecasts[5] and lowered our price target to $0.425 to account for delays in our investment thesis. Ackroo came substantially under its target of $2M in their last financing round. As a result, they had to delay the hiring of new employees to support product development activities and sales operations, plus they don't have any capital available to execute on acquisition targets even though it would likely be highly accretive.

Fortunately, finding capital is a much easier task than finding a great operator and capital allocator. **We believe we have found one in Steve Levely, hence we are confident that the market will eventually recognize the tremendous opportunity to invest in AKR shares at such undervalued levels.**

[5] Disclaimer: Projections are based on current information available publicly and assumptions made by Espace MicroCaps.

We expect the FDC partnership and small bolt-on acquisitions to fuel at least 30% annual revenue growth over the next few years. Gross margin should improve to 75% after migrating DRC customers on AKR3, removing the 40% license fee Ackroo currently has to pay on monthly recurring revenue to use Dealer Rewards' platform. The process should take a few months and be over by the end of Q4 2016 or beginning of Q1 2017.

Technically, removing the license fee would bring Ackroo to cash flow breakeven immediately so, add revenue growth in the mix, and we can reasonably expect the company to show positive operating cash flows in the first quarter of 2017 at the latest.

It is important to note that we aren't modeling economies of scale yet in our model by using a 4x revenue multiple on 2018 sales to value Ackroo. If Ackroo succeeds in achieving scale, we expect margins to expand even further and cash flows to increase exponentially in 2019 and beyond. **At Espace MicroCaps, we like to invest in microcaps with lots of optionality. Given the depth of opportunities Ackroo could execute on, the stock definitely meets this criterion.**

Potential short-term catalysts for AKR:

- Recapitalization of Ackroo's balance sheet through an equity financing
- Reporting of the company's Q3 2016 financial performance
- Small bolt-on acquisitions
- New referral and integrated product partners
- Contract with large brands

Financial snapshots

	Q2 16	Q1 16	Q4 15	Q3 15	Q2 15	Q1 15
Revenue	559 223	548 300	601 758	519 766	315 562	385 138
(-) COGS	196 721	189 523	199 815	183 914	91 028	137 141
Gross Profit	362 502	358 777	401 943	335 852	224 534	247 997
(-) OPEX	449 812	447 063	618 250	479 770	513 708	455 140
(-) Grants and tax credits*	-	-	(9 777)	(90 223)	-	-
EBITDAS**	**(87 310)**	**(88 286)**	**(206 530)**	**(53 695)**	**(289 174)**	**(207 143)**
Key Metrics						
Revenue Growth y/y	77%	42%	72%	61%	10%	4%
Gross Margin	65%	65%	67%	65%	71%	64%
Improvement in EBITDAS loss	70%	57%	51%	79%	22%	63%
Working Capital	**(507 582)**	**(1 180 833)**	**(1 130 290)**	**(807 723)**	**(846 879)**	**368 620**

	FY 15	FY 14	FY 13	FY 12
Revenue	1 822 224	1 328 166	1 284 016	681 142
(-) COGS	611 898	360 888	426 451	166 825
Gross Profit	1 210 326	967 278	857 565	514 317
(-) OPEX	2 066 868	2 716 753	3 430 474	4 123 264
(-) Grants and tax credits*	(100 000)	(135 428)	(77 480)	(183 701)
EBITDAS**	**(756 542)**	**(1 614 047)**	**(2 495 429)**	**(3 425 246)**
Key Metrics				
Revenue Growth y/y	37%	3%	89%	
Gross Margin	66%	73%	67%	76%
Improvement in EBITDAS loss	53%	35%	27%	
Working Capital	**(1 130 290)**	**(510 687)**	**176 218**	**3 234 124**

* Grants and tax credits exclude a $100K provision for potential reversal of previous years SRED in FY 15
** EBITDAS excluding foreign exchange gains & losses

Disclosure

Philippe Bergeron-Bélanger, Mathieu Martin and MicroCaps Research Canada Inc., owner of Espace MicroCaps, own collectively 350,000 shares of Ackroo. MicroCaps Research Canada Inc. provides advisory services to Ackroo on a month-to-month basis at a flat rate of 1,500$ per month.

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