

## Core payments business growth

Novatti's overall quarterly sales revenue increased by 60% on pcp, but was down modestly qoq due to seasonality in ATX and a lower margin for an international client.

Novatti's Issuing segment delivered a strong performance in 2Q23 with transaction values up 242% on the prior corresponding period, and passing \$1bn in gross transaction value in the quarter for the first time.

Novatti's acquiring platforms also performed well with gross transaction value of \$54m, a 19% increase on 1Q23 and >13x pcp. Encouragingly, this is supported by rolling technological advancements in its offering, which now enables businesses to accept and make payments 'with and without' cards, in store, on mobiles and online.

Further milestones achieved this quarter are discussed inside.

## Restricted banking license for IBOA

The International Bank of Australia (IBOA), of which Novatti owns a 91% stake, was granted its Restricted Authorised Deposit Taking Institution license (RADI) by APRA in early November. As expected for an establishing enterprise, IBOA launched a Series A raise where Novatti made a \$5m contribution, retaining a 91% interest, along with \$3 million in new external capital. To be able to appropriately capitalise on opportunities accessed through Novatti's payments ecosystem, we expect IBOA to raise significant further external capital to be well positioned for its unrestricted license within 12-15 months, reducing Novatti's interest in IBOA.

## Reckon dividend boosts cash

As of 31 December 2022, Novatti's group cash position was \$25.7m, a result of strong revenue growth of 60% on prior corresponding period to \$9.3, an equity raise delivering \$3m (which was the external investment in IBOA) and a \$12.8m special dividend from Reckon. A little of \$7m of this is within IBOA, with the remaining \$18m in Novatti's core payments businesses. The segment information in Novattti's 1H23 report may provide further details.

## Departure of CFO after 1H23 result

Novatti CFO Steven Stamboultgis has resigned effective of its 1H23 financials lodgement, with a recruitment consultant engaged to fill the position. Please refer to page 9 for a detailed discussion of the risks and sensitivities to our valuation.

# Novatti

Novatti is a leading digital banking and payments fintech. It enables business to pay and be paid, from any device, anywhere. It does this by leveraging its 'ecosystem', which includes technology and platforms, extensive regulatory licences, and global commercial partnership.

Its services capture the entire payments value chain. This includes issuing, such as prepaid Visa cards, acquiring, enabling merchants to accept payment from financial institutions, and processing, including cross-border transfers and automated invoicing.

Stock	NOV.ASX
Market cap	A\$62m
Price	A\$0.20
Valuation	A\$0.67 (unchanged)

### Company data

Net cash:	A\$25.7m
Shares on issue:	338.4m

### Recent events

4Q22 Appendix 4C	31 January 2023
AGM	23 November 2022
\$12.8m Reckon Dividend	22 November 2022
IBOA Launch	7 November 2022

### Next Steps

1Q23 Appendix 4C	Late April 2023
EMI licence	Pending regulators

### NOV Share Price (A\$)



Glen Wellham, Senior Analyst

# Financials

## Novatti Group Limited

NOV-AU

Year end 30 June, AUD unless otherwise noted

### MARKET DATA

Price	\$	0.195
Valuation	\$	0.68
52 week high / low	\$	0.15 - 0.38
Market capitalisation	\$m	66.0
Shares on issue (basic)	m	338.4
Options / rights / ESP / LTIP	m (currently anti-dilutive)	0.0
Other equity	m	0.0
Shares on issue (fully diluted)	m	338.4

### 12-MONTH SHARE PRICE PERFORMANCE



### INVESTMENT FUNDAMENTALS

	FY21A	FY22A	FY23E	FY24E	FY25E
Reported NPAT	\$m (11.9)	(16.6)	(6.2)	(0.5)	2.1
<b>Underlying NPAT</b>	<b>\$m (11.9)</b>	<b>(16.6)</b>	<b>(6.2)</b>	<b>(0.5)</b>	<b>2.1</b>
Reported EPS (diluted)	¢ (5.2)	(5.1)	(1.9)	(0.2)	0.6
<b>Underlying EPS (diluted)</b>	<b>¢ (5.2)</b>	<b>(5.1)</b>	<b>(1.9)</b>	<b>(0.2)</b>	<b>0.6</b>
....Growth	% (17%)	(1%)	(64%)	(92%)	(510%)
<b>PER underlying</b>	<b>x (3.8)</b>	<b>(3.8)</b>	<b>(10.5)</b>	<b>(129.3)</b>	<b>31.5</b>
Operating cash flow per share	¢ (2.4)	(4.0)	1.1	0.0	0.8
Free cash flow per share	¢ (3.8)	(12.0)	2.9	(1.3)	0.6
<b>Price to free cash flow per share</b>	<b>x nm</b>	<b>nm</b>	<b>0.1</b>	<b>nm</b>	<b>0.3</b>
FCF yield	% (19.6%)	(61.8%)	14.9%	(6.7%)	3.1%

<b>Dividend</b>	¢	0.0	0.0	0.0	0.0	0.0
Payout	%	0.0	0.0	0.0	0.0	0.0
<b>Yield</b>	%	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Franking	%	0.0	0.0	0.0	0.0	0.0

<b>Enterprise value</b>	\$m	62.1	60.0	60.2	64.7	62.6
EV/Revenue	x	3.8	1.8	1.2	0.9	0.7
EV/Underlying EBITDA	x	-11.9	-3.5	11.3	36.0	9.8

Book value per share	¢	3.6	10.9	9.1	8.9	9.5
Price to book (NAV)	x	7.4	1.8	2.2	2.2	2.1
Net tangible assets per share	¢	1.6	8.1	6.3	6.1	6.8
Price to NTA	x	16.9	2.4	3.1	3.2	2.9

### KEY RATIOS

	FY21A	FY22A	FY23E	FY24E	FY25E
Net debt / (cash)	\$m (3.9)	(6.0)	(5.7)	(1.3)	(3.4)
Interest cover (Operating NPAT / net interest)	x (1.6)	41.8	(14.5)	(0.3)	11.2
Gearing (net debt / underlying EBITDA)	x 0.7	0.4	nm	nm	nm
Leverage (net debt / (net debt + equity))	x nm	nm	nm	nm	nm

### DUPONT RATIOS

	FY21A	FY22A	FY23E	FY24E	FY25E
Return on Assets	% nm	nm	nm	nm	0.99
Financial Leverage	x 7.2	3.0	6.0	6.7	6.6
<b>Return on Equity</b>	% nm	nm	nm	nm	6.48

### GROWTH PROFILE

	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	% 49.8	97.5	56.1	38.6	23.3
Underlying EBITDA	% (26.5)	(229.4)	131.0	(66.3)	255.3
NPAT	% (11.3)	(40.0)	62.7	91.8	510.0
Underlying Profit	% (19.4)	(91.5)	203.7	308.0	1,710.0
Underlying EPS	% 16.7	1.4	63.8	91.8	510.0
DPS	% n/a	n/a	n/a	n/a	n/a

### HALF YEARLY DATA

	1H22A	2H22A	1H23E	2H23E	1H24E
<b>Revenue</b>	\$m 11.1	15.6	20.7	30.1	30.2
Other income	\$m 1.2	0.6	14.0	1.0	1.2
Cash expenses	\$m -18.2	-33.0	-25.2	-35.3	-31.4
<b>Underlying EBITDA</b>	<b>\$m -5.9</b>	<b>-16.8</b>	<b>9.5</b>	<b>-4.1</b>	<b>0.0</b>
EBITDA	\$m -10.2	-10.5	9.3	-4.3	-0.2
Depreciation, amortisation and impairment	\$m -0.2	-0.8	-10.0	-0.8	-0.8
<b>EBIT</b>	<b>\$m -10.4</b>	<b>-11.2</b>	<b>-0.7</b>	<b>-5.1</b>	<b>-1.0</b>
Associates and JVs	\$m -1.6	0.0	0.0	0.0	0.0
Net interest	\$m 0.5	-0.1	-0.2	-0.2	-0.2
<b>PBT</b>	<b>\$m -11.4</b>	<b>-11.3</b>	<b>-0.9</b>	<b>-5.3</b>	<b>-1.2</b>
Income tax	\$m -0.1	0.0	0.0	0.0	0.0
<b>NPAT</b>	<b>\$m -11.5</b>	<b>-11.2</b>	<b>-0.9</b>	<b>-5.3</b>	<b>-1.2</b>

### PROFIT AND LOSS

	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Revenue</b>	<b>\$m 16.5</b>	<b>32.6</b>	<b>50.8</b>	<b>70.4</b>	<b>86.8</b>
Other income	\$m 1.9	1.8	15.0	2.2	2.2
Cash expenses	\$m -23.6	-51.5	-60.5	-70.8	-82.6
<b>Underlying EBITDA</b>	<b>\$m -5.2</b>	<b>-17.2</b>	<b>5.3</b>	<b>1.8</b>	<b>6.4</b>
EBITDA	\$m -5.9	-15.2	4.9	1.4	6.0
Depreciation, amortisation and impairment	\$m -1.5	-1.9	-10.7	-1.5	-1.5
<b>EBIT</b>	<b>\$m -7.4</b>	<b>-17.0</b>	<b>-5.8</b>	<b>-0.1</b>	<b>4.5</b>
Associates, JVs and fair value adjustments	\$m 0.0	0.0	0.0	0.0	0.0
Net interest	\$m -4.5	0.4	-0.4	-0.4	-0.4
<b>PBT</b>	<b>\$m -11.9</b>	<b>-16.6</b>	<b>-6.2</b>	<b>-0.5</b>	<b>4.1</b>
Income tax	\$m 0.0	0.0	0.0	0.0	-2.0
<b>NPAT</b>	<b>\$m -11.9</b>	<b>-16.6</b>	<b>-6.2</b>	<b>-0.5</b>	<b>2.1</b>

Weighted average diluted shares on issue	m	228.8	325.0	335.3	335.3	335.3
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### BALANCE SHEET

	FY21A	FY22A	FY23E	FY24E	FY25E
Cash & equivalents	\$m 8.8	6.1	15.8	11.4	13.4
Trade & other receivables	\$m 4.1	8.4	8.9	9.5	10.1
Financial assets - funds in trust	\$m 39.0	52.4	120.6	135.5	143.8
Investments accounted for using the equity method	\$m 0.8	0.1	0.1	0.1	0.1
Other investments	\$m 1.0	27.7	27.7	27.7	27.7
Net Property Plant And Equipment	\$m 0.5	0.5	0.5	0.5	0.5
Right of use assets	\$m 1.9	1.8	1.8	1.8	1.8
Intangibles	\$m 5.0	9.3	9.3	9.3	9.3
Deposits	\$m 2.2	3.7	-2.1	2.3	2.9
Other	\$m 0.3	0.9	0.9	0.9	0.9
<b>Total Assets</b>	<b>\$m 63.8</b>	<b>111.0</b>	<b>183.6</b>	<b>199.0</b>	<b>210.5</b>

Trade and other payables	\$m 6.8	16.2	17.2	18.3	19.4
Settlement and remittance funds payable	\$m 38.6	52.1	119.7	134.5	142.7
Lease liabilities	\$m 2.2	2.1	2.1	2.1	2.1
Unearned revenue	\$m 0.2	0.3	0.3	0.3	0.3
Borrowings, including convertible notes	\$m 4.9	0.0	10.0	10.0	10.0
Employee benefits	\$m 1.5	2.9	3.0	3.1	3.3
Other	\$m 0.6	0.8	0.8	0.8	0.8
<b>Total liabilities</b>	<b>\$m 54.9</b>	<b>74.4</b>	<b>153.1</b>	<b>169.1</b>	<b>178.5</b>
Net assets	\$m 8.9	36.6	30.4	29.9	32.0

Contributed equity	\$m 44.1	89.3	89.3	89.3	89.3
Reserves	\$m 3.8	5.0	5.0	5.0	5.0
Retained earnings	\$m -41.0	-57.7	-63.9	-64.4	-62.3
<b>Shareholder's equity</b>	<b>\$m 8.9</b>	<b>36.6</b>	<b>30.4</b>	<b>29.9</b>	<b>32.0</b>

Basic shares on issue	m	244.2	335.3	335.3	335.3	335.3
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### CASH FLOW

	FY21A	FY22A	FY23E	FY24E	FY25E
Net Income (Cashflow)	\$m -12.3	-16.6	-6.2	-0.5	2.1
Depreciation & Amortization	\$m 1.5	1.9	1.5	1.5	1.5
Change in Net Operating Assets	\$m -2.8	4.0	-1.6	-1.7	-1.8
Other Non-Cash Items, Total	\$m 5.2	-2.4	10.0	0.8	0.8
Other	\$m 2.9	0.0	0.0	0.0	0.0
<b>Operating cash flow</b>	<b>\$m -5.4</b>	<b>-13.0</b>	<b>3.7</b>	<b>0.1</b>	<b>2.6</b>

Capital expenditure	\$m -2.4	-2.1	-0.3	-0.3	-0.3
Acquisitions/divestment/other	\$m -0.3	-24.6	-4.0	-4.0	0.0
<b>Investing cash flow</b>	<b>\$m -2.6</b>	<b>-26.7</b>	<b>-4.2</b>	<b>-4.2</b>	<b>-0.3</b>

Equity	\$m 15.1	36.0	0.0	0.0	0.0
Debt (including convertible)	\$m -0.4	-0.8	10.5	0.0	0.0
Leases	\$m -0.3	-0.2	-0.3	-0.3	-0.3
<b>Financing cash flow</b>	<b>\$m 14.4</b>	<b>36.6</b>	<b>10.2</b>	<b>-0.3</b>	<b>-0.3</b>

<b>Net cash flow</b>	<b>\$m 6.3</b>	<b>-3.1</b>	<b>9.7</b>	<b>-4.4</b>	<b>2.0</b>
Free cash flow	\$m -8.74	-39.141	9.7268	-4.4026	2.03258

Source: Company reports and MST Access estimates

Source: Company reports and MST Access estimates

Figure 1 –Novatti December quarter highlights



Source: Company reports

## Business Updates

### Core Acquiring and Issuing Business

Novatti's payments business enables its business customers to pay and be paid with card-present and card not-present; in store, on mobiles and online. While it was originally envisaged to facilitate online card not present online payments, advances in technology have allowed Novatti to expand its offering to both physical and virtual cards in digital wallets from Apple Pay, Google Pay and Samsung Pay, credit, debit and prepaid cards, both present and not present, from all major card networks and overseas provider such as UnionPay, Alipay and WeChat Pay, thus broadening its payments offering.

The December quarterly activities report highlights key technological milestones achieved in the quarter:

- “Tap and Pay” for Android enabling payments using Android phones without the need for additional payment terminals or hardware (so called “pay on glass”).
- Acquiring solutions for Reckon, an accounting software which Novatti holds a 19.99% strategic stake in, which enables payments to take place directly through the invoice. Reckon's platform currently has 117,000 clients.
- Partnership with Riskfield to detect fraudulent charge backs.
- Partnership with DataMesh Group to integrate its card-present point of sale terminal with Novatti end-to-end merchant acquiring payment ecosystem, providing opportunities to cross-selling throughout a network of potentially thousands of businesses throughout Asia.

### Australian Dollar Stablecoin

Novatti also launched a stablecoin in 2Q23, the AUDD, which is fixed to the Australian dollar, and 100% fiat backed. The goal of AUDD is to enable current and remittances to be sent globally with reduced friction points, near-

instantaneously. Novatti report over 100 accounts have already been created registering for use. Recent Australian dollar stablecoin launches from NAB and ANZ highlight the considerable growth in the Australian stablecoin space, and may be complimentary through validating Novatti’s offering, rather than providing competition given the different uses implemented.

## International Bank of Australia (“IBOA”)

Following the receipt of a restricted authorised deposit licence in November, International Bank of Australia building towards an unrestricted banking license which is targeted within 12-15 months.

- To build scale initially required in its target markets, one being the underserved migrant sector, Novatti reports discussions with 50 potential channel partners, including migration travel and education agencies.
- The bank has appointed a Chief Risk Officer, auditor and its own core banking provider, which will assist in demonstrating operational capacity to APRA.
- Focusing on partnering with fintech’s who need an innovative partner with best-in-class technologies, leveraging the Novatti payments ecosystem.

We also note that the bank will need to raise substantial additional capital before it can receive its unrestricted authorised deposit institution licence. We expect that this will likely see Novatti’s current 91% stake in the bank diluted, to the extent that it will no longer be able to consolidate the bank within its results.

Figure 2 –Novatti Outlook presented at its quarterly update

## What to expect going forward

**Novatti**

Novatti’s business has shifted from an investment and development phase to driving increased margin. Focus on scaling for growth in FY23:



### Shift to positive cashflow

- Focus already shifted to delivering positive cashflow
- 47% decrease in September quarter cash use YoY
- Objective is positive cashflow in Q4 FY23



### Drive returns from existing investment

- Drive sales traction from ecosystem globally
- Leverage scalable solutions for growth – particularly Acquiring



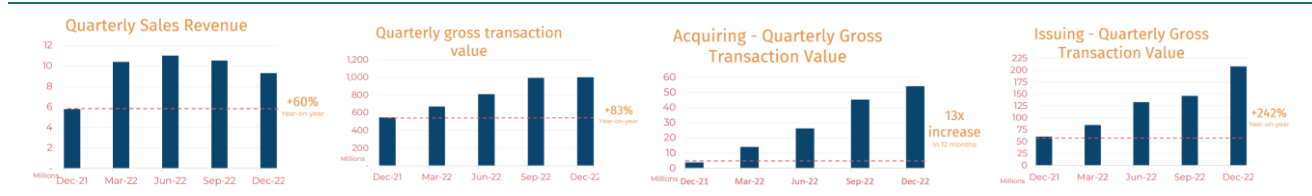
This presentation has been approved for release to the ASX by Peter Cook, Managing Director  
[www.novatti.com](http://www.novatti.com)

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## Quarterly Activities Report and Appendix 4C Cashflow Analysis

### 2Q23 revenue down qoq, but still up strongly on pcp

Figure 3 – Novatti quarterly revenue trends



Source: Company reports

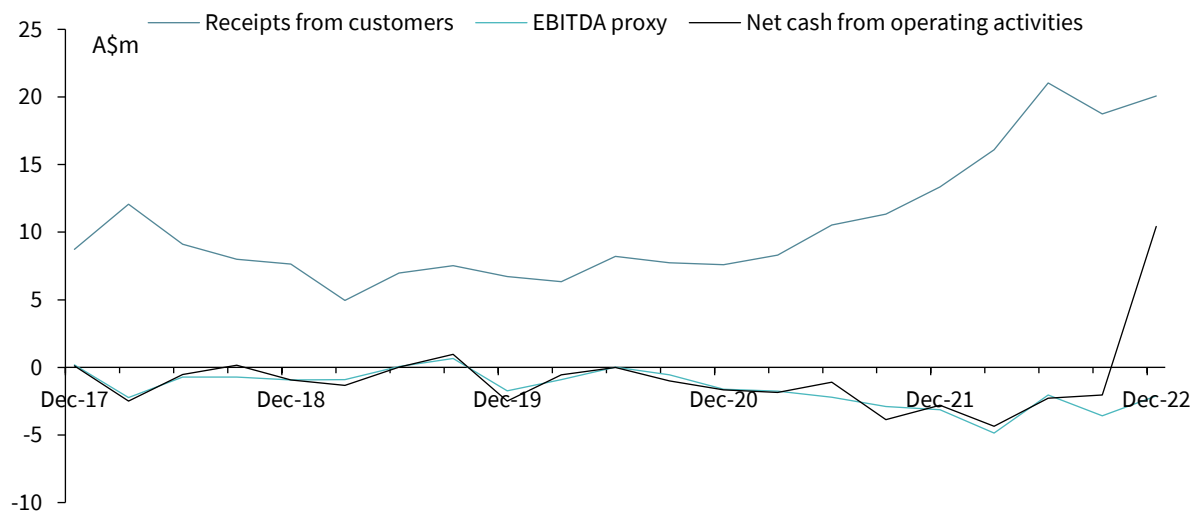
Novatti’s overall quarterly sales revenue increased by 60% on pcp, but was down modestly qoq due to seasonality in ATX and a lower margin for an international client.

Novatti’s Issuing segment delivered a strong performance in 2Q23 with transaction values up 242% on the prior corresponding period, and passing \$1bn in gross transaction value in the quarter for the first time.

Novatti’s acquiring platforms also performed well with gross transaction value of \$54m, a 19% increase on 1Q23 and >13x pcp. Encouragingly, this is supported by rolling technological advancements in its offering, which now enables businesses to accept and make payments ‘with and without’ cards, in store, on mobiles and online.

### Cash receipts continue to rise, second highest quarter on record

Figure 4 – Quarterly cash receipts and operating cashflow



Source: Company reports, MST Access estimates

Novatti delivered \$10.4m in operating cash flows in 2Q22, with two key distorting components:

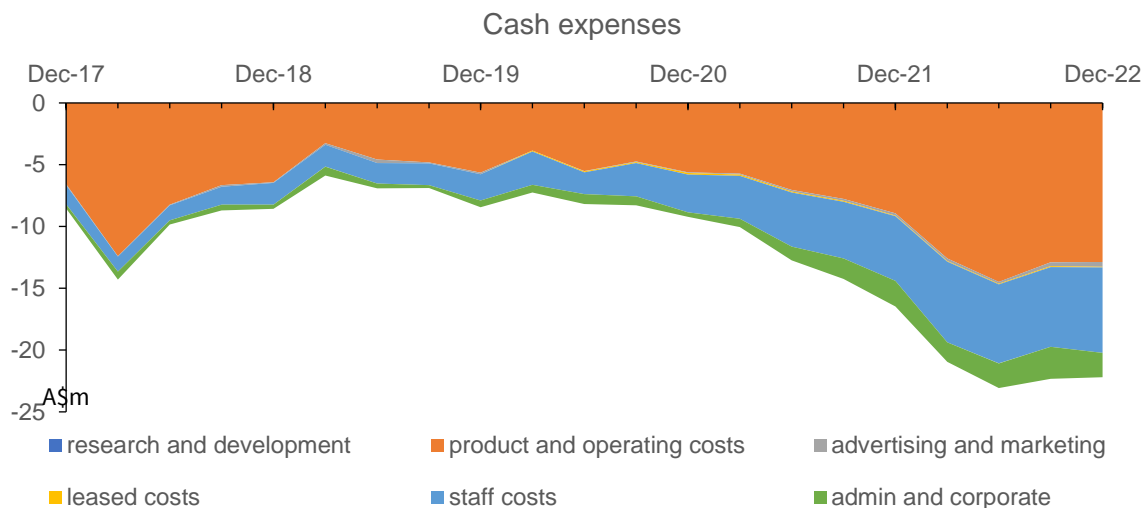
- the \$12.8m special dividend from Reckon and
- \$850k in IBOA related expenses, which are consolidated with Novatti’s payments businesses.

Thus, at an underlying level, the business continues to burn cash, albeit this is rapidly decreasing as Novatti aggressively chases becoming cashflow breakeven.

Contributing to this improved underlying performance was a 7% increase in receipts from customers from the September quarter to \$20.1m. In its accompanying briefing, Novatti have highlighted the next 6-9 months as a period of top-line acceleration, with operating leverage driving positive cashflow.

The consolidated group’s EBITDA, which excludes the special dividend, has improved by 32% on prior corresponding period, and 41% month on month to -\$2.1 million.

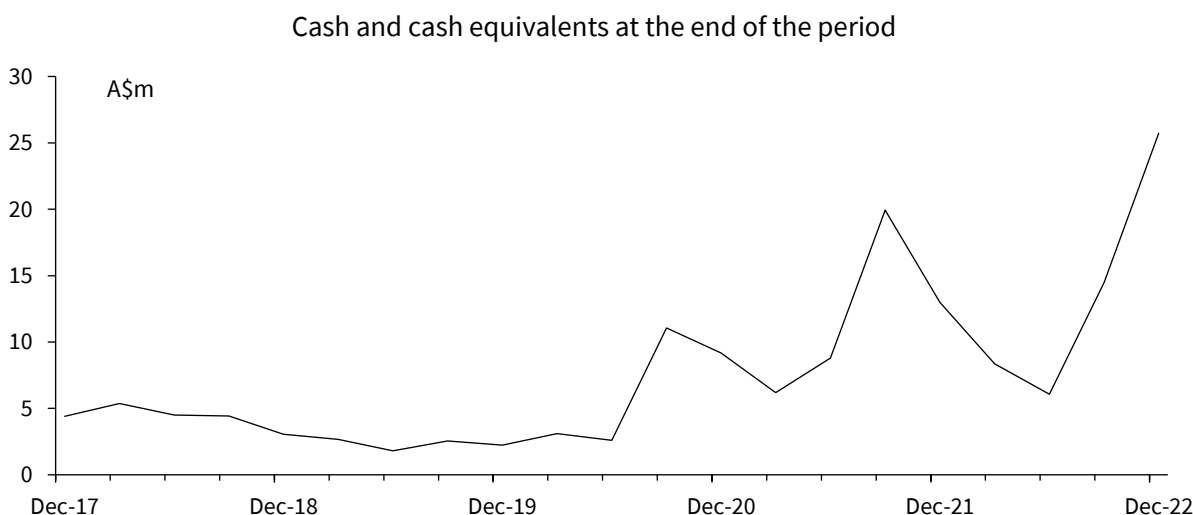
Figure 5 – Cash operating expenses



Source: Company reports, MST Access estimates

Novatti’s December quarter continued the cost discipline displayed in its recent September and June quarters, consistent with Novatti’s outlook commentary at its FY22 result for FY23. Novatti has again highlighted its focus on control of administration and corporate costs in 2Q23, along with an expected a \$3m annual saving in costs annually, post deconsolidation of the Bank.

Figure 6 – Novatti quarterly cash balance



Source: Company reports, MST Access estimates

Due to the 4C reporting requirements for consolidated entities, this cash position represents both Novatti’s core payments business and IBOA, split approximately \$18m to Novatti Payments and \$7.2m, to International Bank of Australia.

After adjusting for the special dividend and \$0.85m expended by IBOA, Novatti had a core underlying operating cash outflow for the period of \$1.8m, which suggests almost 12 quarters runway on its current cost base. This is a generous buffer for the payment’s operations given managements near-term cash positive target by Q423. We expect IBOA to raise further capital, which will see Novatti’s holding diluted, and eventually deconsolidated, within the next 12-18 months.



Figure 7 – Novatti adjusted cash runway

	2023 Q2 A\$K	Adjustments A\$K	Adjusted A\$m	Comments
Net cash from / (used in) operating activities	10,420	-11,985	-1,565	Remove Reckon special dividend and IBOA expenditures
Cash and cash equivalents at quarter end	25,721	-7,200	18,521	Remove cash allocated to IBOA
Unused finance facilities available at quarter end	0		0	
Total available funding available	25,721		18,521	
<b>Estimated periods of funding available</b>	<b>-2.5</b>		<b>11.8</b>	

Source: Company reports, MST Access estimates

Post 2Q23, on 23 January 23 Novatti announced the business has been awarded a \$2.3m grant from the Australian Government's Cooperative Research Centre's Projects Grants Programs for an anti-money laundering and fintech program for SMEs. As the first \$830k is not due until 30 June 2023, we have not adjusted our cash runway calculation for this.

## No earnings revisions

Following Novatti's 2Q23 quarterly activities update and cashflow release, we make no changes to our earnings estimates ahead of its 1H23 result next month. Full details of our earnings estimates appear in the financial summary on page 2.

## Valuation

Figure 8 –MST Access valuation of Novatti

Current date		1-Feb-23														
Next balance date		31-Dec-22														
		Dec-22	Jun-23	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26	Dec-26	Jun-27	Dec-27	Jun-28	Dec-28	Jun-29	
<b>Free cash flow to equity</b>	<b>A\$m</b>	<b>9.8</b>	<b>-5.1</b>	<b>-5.2</b>	<b>0.8</b>	<b>0.6</b>	<b>1.4</b>	<b>2.3</b>	<b>3.7</b>	<b>4.6</b>	<b>7.5</b>	<b>8.2</b>	<b>11.8</b>	<b>10.6</b>	<b>14.5</b>	
<b>Discounted cash flow</b>	<b>A\$m</b>	<b>9.5</b>	<b>-4.7</b>	<b>-4.5</b>	<b>0.6</b>	<b>0.5</b>	<b>1.1</b>	<b>1.7</b>	<b>2.6</b>	<b>3.0</b>	<b>4.7</b>	<b>4.9</b>	<b>6.7</b>	<b>5.8</b>	<b>7.5</b>	
Sum of discount streams	A\$m	39.3	<b>CAPM</b>													
Future value into perpetuity	A\$m	358.5	Risk free rate				4.00%									
NPV of terminal value	A\$m	185.5	Equity beta				1									
add net cash at FY22	A\$m	6.1	Equity risk premium				6.00%									
<b>Value of total equity</b>	<b>A\$m</b>	<b>230.8</b>	Cost of equity				10.0%									
Diluted shares on issue	m	338.4														
<b>Value per share</b>	<b>A\$</b>	<b>0.68</b>	Terminal growth				3.0%									

Source: Company reports, MST Access estimates

We continue to use a DCF of free cash flow to equity forecasting out 7 years before applying a terminal value. Our valuation assumptions remain unchanged: our cost of equity remains at 10%, composing of a 4% risk free rate, 6% equity risk premium and beta of 1, and we continue to assume a 3.0% terminal growth rate. Based upon our financial forecasts, this leads to our valuation of 68c (unchanged).

We also consider the trading multiples of a range of peers across the multiple industries in which NOV operates as reference for potential price to book and price to NTA multiples that NOV might trade on.

While Novatti currently has its primary industry classification as application service provider under software, we believe a more appropriate industry classifications are:

- internet merchant services within the information technology sector, which encompasses payment processors, payment service providers and gateways, and payment wallets, as well as
- electronic funds transfer and transaction services within specialised finance.

Using these industry classifications, we believe deliver a more appropriate peer group to which to compare Novatti.

Refining these screens deliver the peers and respective multiples in the following figure.

With Novatti being the Australian partner for Marqeta, we see that as its main peer, trading on 2.9x forward EV/Revenue. In comparison, on our forecasts Novatti is trading on 1.2x.

Other equity market considerations such as short sales; any likely forthcoming changes in index inclusion; depth of stock research coverage; composition of and change in the mix of investors (such as founders, board and staff, domestic institutions, foreign institutions, and retail investors) are not incorporated in our valuation; however investors should consider such factors if they seek to develop a price target for the company.

Figure 9 – Selected peer comparable companies' valuation multiples

Identifier (RIC)	Company Name	Forward EV / Revenue	Forward EV / EBITDA	Forward P/E	Forward Price / Cash Flow	P/B
NOV.AX	Novatti Group Ltd	1.2	11.3	-10.5	6.7	1.4
A2B.AX	A2B Australia Ltd	0.8	6.1	7.6	6.6	1.6
CCA.AX	Change Financial Ltd	1.4	-17.1	-19.0	-14.3	4.2
EML.AX	EML Payments Ltd	n.a.	n.a.	32.3	5.4	1.1
SMP.AX	SmartPay Holdings Ltd	4.2	19.5	57.6	n.a.	4.7
TYR.AX	Tyro Payments Ltd	1.8	21.4	264.7	29.6	1.9
	<b>Australian average</b>	<b>2.1</b>	<b>7.5</b>	<b>68.6</b>	<b>6.8</b>	<b>2.7</b>
	<b>Australian median</b>	<b>1.6</b>	<b>12.8</b>	<b>32.3</b>	<b>6.0</b>	<b>1.9</b>
AMA.MC	Amadeus IT Group SA	6.6	18.3	35.5	19.6	7.2
SQ	Block Inc	2.8	53.3	77.7	60.8	22.9
FIS	Fidelity National Information Services Inc	4.3	10.1	11.6	10.8	1.4
FISV.O	Fiserv Inc	5.2	12.2	16.7	14.2	2.2
MQ.O	Marqeta Inc	2.9	n.a.	n.a.	n.a.	5.9
MA	Mastercard Inc	14.5	23.8	30.6	29.7	52.8
NETW.L	Network International Holdings PLC	4.7	11.6	23.8	12.1	3.6
PAY.TO	Payfare Inc	1.8	59.3	n.a.	n.a.	8.1
PYPL.O	PayPal Holdings Inc	3.4	13.9	20.3	15.7	10.1
PAYP.L	PayPoint plc	3.0	6.4	9.1	n.a.	4.8
PSFE.K	Paysafe Ltd	1.0	3.7	n.a.	4.6	1.1
V	Visa Inc	14.9	21.2	27.2	22.7	11.0
WU	Western Union Co	1.5	6.3	7.9	6.1	19.8
WEX	WEX Inc	4.5	10.0	14.3	14.4	3.4
WLN.PA	Worldline SA	3.9	15.4	20.0	14.4	1.5
	<b>International average</b>	<b>5.0</b>	<b>19.0</b>	<b>24.6</b>	<b>18.8</b>	<b>10.4</b>
	<b>International median</b>	<b>3.9</b>	<b>13.0</b>	<b>20.1</b>	<b>14.4</b>	<b>5.9</b>

Source: IBES, Refinitiv, MST Access estimates for Novatti, A2B Australia and Change Financial

## Investment thesis

With a moat provided by a trifecta of technology, licences and partnerships difficult, time consuming and costly to replicate, the ability of new entrants to join the payments industry is limited. This barrier to entry has led many existing payments providers to rest on their laurels, which Novatti is taking advantage of through its innovative offerings for digital payments.

Novatti provides investors with exposure to several fast-growing areas of the banking and payments industry:

- Through investing in fintech start-ups and providing underlying payment technologies for these start-ups.



- By participating in segments of the payments industry that have seen traditional, major financial institutions become uncompetitive due to tech disruption, including general payments and also transfers and card payments for gambling companies and remittance payments.

We expect that Novatti's strong revenue growth will continue into the foreseeable future. This should see revenues rise sufficiently to lift the group to profitability within the next few years.

The diversification that Novatti has in its business model across a variety of technology, licenses and partnerships is demonstrating resilience to disruptive developments, such as its recent launch of merchant acceptance on Android smartphones, providing it with a first mover advantage over Westpac which has also flagged a similar launch on Android, and the likely forthcoming launch by Apple of 'tap to pay on iPhone' in Australia; however, it does again highlight that there meaningful potential downside risks for Novatti and its stock.

Given the recent sell off in the stock and its peers, it is trading well below our assessed intrinsic valuation for the company, although perhaps doesn't look quite as attractive on some multiples relative to peers which have sold off further.

## Key Risks and Sensitivities

### Macroeconomic impacts

Key influences on our valuation include:

- Economic conditions, influencing exchange rates, interest rates, inflation and bad debts.
- Equity and debt markets, influencing investment returns and risk premiums.

NOV has a direct sensitivity, and an indirect sensitivity to economic conditions and financial markets and their associated risks, including liquidity, price/volatility, credit, counterparty, and duration. We discuss these briefly below, and in more detail later in the report.

The direct sensitivity is quantifiable, driven by its payments businesses, with earnings increasing and decreasing with transaction volumes. Exchange rates can vary these volumes, and lead to considerable volatility of profit.

The indirect sensitivity is potentially more significant, yet harder to quantify. Business confidence, consumer confidence and market conditions play a significant influence on lending demand, while immigration can have a significant impact on foreign investment and FX flows.

### Regulatory Requirements

As a Financial Institution, Novatti is subject to a significant number of regulatory requirements, and could suffer from adverse changes to the requirements, including in Australia:

- Anti-money laundering and counter terrorist financing requirements administered by Austrac;
- Authorised Deposit Institution regulation administered by the Australian Prudential Regulatory Authority;
- Foreign Investment restrictions administered by the Foreign Investment Review Board;
- Privacy requirements administered by the Privacy Commissioner;
- Financial Service licencing and Credit licencing requirements administered by the Australian Securities and Investments Commission (ASIC);
- Australian Consumer Law and unfair contract terms contained in the Corporations Act administered by the Australian Competition and Consumer Commission (ACCC);
- Restrictions on merchant pricing, or interchange fees, administered by the Reserve Bank of Australia (RBA) leading to fee compression;
- Taxation legislation administered by the Australian Taxation Office (ATO);
- Accounting standards required under the Corporations Act administered by the Australian Accounting Standards Board (AASB) and ASIC;

- Design and distribution obligations, several of which will be governed by contract law.

Of these, we would call out a few specific risks we see Novatti facing due to this regulatory framework:

- The recent October 2022 Federal Budget clarified the taxation treatment of cryptocurrency as assets, rather than as currency. This might impact the uptake and adoption of Novatti's AUDD stablecoin.
- Novatti needs to keep ownership by any single foreign shareholder below 20% in order to be considered an Australian institution. Several of its investments, including its yet-to-be-licensed banking subsidiary, sit right on this threshold. Any investor over this 20% threshold needs to meet APRA's fit and proper test. This may limit its ability to raise additional finance in excess of pro-rata rights to Australian investors unless it seeks the Treasurer's approval.
- As a payment processor, Novatti has substantial regulatory compliance requirements, including with AML/CTF regulations, APRA and ASIC requirements. Failure to comply could see the company face civil and criminal prosecution, substantial fines, and potentially the loss of key licenses enabling it to operate various services.

Ultimately a significant proportion of NOV's success will be determined by the human capital within the business, therefore NOV's ability to attract and retain talent is fundamental to its long-term success as it will drive innovation across the Group.

All key management are highly aligned with shareholdings and sizeable option packages. NOV has a quality management team that is highly aligned to the future success of the business. We see this a fundamental to any business with significant growth ambitions.

### Growing pains

The challenge of managing explosive growth – including hiring people with appropriate qualifications, experience and background clearances while maintaining the company's culture, training staff to have an in depth knowledge of the company's products and features, scaling fixed infrastructure and managing customer and investor expectations can be challenging, and there are many examples where problems have emerged because growth has occurred faster than management has been able to suitably manage it. It's a high-quality problem to have, but can lead to missed expectations.

Under this category we would also include execution risks around its plans to cross sell into Reckon's customer base given the lack of prior notice to Reckon prior to acquiring a 19.9% strategic stake

### Reputational risks

Reputational risks could threaten Novatti's entire business model and social license to operate. As a payments' provider, should a prolonged disruption occur at Novatti or with its partners (as happened early last calendar year to Tyro Payments), leading to a loss of customer and/or investor confidence, this could in turn threaten its financial viability. Similarly, should it launch bridges between blockchains for its AUDD stablecoin, a cyberattack on these bridges could lead to the realization of these reputation risks.

### Technology Changes

In addition to continued product development, Novatti will be required to also stay abreast of emerging technology platforms, competitors, and disruptions in order to take advantage of new payment methods and/or protect against direct impacts to its capabilities. Furthermore, its service offering relies on a handful of external software and hardware vendors which contribute to its capabilities, and adverse changes to the products provided by these vendors could lead to Novatti needing to impair intangible assets related to functionality or features.

### Market & Shareholder Support

As a listed company, Novatti is hostage to market conditions. In volatile markets, this can result in a lack of liquidity; which can lead to volatile trading where the shares trade at prices significantly diverged from their intrinsic value.

While our modelling suggests that NOV is likely to improve its cash position; there is a risk that should the company identify an additional high growth market it wishes to address, it might seek additional capital from the financial markets. We consider it unlikely that the company would seek to dilute existing shareholders in order to acquire

additional businesses, and any acquisition is likely to instead be assessed by management as highly accretive over the long term.

The level of the company's share price is likely to also influence the approach management takes to growing the company. When the company trades on high revenue multiples, and capital is cheap, this incentivises management to aggressively chase further growth, potentially raising capital to fund investments to achieve this growth. Lower revenue multiples provide less incentive to aggressively chase sales growth. As a payments company, a large proportion of expenses are largely fixed, so greater revenue growth translates rapidly into improving operational leverage.

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## Company Description

Novatti is a leading digital banking and payments fintech. It provides services that enable financial transactions to take place digitally, on any device, anywhere. It does this by leveraging its 'ecosystem', which includes technology and platforms, extensive regulatory licences, and global commercial partnership.

Its services capture the entire payments value chain. This includes issuing, such as prepaid Visa cards, acquiring, enabling merchants to accept payment from financial institutions, and processing, including cross-border transfers and automated invoicing.

Novatti holds all necessary regulatory licences and registrations, including an Australian Financial Services Licence (No 448066) through its subsidiary Flexewallet Pty Ltd, registration in New Zealand as a Financial Services Provider (FSP613789) through subsidiary Flexewallet (NZ) Limited, is registered with AUSTRAC as a Remittance Network Provider, and is a 91% owner of International Bank of Australia Pty Ltd which has a Restricted ADI. It is also in the process of applying for an EMoney Issuing (EMI) licence in Europe.

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