

Indoor Skydive Australia Group

Penrith growth and new tunnels create a positive tailwind

With the current Penrith EBITDA already covering its own tunnel and corporate costs, further growth from Penrith, a full 12 month's positive contribution from the Gold Coast and 6 months from Perth tunnels will result in escalating EBITDA and Cash Flow in FY17 onwards, on a fairly fixed Corporate base.

FY16 Result impacted by late opening of the Gold Coast

IDZ reported a Tunnel EBITDA increase of 32.3% to \$4.1m, on a 26.8% increase in Revenue to \$8.2m with a further increase in Penrith and an initial contribution from the Gold Coast.

However, Group EBITDA growth was held back by the loss of \$1.1m in EBITDA from the 3 month delay in opening the Gold Coast Tunnel, and some initial costs on the Perth expansion. Key Features of the result were:

- Utilisation across the 2 tunnels was 76%, based on a 12 hour day.
- Penrith Tunnel Occupancy increased above the 82.5% in FY15, with further Revenue growth of around 6% and margins of around 55%.
- An initial 4½ month contribution from the Gold Coast in the seasonally low part of the year, with a small initial EBITDA contribution.
- With the addition of the Gold Coast, higher yielding first time flyers increased from 53% of average weekly revenue to 58%, increasing the overall yield from \$119 to around \$124 per flyer across 50,025 unique visitors.
- Underlying Head Office costs were steady at around \$2.9m pa.
- With Cash on Balance Sheet of \$2.6m, expected cash flow and unused debt facilities, IDZ has the resources to complete Perth and support ongoing growth.

Continued New Tunnel Development program

IDZ's development program is well underway, with Perth scheduled for completion in 2Q FY17 at a capital cost of around \$14m and IDZ actively pursuing projects in Australia and South East Asia, including Hong Kong.

Forecasts amended for delayed openings

Our forecasts for FY17 have been adjusted for the FY16 result and ahead of the Perth start. A strong improvement in performance is expected from the Gold Coast, especially in the peak September and Christmas holidays, the Commonwealth Games in FY18 and inclusion of inbound tourist programs. Further Growth is expected at Penrith with increased usage in off-peak times and yield.

We now expect Group EBITDA of \$5.3m for FY17 on Revenue growth of 96.5% to \$16.0m, boosted by tunnel openings. For FY18, the first year of full operation of the 3 tunnels, we expect a further 24.8% increase in Revenue to \$20.0m and 40.3% in EBITDA to \$7.4m.

Recommendation

We retain our BUY recommendation and Target Price of \$0.52 ps, based on:

- The success of Penrith provides proof of concept for the Gold Coast and new Perth tunnels and any proposed expansion in Australia and Asia.
- A quantum increase in profitability and escalating Cash Flow from the full inclusion of the Gold Coast and an initial Perth contribution in FY17, each capable of generating investment returns similar to Penrith.
- The significant discount of the current share price to our Valuation of \$0.52ps and other key participants in the leisure market.

IDZ.ASX

BUY

19 September 2016

Price	\$0.42
Price Target	\$0.52
Valuation method	EVR
GICS sector	Consumer Services
12 Mth Price Range	\$0.35 - 0.50
Avg monthly share turnover	0.9m
Market Capitalisation	\$50m
Shares on Issue	120.2m
Enterprise Value	\$56m
Previous Rating	BUY

Year Ended	June 30	15A	16A	17E	18E
Tunnel Revenue	\$m	6.4	8.2	15.6	20.0
Increase	%	530.0	26.8	90.9	28.3
Tunnel EBITDA	\$m	3.1	4.1	7.8	10.5
Increase	%	na	32.3	91.0	34.7
Head Office Costs	\$m	-2.9	-4.0	-3.1	-3.1
EBITDA*	\$m	0.2	0.2	4.8	7.4
Increase	%	na	-11	2238	54.1
EBITDA margin	%	3.6	2.5	31.0	37.3
EBIT*	\$m	-0.7	-0.9	3.5	5.9
EBIT margin	%	-10.2	-10.8	22.6	29.7
NPAT (adjusted)	\$m	-0.5	-0.8	3.2	4.9
NPAT growth	%	na	73	-486.6	52.7
NPAT (Reported)	\$m	-1.9	-1.3	2.8	4.9
EPS*	¢ps	-0.4	-0.7	2.7	4.1
EPS growth	%		55	-485.0	52.7
DPS	¢ps	0.0	0.0	0.0	0.0
Franking	%	0.0	0.0	0.0	0.0
PER*	x	-100.2	-59.6	15.5	10.1
Dividend yield	%	0.0	0.0	0.0	0.0
NTA/share	¢ps	23.9	23.2	25.6	29.8
EV/Revenue	x	7.4	6.6	3.6	2.4
EV/EBITDA	x	206.5	261.0	11.7	6.4
Gearing (D:E)	x	0.0	23.3	28.3	7.1
P/OCF	x	70.5	181.8	10.3	6.5
ROA	%	-0.7	-1.4	8.0	12.1
ROE	%	0.0	-1.7	8.2	15.3
Interest cover (EBIT)	x	-2.7	29.7	29.7	29.7

* Excludes charges for Performance options

IDZ v XSO (S&P/ASX Ordinaries Index)



Activities

The operation of Indoor Skydiving Centres in Australia, Asia and New Zealand

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FY16 Result

The result was below our expectations, due to the 3 month delay in opening the Gold Coast, missing the peak Christmas period and opening in a seasonally weaker period. The results also incorporated lease costs prior to opening in the Gold Coast (which were initially capitalised in FY15) and Perth.

Profit & Loss				Cash Flow					
12 Mths to Jun (\$m)		2015	2016	% ch	12 Mths to Jun (\$m)		2015	2016	
Tunnel Revenue		6.4	8.2	26.8	Operating Cash Flow		0.7	0.3	-60.0
Direct Costs		-3.3	-4.0	20.4	Capex		-8.9	-12.7	
Tunnel EBITDA*		3.1	4.1	33.6	Investment/Acquisitions		0.0	0.0	
Head Office Costs**		-2.9	-4.0	38.9	Equity		13.8	0.0	
Group EBITDA		0.2	0.2		Debt		-1.5	9.1	
Depreciation		-0.4	-0.7		Dividends		0.0	0.0	
Amortisation		-0.5	-0.3		Net Cash Flow		4.2	-3.2	-177.6
EBIT		-0.7	-0.9		Balance Sheet		2015	2016	
Interest (Net)		-0.1	-0.1		Current Assets		6.3	3.3	
Pre-Tax Profit		-0.8	-1.0		Non Current Assets		26.3	40.3	
Tax		0.3	0.2		Total Assets		32.5	43.6	34.2
Normalised Profit		-0.5	-0.8	73.4	Current Liabilities		3.4	5.4	
One-off Items (Net)		-1.4	-0.5		Non Current Liabilities		0.0	10.0	
Reported Profit		-1.9	-1.3	-30.9	Total Liabilities		3.4	15.4	348.2
Tunnel Utilisation (%)		64	66		Shareholder Funds		29.1	28.3	-2.9
Tunnel Margin (%)		48.2	50.8		Cash (¢ ps)		4.7	0.0	
Group EBITDA Margin (%)		3.6	2.0		Net Debt (\$m)		0.0	6.6	
Effective Tax Rate (%)		na	na		Gearing D:E (%)		0.0	23.3	
EPS (¢ ps)*		-0.4	-0.7	55.2	Operating Leases (\$m)		15.1	15.9	
Cash Flow (¢ ps)		0.6	0.2	-64.2	Revenue/Working Capital		-4.5	-3.0	
DPS (¢ ps)		0.0	0.0		NTAV (¢ ps)		23.9	23.2	-2.9
Ent Value / Revenue		7.4	6.1		Net Assets (¢ ps)		24.4	23.5	-3.8
Ent Value / EBITDA		206.5	312.3		Current Ratio (x)		1.8	0.6	

Source: IDZ

* excludes One-off items (iShare based payments)

** includes lease costs & some Perth costs

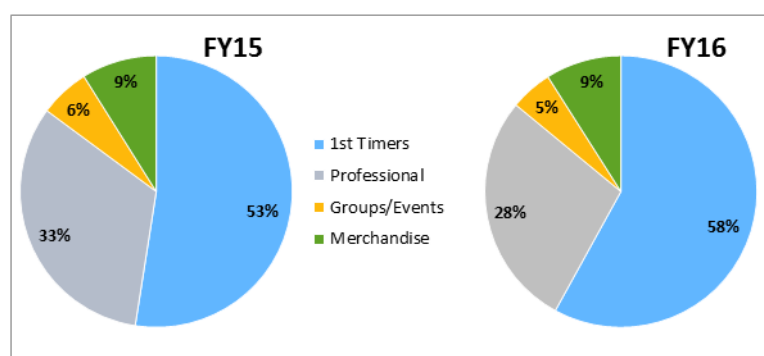
Key Elements:

Tunnel Utilisation – Utilisation across the 2 tunnels was 76% (based on a 12 hour day, 61% on a 15 hour day).

Perth – Continued to improve with utilisation increasing above the 82.5% in FY15 (based on a 12 hour day), helped by growth in first timers and an increase in return flyers and professionals, including training for Championships in early September.

Gold Coast – Was affected by the delayed opening, as the February to May period is expected to be the quietest period annually. While there was an improvement in June with increased marketing, the school holidays in July drove utilisation substantially higher. A large proportion of flyers are walk-ins with the balance split between online and agents such as Red Balloon, Adrenalin and Groupon.

With the addition of the Gold Coast, higher yielding first time flyers increased from 53% of average weekly revenue to 58%. Professional/military (fell from 33% to 28%) was the other main contributors, with Groups and Merchandise constant at 5% and 9% of revenue. This increased overall yield from \$119 to around \$124 per flyer across 50,025 unique visitors.



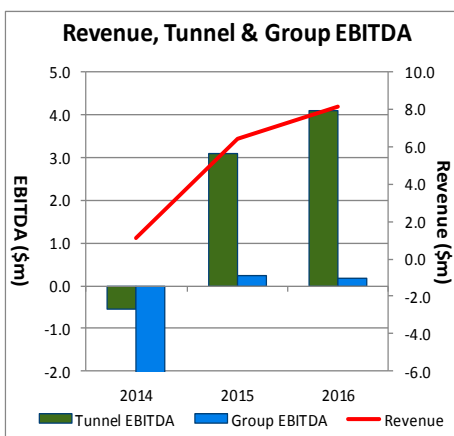
Revenue – Increased by 26.8% to \$8.2m, comprising \$7.9m from tunnels and \$0.3m in other related Revenue. Veritas estimates that Penrith contributed a 6% increase in Revenue to around \$6.5m, with the improvement due to a combination of growth in new flyers, return flyers, professionals and groups/corporate.

The Gold Coast Tunnel opened on 6/2/16 after a 3 month delay, at an increased capital cost of \$13.0m. IDZ is charging a flat \$99 for 2x50 second first timer flights, compared to \$89 weekday and \$109 weekend rates at Penrith. IDZ has only leased 1 of the 4 attached tenancies, with the balance expected to be leased over the next 12 months.

Deferred revenue (prepaid sales) fell by \$0.3m to \$1.0m with the use of some presales for the Gold Coast. We expect pre-sales to increase with the opening of the Perth VWT.

Note: This excludes presales through Adrenalin and Red Balloon and other third party resellers.

Direct Costs – Increased by 20.4%, due to the increase in costs from the inclusion of the Gold Coast, which included lease expenses, employee and related expenses for an extra 3 to 4 months, and ease expenses for Perth. Lease expenses prior to opening are not capitalised.



Tunnel EBITDA – Veritas has estimated that underlying Tunnel EBITDA increased by 33.6% to \$4.1m, with margins of around 50.8%, comprising around 55% for Penrith and around 40% for Gold Coast. EBITDA for FY15 was restated by \$0.2m to include lease costs prior to opening of the Gold Coast tunnel, which had been capitalised.

Head Office Costs – Underlying costs were steady at around \$2.9m pa.

Group EBITDA – Steady at \$0.2m, before share based payments of \$0.5m, related to the issue of performance options to the founders.

Depreciation – Increased with the addition of the Gold Coast tunnel.

Amortisation – Mostly represents the amortisation of the Exclusive Development Agreement at the rate of 40% pa.

One-off items – Covers the issue of \$0.1m in performance based shares to Founders, based on the performance of Penrith. There remains 1.2m performance shares on issue, mainly related various performance measures.

Cash Flow – Operational Cash Flow was positive at \$0.3m even with additional Gold Coast costs, reflecting the strong Cash Flow model. The Net Cash Outflow of \$3.2m followed capex of \$12.7m related to both the Gold Coast and Perth tunnels, partly offset by a \$9.1m increase in Debt.

Balance Sheet – Features include:

- Payables of \$3.4m which includes \$2.0m (non-cash) related to the issue of shares in the Gold Coast and Perth tunnels to SkyVenture.
- An increase in Debt to \$9.1m and an increase in Net Debt to \$6.6m, resulting in gearing (D:E) of 23.3%. IDZ has an existing \$11.1m debt facility in place with Westpac.
- The value of Tunnels increased by \$14.2m to \$38.1m, with the \$12.7m of capex and the Provision for Site Restoration of \$1.6m (amortised over 40 years).
- Deferred Tax Assets of \$1.8m, mostly related to past years tax losses (\$1.5m).
- Pre-sales fell by \$0.3m with tunnel usage. However, these have subsequently increased with pre-sales for Perth.

With Cash on Balance Sheet of \$2.6m, cash flow and unused debt facilities (within the \$11.2 m Westpac facility), IDZ has the resources to complete Perth (around \$6.9m capital commitment) and support ongoing growth.

Balance Sheet has financing capacity

Perth tunnel



Source:IDZ

Tunnels under Development

Perth

IDZ is developing a third tunnel in Perth, on a 3,931 m² site on the Great Eastern Highway between the Burswood Casino and the Perth Airport. IDZ is constructing a 14ft tunnel using the latest technology at a cost between \$14m and \$15m, with over \$7.5m already spent. The tunnel completion and opening is expected towards the end of Q2 FY17, ahead of the peak Christmas holiday period.

Adelaide

IDZ has a preliminary agreement with developers in Adelaide, to fund the construction of a 12ft tunnel.

Other - Further wind tunnels are under consideration in Australia and SE Asia, with IDZ continuing negotiations with a number of potential partners. We suspect the most likely sites are in Malaysia and a second Sydney location. IDZ has developed systems that can be used for the operation of tunnels internationally, linking with its existing systems.

Exclusive Territory Development Agreement (ETDA)

Under the ETDA, SkyVenture has commenced construction of a tunnel in Melbourne, scheduled to be completed in mid-2017, to be marketed under the iFly brand. IDZ has the right to invest \$1m in the tunnel, with an option (subject to approval from SkyVenture) to increase the investment to 50% of total build cost, for a similar return.

Outlook

Penrith – Further growth is expected, helped by:

- Continued growth in First Timers from a large catchment area covering a population of over 1.8m within a 25km radius. This is based on continued awareness through Social Media, including Facebook and Instagram, word-of-mouth and continued media coverage.
- Practice and use during National Championship with 180 competitors across 73 teams, at the end of August. This included a significant number of foreign team and media coverage, further increasing awareness.
- Growth in return flyers, including its frequent flyers club (3 nights a week) and increased corporate and schools usage.

Gold Coast – A strong FY17, with the benefit of:

- July, September and Christmas school holidays, events such as schoolies, V8 Supercars and the Commonwealth Games (2H 2018).
- Increased awareness with advertising campaigns, including Brisbane. The Gold Coast will be launched on Flight Centre and Viator inward bound tourist programs.
- Increased flexibility and optimisation of Gold Coast operations, especially interchange of staff/instructors.
- Take-up of remaining leases.
- Increased professional use, from co-ordination with drop zone operators, especially in the Gold Coast with tandem outdoor skydive operator as a tenant.

Perth - Construction is on schedule for completion before the Christmas period, with equipment under assembly. A highly successful pre-sales campaign in early September raised around \$0.4m.

Perth may also generate sub-lease rental, with further development once the tunnel is completed.

Revenue of \$20m and EBITDA of \$7.4m to be reached in FY18 with full operation of the 3 tunnels

Combined Tunnel Forecasts

The combined forecasts for FY17 and FY18 below include:

FY17 – An extra 7½ months’ contribution from the Gold Coast, including the key Christmas holiday period and an initial 6 months from Perth, adjusted for lease costs ahead of the opening.

FY18 – A full 12 months’ contribution from all 3 VWTs. We have not included any expected additional tunnels.

The treatment of leases ahead of the Perth Tunnel as operating expenses (previously capitalised).

Combined Results/Forecasts		FY15	FY16	FY17	FY18
Combined Revenue	\$m	6.4	8.1	15.6	20.0
<i>Increase</i>	<i>%</i>	<i>481.8</i>	<i>27.1</i>	<i>91.4</i>	<i>28.3</i>
Direct Expenses	\$m	-3.3	-3.9	-7.7	-9.4
<i>Increase</i>	<i>%</i>	<i>na</i>	<i>18.7</i>	<i>96.5</i>	<i>21.9</i>
Combined Facility EBITDA	\$m	3.1	4.1	7.8	10.5
<i>Increase</i>	<i>%</i>	<i>na</i>	<i>32.3</i>	<i>91.0</i>	<i>34.7</i>
<i>Margin</i>	<i>%</i>	<i>48.4</i>	<i>50.4</i>	<i>50.3</i>	<i>52.8</i>
Group Corporate Costs	\$m	-2.9	-3.9	-3.0	-3.1
Group EBITDA	\$m	0.2	0.2	4.8	7.4
<i>Increase</i>	<i>%</i>	<i>-111.3</i>	<i>0.0</i>	<i>1983.4</i>	<i>54.1</i>
<i>Group Margin</i>	<i>%</i>	<i>3.6</i>	<i>2.9</i>	<i>31.0</i>	<i>37.3</i>
Total Amortisation	\$m	-0.5	-0.2	-0.3	-0.2
Total Depreciation & Amortisation	\$m	-0.9	-1.1	-1.4	-1.5
EBIT	\$m	-0.7	-0.9	3.4	5.9
EPS	¢ ps	-0.4	-0.7	2.7	4.6

Source: Veritas

Note: The above Net Profit (before One-offs) forecasts exclude the costs associated with the issue and exercise of performance rights, which are treated as One-Off items.

Valuation

Valuation of \$0.52 ps

We have a valuation for IDZ of \$0.52 ps on a fully diluted basis, based on an EVR model, including:

- Enterprise Value to EBITDA ratio of 8.0x for FY18, the first year of full operation of all 3 tunnels. This is below the weighted average ratio for the key participants in the leisure sector.
- Expected cash of \$3.5m at the end of FY17, with completion of capex on the 3 tunnels. If forecast cash at the end of FY18 is included, the Price Target increases to \$0.52 ps.

VALUATION				
EVR	2018	Breakup Valuation		
	EBITDA	Multiple	\$m	¢ ps
Operations	7.4	8.5	63.3	54
Net Cash/ Debt Adjustment FY18			-2.6	-2
Valuation	\$m		60.7	52
Current Price	cps		42	
Discount			19%	

Source: Veritas

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RATING

BUY – anticipated stock return is greater than 10%
 SELL – anticipated stock return is less than -10%
 HOLD – anticipated stock return is between -10% and +10%
 SPECULATIVE – High risk with stock price likely to fluctuate by 50% or more

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