

1 June 2017

ASX CODE: DTS

Speculative Buy

Capital Structure

Sector	Software & Services
Share Price (A\$)	0.24
Shares (m)	173.5
Options (ex \$0.25, exp. 31/12/2018)(m)	1.5
Performance Shares (m)	25.0
Market Capitalisation (undil) (A\$m)	41.6
Market Capitalisation (dil) (A\$m)	48.0
Share Price Year H-L (A\$)	0.35 - 0.19
Approx. Cash (A\$m)	4.2

Directors

Paul Steele	Chairman
Ido Levanon	Managing Director
Yehuda Shamai	Non-executive Director
Ron Zuckeran	Non-executive Director
Adam Sierakowski	Non-executive Director

Major Shareholders

Founding members (aggregated)	46.7%
Bonale Foundation	4.9%
Religion Gadel Enterprise & Management	3.1%
Bauhmanns	2.8%
Trident Capital Pty Ltd	2.0%

Analyst

Lindsay Grugeon B.E.

Share Price Performance



DRAGONTAIL SYSTEMS

Proven software— set for global rollout

Dragontail Systems Ltd (Dragontail) have spent 4 years and over A\$2.6 million on developing their flagship product, *Algo*, for managing Quick Service Restaurant (QSR) kitchens and dispatching processes. Developed in Israel, it is now in over 200 QSR's. Recently gaining traction in Canada, Dragontail continues a successful rollout to Pizza Hut stores and securing additional accounts. This is the first step in this product being taken up by the thousands of Quick Service Restaurants (QSR) around the world.

The QSR figures are large, here are just a few figures:

- Pizza Hut alone has 7,700 restaurants in the US and 16,400 globally.
- Global QSR revenue of US\$ 600 billion.¹

The Product

The *Algo* software manages and optimizes the kitchen of quick service restaurants, informing staff when to start preparing and cooking each order so that delivery drivers are utilized efficiently and food arrives as hot and fresh as possible. This simultaneously improves the customer experience and reduces costs.

Highlights

- Proven and well tested software.
- Small and solid foothold in a very large industry.
- Rapid growth of food delivery services (global markets have seen much greater adoption than in Australia).
- First mover advantage.
- Installed in variety of businesses e.g. Frozen yoghurt stores and fuel management services.
- The number of users to accelerate as the 'early majority' can see efficiency gains demonstrated by 'early adopters'.

Outlook

The business is well positioned for growth. Given the tens of thousands of QSRs we expect thousands of installations of *Algo* over the next few years, and forecasting a maiden profit in CY2018 This growth aligns with management incentives of performance options that vest only on the company reaching an EBITDA of US\$ 5.5m.

Action and Recommendation

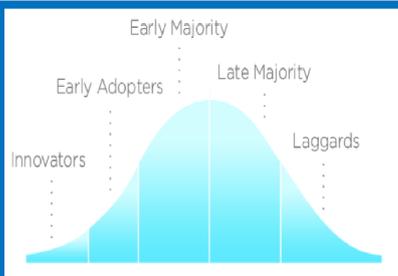
RM Research recommends **Dragontail** as a **Speculative Buy** up to **49 cents**, based on forecast of operating earnings of circa \$8.8m in CY19.

EARNINGS FORECAST	2015A	2016A	2017F	2018F	2019F
Revenue (A\$'000)	146	161	2,640	10,318	21,105
Op. Expenses (A\$'000)	1,119	3,838	3,748	6,353	12,321
Op. Earnings (A\$'000)	-973	-3,677	-1,108	3,965	8,784
Op. Earnings per share(diluted)(c)	-0.5	-1.8	-0.6	2.0	4.4
Price / Op. Earnings	-43	-11	-38	11	5

GROWTH

The 'Technology Adoption Lifecycle' model fits the *Algo* software as there is learning and training costs as well as some perceived risks for a restaurant to switch to using the *Algo* system. Hence, we expect take up to be initially slow in each geographically defined market and in each vertical, until the early adopters demonstrate to their peers and/or competitors the efficiencies gained. The number of users should accelerate (snowball) as the 'early majority' start adopting the *Algo* system.

INDUSTRY OVERVIEW (1)



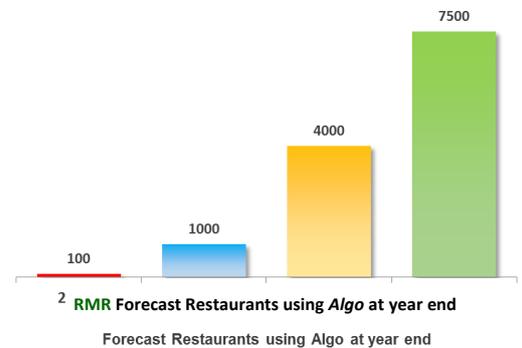
Technology Adoption Lifecycle

The take-up or adoption of new technology often follows the well documented, 'technology adoption lifecycle'. It describes how new ideas or products are first used by innovators and 'early adopters' before being used by the majority which are more conservative. The 'early majority' will only move to the new technology after then can see be successfully implemented by existing peers (one or more of the early adopters). Once a near majority of users of their peers are using the technology the late majority follow out of a fear of being left behind or being left in the minority.

Quick Service Restaurants

The QSR industry is extremely large, with a global market size of over \$600 billion (bigger than the GDP of most countries) and employing over 13 million people worldwide¹. It has grown at a rate of 2.3% per annum. Forward estimates of growth range from 2.5% to 6% CAGR for the next few years.

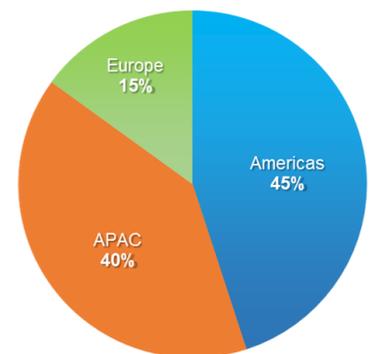
More than 232,000 fast food restaurants dot the United States and approximately 50 million Americans eat at one of them every single day^{2,3}. In the USA, the market is dominated by hamburger restaurants, accounting for over 30% of total sales although this share has been declining with alternatives such as Mexican restaurants edging up in market share².



Online Restaurant Delivery

Restaurant delivery sales in the US have seen double-digit annual growth over the past three to five years, reaching an estimated \$25 billion to \$30 billion in 2016 and accounting for about 5% of the total restaurant market. Recent BCG research found that more than 40% of restaurant users order delivery at least once a month⁵.

It is important for Australian investors to understand how popular online food delivery is in other large economies such as North America and China. Food delivery has always been a significant part of the food consumption market, however, online delivery in Australia is only 22% of total food delivery. Conversely, Australia has one of the highest mobile penetration rates, with 3 out of every 4 Australians owning a smartphone (even back in 2014)⁸. QSR restaurants in other markets deliver many different foods other than just pizza's, e.g. burgers, frozen yoghurt, sushi, etc. Significantly, DTS has demonstrated it can cater for these different product restaurants with frozen yoghurt QSR restaurants in the US successfully using *Algo*.



INDUSTRY OVERVIEW (2)

Delivery models

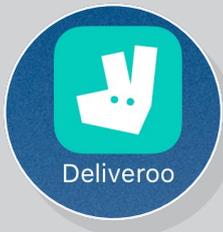
Some QSRs still offer their own home delivery service, i.e. they have their own delivery riders while others use third-party aggregators like Deliveroo and Uber Eats and some use a combination of both.

Recent years have seen many new startups in the food delivery segment due to the soaring popularity of such services. In Southeast Asia, FoodPanda and Deliveroo are two such successful companies with strong customer bases. Worldwide, Deliveroo and UberEats seem to be popular options. However, in the US, UberEats is quite far away from the market leader, Grubhub, which operates services in over 1000 US cities compared to UberEats. Postmates success is attributed to its ability to treat food delivery as a third-party service provider, which has led to exclusive partnerships with companies such as Starbucks. In summary, there are more than 50 recognized digital food delivery providers in the US, but the top two—GrubHub and Yelp Eat24—hold 65% of the market⁵.

Third-party digital aggregators include delivery startups like Deliveroo and UberEats which allow consumers to order restaurant food online or via a mobile app and have them delivered to their homes. These aggregators are said to accelerate the rise of delivery and generate new types of demand. Although aggregators hold only about a 15% share of total delivery sales in the US market today, their total sales have grown at a rate of 50% annually since 2010, and growth is projected to continue at about 30% a year through 2020⁵.

Aggregators follow two primary models: partner and delivery runner. The partner model often links with the brand's point-of-sale (POS) systems for relatively seamless order transfers. Under the delivery runner model, the aggregator's system does not link with the brand's POS systems; instead, consumers place orders through the runner's platform, and the aggregator dispatches the orders to a delivery runner in the field. The runner places each order at the appropriate restaurant, picks it up, and delivers it to the customer. E.g. Favor and DoorDash¹²

The top five QSR aggregators are valued at more than 1 billion!⁹



INDUSTRY OVERVIEW (3)

Competition

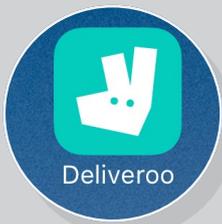
DragonTail appears to have first mover advantage. We expect others to enter this market as *Algo* becomes a victim of it's own success as the concepts are widely adopted, attracting other entrants. Given the size of the market, several competing products should be able to coexist at profitable margins.

The only direct competitor we could find was small Australian company, Delivery Command. Their product is significantly less developed, it's main feature is driver tracking and hasn't taken the next step of optimizing the kitchen operations. Another software provider in a similar space is QSR Automations base in Louisville, Kentucky. They have developed a suite of applications for restaurants that assist managing tables and bookings as well as an application that goes some way to managing kitchens.

Many other companies have focused on providing a market place for online delivery. E.g. **UberEats**, **Deliveroo** and **GrubHub**. These companies have not optimized driver deliveries with multiple orders and don't offer solutions for managing the kitchens producing the goods.

There are also many Point of Sale solution providers. It seems feasible that their software could be expanded in to managing the kitchen flows, however it appears they haven't taken this focus yet.





References:

1. www.ibisworld.com/industry/global/global-fast-food-restaurants.html
2. www.franchisehelp.com/industry-reports/fast-food-industry-report/
3. www.statista.com/topics/863/fast-food/
4. www.businessinsider.com/ubereats-should-thrive-in-this-market-where-it-justdebuted-2016-5?IR=T&r=US&IR=T
5. www.bcgperspectives.com/content/articles/technology-digital-how-digital-deliveryputs-the-restaurant-value-chain-up-for-grabs/?chapter=2
6. www.statista.com/outlook/376/100/restaurant-delivery/worldwide#marketglobal
7. www.statista.com/outlook/374/100/food-delivery/worldwide#market-global
8. PMA Retail Trends, June 2104
9. www.mckinsey.com/industries/high-tech/our-insights/the-changing-market-for-food-delivery

THE ALGO DISPATCHING SYSTEM

What is “Algo”?

Using a sophisticated patent-pending optimization algorithm, the Algo optimizes and manages the entire process starting from food preparation all the way to its delivery to the customer, streamlining the food preparation and delivery processes.

The Algo Dispatching System is the only system in the world that fully automates the kitchen flow combined with the process of dispatching drivers.

The system is equivalent to smart manager that is looking at every single order location, every driver location, every meal status in the kitchen and the pack station, and manages the order of the items that need to be prepared in the kitchens as well as makes dispatching recommendations.

QSR's are busy businesses, where things are changing so fast, with many details to look out for and multiple tasks that managers have to handle at once, The "Algo" is calculating in real-time, and in the background, whilst displaying the best possible decisions both in the kitchen and on the dispatching station.

Customers report:

- **Decreased labour costs**
- **Increased repeat customers**
- **Increased sales**
- **Improved delivery times**
- **1,320% ROI !**

www.dragontailsystems.com

Benefits Of “Algo”

Dragontail's technology totally changes the restaurants operations and management concepts in Fast Food/QSR industry. The food preparation, delivery, marketing operations and Customer Relationship Management (“CRM”) are integrated into a single GPS-based algorithm and management software, which optimizes, manages and controls the operations chain in the restaurant.

◆ **Operational Efficiency**

The system assists in optimal personnel assignment (from food preparation to delivery) as well as delivery route optimization.

◆ **Costs Reduction**

Efficient labor allocation, reduced chargebacks by customers, increased customer retention and increased sales volumes.

◆ **Customer Satisfaction**

Out of Oven, Out the Door™ - timely delivery of a quality product combined with a personalized targeted marketing (personalized inserts, bonuses, etc). The system allows to identify and manage late deliveries ahead of time and to address customer dissatisfaction by offering free coupons, bonuses and additional products.

◆ **Management & Control**

Real time employee control management system accessible through any platform: PC, mobile, Ipad. Detailed alerts and reporting system, which provides valuable real time data about employees' productivity, late deliveries, problems during preparation or other “events” as defined by the manager.

Operating Earnings Forecast and Valuation

Income Model (A\$'000s)	Notes	2015A	2016A	2017F	2018F	2019F
Revenue	1	146	161	2640	10318	21105
Research and development expense	2	863	1185	1421	1706	2047
Selling and marketing expenses	3	165	584	1461	3652	9129
General and administrative expenses	4	91	753	866	996	1145
Share based payment expense			1316			
Total operating expenses		1119	3838	3748	6353	12321
Operating profit/loss		-973	-3677	-1108	3965	8784

Revenue Forecasts

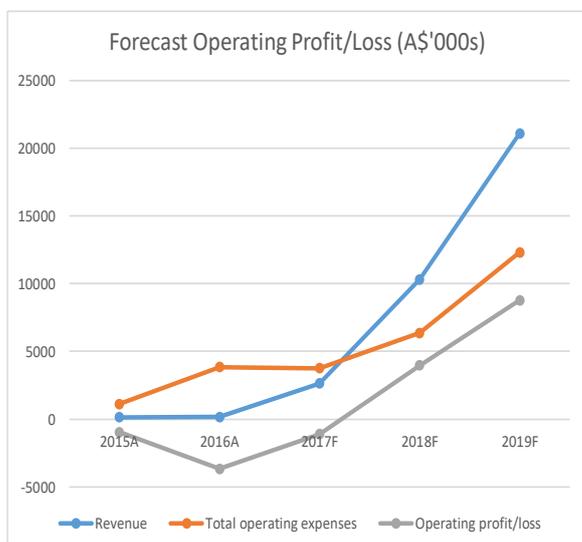
	Notes	2015A	2016A	2017F	2018F	2019F
Number of QSR's at year end	5		100	1000	4000	7500
Reoccurring revenue	6			1769	8040	18492
Revenue from POS integrations	7			268	268	268
Setup fees	8			603	2010	2345

Float	Notes	
Current shares on issue		173,500,000
Performance options		25,000,000
Options		1,500,000
		200,000,000

Valuation (A\$ '000s)	Notes	per share (diluted)
US/AUD exchange rate		1.34
Estimated EV in 2019		131,760
Opportunity Cost of Capital		8%
Present Value		108,699
Risk adjusted Present Value (25% discount)		81,524
gain over present value		69.8%

Notes

- Revenue figures for 2017 onwards derived from summation of forecasts of reoccurring revenue, POS integration fees and setup fees
- Research and Development expense forecasts assume compound yearly growth of 20%
- Selling and Marketing expense forecasts assume compound yearly growth of 150% (this includes cost of training staff new stores)
- General and Administrative expense forecasts assume compound yearly growth of 15%
- Cumulative restaurants at year end assumes 7500 restaurants are using Algo by end of CY19. We believe this is an attainable figure given the numbers of Pizza Hut restaurants and other QSR restaurants, both in North America and globally.
- Reoccurring revenue assumes average monthly charge of \$268 (US\$ 200) per restaurant.
- Revenue from POS integrations assumes there are 4 integrations per year with an average charge of \$67,000 (US\$ 50,000).
- Setup fees figures assume average charge of \$670 per new restaurant.
- Assuming this company will still be considered in 'growth phase' in 2019 we've used a valuation multiple of 15 times operating profit.
- Assumed a US\$/AUD\$ exchange rate of 1.34.





Paul Steele

Non-Executive Chairman

Paul Steele has executive level experience in software technology, property development, management consulting, not-for-profit, healthcare, telecommunication and charitable foundations, and has served as a director on both for-profit and not-for-profit boards.

Paul is a graduate member of the Australian Institute of Company Directors.

Paul is currently holds the following directorships:

- Executive Chairman of The Difference Incubator Ltd;
- Director of Benefit Capital Pty Ltd and Ethical Property Australia Pty Ltd;
- Director of Insights Systems LLC (USA), a contract execution management software as a service company that Paul founded; and
- Advisory Board Member of the Australia Advisory Board to the G8 Impact Investment Taskforce.

Paul is a graduate member of the Australian Institute of Company Directors.



Ido Levanon

Managing Director

Ido has 20+ years' experience and proven track record in successful management and turnaround of various international companies. He was CEO and seed investor in several technology start-ups. Financial Planning Manager for Fujitsu USA (managed the merger of Fujitsu and ICL).

Ido also served as a captain in the Israeli Armed Forces for the artillery corps, commanding over 120 soldiers and officers.

Ido holds MBA San Diego University (1989, Magna cum laude), B.Sc. Math & Computer Science Tel Aviv University.

He has been part of DT Israel since its inception in 2013 as one of the founding investors.



Yehuda Shamai

Non-Executive Director

Yehuda Shamai has established and managed large Israeli entities with international brands such as Pizza Hut, KFC and Domino's Pizza.

In the past, Yehuda served as Business Development Manager for Israel Corporation Ltd and as such has been involved in some of the largest mergers and acquisitions in Israel.

Yehuda has a vast knowledge of management software tools and e-payments, and is involved as a director and investor in several existing companies and startups developing and marketing advanced physical and virtual payment solutions.



Adam Sierakowski

Non-Executive Director

Adam Sierakowski is a lawyer and a founding director of the legal firm Price Sierakowski. He has over 20 years of experience in legal practice, much of which he has spent as a corporate lawyer consulting and advising on a range of transactions to a variety of large private and listed entities.

Adam is also a co-founder and director of Perth based corporate advisory business, Trident Capital, where for 15 years he has advised a variety of large private and public companies on structuring their transactions and coordinating fundraisings both domestically and overseas.

Adam has held a number of directorships with ASX-listed companies, and he is a member of the Australian Institute of Company Directors and the Association of Mining and Exploration Companies.



Ron Zuckerman

Non-Executive Director

Ron Zuckerman has been active as a tech entrepreneur and investor for most of the last 25 years.

Ron was one of the founders of Sapiens International, a software company he took public on NASDAQ in 1990 and which is currently trading with a market cap of over \$700m. Ron acted as Chairman and CEO of Sapiens from early 1995 until late 1999.

He was the founder and Executive Chairman of Precise Software Solutions, another software company he took public on NASDAQ in 2000, until its acquisition in late 2003 by VERITAS in a cash transaction valued at over \$600 Million.

Ron was a founder, first round investor and a board member in GVT Holding SA, a large telephone operator in Brazil until it's acquisition in late 2009 by The Vivendi Group of France for over \$4.7 Billion. Ron was an early investor and a board member at Wintegra Inc. which was acquired in 2010 by PMC Sierra for over \$200m.

In 2000, Ron was chosen by the World Economic Forum as leading one of the most influential tech ventures (i.e. Sapiens), together with such individuals as Masayoshi Son of SoftBank Group, Jerry Yang of Yahoo! and Michael Dell of Dell Computers.

Registered Offices

Perth

Level 1, 143 Hay St
Subiaco WA 6008

PO Box 154
West Perth WA 6872

Email / Website

info@rmresearch.com.au
www.rmresearch.com.au

Phone : +61 8 6380 9200

Fax : +61 8 6380 9299

RM Research Recommendation Categories

Care has been taken to define the level of risk to return associated with a particular company. Our recommendation ranking system is as follows:

Buy	Companies with 'Buy' recommendations have been cash flow positive for some time and have a moderate to low risk profile. We expect these to outperform the broader market.
Speculative Buy	We forecast strong earnings growth or value creation that may achieve a return well above that of the broader market. These companies also carry a higher than normal level of risk.
Hold	A sound well managed company that may achieve market performance or less, perhaps due to an overvalued share price, broader sector issues, or internal challenges.
Sell	Risk is high and upside low or very difficult to determine. We expect a strong underperformance relative to the market and see better opportunities elsewhere.

Disclaimer / Disclosure

This report was produced by RM Research Pty Ltd, which is a Corporate Authorised Representative (343456) of RM Capital Pty Ltd (Licence no. 221938). RM Research received a payment for the compilation and distribution of this research report. RM Research Pty Ltd has made every effort to ensure that the information and material contained in this report is accurate and correct and has been obtained from reliable sources. However, no representation is made about the accuracy or completeness of the information and material and it should not be relied upon as a substitute for the exercise of independent judgment. Except to the extent required by law, RM Research Pty Ltd does not accept any liability, including negligence, for any loss or damage arising from the use of, or reliance on, the material contained in this report. This report is for information purposes only and is not intended as an offer or solicitation with respect to the sale or purchase of any securities. The securities recommended by RM Research carry no guarantee with respect to return of capital or the market value of those securities. There are general risks associated with any investment in securities. Investors should be aware that these risks might result in loss of income and capital invested. Neither RM Research nor any of its associates guarantees the repayment of capital.

WARNING: This report is intended to provide general financial product advice only. It has been prepared without having regarded to or taking into account any particular investor's objectives, financial situation and/or needs. Accordingly, no recipients should rely on any recommendation (whether express or implied) contained in this document without obtaining specific advice from their advisers. All investors should therefore consider the appropriateness of the advice, in light of their own objectives, financial situation and/or needs, before acting on the advice. Where applicable, investors should obtain a copy of and consider the product disclosure statement for that product (if any) before making any decision.

DISCLOSURE: RM Research Pty Ltd and/or its directors, associates, employees or representatives may not effect a transaction upon its or their own account in the investments referred to in this report or any related investment until the expiry of 24 hours after the report has been published. Additionally, RM Research Pty Ltd may have, within the previous twelve months, provided advice or financial services to the companies mentioned in this report. As at the date of this report, the directors, associates, employees, representatives or Authorised Representatives of RM Research Pty Ltd and RM Capital Pty Ltd may hold shares in this company.