



Freelancer Ltd (FLN.ASX)

New product and new business to offer synergies

Event:

- We review FLN's launch of Local Jobs and its purchase of Escrow.com.

Investment Highlights:

- Local Jobs.** Last month FLN announced the launch of local jobs – its entry into the burgeoning online local services market. In addition to hiring workers from anywhere in the world to undertake work on-line, hirers can choose a freelancer to undertake a local job on-premises.
- Local services a US\$400b-\$745b market.** MBO Partners estimated that of the US\$1.2 trillion jobs undertaken by US independent workers, 64% or US\$745b was conducted within the local metro area. Angie's List estimates globally it is worth US\$400b. These figures are up to 10x larger than FLN's estimates of the global online freelancing market.
- A number of players exist in the online local services market, TaskRabbit being the most prominent. Amazon itself recently launched Amazon Home Services,** which offers over 700 services, testimony to the lucrativeness of the market.
- While the market is large, scalability is an issue due to constraints posed by geographic constraint of services offered being local. In essence each new metro area or city is a vertical. TaskRabbit, despite being founded in 2008, is present in only 20 cities in the USA.
- FLN and Amazon have existing users that they can market local services to, making it attractive and synergistic.** This significantly lowers their cost of customer acquisition vs competitors. TaskRabbit and other local service providers do not enjoy these advantages. FLN has 15M users.
- Escrow.com.** In April FLN also announced the purchase of Escrow.com, a leading provider of secure on-line payments, for US\$7.5M funded from a A\$10M placement. Escrow.com acts as a secure third party that collects, holds and releases fund according to buyer and seller instructions. This is critical where valuables such as autos, jewellery, antiques, and domain names traded online.
- Escrow.com is used by major marketplaces such as eBay (since 2002) and cars.com, and freighters such as FedEx.** FY14 revenues were US\$5M and EBITDA US\$1.2M. We expect that FLN management will be able to grow revenues more aggressively than what Escrow.com has achieved in the past few years.

Earnings and Valuation:

- We have incorporated Escrow.com in our model.** While sales forecasts have increased, there is no material change to our NPAT forecasts in the next four years, as we assume any earnings will be channeled into investing in both Escrow.com and the core business. However our NPAT forecasts post 2019 have increased. We have made no changes due to Local Jobs at this stage.
- Our valuation has increased to \$1.60/share from \$1.35.** This is due to 1) Adopting a purely DCF approach; 2) Rolling forward our model by six months; and 3) The longer term earnings impact of Escrow.com. These more than offset the dilutionary impact of the recent share placement on our NPV.

Recommendation

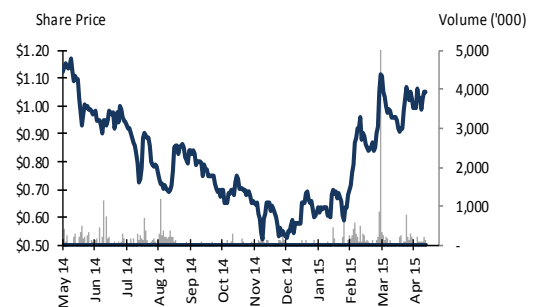
- We maintain our Buy recommendation and increase our price target to \$1.60/share** in line with our updated valuation.

Recommendation	Buy
Previous	Buy
Price Target	\$ 1.60
Previous	\$ 1.35
Share Price (A\$)	1.01
ASX Code	FLN
52 week low - high (A\$)	0.515-1.19
Valuation	\$1.60/share
Methodology	DCF
Risk	Med
Capital structure	
Shares on Issue (M)	444.2
Market Cap (A\$m)	448.6
Pro-forma Net Debt/(Cash) (A\$m)*	-22.5
EV (A\$m)	426.1
12mth Av Daily Volume ('000)	179.2

* Assumes Escrow.com consideration is paid

Y/e Dec est.	2014a	2015e	2016e	2017e
Revenue A\$m	25.7	38.0	57.4	67.5
Revenue growth	39%	48%	51%	18%
NPAT A\$m	-1.8	-0.2	-0.3	-0.3
EV/sales	16.7x	11.4x	7.3x	6.2x

Share Price Graph



Analyst: Mark Fichera
mark.fichera@fostock.com.au

+61 2 9993 8162



Freelancer Ltd (FLN)

Full Year Ended 31 December

Profit and Loss A\$M	2014a	2015e	2016e	2017e
Sales revenue	25.7	38.0	57.4	67.5
Other revenue	0.2	0.3	0.4	0.5
Operating Costs	28.2	38.3	57.9	68.0
EBITDA	-2.1	0.0	0.0	0.0
D&A	0.3	0.4	0.7	0.8
EBIT	-2.4	-0.4	-0.7	-0.8
Net Interest exp / (income)	0.0	-0.2	-0.3	-0.4
Profit before tax	-2.8	-0.2	-0.4	-0.4
Tax exp / (benefit)	-1.0	-0.1	-0.1	-0.1
NPAT before minorities	-1.8	-0.2	-0.3	-0.3
Minority interest	0.0	0.0	0.0	0.0
Rep. NPAT	-1.8	-0.2	-0.3	-0.3
Significant items	0.0	0.0	0.0	0.0
NPAT attributable reported	-1.8	-0.2	-0.3	-0.3
EPS diluted (c)	4.8	0.2	-0.4	0.0

Cashflow A\$M	2014a	2015e	2016e	2017e
EBITDA	-2.1	0.0	0.0	0.0
Change in WC	1.8	6.2	15.0	4.2
Tax paid	-0.2	0.1	0.1	0.1
Net interest	0.2	0.2	0.3	0.4
Other	0.2	0.2	0.2	0.2
Operating Cashflow	-0.1	6.7	15.6	4.9
Acquisitions	-4.1	-9.6	0.0	0.0
Capex	-0.9	-0.7	-0.8	-1.0
Investing Cashflow	-5.0	-10.3	-0.8	-1.0
Financing Cashflow	-0.1	10.0	0.0	0.0
Net Cashflow	-5.2	6.4	14.8	3.9

Balance Sheet A\$M	2014a	2015e	2016e	2017e
Cash	20.2	26.6	41.4	45.3
Receivables	3.0	4.7	7.0	8.3
PPE	1.1	1.3	1.4	1.6
Intangibles	13.0	22.6	22.6	22.6
Deferred tax	1.8	1.8	3.1	3.4
Other	1.2	1.8	2.7	3.2
Total Assets	40.2	58.7	78.3	84.3
Accounts payable	21.8	29.6	47.0	52.4
Provisions	1.2	1.6	2.5	2.9
Deferred revenue	0.4	0.6	0.9	1.0
Other	0.0	0.2	1.6	1.9
Total Liabilities	23.4	32.1	51.9	58.2
Reserves and capital	17.6	27.6	27.6	27.6
Retained earnings	-0.8	-1.0	-1.2	-1.5
Total Equity	16.8	26.6	26.4	26.1

Source: Company; Foster Stockbroking estimates

Financial Metrics	2014a	2015e	2016e	2017e
Sales growth %	39%	48%	51%	18%
EPS growth %	nm	nm	nm	nm
EBITDA margin	-8%	0%	0%	0%
EBIT margin	-9%	-1%	-1%	-1%
Gearing (ND/ND+E)	nm	nm	nm	nm
Interest Cover (EBIT/net int)	nm	nm	nm	nm
Average ROE %	-10%	-1%	-1%	-1%
Average ROA %	-14%	-2%	-3%	-3%
Wtd ave shares (M)	404	441	444	444
Wtd ave share diluted (M)	437	445	449	449

Valuation multiples	2014a	2015e	2016e	2017e
P/E x	nm	nm	nm	nm
EV/EBITDA x	nm	nm	nm	nm
EV/EBIT x	nm	nm	nm	nm
EV/sales x	16.7	11.4	7.3	6.2
Dividend yield %	0	0	0	0

Equity Valuation - DCF	A\$M	A\$/share
Enterprise value	6	1.55
Net debt (cash)	23	0.05
Equity (NPV)	727	1.60

Shares on issue	M
Ordinary shares	444.2
Options	4.3
Fully Diluted	448.5

Major shareholders	Interest
Matt Barrie	44.7%
Simon Clausen	38.4%
Darren Williams	2.8%

Board	
Matt Barrie	CEO & Chairman
Simon Clausen	Non Executive Director
Darren Williams	CTO & Executive Director



LAUNCH OF LOCAL JOBS MARKETPLACE

FLN launches Local Jobs, with 100 location-specific skills such as pickup & delivery, photography, & electricians.

- On the 20th April Freelancer announced it had launched *Local Jobs* – its entry into the burgeoning local services market. In addition to hiring workers or freelancers from all over the world to undertake work on-line, an employer (or poster) on Freelancer.com can now hire someone to work locally – whether to undertake delivery of products or to perform a service on-site.
- The company has begun rolling the product first in Australia, and then gradually across all sites. After selecting “Hire” on the homepage, users have the option to choose if their job is location specific or not. Location specific jobs will be matched with the hirees - or freelancers – within the local area
- FLN will use location specific data as part of matching hirees with hirers. Users can see a map of where workers or hires are located, in addition to their ratings and profile and then use this information to select a local hiree.
- FLN will categorise over 100 location-specific skills, including:
 - **Location-based tasks (pick-up and delivery, removals);**
 - **Trades (electricians, plumber, carpenter builder); and**
 - **Professions (event management, catering, photography).**

LOCAL JOBS MARKET SIZE – ESTIMATES RANGE FROM US\$400B to US\$745B

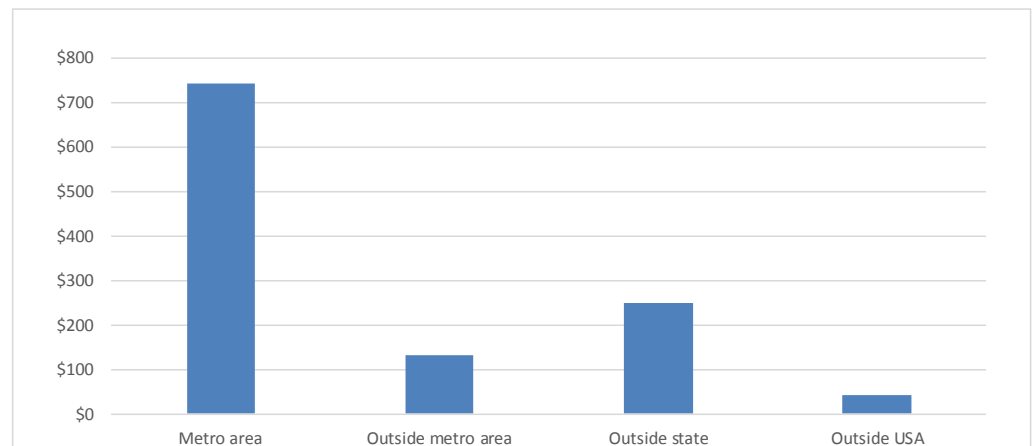
Estimates of the local jobs market range from US\$400b to US\$745b...

- Local jobs encompass a broad range of activities and trades, from unskilled labour to skilled professionals. These can run the gamut from simple, unskilled tasks like collecting laundry, walking the dog, picking up and delivering goods, running errands, to cleaning, removals, installation of home consumer electronics systems, furniture assembly, to more trade/profession orientated work provided by painters, plumbers, interior designers, photographers, electricians, and builders.
- MBO Partners estimated there is 17.9M independent workers in US which generated US\$1.2 trillion during 2014 [“The State of Independence In America”, 4th Annual Independent Workforce Report]. Independent workers included contractors, freelancers, consultants, the self-employed, temps, small businesses with less than four employees, and on-call workers.
- MBO further estimated a breakdown of the \$1.2 trillion market by job location, showing that local jobs comprised ca. 64% of all work, or \$745b (Figure 1).
- Other estimates of local services are similarly large. In 2011, Angie’s List (NASDAQ:ANGI, Market cap US\$342M), a reviewer of services, estimated the global home services industry which includes electricians, plumbers, dog walkers and other manual labour is worth US\$400b p.a.
- The estimates are significantly larger – up to an order of magnitude greater - than the US\$75b FLN has previously assumed for the global on-line freelancing market.

.. these are up to 10x larger than FLN’s estimates of the global online freelancing market.



Figure 1: US Independent Worker Revenues (US\$b) by Location of Jobs in 2013



Source: MBO Partners; Foster Stockbroking estimates.

PRICING MODEL FOR LOCAL JOBS TO BE SIMILAR TO EXISTING STRUCTURE

FLN to maintain same pricing model.

- We understand that FLN will use its existing freelancing pricing model for Local Jobs – i.e. a range of membership packages and fees charged to both poster and local service provider. This will minimise disruption to its model and maintain uniformity and simplicity for its users. FLN’s current take rate is 25% of freelancing projects – this includes 3% and 10% fees charged on freelancers and posters, as well as user upgrades and memberships. This lies well within the range of most on-line local services providers which charge fees of 10% to 40%. Local Jobs will also leverage many of FLN’s website functionalities, such as the Milestone Payment System.

LOCAL SERVICES ONLINE – RIPE FOR AGGREGATION, ATTRACTING TECH GIANTS

- Figure 2 shows some of the major pure online local services marketplaces. The first prominent company was TaskRabbit, which launched in 2008, and is still the most well-known. In the past seven years it has rolled out its product in 20 cities across the USA and has about 30,000 taskers offering services. Most jobs revolve around the home and range from low skilled to trades/professions - cleaning, deliveries, errands, installations, painting, plumbing, home improvements, and lessons.

Figure 2: Major On-line Marketplaces For Local Services

Company	Founded	Cities	Countries	Major Local Services Offered	Comments
TaskRabbit	2008	20	USA	Home	Partnering with Amazon Home Services
Thumbtack	2009	50 states	USA	Home, events, lessons, wellness	\$100M Google investment in 2014
Zaarly	2011	3	USA	Home	
Airtasker	2012	3	Australia	Home, events, catering, trades	
Homejoy	2012	30	USA, UK	Home	Google investment in 2013
Handy	2012	37	USA, Canada, UK	Home, moving, cleaning	
Hassle	2012	6	UK	Cleaning	Accel investment in 2014
Bizzby	2013	1	UK	Local, cleaning, trades	
Pro.com	2013	1	USA	Home improvements	Jeff Bezos investment
Homlux	2014	1	USA	Home	Partnering with Amazon Home Services
Amazon Home Services	2015			Home, professionals, lessons, auto	

Source: Companies; Foster Stockbroking estimates.



Amazon entering local services market is testimony to the lucrativeness and size of the market.

- In addition to the pure local jobs providers, there are sites such as Angie's List and Yelp (NYSE:YELP, Market cap US\$3.0b), which offer reviews of local services, and Craigslist where provider list but are not rated or vetted,
- Probably the most important milestone in the sector has been the launch of Amazon Home Services (AHS) this year by Amazon (NASDAQ:AMZN, Mkt cap US\$197b). While previously Google (NASDAQ:GOOG, Mkt cap US\$188b) and Amazon Jeff Bezos have undertaken investments in the sector, AHS represents the first direct entry into the market, and underscores the attractiveness of the huge market size. AHS will offer over 700 local services, including from licensed professionals.
- Home Depot (NYSE:HD, Market cap US\$142b) has also entered the market via its subsidiary Redbeacon, which offers online local services specialising in home improvements and renovations.

SCALABILITY CHALLENGES FAVOUR ESTABLISHED NETWORKS SUCH AS FLN

- The increasing popularity of accessing local services via one-stop online portal has resulted in a number of entrants into the market. However the signing up of enough service providers to enable scale, liquidity, and make the service attractive to hirers can be a lengthy process. This is because scalability is limited by the geographic constraint imposed by the service offered being local. Each new local area or city is a vertical that needs to be built. Companies are rolling out in (typically) their home cities first, then repeating in other cities.
- A trend that has started is aggregation of aspect local service marketplaces. This is logical given the number of local services already in existence, and the frequent absence of local area overlap. TaskRabbit and the New York local service provider Homlux have both have partnered with Amazon by allowing their services to be offered through AHS, who acts as an aggregator.

Like Amazon, FLN has the advantage of a large existing customer base to leverage local services. This minimises the scalability and customer acquisition challenges faced by other players.

THE ASSET THAT DERISKS LOCAL JOBS – A GLOBAL 15M REGISTERED DATABASE

- Local Jobs is a logical addition to FLN's product offering. While Local Jobs is a new product, FLN has the advantage of a large existing user database that it can instantly promote its offering to. It is the same rationale that Amazon is using. For example, Amazon has 85M customers that purchase products requiring installation – this would be a low acquisition cost as it targets these customers for local service say on checkout. FLN offers local jobs to its 15m users as one if it options in posting or selecting jobs.
- Starting from scratch, as other local jobs providers have done such as TaskRabbit, involves significant marketing and customer acquisition costs in building scale to make the business profitable. The low hanging fruit are existing customers. Cost of acquisition, and the investment and growth challenges that were and are faced by TaskRabbit, are reduced. Many competitors are regionally focused in across cities or countries only, while FLN advantage is rolling out globally.



PURCHASE OF ESCROW.COM

Escrow.com is a leading secure online payments escrow service.

- FLN announced the acquisition of Escrow.com, a leading provider of secure online payments, ON 27 April 2015 for US\$7.5M cash. Escrow.com acts as a secure third party that collects, holds, and releases funds according to buyer and seller instructions. Escrow services provided by the company are regulated and licensed. This is critical where large transaction are involved online – for example online purchase of valuable goods, such as automobiles, jewellery, antiques, and domain names. FLN used Escrow.com when it bought Warrior forum last year, and we understand it was then that FLN began considering Escrow.com as a potential acquisition
- In many ways escrow online is an alternative to the traditional letter of credit documentation used in purchasing valuable goods, being a speedier and less cumbersome process with minimal bank involvement. Escrow.com tracks and confirms shipments, deliveries, and receipt of funds for buyers and sellers. We see opportunities for Escrow.com in both off-line and on-line worlds.
- Online businesses which use Escrow.com include eBay (since 2002), FedEx, cars.com, goDaddy, and autoTrader.com. Escrow.com achieved FY14 gross payment volumes of US\$265M, net revenue US\$5M, and US\$1.2M EBITDA. The company is headquartered in California and was founded in 1999 by Fidelity National Financial (NYSE:FNF, Mkt cap US\$10b). The company was eventually bought by a private investor in 2004, from whom FLN is purchasing it.

Escrow.com is used by eBay, FedEx, and cars.com.

OPPORTUNITY FOR FLN – INCREASE REVENUE GROWTH AND ENHANCE MARGIN

Synergies exist between payments systems and marketplaces.

- FLN’s purchase of Escrow.com is strategic and synergistic. Benefits include:
 - **Aligning and modifying Escrow.com’s payments platform so it better matches with the requirement of FLN’s customers and other third party business users.** A salient example of a marketplace acquiring a payment system was eBay’s purchase of Paypal. As with Paypal, FLN will continue to run Escrow.com as a standalone business. This is especially important in growing business with third parties
 - **Adding value to Escrow.com from FLN management experience.** The revenue growth of Escrow.com in the past two years falls well short of what one would expect in a dynamic online payments field (Figure 3). Escrow.com’s low margin indicates ample opportunity for FLN to enhance this given its track record; and
 - **The continuing growth of online marketplaces and internet penetration,** especially in developing economies, should feed into Escrow.com’s future potential.

Figure 3: Escrow.com Historical Financials

Year	Net Revenue US\$M	Growth
2010	3.3	
2011	4.1	26%
2012	4.6	13%
2013	4.8	3%
2014	5.0	5%

Source; FLN; Foster Stockbroking estimates.

Escrow.com’s recent revenue growth has been less than stellar. We expect FLN to improve sales growth and margin.

- We expect the acquisition to begin contributing in 2H 2015 post settlement. The purchase is subject to regulatory approvals and we expect closure by end July 2015.

**CAPITAL RAISING – IMPROVES FREE FLOAT AND FUNDING**

Capital raising funds acquisition while leaving enough cash to grow business. Free float improves as well.

- FLN recently completed a share placement of A\$10M, comprising 10M shares at \$1.00, the primary purpose of which was to fund the Escrow.com purchase. Even though the company had more than sufficient cash on its balance sheet (>\$22M), we believe most of it is already earmarked for investment in the business. Another benefit of the placement is improving FLN's freefloat, rising to 12.4% from 10.4%, since no directors participated in the placement.

Figure 4: FLN Major Shareholders Post Placement

Shareholder	Post-placement	Previous
Matt Barrie	44.7%	47.3%
Simon Clausen	38.4%	40.6%
Darren Williams	2.8%	2.9%
Total	85.9%	90.8%

Source: Company; Foster Stockbroking estimates.

Earnings revisions – NPAT forecast unchanged in near-term, but increase in long-term.

EARNINGS REVISIONS – INCREASE IN SALES BUT NPAT UNCHANGED IN NEAR-TERM

- We have incorporated Escrow.com in our model. We conservatively assume sales growth of 4% p.a. for this business. However we believe risk to revenue growth is to the upside, especially under the stewardship of FLN. At the EBIT level we assume break-even, expecting that Escrow.com's earnings will be funnelled into marketing and development costs for both it and the exiting FLN business over the next four years. Consequently, our NPAT estimates are materially unchanged for the next four years. However post 2019 our earnings forecasts have increased.
- We have not changed any of our estimates due to the launch of Local Jobs at this stage, adopting a conservative approach. Again, we believe risk lies to the upside.

VALUATION – INCREASES to \$1.60 FROM \$1.35

Valuation \$1.60/share by DCF.

- Our valuation of FLN has increased to \$1.60/share, up from \$1.35/share. Reasons for increase are:

1. Adopting a pure DCF methodology. Previously we used an equally blended DCF and Sales Multiple approach (+\$0.11/share);
2. Rolling forward our DCF model by six months (+\$0.09);
3. Incorporating Escrow.com in our model, which increases earnings longer-term (+\$0.09);
4. These increases are offset partially by the dilutionary impact of the placement shares on our DCF (-\$0.04/share).

Buy Recommendation maintained, and 12-month price target increases to \$1.60/share.

RECOMMENDATION – BUY WITH PRICE TARGET \$1.60/SHARE

- We maintain our Buy recommendation and increase our 12-month price target to \$1.60/share from \$1.35/share, in-line with our valuation.



FOSTER STOCKBROKING DIRECTORY

Name	Role	Phone	Email
Stuart Foster	Chief Executive Officer	+61 2 9993 8131	stuart.foster@fostock.com.au
Chris Francis	Executive Director	+61 2 9998 8167	chris.francis@fostock.com.au
Haris Khaliqi	Executive Director	+61 2 9993 8152	haris.khaliqi@fostock.com.au
Martin Carolan	Executive Director	+61 2 9993 8168	martin.carolan@fostock.com.au
Mark Fichera	Executive Director	+61 2 9993 8162	mark.fichera@fostock.com.au
Mark Hinsley	Executive Director	+61 2 9993 8166	mark.hinsley@fostock.com.au
Kevin Massey	Senior Equities Dealer	+61 2 9993 8130	kevin.massey@fostock.com.au
Tolga Dokumcu	Execution & Dealing	+61 2 9993 8144	tolga.dokumcu@fostock.com.au
George Mourtzouhos	Execution & Dealing	+61 2 9993 8136	george.mourtzouhos@fostock.com.au

Foster Stockbroking Pty Ltd
A.B.N. 15 088 747 148 AFSL No. 223687
Level 25, 52 Martin Place, Sydney, NSW 2000 Australia
General: +612 9993 8111 Equities: +612 9993 8100 Fax: +612 9993 8181
Email: contact@fostock.com.au
PARTICIPANT OF ASX GROUP

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