

Kidoz Inc.

(TSXV: KIDZ / OTC: KDOZF)

Q3 Revenue up 161% QoQ and Beats Expectations

BUY

Current Price: C\$0.52

Fair Value: C\$1.08

Risk*: 4

Sector/Industry: Mobile Games

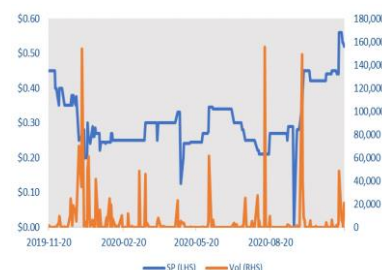
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Highlights

- Q3 revenue was \$1.9M, up 161% QoQ, and 51% YoY. We were **pleasantly surprised by the spike in revenue** as the outlook for ad spending this year had been weak due to the pandemic.
- Gross margin improved YoY (from 41% to 48%), and EBITDA turned positive to \$0.3M in Q3. Kidoz reported \$0.12M in net profit (EPS: \$0.00), making Q3 the first profitable quarter since 2013.
- The company has been able to continue to streamline operations; SG&A expenses were down 7% YoY in Q3. We were expecting higher SG&A expenses in the quarter.
- We are raising our EPS projections for 2020 and 2021. **We expect revenue to grow QoQ in Q4, as Q4 has historically been the best quarter.**
- Global digital ad spending in 2020 is expected to increase 2.4% in 2020, and 17.0% in 2021 (Source: eMarketer).
- KIDZ's share price is up 147% since our previous report in August 2020. Stay-at-home-stocks have been negatively impacted by the recent positive news surrounding vaccines for the pandemic. However, we believe that Kidoz's fundamentals remain sound especially because of the growing market for kids aged two to 11 using smart phones and computers.

Sid Rajeev, B.Tech, CFA, MBA
Head of Research

KIDZ Price and Volume (1-year)



	YTD	12M
KIDZ	86%	16%
TSXV	27%	41%

Company Data

52-Week Range	C\$0.12 - C\$0.56
Shares O/S	131,124,989
Market Cap.	C\$68M
Current Yield	N/A
P/E (forward)	N/A
P/B	6.5x

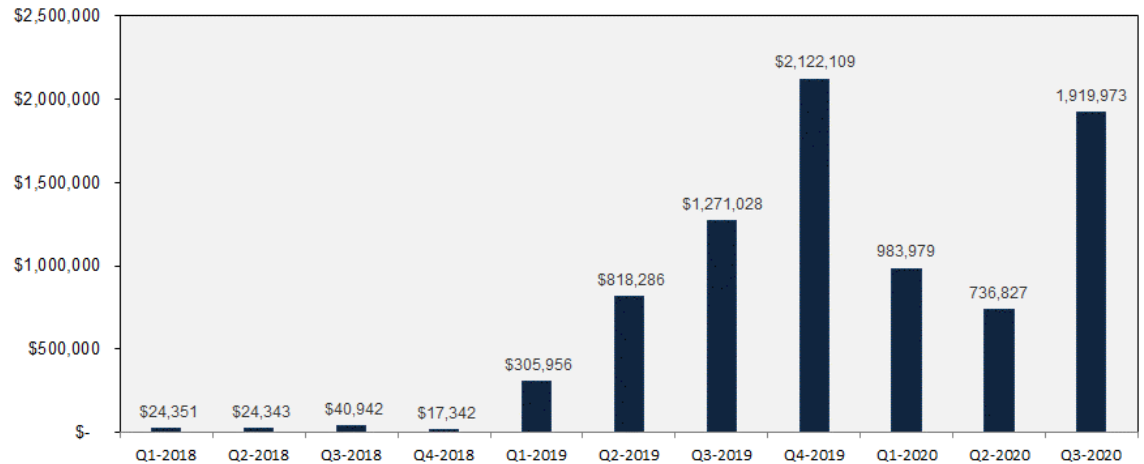
Key Financial Data (FYE - Dec 31) (US\$)	2018	2019	2020E	2021E
Cash	641,536	967,212	1,127,350	3,065,303
Working Capital	662,573	2,192,505	2,391,037	4,386,888
Total Assets	769,633	9,786,640	8,975,403	10,824,802
LT Debt to Capital	0.0%	0.0%	0.0%	0.0%
Revenues	106,978	4,517,379	5,968,750	12,368,750
Net Income	(2,592,831)	(14,654,232)	(522,739)	1,293,737
EPS	-0.04	-0.12	0.00	0.01

*See last page for important disclosures, rating, and risk definitions. All figures in US\$ unless otherwise specified.

Revenue

(in US\$) - YE Dec 31st	Q1-2020	Q2-2020	Q3-2019	Q3-2020	QoQ	YoY	2019-9M	2020-9M
Ad Revenues	895,555	611,709	1,165,609	1,809,169	196%	55%	1,975,523	3,316,433
Content Revenues	88,424	125,118	105,419	110,804	-11%	5%	419,747	324,346
Total Revenue	983,979	736,827	1,271,028	1,919,973	161%	51%	2,395,270	3,640,779

Quarterly Revenue



Source: Company, FRC

Margins, EPS and Cash Flows

Margins	Q1-2020	Q2-2020	Q3-2019	Q3-2020	2019-9M	2020-9M
Gross	45.1%	44.2%	40.68%	47.64%	37.11%	46.27%
EBITDA	-25.8%	-28.8%	-8.15%	13.88%	-47.77%	-5.07%
EBIT	-40.2%	-49.8%	-10.20%	5.73%	-50.69%	-17.93%
Net	-41.1%	-49.0%	-4.64%	6.07%	-53.59%	-17.82%

	Q1-2020	Q2-2020	Q3-2019	Q3-2020	2019-9M	2020-9M
EBITDA	-\$254,163	-\$212,282	-\$103,579	\$266,424	-\$1,144,153	-\$184,649
EBITDA (excl. development costs)	\$45,932	\$28,848	\$145,890	\$545,788	-\$392,426	\$620,568
Net Loss	-\$403,924	-\$361,399	-\$58,932	\$116,634	-\$1,283,532	-\$648,689
EPS	-\$0.00	-\$0.00	-\$0.00	\$0.00	-\$0.01	-\$0.00

Our calculation of EBITDA differs from what KIDZ has reported due to our inclusion of stock-based compensation and the inclusion/exclusion of other small line items.

Summary of Cash Flows	2018 (9M)	2019 (9M)	2020 (9M)
Cash Flows from Operations	-\$1,752,786	-\$1,408,578	\$171,612
Cash Flows from Investing	-\$8,720	\$169,388	-\$9,632
Cash Flows from Financing	\$2,284,819	\$1,410,131	\$7,807
Net Change	\$523,313	\$170,941	\$169,787
Free Cash Flows	-\$1,761,506	-\$1,239,190	\$161,980

Source: Company, FRC

Q3 revenue up 161% QoQ and 51% YoY; ad revenue accounted for 94% of Q3 revenue; we were pleasantly surprised by the spike in revenue as the outlook for ad spending this year had been weak due to the pandemic

Gross and EBITDA margins improved in Q3 and beat our expectations

Reported net profit of \$0.12M/EPs: \$0.00 in Q3; making Q3 the first profitable quarter since 2013

Positive free cash flows in 2020 (9M)

Healthy balance sheet with no debt

Balance Sheet

Liquidity Analysis	2019	Q1-2020	Q2-2020	Q3-2020
Cash	\$967,212	\$545,512	\$1,115,332	\$1,136,999
Working Capital	\$2,192,505	\$1,927,546	\$1,753,820	\$2,094,123
Current Ratio	2.72	3.38	3.68	2.72
Debt / Capital	0.0%	0.0%	0.4%	0.4%
LT Debt / Capital	0.0%	0.0%	0.4%	0.4%
EBIT Interest Coverage Ratio	n/a	n/a	n/a	n/a

Source: Company, FRC

Stock Options and Warrants

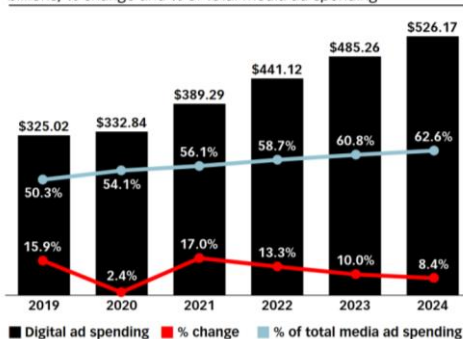
At the end of Q3-2020, KIDZ had 5.88M options (weighted average exercise price of \$0.40) and nil warrants outstanding. 3.7M options are in the money, implying potential to raise up to \$1.2M.

Market Update

Digital ad spending is expected to continue to gain market share in the overall media ad spending market. Global digital ad spending in 2020 is expected to be \$333 billion (54% of total ad spending), reflecting a YoY increase of 2.4%. In 2021 and 2022, global digital ad spending is expected to grow 17% and 13%, respectively (Source eMarketer).

Digital ad spending to rebound in 2021

Digital Ad Spending Worldwide, 2019-2024
billions, % change and % of total media ad spending



Source: eMarketer

Digital Ad Spending Growth in the US, by Industry, 2017-2021
% change

	2017	2018	2019	2020	2021
Computing products & consumer electronics	29.6%	29.1%	24.3%	18.0%	28.2%
Healthcare & pharma	21.4%	21.7%	15.4%	14.2%	18.0%
Telecom	24.7%	32.7%	26.4%	12.0%	23.0%
Financial services	24.0%	29.4%	27.4%	9.7%	20.1%
CPG & consumer products	24.2%	22.7%	14.5%	5.2%	16.4%
Retail	24.7%	23.8%	16.3%	3.1%	25.7%
Entertainment	25.7%	36.1%	28.2%	-6.9%	20.7%
Media	17.4%	21.5%	14.9%	-9.3%	14.2%
Automotive	15.1%	17.0%	14.2%	-18.2%	21.4%
Travel	26.3%	29.1%	17.1%	-41.0%	15.3%
Other	27.0%	25.8%	17.8%	1.1%	14.0%
Total	23.2%	25.3%	19.2%	1.7%	21.1%

Source: eMarketer

In the U.S., digital ad spending of 1.7% is expected to grow slower than the global average in 2020, followed by stronger rebound (to 21%) in 2021. Sectors specific to kids (such as consumer products and retail) are expected to report stronger than average growth.

Another major driver for Kidz is that an increasing number of kids aged two to 11 are shifting away from television. We believe individuals in this age group are not actively choosing to move away from television, rather, it is parents who are enabling the adoption of digital mediums for kids. **Overall, we believe that Kidz's target market (kids digital ads) will grow faster than the broader digital ad**

space through increasing adoption of smartphones and related technologies.

Competitors and Revenue Projections

The company’s kid-safe ad technology is currently installed in over 3,800 different apps, with a combined reach of over 100M kids per month. Q3-2020 revenue reflects an annual run rate of \$7.7M, which is \$0.07 per user, or \$2k per app. We estimate that the industry average is approximately \$2.3k per app, as shown in the table below. The table shows a few of the leading ad network SDKs (Software Development Kits). Google’s AdMob (NASDAQ: GOOGL) dominates the space, as over 90% of apps use AdMob. An app typically uses three to five SDKs.

Kidoz generated annualized revenue of approximately \$2k per app in Q3

Ad SDKs	Total Apps (1,000s)	Total Downloads (billions)	Downloads per app	Market Share	Games	Total Downloads	Downloads per app	Revenue (\$M)	Revenue per app
1 Google Ads AdMob	1,410	405	287,326	91%	270	118	436,298		
2 Facebook Audience Network	300	203	676,356	19%	53	106	2,016,144		
3 Unity Ads	189	166	878,138	12%	119	137	1,147,934	\$300	\$1,589
4 Startapp	131	14	109,065	8%	18	6	323,857	\$69	\$530
5 AppLovin MAX	89	105	1,189,826	5%	45	82	1,812,653	\$234	\$2,639
6 InMobi	28	63	2,306,434	1%	15	40	2,770,661	\$375	\$13,631
7 AdColony	83	81.76	987,201	5%	33.59	68.26	2,032,152	\$484	\$5,844
8 Tapjoy	30	45.91	1,540,087	1%	19.67	39.78	2,022,369	\$100	\$3,355
9 Chartboost	58	64.5	1,115,724	3%	40.66	56.84	1,397,934	\$13	\$223
10 AppNext	44	5.32	122,158	2%	3.68	1.44	391,304	\$84	\$1,931
Average (excl outliers)			921,232				1,435,131		\$2,302

Source: 42matters, Owler, FRC

The fact that Kidoz’s SDK is generating \$2k per app is highly encouraging, as it shows that **Kidoz offers similar monetization capabilities** to app developers and owners. Kidoz’s main competitive advantage is that its SDK is Child Online Privacy Protection Act (COPPA) and GDPR (European equivalent of the U.S. COPPA) compliant. **Kidoz’s network is one of only 12 SDKs that are approved by Apple (NASDAQ: AAPL,) and Google as safe ad networks for kids.**

FRC Projections

We are raising our long-term (2022+) revenue projections as we expect a faster ramp up

Kidoz	2020E	2021E	2022E	2023E	2024E	2025E
Revenues @ \$2k per app	\$5,500,000	\$11,400,000	\$25,000,000	\$50,000,000	\$80,000,000	\$110,000,000
Apps	3,800	5,700	12,500	25,000	40,000	55,000

Raising our EPS projections for 2020 and 2021 from higher revenue, gross margin, and lower SG&A expense forecasts

	Old		New	
	2020	2021	2020	2021
Revenue (\$M)	\$5,297,750	\$12,351,721	\$5,968,750	\$12,368,750
EBITDA (\$M)	-\$555,676	\$974,037	\$122,526	\$1,888,343
Net Income (\$M)	-\$1,200,941	\$379,430	-\$522,739	\$1,293,737
EPS (\$)	-\$0.01	\$0.00	\$0.00	\$0.01

Source: FRC

Valuation

DCF Valuation	2021E	2022E	2023E	2024E	2025E
Funds Flow from Operations (US\$)	2,045,851	4,225,225	9,050,156	14,383,102	18,984,555
Change in Working Capital (US\$)	(57,898)	(1,328,188)	(2,765,313)	(3,121,029)	(3,534,872)
Cash from Operations (US\$)	1,987,953	2,897,037	6,284,843	11,262,073	15,449,682
CAPEX (US\$)	(50,000)	(50,000)	(50,000)	(50,000)	(50,000)
Free Cash Flow (US\$)	1,937,953	2,847,037	6,234,843	11,212,073	15,399,682
Present Value (US\$)	1,672,640	2,184,238	4,251,869	6,796,537	8,297,763
Discount Rate	12.5%				
Terminal Growth	3%				
Present Value (US\$)	\$113,166,477				
Cash - Debt (US\$)	\$1,107,069				
Fair Value (US\$)	\$114,273,546				
Shares O/S*	132,247,201				
Value per Share (C\$)	\$1.08				

Source: FRC

We are maintaining our BUY rating, and raising our fair value estimate from C\$0.94 to C\$1.08 per share. We are expecting record Q4 revenues. Other catalysts for the share price are favorable market conditions, and increasing adoption of smartphones by kids.

Risks

The following risks, though not exhaustive, may cause our estimates to differ from actual results:

- Any unfavorable changes in regulations in the future may impact the company's business.
- Ability to attract publishers and brands will be key to long-term growth.
- Long-term impact of COVID-19 is uncertain.
- The company is operating in a highly competitive space.

We are maintaining our risk rating of 4 (Speculative).

DCF valuation increased from C\$0.94 to C\$1.08 per share

Maintaining risk rating of 4

Appendix

INCOME STATEMENT				
(in US\$) - YE Dec 31st				
	2018	2019	2020E	2021E
Total Revenue	106,978	4,517,379	5,968,750	12,368,750
Cost of Sales		2,778,911	3,055,625	6,362,625
Gross Profit	106,978	1,738,468	2,913,125	6,006,125
Expenses	2,195,160			
Selling & Marketing	352,770	369,321	400,000	400,000
Development	948,334	1,014,041	1,115,445	1,394,306
Stock Based Compensation	595,580	15,890	126,006	157,508
Compensation, Salaries & Provision for Doubtful Accounts	622,779	732,241	517,368	776,052
Bad Debt Expense				
G & A	271,277	717,142	631,780	1,389,916
EBITDA	-2,683,762	-1,110,167	122,526	1,888,343
Amortization & Depreciation	5,614	546,270	645,265	594,607
EBIT	-2,689,376	-1,656,437	-522,739	1,293,737
Interest & Bank Charges	-28,456	3,302		
Exchange Rate and Unusual Items	-9,092	26,008		
EBT	-2,726,924	-1,627,127	-522,739	1,293,737
Unusual Gain or Loss	44,572	-13,877,385		
Income Taxes	-89,521	-850,280		
Net Earnings for the period	-2,592,831	-14,654,232	-522,739	1,293,737
EPS	-0.04	-0.12	0.00	0.01

BALANCE SHEET (in US\$)- YE Dec 31st	2019	2020E	2021E
Assets			
Cash	967,212	1,127,350	3,065,303
Accounts receivable	2,392,778	2,039,188	2,402,450
Prepaid expenses	109,914	87,394	180,184
Current Assets	3,469,904	3,253,932	5,647,937
Property and equipment	27,182	44,919	65,188
Other Assets			
Goodwill, intangible assets, and other	6,289,554	5,676,553	5,111,676
Total Assets	9,786,640	8,975,403	10,824,802
Liabilities & Shareholders' Equity			
Accounts payables & accrued liabilities	1,251,684	837,180	1,235,335
Derivative			
Lease	25,715	25,715	25,715
Related parties			
Current Liabilities	1,277,399	862,895	1,261,050
Loans payable			
Lease	101,900	101,900	101,900
Shareholder's Equity			
Share Capital	48,935,213	49,061,219	49,218,727
Foreign Currency Translation	24,580	24,580	24,580
Deficit	-40,552,452	-41,075,191	-39,781,454
Total Liabilities & Shareholders' Equity	9,786,640	8,975,403	10,824,802

STATEMENTS OF CASH FLOWS			
(in US\$)- YE Dec 31st	2018	2019	2020E
Operating Activities			
Net earnings for the period	-2,592,831	-14,654,232	-522,739
Items not involving cash			
Depreciation	5,614	546,270	645,265
Gain on sale of domain name/others	-7,482		
Deferred income tax recovery		-752,205	
Stock Based Compensation	595,580	15,890	126,006
Impairment		13,877,385	
	-1,999,119	-966,892	248,532
Accounts Receivable	2,919	-963,129	353,591
Prepaid Expenses	-45,025	25,004	22,520
Accounts payable and accrued expenses	-67,572	694,660	-414,504
Changes in working capital	-109,678	-243,465	-38,394
Cash from (used in) operations	-2,108,797	-1,210,357	210,138
Financing activities			
Proceeds from secured borrowings, net	-1,923	-278,063	
Private Placement	2,279,408	1,763,200	
Payment on operating lease liabilities and ROU assets		-79,715	
Options / Warrants	6,600		
Cash provided by financing activities	2,284,085	1,405,422	-
Investing activities			
Acquisition of equipment/subsidiary	-12,149	-6,514	-50,000
Proceeds from sale of subsidiary		183,264	
Goodwill / Others		-46,139	
Cash used in investing activities	-12,149	130,611	-50,000
Increase (decrease) in cash	163,139	325,676	160,138

Fundamental Research Corp. Equity Rating Scale:

Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk.

Hold – Annual expected rate of return is between 5% and 12%

Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk

Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

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2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues and may rely on external funding. These stocks are considered highly speculative.

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