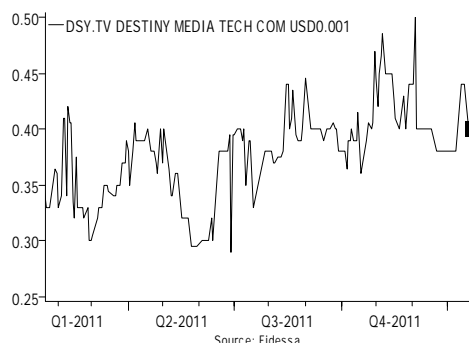


# Destiny Media Technologies 44c

## Sound Q1 Sales, Legal Costs Impact Net Income

27 January 2012



**12m High:** 49c  
**12m Low:** 29c  
**Market Cap:** CAD 22m  
**Shares in Issue:** 50.4m

**Gearing:** Nil (\$1.0m net cash)  
**Interest Cover:** n.a. (net interest income)

**EPIC Code:** TSXV: DSY.V  
**Sector:** Technology  
**Market:** Toronto Venture Exchange  
 (Subsidiary quotes on Frankfurt, Stuttgart and US OTCQX)  
**Broker/Financial Adviser:** None  
**Website:** www.dсны.com

**Description:** Destiny Media's software, MPE<sup>®</sup>, enables record companies to download music securely to radio stations and music journalists worldwide. It is market leader in this field. Destiny Media also owns patented proprietary video streaming technology that is currently largely unexploited.

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Destiny Media's Q1 results show sales revenue up by 6% year on year, a steady performance very much in line with our expectations. Sales from Play MPE, representing over 96% of total revenue, were up 9%.

The sales numbers hid a 29% growth in revenues from Europe, and Europe now accounts for almost half of group sales revenue. Destiny Media is currently strongest in Britain and Scandinavia, but has hopes for growth in Germany following adjustments to its product to take account of the country's unique privacy laws. Destiny's management says that it intends to "grow sequentially" rather than over-extend itself by trying to expand in all potential markets at the same time.

The EBITDA and net income figures for the quarter are down compared to the same period last year. This is entirely due to legal costs; all other cost areas appear to be well controlled. The quarterly net income figure after taxes is running at just 1% of sales revenue. Legal fees cost c. \$270,000 during the quarter. For any company of this nature, legal defense of IP assets is a normal ongoing expense, but even so the additional professional fees of \$133,000 spent during the quarter is very significant. If "professional fees" – largely legal costs – were to be held at the same level as in 1Q 2011, operating profits would be up 54%.

Cash outflow in the quarter was c. \$237,000, compared to an outflow of c. \$249,000 in 1Q 2011. The largest factor in this outflow was the increase in accounts receivable c. \$180,000 in this quarter. We view this as a temporary issue. Destiny Media still has \$1m cash in the bank, and the company's own measure of Adjusted EBITDA has been positive in four of the last five quarters.

We are satisfied with these numbers. The next set of results, Q2, covers a seasonally weak quarter. The Q3 numbers, which should show benefit from MPE's expansion in Germany and Japan. Following the successful introduction of the next generation Clipstream in the HTML5 Summit in November 2011, Destiny is expecting to officially re-launch Clipstream at the end of Q2 this year, and the first financial impact of the re-launch is what we are really waiting for.

Y/E	Group Sales	Declared PBT	Adjusted PBT	Adjusted EPS	P/E ratio	Dividend	Yield
August	\$m	\$m	\$m	c.	x	p	%
2010A	3.8	0.8	0.8	3.2	13.7	-	-
2011A	4.0	0.8	0.5	0.7	62.9	-	-
2012E	4.5	1.0	1.0	1.6	27.5	-	-
2013E	5.8	1.3	1.3	2.0	22.0	-	-

Source: Company & Hardman & Co

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## The Q1 Results

3m to end-November (\$ 000)	2011	2010	Change, %
Sales Revenue	1,124.6	1,056.6	+6.4%
US	583.2	611.1	-4.6%
Europe	504.1	390.1	+29.2%
Australia	37.4	55.0	-32.0%
G & A Expenses	-477.9	-364.2	+31.2%
Sales & Marketing	-198.9	-215.5	-7.7%
Research & Development	-418.1	-363.9	+14.9%
Depreciation and Amortisation	-14.4	-16.7	-13.9%
Income from Operations	15.4	96.4	-84.0%
Other Income	0.0	3.0	
Net Interest Income	2.2	2.5	-12.8%
Income Before Tax	17.6	101.9	-82.8%
Net Income	12.6	72.9	-82.8%
Adjusted EBITDA	31.2	117.6	-72.5%
Cash Outflow	-237.5	-248.7	-4.5%
Net Cash in Balance Sheet	1,000.7	1,238.2	-19.2%
Stockholders' Equity	2,365.2	2,405.9	-1.7%

Source: Company

The key item in the sales revenue line is the strength of Europe, which is mostly contributed by the strong increase in the UK and Scandinavia. There is considerable scope for growth here if the re-engineered offering in Germany finds acceptance in the local marketplace. The fall in US revenue is largely a result of a fall in Clipstream and Radio Destiny sales revenues; Clipstream was awaiting a major product upgrade and re-launch which only took place after the end of the quarter and is unlikely to impact the sales revenue line in any significant way until Q4.

The company continues to be very much focused on a small number of major accounts. The three largest customers represented 66% of total revenues.

In terms of expenditure, the increase in R&D spend is a reflection of the effort being put into the new Clipstream upgrade. All Destiny Media's research and product development is expensed out of revenue. The only items that are capitalised are purchases of equipment that were relatively modest during the quarter at \$39,816.

Within the G&A expense, professional fees accounted for \$301,821 vs. \$168,865 in Q1 2011; 90% of professional fees relate to legal costs. The company is expecting the litigation fees to be substantially reduced following the trial in Q3 2012. Professional fees were equivalent to 27% of sales revenues during the quarter.

If 'professional fees' were to be held at the same level as in Q1 2011, the operating profit would have been up by 54%. On this basis, Operating Margins were higher also. For a company in North America particularly, ongoing legal defence of IP rights is an unavoidable ongoing cost (look at Apple, Microsoft, Facebook). But this does indicate that the underlying position of the company is healthy, and that if the litigation fees are to be substantially reduced following the trial in Q3, there is the potential for a couple of very profitable quarters at the end of the year.

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**Profit & Loss Account**

Year at 31<sup>st</sup> August (\$m)

	<b>2010</b>	<b>2011</b>	<b>2012E</b>	<b>2013E</b>
<b>Revenue</b>	<b>3.77</b>	<b>4.01</b>	<b>4.49</b>	<b>5.75</b>

Growth Rate %	47.3%	6.3%	12.0%	30.0%
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**Operating expenses**

General & Admin	-1.05	-0.76	-0.77	-1.00
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Sales & Marketing	-0.79	-0.82	-0.94	-1.20
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R&D	-1.19	-1.56	-1.68	-2.18
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Depreciation & Amortization	-0.05	-0.06	-0.08	-0.10
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	-3.08	-3.21	-3.47	-4.48
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**Operating income**

	<b>0.69</b>	<b>0.80</b>	<b>1.02</b>	<b>1.26</b>
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**Other income**

Other income	0.12	0.00	0.00	0.00
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Gain on Settlement of Debt	0.00	0.00	0.00	0.00
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Interest income	0.00	0.01	0.02	0.03
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Interest and other expense	0.00	0.00	0.00	0.00
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	0.12	0.01	0.02	0.03
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**Profit before tax**

	0.81	0.81	1.04	1.30
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Taxation	0.88	-0.17	-0.26	-0.32
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Tax rate %		21%	25%	25%
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**Net Income**

	<b>1.69</b>	<b>0.64</b>	<b>0.78</b>	<b>0.97</b>
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EPS (basic) cents	3.27	1.26	1.59	1.98
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EPS (diluted) cents	3.23	1.25	1.58	1.97
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Source: Hardman & Co Estimates & Published Company Data

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**Balance Sheet**

Year at 31 <sup>st</sup> August (\$m)	2010	2011	2012E	2013E
<b>Current Assets</b>				
Cash & cash equivalents	0.49	1.24	2.05	3.03
Accounts receivables	0.54	0.39	0.63	0.80
Other receivables	0.05	0.06	0.05	0.05
Prepaid expenses	0.03	0.02	0.03	0.03
Deposits	0.00	0.01	0.00	0.00
Deferred tax assets	0.38	0.29	0.38	0.00
	<b>1.49</b>	<b>2.01</b>	<b>3.13</b>	<b>3.91</b>
Deposits	0.01	0.04	0.01	0.01
Property and Equipment	0.13	0.14	0.16	0.18
Deferred commission costs	0.00	0.00	0.00	0.00
Deferred tax assets	0.95	0.87	0.61	0.28
	<b>1.09</b>	<b>1.05</b>	<b>0.77</b>	<b>0.48</b>
<b>Total Assets</b>	<b>2.58</b>	<b>3.06</b>	<b>3.91</b>	<b>4.38</b>
<b>Current Liabilities</b>				
Accounts payable	0.22	0.29	0.45	0.57
Accrued liabilities	0.26	0.31	0.26	0.26
Shareholder loan payable	0.00	0.00	0.00	0.00
Deferred leasehold inducement	0.00	0.00	0.00	0.00
Deferred revenue	0.03	0.04	0.03	0.03
Obligation under capital lease	0.01	0.00	0.00	0.00
	<b>0.52</b>	<b>0.65</b>	<b>0.73</b>	<b>0.86</b>
Obligation for share settlement	0.00	0.00	0.00	0.00
Obligation under capital lease	0.00	0.00	0.00	0.00
<b>Total Liabilities</b>	<b>0.52</b>	<b>0.65</b>	<b>0.73</b>	<b>0.86</b>
<b>Stockholders' equity</b>	<b>2.06</b>	<b>2.41</b>	<b>3.18</b>	<b>3.52</b>

Source: Hardman & Co Estimates & Published Company Data

## Destiny Media Technologies

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