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## Smith Micro Software, Inc. (NASDAQ: SMSI)

March 10, 2023

### Buy: Q4 Results as Expected. Positive CF in Sight.

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*Q4 revenue was in line with our estimate and EBITDA was better than we modeled. The company is implementing an aggressive cost-cutting program and we expect positive EBITDA in the second half and rapid EBITDA growth in 2024. We maintain our Buy recommendation.*

Q4 revenue of \$11.4 million was in line with our estimate and the EBITDA loss was better than we had modeled. In the wake of Verizon's termination of its family safety solutions agreement with Smith, the company is reducing expenses by \$4 million per quarter. The company intends to have at least \$3 million of these cuts in place by the end of Q2. These cuts should more than offset the loss of Verizon, and we expect positive EBITDA for the second half and significant growth in 2024.

Q1 revenue is expected to decline between 2% and 5% as the attrition of the Sprint customer base continues, not yet offset by T-Mobile marketing the family safety service aggressively to its customer base. AT&T is expected to begin growing its subscribers to the family safety service in Q2 while Verizon will be flat for the year. We have modeled a second-half growth based on the assumption that both AT&T and T-Mobile actively grow their family safety subscribers.

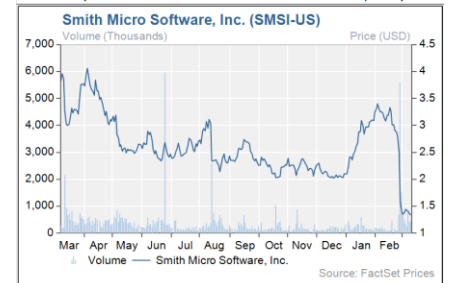
Q1 2024 revenue is expected to decline as the Verizon business ceases, but we expect sequential growth to resume in Q2. EBITDA for the year is modeled at \$8.6 million with EBITDA improving as revenue ramps and expense growth is restrained. The company is pursuing additional family safety and ViewSpot customers, domestically and abroad, but we have not included new wins in our model.

The scale and pace of the cost-cutting puts the company in a better position to meet the \$15 million convertible note obligation that begins to amortize on April 1. \$5 million of principal is due per quarter for the next three quarters. The company can pay the amount due in cash or stock. As of the quarter-end, Smith had \$14 million in cash but will need up to \$5 million to fund operating losses in the first half. Paying the obligation in cash will be challenging but Smith has the option of payment in stock.

**Valuation:** Our price target of \$3.50 is based on an EV/Sales multiple of 3.5x on our 2024 revenue estimate of \$51.4 million. Our target multiple is a discount to the group median EV/Sales multiple of 4.8x.

**Risks:** Risks to achieving our price target include declines in the CommSuite product line, disruptions from the T-Mobile acquisition of Sprint, integration of the Family Safety business, continuing impacts of the COVID pandemic and customer concentration.

Current Price				\$1.34
Price Target				\$3.50
<b>Estimates</b>	<b>F2022A</b>	<b>F2023E</b>	<b>F2024E</b>	
Revenues (\$M's)	\$ 48.5	\$ 48.2 E	\$ 51.4	
1Q March	\$ 12.7	\$ 10.9 E	\$ 10.3	
2Q June	\$ 12.7	\$ 11.5 E	\$ 12.1	
3Q September	\$ 11.7	\$ 12.5 E	\$ 13.6	
4Q December	\$ 11.4	\$ 13.3 E	\$ 15.4	
	<b>F2022A</b>	<b>F2023E</b>	<b>F2024E</b>	
EBITDA (\$M's)	\$ (16.4)	\$ (0.0) E	\$ 8.6	
1Q March	\$ (3.9)	\$ (3.7) E	\$ (1.5)	
2Q June	\$ (4.2)	\$ (1.8) E	\$ 0.0	
3Q September	\$ (4.9)	\$ (0.1) E	\$ 1.2	
4Q December	\$ (3.6)	\$ 0.6 E	\$ 2.7	
EV/Sales	1.5 x	1.6 x	1.5 x	
EV/EBITDA	NM	NM	8.7 x	
<b>Stock Data</b>				
52-Week Range	\$1.31	-	\$4.18	
Shares Outstanding (mil.)				56.4
Market Capitalization (mil.)				\$76
Enterprise Value (mil.)				\$75
Debt to Capital				15%
Cash (mil.)				\$14
Cash/Share				\$0.25
Average Three Months Trading Volume (K)				92
Insider Ownership				11.9%
Institutional Ownership				17.2%
Short interest (mil.)				2.5%
Dividend / Yield				\$0.00/0.0%



**Actual v Estimates**

<b>Q4 22</b>			
<b>\$ in 000's except per share</b>	<b>Actual</b>	<b>Estimates</b>	<b>Delta</b>
Revenue	\$ 11,405	\$ 11,000	4%
COGS	3,328	3,410	
Gross Profit	8,077	7,590	6%
SG&A	3,196	2,520	
R&D	6,732	7,057	
G&A	3,764	3,667	
Amort. of Intangible asset	1,545	1,545	
Opex	15,237	14,790	
Operating Income	\$ (7,160)	\$ (7,200)	
Interest Income	0	0	
Interest Expense	(1,782)	(225)	
Change in Warrant Liability	1,212	0	
Other Income (Expense)	(125)	(29)	
Pretax Income	(7,855)	(7,454)	
Taxes	148	25	
Net Income	(8,003)	(7,479)	
Basic Shares	56,228	58,615	
Diluted Shares	56,228	60,615	
Basic EPS	\$ (0.14)	\$ (0.13)	
Diluted EPS	\$ (0.14)	\$ (0.12)	
Operating Income	(7,160)	(7,200)	
Depreciation & Amortization	1,805	1,869	
Stock Comp	1,099	1,095	
Other	616	0	
EBITDA	\$ (3,640)	\$ (4,236)	14%
Margin	-31.9%	-38.5%	

*Source: Smith Micro Software, Inc. and Dawson James Securities estimates*

Past the loss of Verizon, Smith will benefit will be a resumption of revenue growth. With all development and migration work complete we expect Smith and its carrier customers to begin actively marketing the family safety services to its customer base. This is a large opportunity for Smith and the carriers. Before Sprint's acquisition by T-Mobile, Smith was generating \$30 to \$35 million in annualized revenue from Sprint, the smallest of the then-major carriers. Since then, Smith has consolidated the industry and will serve two of the three major domestic carriers, whose combined post-paid subscriber base is 5x the number of post-paid subscribers served by Sprint. This suggests an annual revenue opportunity of \$150 million.

Smith estimates the number of multi-line accounts served by each of the three carriers at between 15 and 20 million and the number of accounts that could be served by Smith at between 3 and 5 million per carrier. This equals 9 to 15 million accounts each paying on average \$10 per month, or a revenue contribution to the carriers of between \$1.1 and \$1.8 billion annually. Smith's contract terms with its carrier customers are proprietary but we estimate Smith takes between 25% and 50% of the total revenue. At 25%, this is a revenue opportunity of \$270 million to \$450 million annually. For the two remaining carrier customers this is a potential market of \$180 million to \$300 million This is consistent with the revenue opportunity estimate derived by comparing Smith's revenue from Sprint and applying that to the much larger base now served.

We believe Verizon will attempt to develop its own family safety platform, and it is unlikely to offer it as a competitive solution leaving Smith as the dominant provider of family location and safety services to the U.S. wireless carrier market. We expect the SafePath platform can expand into the home and international markets that are at least equal in size to the domestic market.

### Outlook

Our revenue estimate for 2023 reflects the roll-out of SafePath 7 to AT&T and T-Mobile and stable revenues at Verizon. T-Mobile will begin marketing this year and we expect AT&T growth to begin Q2. Assuming lags between marketing and subscription as well as trial periods common to the industry, we expect modest SafePath Q/Q revenue growth beginning Q2 and a more aggressive growth rate in the second half.

EBITDA and margins should follow revenue growth. Gross margin is modeled to improve near year-end and is estimated to achieve 80% by year-end 2023. EBITDA and EBITDA margin should grow as revenue scales, and we expect EBITDA margin to approach 20% by the end of 2024.

### Valuation

Our price target of \$3.50 is based on an EV/Sales multiple of 3.5x on our 2024 revenue estimate of \$51.4 million. This multiple is a discount to the peer group with a median multiple of 4.8x.

		Price	FTM EPS	P/E	TEV (in M's)	FTM Sales (in M's)	EV/ Sales	FTM EBITDA (in M's)	EV/ EBITDA
ADBE	Adobe Incorporated	\$ 338.37	\$ 15.88	21.3	\$156,862.6	\$ 19,808.5	7.9x	\$ 9,598.9	16.3 x
ASAN	Asana, Inc. Class A	21.17	(0.60)	NM	3,302.8	659.0	5.0x	(112.9)	NM
TEAM	Atlassian Corp Class A	169.99	1.90	89.3	45,414.7	4,048.5	11.2x	761.5	59.6 x
DOCU	DocuSign, Inc.	64.41	2.32	27.8	13,064.9	2,709.8	4.8x	676.6	19.3 x
DBX	Dropbox, Inc. Class A	19.61	1.73	11.3	7,963.7	2,502.6	3.2x	907.3	8.8 x
HUBS	HubSpot, Inc.	392.93	4.47	87.8	19,320.4	2,141.9	9.0x	340.4	56.8 x
NTNX	Nutanix, Inc. Class A	24.91	0.39	64.0	6,044.2	1,952.8	3.1x	183.2	33.0 x
ONTF	ON24, Inc.	7.50	(0.03)	NM	47.3	168.4	0.3x	(4.4)	NM
RNG	RingCentral, Inc. Class A	33.86	3.21	10.5	4,925.0	2,240.9	2.2x	527.0	9.3 x
SMAR	Smartsheet, Inc. Class A	43.11	(0.05)	NM	5,515.1	985.0	5.6x	11.7	472.9 x
TWLO	Twilio, Inc. Class A	68.90	1.11	61.9	10,590.5	4,446.7	2.4x	590.5	17.9 x
WDAY	Workday, Inc. Class A	181.47	5.21	34.8	44,642.7	7,340.4	6.1x	2,074.8	21.5 x
ZM	Zoom Video Communications, Inc. Class A	67.62	4.21	16.1	14,918.0	4,489.8	3.3x	1,753.9	8.5 x
	Median			31.3			4.8x		19.3 x
SMSI	Smith Micro Software, Inc.	\$ 1.34	\$ (0.01)	NM	\$ 68.9	\$ 48.8	1.4x	\$ 1.6	43.6 x

Source: FactSet and Dawson James Securities estimates.

### Risk Analysis

Risks to achieving our price target include declines in the CommSuite product line, disruptions from the T-Mobile acquisition of Sprint, integration of the Family Safety business, continuing impacts of the COVID pandemic and customer concentration.



**Exhibit 1. Income Statement**

\$ in 000's	2020	2021	2022	Q1 23 E	Q2 23 E	Q3 23 E	Q4 23 E	2023 E	2024 E
Revenue	\$ 51,300	\$ 58,422	\$ 48,513	\$ 10,925	\$ 11,509	\$ 12,509	\$ 13,289	\$ 48,232	\$ 51,404
COGS	5,190	12,698	14,210	3,078	2,828	2,578	2,658	11,142	9,939
Gross Profit	46,110	45,724	34,303	7,847	8,681	9,931	10,631	37,090	41,465
	89.9%	78.3%	70.7%	71.8%	75.4%	79.4%	80.0%	76.9%	80.7%
SG&A	9,090	11,581	12,887	2,875	2,622	2,369	2,369	10,236	9,144
R&D	17,759	26,197	29,870	5,835	5,303	4,770	4,770	20,678	18,747
G&A	12,801	17,920	16,161	3,282	2,984	2,687	2,687	11,640	10,413
Amort. of Intangible asset	2,920	8,100	6,312	1,469	1,469	1,469	1,469	5,874	5,874
Restructuring/Other	19	12,864	0	0	0	0	0	0	0
Opex	42,589	76,662	65,230	14,333	13,333	12,833	12,833	48,428	44,178
Operating Income	\$ 3,521	\$ (30,938)	\$ (30,927)	\$ (6,486)	\$ (4,652)	\$ (2,902)	\$ (2,202)	\$ (11,338)	\$ (2,713)
Interest Income	96	34	0	0	0	0	0	0	0
Interest Expense	0	(2)	(2,680)	(225)	(188)	(113)	(38)	(563)	(563)
Change in Warrant Liability	0	0	4,669	0	0	0	0	0	0
Other Income (Expense)	708	78	(115)	25	25	25	25	100	100
Pretax Income	4,325	(30,828)	(29,053)	(6,686)	(4,815)	(2,990)	(2,215)	(11,800)	(3,175)
Taxes	160	215	226	25	25	25	25	100	100
Net Income	4,165	(31,043)	(29,279)	(6,711)	(4,840)	(3,015)	(2,240)	(11,900)	(3,275)
Preferred Dividends	0	0	0	0	0	0	0	0	0
Net to Common	\$ 4,165	\$ (31,043)	\$ (29,279)	\$ (6,711)	\$ (4,840)	\$ (3,015)	\$ (2,240)	\$ (11,900)	\$ (3,275)
Basic Shares	40,808	51,232	55,422	59,274	59,759	60,419	60,994	60,112	64,841
Diluted Shares	42,764	51,232	55,422	59,274	59,759	62,419	62,994	60,112	64,841
Basic EPS	\$ 0.10	\$ (0.61)	\$ (0.53)	\$ (0.11)	\$ (0.08)	\$ (0.05)	\$ (0.04)	\$ (0.20)	\$ (0.05)
Diluted EPS	\$ 0.10	\$ (0.61)	\$ (0.53)	\$ (0.11)	\$ (0.08)	\$ (0.05)	\$ (0.04)	\$ (0.20)	\$ (0.05)
Stock Comp	3,063	4,848	4,370	1,099	1,099	1,099	1,099	4,396	4,396
Amortization	2,920	8,100	6,312	1,469	1,469	1,469	1,469	5,874	5,874
Other	918	15,852	(201)	0	0	0	0	0	0
Non-GAAP Net Income	11,066	(2,243)	(18,798)	(4,144)	(2,272)	(447)	328	(1,630)	6,995
Non-GAAP EPS	\$ 0.26	\$ (0.04)	\$ (0.34)	\$ (0.07)	\$ (0.04)	\$ (0.01)	\$ 0.01	\$ (0.03)	\$ 0.11
Operating Income	3,521	(30,938)	(30,927)	(6,486)	(4,652)	(2,902)	(2,202)	(11,338)	(2,713)
Depreciation & Amort.	3,582	9,338	7,556	1,729	1,729	1,729	1,729	6,914	6,914
Stock Comp	3,064	4,848	4,948	1,099	1,099	1,099	1,099	4,396	4,396
Other	927	15,447	2,015	0	0	0	0	0	0
EBITDA	\$ 11,094	\$ (1,305)	\$ (16,408)	\$ (3,659)	\$ (1,825)	\$ (75)	\$ 625	\$ (28)	\$ 8,597
Margin	21.6%	-2.2%	-33.8%	-33.5%	-15.9%	-0.6%	4.7%	-0.1%	16.7%

Source: Smith Micro Software, Inc. and Dawson James Securities estimates

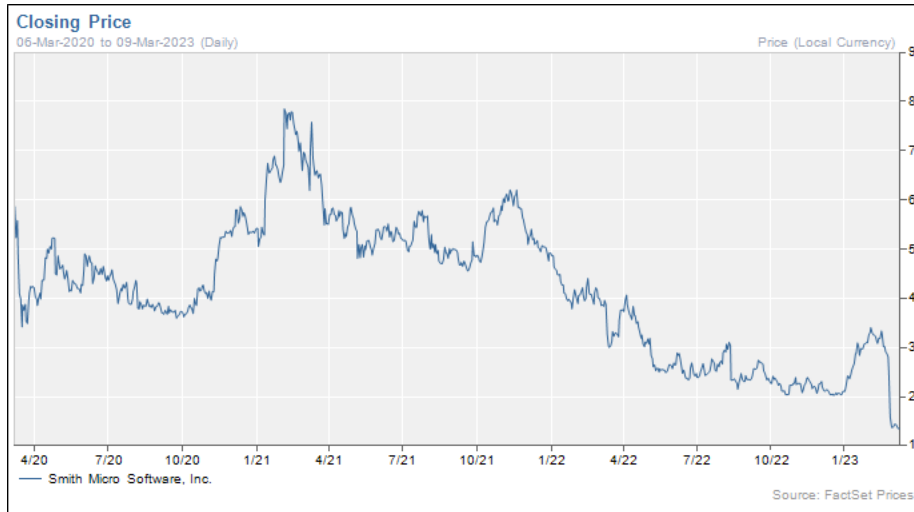
**Exhibit 2. Balance Sheet and Cash Flow Statement**

(\$ in 000's)	2020	2021	2022	2023 E	2024 E
Cash	25,754	16,078	14,026	11,754	12,395
A/R	12,347	10,590	10,501	10,194	11,796
Prepaid Expenses & Other	1,189	1,988	1,983	2,311	2,674
<b>Current Assets</b>	<b>\$ 39,290</b>	<b>\$ 28,656</b>	<b>\$ 26,510</b>	<b>\$ 24,258</b>	<b>\$ 26,865</b>
Equipment & Improvements	2,170	2,698	1,498	1,458	1,418
Right-of-use asset	5,785	5,710	3,722	3,722	3,722
Deferred Tax Assets	0	0	0	0	0
Other	694	620	490	490	490
Intangible Assets	12,698	42,631	36,320	30,446	24,572
Goodwill	12,266	35,041	35,041	35,041	35,041
<b>Total Assets</b>	<b>\$ 72,903</b>	<b>\$ 115,356</b>	<b>\$ 103,581</b>	<b>\$ 95,415</b>	<b>\$ 92,108</b>
A/P	2,282	3,301	3,236	3,771	4,363
Accrued Payroll & Benefits	2,867	4,055	3,883	4,524	5,235
Operating Lease	1,433	1,400	1,441	1,441	1,441
Other Accrued Liab.	216	436	1,589	1,851	2,142
Deferred Revenue	1,572	176	0	0	0
Convertible Note payable	0	0	9,007	0	0
Derivative liabilities			1,575	0	0
<b>Current Liabilities</b>	<b>\$ 8,370</b>	<b>\$ 9,368</b>	<b>\$ 20,731</b>	<b>\$ 11,587</b>	<b>\$ 13,182</b>
Cv. Notes due 2023	0	0	0	0	0
Warrant Liability	0	0	3,317	0	0
Lease Liabilities	4,805	4,467	2,976	2,976	2,976
Other LT Liabilities	125	117	178	207	240
Equity	\$ 58,716	\$ 100,560	\$ 76,379	\$ 80,645	\$ 75,710
<b>Total Liabilities &amp; Equity</b>	<b>\$ 72,903</b>	<b>\$ 115,356</b>	<b>\$ 103,581</b>	<b>\$ 95,415</b>	<b>\$ 92,108</b>
	2020	2021	2022	2023 E	2024 E
Net Income	4,165	(31,043)	(29,279)	(16,805)	(9,430)
Depreciation & Amortization	3,582	9,338	7,556	6,914	6,914
Stock Comp	3,064	4,848	4,948	4,396	4,396
Working Capital & Other	(2,887)	3,941	(2,486)	1,447	(338)
<b>Operating CF</b>	<b>\$ 7,924</b>	<b>\$ (12,916)</b>	<b>\$ (19,261)</b>	<b>\$ (4,048)</b>	<b>\$ 1,542</b>
Capx	(1,323)	(830)	(49)	(1,000)	(1,000)
Acquisitions	(13,500)	(56,865)	0	0	0
Other	142	192	164	0	0
<b>Investing Activities</b>	<b>\$ (14,681)</b>	<b>\$ (57,503)</b>	<b>\$ 115</b>	<b>\$ (1,000)</b>	<b>\$ (1,000)</b>
Equity	4,214	60,743	3,000	100	100
Debt	0	0	14,036	2,676	0
Other	29	0	58	0	0
<b>Financing</b>	<b>\$ 4,243</b>	<b>\$ 60,743</b>	<b>\$ 17,094</b>	<b>\$ 2,776</b>	<b>\$ 100</b>
<b>Change in Cash</b>	<b>\$ (2,514)</b>	<b>\$ (9,676)</b>	<b>\$ (2,052)</b>	<b>\$ (2,272)</b>	<b>\$ 642</b>

Source: Smith Micro Software, Inc. and Dawson James Securities estimates

**Important Disclosures:**

**Price Chart:**



**Price target and ratings changes over the past three years:**

- Initiated – Buy – May 4, 2021 – Price Target \$11.10
- Price Target Change – Buy – May 6, 2021 – Price Target changed from \$11.10 to \$11.40
- Update – Buy – July 21, 2021 – Price Target \$11.40
- Update – Buy – August 5, 2021 – Price Target \$11.40
- Update – Buy – November 11, 2021 – Price Target \$11.40
- Price Target Change – Buy – March 11, 2022 – Price Target changed from \$11.40 to \$8.30
- Update – Buy – April 4, 2022 – Price Target \$8.30
- Update – Buy – May 5, 2022 – Price Target \$8.30
- Update – Buy – August 12, 2022 – Price Target \$8.30
- Update – Buy – October 10, 2022 – Price Target \$8.30
- Update – Buy – November 7, 2022 – Price Target \$8.30
- Update – Buy – November 10, 2022 – Price Target \$8.30
- Update – Buy – January 18, 2023 – Price Target \$8.30
- Price Target Change – Buy – February 28, 2023 – Price Target changed from \$8.30 to \$3.50
- Update – Buy – March 10, 2023 – Price Target \$3.50

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- 1) **Buy:** The analyst believes the price of the stock will appreciate and produce a total return of at least 20% over the next 12-18 months;
- 2) **Neutral:** The analyst believes the price of the stock is fairly valued for the next 12-18 months;
- 3) **Sell:** The analyst believes the price of the stock will decline by at least 20% over the next 12-18 months and should be sold.

The following chart reflects the range of current research report ratings for all companies, followed by the analysts of the Firm. The chart also reflects the research report ratings relating to those companies for which the Firm has performed investment banking services.

Current as of 03-Mar-23

	<b>Company Coverage</b>		<b>Investment Banking</b>	
<b>Ratings Distribution</b>	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	24	69%	1	3%
Market Perform (Neutral)	11	31%	2	6%
Market Underperform (Sell)	0	0%	0	0%
<b>Total</b>	<b>35</b>	<b>100%</b>	<b>3</b>	<b>9%</b>

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