

August 10, 2022

**TUCOWS INC. (TC-TSX, C\$65.11)**

Rating: **BUY**

New Target Price: **\$150.00**

**STILL FIRING ON ALL CYLINDERS; RECALIBRATING TARGET PRICE**

Old Target Price: **\$180.00**

Tucows Inc. TC			
<i>(Currency is US\$ unless noted otherwise)</i>			
Last Price (\$)	C\$65.11		
Target Price (\$)	C\$150.00		
Return to Target (%)	130%		
52-Week Trading Range (\$)	C\$49.38 / C\$116.94		
Average Daily Volume (90-Day)	12.8K		
MARKET INFO			
Basic Shares Outstanding (M)	10.8		
FD ITM Shares Outstanding (M)	10.8		
Market Capitalization (\$M)	C\$700.9		
Enterprise Value (\$M)	C\$999.3		
FYE: DEC 31	F2021A	F2022E	F2023E
Revenue (\$M)	\$304.0	\$330.3	\$367.1
Adj. EBITDA (\$M)	\$48.8	\$39.2	\$47.7
Adj. EBITDA Margin (%)	16%	12%	13%
MOST RECENT QUARTER Jun-21			
Revenue (\$M)	\$83.1		
EBITDA (\$M)	\$11.7		
EBITDA Margin (%)	14%		
Debt (\$M)	\$243.3		
Cash (\$M)	\$6.5		
EV/EBITDA	F2021A	F2022E	F2023E
Tucows Inc.	16.2x	20.2x	16.6x
Domain Services Peer Group	17.8x	20.1x	18.4x
Fiber & Bandwidth Peer Group	8.7x	8.1x	7.7x
DISCLOSURE CODE: 2			
<i>(Please refer to applicable disclosures on the back page)</i>			
Source: M Partners, FactSet, Bloomberg, Company Documents			



Tucows is a provider of network access, mobile technology services, domain names, and other internet services. Ting Internet delivers fixed fiber internet access with outstanding customer support. Tucows Domains manages approximately 25 million domain names and millions of value-added services through a global reseller network of over 36,000 web hosts and ISPs. Tucows' Wavelo platform provides OSS/BSS services to communication service providers.

**Yesterday after market close, Tucows Inc. reported Q2/22 financial results that beat our expectations once again.** Tucows posted adjusted EBITDA of \$11.7M (+5% YoY), ahead of our estimate of \$8.7M and revenue of \$83.1M (+11% YoY), beating our estimate of \$80.9M.

**Tucows Domain Services:** The domains business posted \$61.1M in revenue (-2% YoY, wholesale -1% YoY, retail -5% YoY) compared to our estimate of \$61.5M and \$12.1M in adjusted EBITDA (flat YoY), beating our estimate of \$11.7M. The quarter puts Tucows on pace to reach its 2022 adjusted EBITDA guidance of \$45M, illustrating the reliable cash generation of the business. Domains under management declined <1% QoQ to 24.8M (Figure 2), consistent with trends in the global domains industry in response to demand pull-forward in 2020/2021. Total new, renewed and transferred-in domains came in at 5.4M vs. 5.7M in Q2/21 while the overall renewal rate was 82% (vs. 81% last quarter). We remain encouraged by the pricing power in the domains business given the decline in global domains.

**Ting Internet:** The fiber business generated \$10.2M in revenue during the quarter (+84% YoY, +4% QoQ), in line with our estimate of \$10.2M. Adjusted EBITDA came in at -\$6.2M, slightly missing our estimate of -\$5.1M. Ting Internet ended the quarter with 731K potential serviceable addresses (415K owned and 315K leased) and has completed 104K addresses (85K owned, 18K leased). Ting Internet deployed a record \$24.9M in fiber capex during the quarter compared to \$14.1M last quarter. Subscribers grew 9% QoQ to 30K at a \$112/month ARPU (Figure 4). Our implied take-rate for the quarter came in at 29% compared to 28% in Q1.

Yesterday morning, Ting announced that it has secured up to \$200M in financing from sustainable infrastructure investment firm, Generate Capital. The financing is in preferred stock and includes \$60M upon closing and \$140M based on operational milestones at a 15% coupon and six-year term. The preferred shares only convert to equity in the event of a default. The \$200M should translate into 130K homes passed or \$17/share to our target assuming \$3,000/pass. Ting and Generate will also enter into an Equity Capital Contribution Agreement providing up to \$400M in additional capital, where Generate will fund the equity and buildout of new fiber networks that Ting will serve as the anchor tenant for. Tucows was also able to extend its existing credit facility to June 2024 and reorganize the facility to exclude Ting Internet; this means the fiber EBITDA losses will not be included in the future covenant calculations. CEO Elliot Noss commented that investors should expect Ting to pursue additional debt to continue with the capex momentum.

**Wavelo:** In Q1, Wavelo posted \$9.0M in revenue (+31% QoQ) and \$3.9M in adjusted EBITDA, compared to our expectations of \$7.2M and \$1.1M respectively. This puts Wavelo ahead of schedule for its full year guidance of \$3-6M in EBITDA. The Company is concluding its professional services work with DISH and expects the business to become more predictable and higher margin as it moves to a subscription model. The DISH migration was again not a focus in Q2, but Wavelo CEO Justin Reilly outlined that migrations will ramp significantly in H2/22. Reilly also highlighted that Wavelo is seeing interest from global telecom firms and that only 5% of telecom firms have

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moved operations to the cloud. Furthermore, DISH decided not to exercise its option to acquire the Ting brand during the quarter but will remain using the brand until the end of the year.

**Tucows Corporate:** Tucows Corporate generated \$2.8M in revenue and \$1.9M in adjusted EBITDA during the quarter, compared to our estimates of \$2.0M in revenue and \$1.0M in adjusted EBITDA. The adjusted EBITDA figure includes a \$4.5M gain from the sale of Ting customer assets, compared to \$4.8M last quarter. The decline in the Ting Mobile customer gain has been much more modest than we originally anticipated, providing even more non-dilutive financing for the fiber deployment.

Management will be taking questions from shareholders and analysts via email (ir@tucows.com) until August 16<sup>th</sup> and will post its responses through an audio recording and transcript on August 25<sup>th</sup> at 4PM ET.

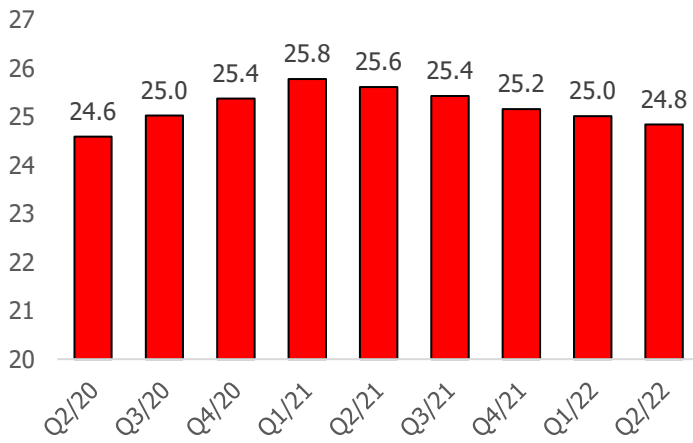
**Our Thoughts:** Q2 marked another stellar quarter for all three of TC's businesses, but again we were most impressed by the continued deployment of capex and secured financing for the fiber business. We continue to believe that we are still in the early innings of FTTH adoption in the U.S., with FTTH holding only 20% market share and covering ~30% of U.S. homes (vs. 60%+ for other developed nations).

We believe the Tucows management team will continue to replicate its success in capital allocation through rapidly growing its Ting Internet and Wavelo businesses while the domains business continues to grow at low-single-digits. Given the multiple compression seen across technology firms and the increased cost of capital, we are recalibrating our valuation assumptions to 11x 2023E EBITDA for the domains business (previously 13x) and an 9% WACC for the fiber business (previously 7%). **We are maintaining our BUY rating and revising our target price to C\$150.00/share (previously C\$180.00/share) based on a sum-of-the-parts valuation.**

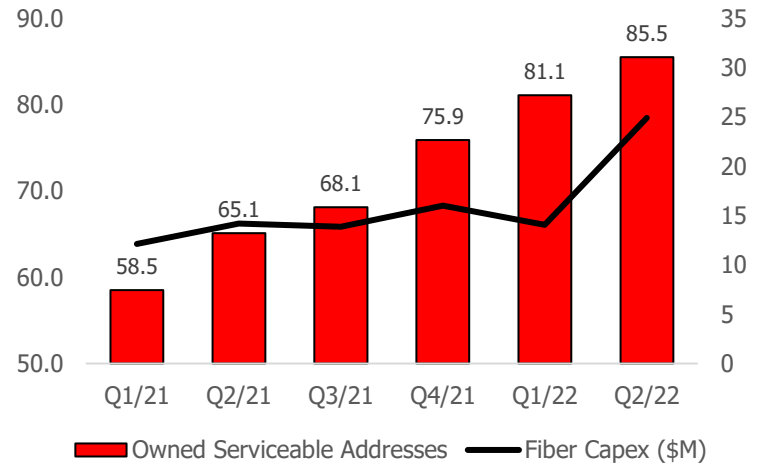
SOTP Valuation	
<b><i>Ting Internet</i></b>	
Enterprise Value (DCF Valuation)	1090.8
<b><i>Tucows Domains</i></b>	
2023E EBITDA Multiple	11.0x
Enterprise Value	541.2
<b><i>Wavelo</i></b>	
2023E EBITDA Multiple	12.0x
Enterprise Value	119.7
<b><i>Tucows Corporate</i></b>	
2023E EBITDA Multiple	10.0x
Enterprise Value	40.0
<b>Consolidated Enterprise Value</b>	<b>1791.8</b>
(-) Projected Debt	331.9
(-) Preferred Stock	200.0
(+) Cash	6.5
Implied Equity Value	1266.4
<b>Target Price (Rounded)</b>	<b>C\$150.00</b>
<i>Upside</i>	<i>130%</i>

**Figure 1: Sum-of-the-Parts Valuation**

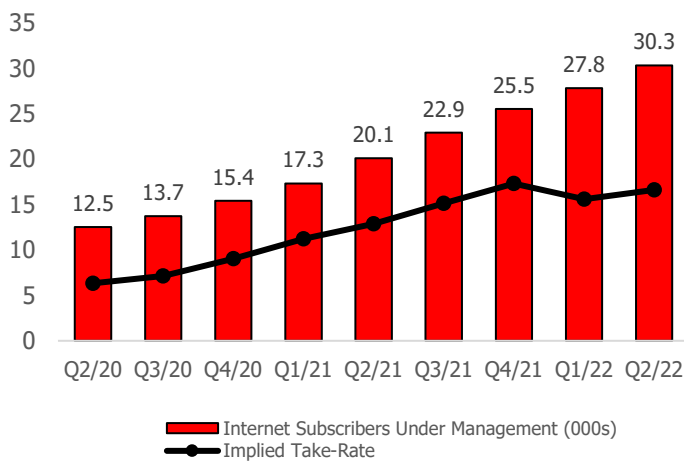
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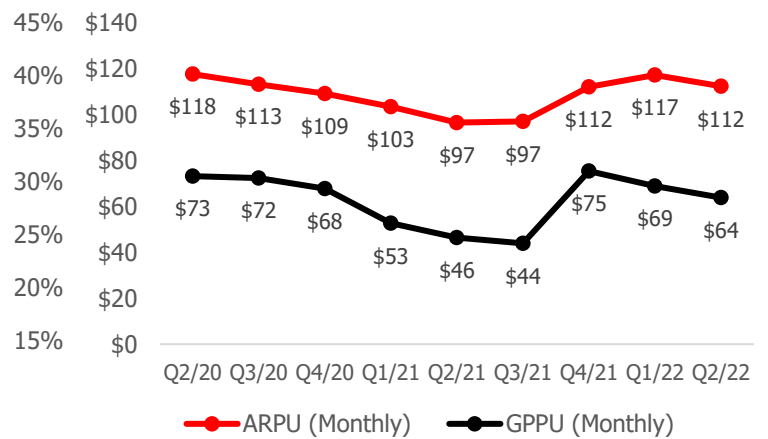
**Figure 2: Domains Under Management (Millions)**



**Figure 3: Owned Addresses Passed & Fiber Capex**



**Figure 4: Ting Internet Operating Metrics**



**Figure 5: Ting Internet ARPU & GPPU**

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	1Q21A	2Q21A	3Q21A	4Q21A	FY21A	1Q22A	2Q22A	3Q22E	4Q22E	FY22E	FY23E
<b>Ting Internet</b>											
Revenue	5.1	5.8	6.7	8.6	26.2	9.8	10.2	11.7	12.9	44.6	77.2
% YoY	18%	32%	43%	70%	42%	93%	75%	76%	50%	71%	73%
Gross Profit	2.4	2.8	3.0	5.8	14.0	5.8	5.8	5.9	6.4	23.9	46.3
% margin	48%	48%	45%	67%	54%	59%	57%	50%	50%	53%	60%
Adjusted EBITDA	-2.6	-3.3	-4.4	-3.6	-13.8	-4.3	-6.2	-5.3	-5.8	-21.6	-15.4
% margin	-51%	-57%	-65%	-42%	-53%	-44%	-61%	-45%	-45%	-48%	-20%
<b>Tucows Domains</b>											
Revenue	61.2	62.3	60.7	61.4	245.6	61.5	61.1	61.1	60.6	244.3	246.0
% YoY	3%	4%	0%	-1%	1%	1%	-2%	1%	-1%	-1%	1%
Gross Profit	20.5	19.5	18.5	19.7	78.1	30.9	20.0	19.0	18.8	88.6	76.3
% margin	33%	31%	30%	32%	32%	50%	33%	31%	31%	36%	31%
Adjusted EBITDA	13.8	12.8	12.0	11.6	50.2	11.8	12.1	11.6	11.5	47.0	49.2
% margin	23%	20%	20%	19%	20%	19%	20%	19%	19%	19%	20%
<b>Wavelo</b>											
Revenue	4.3	7.0	8.5	12.5	32.3	6.8	9.0	7.8	8.0	41.3	39.9
% YoY	N/A	N/A	-4%	217%	-36%	60%	28%	-8%	-36%	28%	-3%
Gross Profit	1.5	3.7	4.9	8.8	18.9	5.9	7.8	3.9	4.0	21.5	20.0
% margin	35%	53%	57%	70%	58%	86%	87%	50%	50%	52%	50%
Adjusted EBITDA	4.5	5.3	7.6	8.6	26.0	2.0	3.9	1.2	1.2	8.3	10.0
% margin	105%	75%	90%	69%	80%	30%	43%	15%	15%	20%	25%
<b>Corporate</b>											
Revenue						2.9	2.8	2.0	2.0	9.7	4.0
Adjusted EBITDA	-3.0	-3.6	-3.1	-3.9	-13.6	1.9	1.9	0.9	0.9	5.6	4.0
<b>Total Revenue</b>	<b>70.6</b>	<b>75.1</b>	<b>75.9</b>	<b>82.5</b>	<b>304.0</b>	<b>81.1</b>	<b>83.1</b>	<b>82.6</b>	<b>83.5</b>	<b>330.3</b>	<b>367.1</b>
<b>Total Gross Profit</b>	<b>24.4</b>	<b>26.0</b>	<b>26.4</b>	<b>34.3</b>	<b>111.0</b>	<b>42.5</b>	<b>33.5</b>	<b>28.7</b>	<b>29.2</b>	<b>133.9</b>	<b>142.5</b>
<b>Total Adj. EBITDA</b>	<b>12.7</b>	<b>11.2</b>	<b>12.2</b>	<b>12.7</b>	<b>48.8</b>	<b>11.3</b>	<b>11.7</b>	<b>8.4</b>	<b>7.8</b>	<b>39.2</b>	<b>47.7</b>

Figure 6: Financial Assumptions

Disclosure Code: 2

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TC	1	2	3	4	5	6	7
	NO	YES	NO	NO	NO	NO	NO

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Buy:	Price expected to rise
Speculative Buy:	Buy rating with increased risk
Hold:	Properly priced
Sell:	Price is inflated and expected to decrease
Under Review (U/R):	Under review
Not Rated (N/R):	Not currently rated

Summary of Recommendations	
Buy	17
Speculative Buy	1
Hold	0
Sell	0
U/R	1
<b>Total</b>	<b>19</b>