

NexTech AR Solutions Corp. (NEXCF)
Rating: Buy

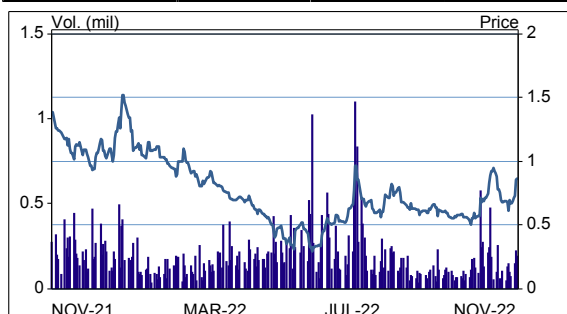
 Scott Buck
 212-856-5730
sbuck@hcwresearch.com
**3Q Results Showcase Increasing Demand for 3D Models;
 Momentum to Carry Into 2023; Reit. Buy, \$2.50 PT**

Stock Data		11/17/2022		
Price				\$0.84
Exchange				OTC
Price Target				\$2.50
52-Week High				\$1.63
52-Week Low				\$0.25
Enterprise Value (M)				\$79
Market Cap (M)				\$85
Shares Outstanding (M)				101.3
3 Month Avg Volume				126,133
Short Interest (M)				NA
Balance Sheet Metrics				
Cash (M)				\$5.3
Total Debt (M)				\$0.0
Total Cash/Share				\$0.05
EPS (\$) Adjusted				
Full Year - Dec	2021A	2022E	2023E	
1Q	(0.12)	(0.08)A	(0.06)	
2Q	(0.07)	(0.09)A	(0.06)	
3Q	(0.09)	(0.04)A	(0.04)	
4Q	(0.11)	(0.06)	(0.04)	
FY	(0.39)	(0.28)	(0.21)	
Revenue (C\$M)				
Full Year - Dec	2021A	2022E	2023E	
1Q	7.7	3.5A	1.5	
2Q	6.1	3.2A	2.7	
3Q	5.7	3.0A	5.0	
4Q	6.4	1.7	5.8	
FY	25.9	11.4	15.0	
EBITDA (\$) Adjusted				
Full Year - Dec	2021A	2022E	2023E	
1Q	(4.5)	(6.0)A	(4.9)	
2Q	(6.0)	(5.5)A	(4.8)	
3Q	(8.7)	(4.1)A	(2.6)	
4Q	(5.9)	(4.8)	(2.3)	
FY	(27.5)	(20.4)	(14.7)	

Large new orders should drive accelerating technology service revenue growth. After the market close on November 17, NexTech AR Solutions Corp. reported 3Q22 operating results that included revenue of C\$3.0M, consistent with 2Q22 levels and largely in line with our C \$3.2M estimate. More important than the consolidated revenue number, technology service revenue of C\$920.8K was up 66.4% sequentially and is expected to increase further in 4Q22 as the company delivers a single C\$700.0K order. Momentum should carry into calendar 2023, as the company is expected to deliver on a C\$6.7M 3D model order for Amazon.com, Inc. (AMZN; not rated), announced in October of this year. We believe this relationship could potentially be expanded in 2023 and expect the company to announce additional 3D modeling contracts with other large e-commerce companies over the coming months. At 60.0%-plus margins, we believe revenue growth, coupled with recent operating expense reductions, should result in significant operating leverage and potentially positive EBITDA as early as 2024. We recommend investors take advantage of this period of business transition to accumulate NEXCF shares at what we view as a meaningful discount and ahead of what we anticipate being a significant improvement in operating results.

Operating results. The company reported 3Q22 revenue of C\$3.0M, just below our C\$3.2M estimate. Lower than expected legacy e-commerce sales was largely offset by higher-than-expected technology service revenue, which we view as more valuable given its margin profile. Gross margin was 44.6%, down sequentially from 52.2%. We suspect some sequential margin pressure was due to discounting as the business looks to liquidate its remaining e-commerce inventory. As the legacy business continues to wind down, we expect consolidated margins to increase. Operating expenses totaled C\$5.5M, down from C\$7.2M sequentially, reflecting recent cost reductions and the spinout of ARway. As slightly lower revenue was more than offset by lower operating expense, EBITDA in the quarter was a loss of C\$4.1M, better than our C\$5.1M loss estimate. The company ended the quarter with approximately C\$5.3M of available cash and, given announced cost-cutting, is not expected to require additional capital over the next 12-months. In addition, following the spinout of ARway last month, the company has C\$26.0M of investment available on its balance sheet.

3D modeling momentum shows no signs of slowing. After quarter end, NexTech AR announced a record purchase order for C\$6.7M, which is expected to be delivered during calendar 2023. The order, which is for Amazon's Prime Marketplace, could potentially grow to as much as \$1.0M per month. Further, the company continues to negotiate 3D modeling contracts with other large enterprise customers, which we believe could be announced over the coming weeks and months. This should begin to provide some strong visibility on 2023 revenue, which we are modeling at C\$15.0M. With the e-commerce industry exceeding C\$5.5T, we believe there is a meaningful opportunity for NexTech AR to continue to grow wallet share within the current customer footprint as well as add new 3D model customers over time.



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Adjusting estimates to reflect exit from legacy business lines, price target unchanged at \$2.50. We are making some meaningful reductions in our revenue forecast for 2022 and 2023 reflecting the closure of the e-commerce business line, which the company should exit entirely during 4Q22. We are now modeling 2022 revenue of C\$11.4M, down from C\$13.8M. Our 2023 revenue forecast is reduced to C\$15.0M from C\$20.0M previously. On the revenue mix shift towards technology services, we expect gross margin to improve to over 60.0% by year-end 2023. We are now modeling EBITDA losses of C\$20.4M in 2022 and C\$14.7M in 2023. Should revenue growth, or gross margin expansion exceed our current expectation, we believe the company could be positioned to start delivering quarterly positive EBITDA as early as late 2023. As this path to profitability becomes clearer, we expect NEXCF shares to draw significant new interest from investors. Our price target remains \$2.50.

Valuation attractive given meaningful revenue growth opportunity and path to profitability. We are valuing NEXCF shares at \$2.50, reflecting a 20.0x EV/revenue multiple on our 2023 revenue estimate of \$15.0M. Our \$2.50 price target represents approximately 200.0% upside from recent trading levels. A targeted 20.0x EV/revenue multiple represents a premium to other small capitalization technology peers operating within the augmented reality, virtual reality, and metaverse space. We view this as warranted in the near term as the business should begin to ramp quickly given recent partnership announcements and anticipated revenue generation. As the company begins to demonstrate its ability to drive meaningful revenue growth, improve gross margin expansion, and achieve consistent profitability we believe new investors should be attracted to NEXCF shares. In addition, we suspect positive news flow, including new contract and partnership announcements to serve as a near term catalyst, ahead of the 2023 acceleration in higher margin technology revenue.

Risks. (1) Dilution risk should the company raise additional capital given current cash burn; (2) high levels of industry competition; (3) technology risk; (4) M&A and integration risk; (5) partnership risk given partnership agreements; (6) foreign operation risk as the company operates in several jurisdictions with different levels of regulatory oversight; and (7) liquidity risk.

NexTech AR Solutions Corp. Model - NEXCF H.C. Wainwright & Co., LLC (Canadian dollar \$000s); December Year-End																	
Fiscal Year in \$ 000's	2019	2020	2021					2022					2023				
	2019E	2020A	1Q21A	2Q21A	3Q21A	4Q21A	2021A	1Q22A	2Q22A	3Q22A	4Q22E	2022E	1Q23E	2Q23E	3Q23E	4Q23E	2023E
Revenue																	
Product Sales		13,933	6,009	4,431	4,580	4,226	19,245	2,988	2,681	2,092	634	8,395	0	0	0	0	0
Technology Services		3,418	1,350	1,371	931	1,643	5,296	37	35	46	55	173	72	105	145	245	567
Renewable software licenses		335	367	290	226	510	1,394	459	518	875	968	2,820	1,447	2,589	4,813	5,585	14,434
Gross revenue	4,004	17,686	7,727	6,092	5,738	6,379	25,935	3,484	3,235	3,012	1,657	11,388	1,519	2,694	4,958	5,830	15,001
Cost of revenue	1,656	7,835	4,412	3,799	3,936	3,949	16,096	2,001	1,546	1,668	812	6,028	669	1,132	1,983	2,215	5,998
Net revenue	2,348	9,851	3,314	2,293	1,801	2,430	9,839	1,483	1,688	1,344	845	5,361	851	1,563	2,975	3,614	9,003
Gross margin	58.6%	55.7%	42.9%	37.6%	31.4%	38.1%	37.9%	42.6%	52.2%	44.6%	51.0%	47.1%	56.0%	58.0%	60.0%	62.0%	60.0%
Operating expenses:																	
Sales and marketing	2,608	9,609	4,640	4,048	4,359	3,768	16,815	2,617	1,827	1,703	1,696	7,842	1,963	1,644	1,618	1,730	6,954
General and administrative	1,762	5,841	3,748	3,418	3,735	2,980	13,881	3,821	4,503	2,592	2,831	13,747	2,674	3,828	2,722	2,973	12,197
Research and development	721	3,592	1,793	1,331	1,864	1,624	6,612	1,027	880	1,157	1,137	4,202	1,130	933	1,227	1,239	4,529
Total costs and expenses	5,092	19,042	10,181	8,797	9,958	8,373	37,308	7,465	7,211	5,452	5,664	25,792	5,767	6,405	5,566	5,942	23,680
Operating income	(2,744)	(9,191)	(6,867)	(6,504)	(8,156)	(5,943)	(27,470)	(5,981)	(5,522)	(4,108)	(4,819)	(20,431)	(4,916)	(4,842)	(2,592)	(2,327)	(14,678)
EBITDA	(2,744)	(9,191)	(6,867)	(6,504)	(8,156)	(5,943)	(27,470)	(5,981)	(5,522)	(4,108)	(4,819)	(20,431)	(4,916)	(4,842)	(2,592)	(2,327)	(14,678)
EBITDA margin	-116.9%	-93.3%	-88.9%	-106.8%	-142.2%	-93.2%	-105.9%	-171.7%	-170.7%	-136.4%	-290.9%	-179.4%	-323.6%	-179.7%	-52.3%	-39.9%	-97.8%
Other expense (income)																	
Stock based compensation	391	5,665	2,403	556	(574)	2,646	5,030	579	878	311	400	2,168	600	700	800	800	2,900
Amortization	190	672	380	179	683	808	2,050	728	750	597	600	2,676	750	700	700	700	2,850
Right of use amortization	0	0	(219)	45	65	316	206	63	64	78	78	282	78	78	78	78	310
Gain on digital assets	0	0	28	0	0	(247)	(219)	0	0	(91)	0	(91)	0	0	0	0	0
Impairment	69	69	0	0	0	0	0	0	2,702	0	0	2,702	0	0	0	0	0
Loss on contingent consideration	0	0	0	(1,516)	102	(160)	(1,573)	0	0	0	0	0	0	0	0	0	0
Depreciation	22	83	0	32	37	64	133	37	37	37	40	151	40	40	40	40	160
Foreign exchange gain (loss)	10	10	(275)	53	(253)	207	(268)	447	(846)	(567)	0	(966)	0	0	0	0	0
Total other income	682	6,500	2,317	(650)	60	3,633	5,360	1,854	3,586	366	1,118	6,923	1,468	1,518	1,618	1,618	6,220
Income (loss) before income taxes	(3,426)	(15,691)	(9,184)	(5,854)	(8,217)	(9,575)	(32,829)	(7,835)	(9,108)	(4,474)	(5,937)	(27,355)	(6,384)	(6,360)	(4,209)	(3,945)	(20,898)
Income tax provision	0	97	0	0	0	177	177	(7)	(7)	(7)	0	(21)	0	0	0	0	0
Deferred income tax recovery								139	122	127							
Net Income	(3,426)	(15,594)	(9,184)	(5,854)	(8,217)	(9,397.9)	(32,652)	(7,703.5)	(9,115.4)	(4,354.7)	(5,936.6)	(27,376)	(6,383.8)	(6,360.0)	(4,209.4)	(3,944.9)	(20,898)
Net Income Margin %																	
Other comprehensive income:																	
Exchange difference on translating foreign operations	0	(253)	(52)	(65)	414	(69)	227	(25)	(25)	(183)	(183)	(416)	(183)	(183)	(183)	(183)	(734)
Comprehensive income (loss)	(3,426)	(15,846)	(9,236)	(5,919)	(7,803)	(9,467)	(32,425)	(7,728)	(9,140)	(4,538)	(6,120)	(27,792)	(6,567)	(6,544)	(4,393)	(4,128)	(21,632)
Basic Earnings Per Share	(\$0.06)	(\$0.23)	(\$0.12)	(\$0.07)	(\$0.09)	(\$0.11)	(\$0.39)	(\$0.08)	(\$0.09)	(\$0.04)	(\$0.06)	(\$0.28)	(\$0.06)	(\$0.06)	(\$0.04)	(\$0.04)	(\$0.21)
Diluted Earnings Per Share	(\$0.06)	(\$0.23)	(\$0.12)	(\$0.07)	(\$0.09)	(\$0.11)	(\$0.39)	(\$0.08)	(\$0.09)	(\$0.04)	(\$0.06)	(\$0.28)	(\$0.06)	(\$0.06)	(\$0.04)	(\$0.04)	(\$0.21)
Average Shares Outstanding (Basic)	58,291	68,657	77,490	82,298	86,125	89,641	83,888	97,551	99,725	98,641	99,134	98,763	99,630	100,128	100,629	101,132	100,380
Average Shares Outstanding (Diluted)	58,291	68,657	77,490	82,298	86,125	89,641	83,888	97,551	99,725	98,641	99,134	98,763	99,630	100,128	100,629	101,132	100,380
Operating Metrics																	
Revenue Growth	n/a	319.6%	145.9%	5.7%	-39.1%	-28.0%	-0.1%	-55.2%	-26.4%	-25.4%	-65.2%	-45.5%	-42.6%	-7.4%	121.3%	327.8%	67.9%
Price	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84	\$0.84
Market Capitalization (CAD\$000s)	\$48,964	\$63,469	\$65,091	\$69,131	\$72,345	\$75,298	\$75,298	\$81,943	\$83,769	\$82,859	\$83,273	\$83,273	\$83,689	\$84,108	\$84,528	\$84,951	\$84,951
Enterprise Value (CAD\$000s)	\$46,115	\$52,784	\$57,191	\$53,736	\$64,087	\$68,152	\$68,152	\$71,161	\$76,706	\$77,580	\$82,683	\$82,683	\$88,697	\$94,375	\$98,186	\$102,028	\$102,028
Price-to-Earnings	n/a	-3.8x	-2.6x	-1.8x	-1.9x	-2.2x	-2.2x	-2.4x	-2.3x	-2.6x	-3.1x	-3.1x	-3.2x	-3.6x	-3.7x	-4.0x	-4.0x
EV to EBITDA	-16.8x	-4.8x	-3.8x	-2.7x	-2.2x	-2.5x	-2.5x	-2.7x	-3.0x	-3.6x	-4.0x	-4.0x	-4.6x	-5.1x	-5.7x	-7.0x	-7.0x
Shareholders Equity	7,066	22,419	17,399	32,668	25,467	24,262	24,262	26,766	18,811	16,524	11,410	11,410	5,856	334	-3,029	-6,118	-6,118
Net Debt	(2,849)	(10,685)	(7,900)	(15,395)	(8,259)	(7,146)	(7,146)	(10,782)	(7,063)	(5,279)	(590)	(590)	5,008	10,267	13,657	17,077	17,077

Source: Factset as of November 17, 2022 and H.C. Wainwright & Co. estimates.

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RETURN ASSESSMENT

Market Outperform (Buy): The common stock of the company is expected to outperform a passive index comprised of all the common stock of companies within the same sector.

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Distribution of Ratings Table as of November 17, 2022

Ratings	Count	Percent	IB Service/Past 12 Months	
			Count	Percent
Buy	572	86.93%	123	21.50%
Neutral	66	10.03%	8	12.12%
Sell	0	0.00%	0	0.00%
Under Review	20	3.04%	4	20.00%

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