

**Action Summary – 21 Aug 2023**

Analyst Theodore R. O'Neill - Robust revenue growth offset by rising costs – *Reiterate our Buy rating and a \$9 PT.*

- **Robust Sales Growth Offset by Shift in Product Mix and Rising Costs.** UCL reported 2Q23 revenue of \$22MM and an EPS of \$0.00 (\$0.02 loss per ADS). We had anticipated revenue of \$21.5MM and an EPS of \$0.00 (\$0.01 gain per ADS). The consensus was for revenue of \$21.65MM and an EPS gain of \$0.01. The unfavorable \$0.03 per ADS EPS variance was primarily due to higher costs of products sold, increased sales and G&A expenses, reduced margins resulting from a greater product over service mix, and fair value losses on other investments.
- **Core data services continue to grow.** The volume of data moving through its platform has grown at a 25% CAGR for the last three years. Total data consumed through its platform in 2Q increased by 5.3% year over year.
- **Revenue continues to rebound with international travel recovery.** The resurgence in international travel is one of the primary drivers behind the significant growth in sales. Average daily active terminals reached a new record of 318,778, up 4.8% from 304,121 in 1Q23 and 9.0% from 292,432 in 2Q22.
- **New products and plans for further expansion.** In July 2023, UCL introduced the GlocalMe SIM card, featuring patented cloud SIM technology, in 10 key countries such as Japan, the U.S., and Australia. Further expansion is planned. Additionally, UCLCLOUDLINK's Internet of Things (IoT) modules are set to be integrated into a major Japanese mobile operator's devices in 2023, which will diversify revenue streams.
- **Attractive Valuation.** Based on our discounted future earnings model, the value of all future earnings is \$9/share. If the shares were to trade at the average multiple of its comparables for 2024 Price to Sales, or 2024 EV to Sales, the share price would be >\$12, surpassing our \$9 target.

8/18 Closing price: <b>\$2.60</b>	Market cap: <b>\$101MM</b>	Market Cap/ 2024 Sales: <b>1.41x</b>	EV/2024 Sales: <b>1.16</b>
Diluted Class A ADS shares outstanding: <b>37MM</b>	Insider ownership: <b>52%</b>	3-mo avg. daily trading volume: <b>&gt;10,000</b>	Dividend /Yield: <b>NA</b>

**GAAP estimates (EPS per ADS - Revenue in USD millions)**

Period	EPS	Revenue	Op Margin
1Q22A	(\$0.27)	\$15.6	
2Q22A	(\$0.22)	\$18.0	
3Q22A	(\$0.15)	\$18.2	
4Q22A	<u>(\$0.03)</u>	<u>\$19.6</u>	
FY22A	<u>(\$0.64)</u>	<u>\$71.5</u>	<u>(26.9%)</u>
1Q23A	\$0.06	\$18.0	
2Q23A	\$(0.02)	\$22.0	
3Q23E	\$0.03	\$24.0	
4Q23E	<u>\$0.05</u>	<u>\$25.0</u>	
FY23E	<u>\$0.12</u>	<u>\$89.0</u>	<u>4.8%</u>
1Q24E	\$0.03	\$22.0	
2Q24E	\$0.06	\$26.0	
3Q24E	\$0.09	\$28.0	
4Q24E	<u>\$0.07</u>	<u>\$27.0</u>	
FY24E	<u>\$0.24</u>	<u>\$103.0</u>	<u>8.4%</u>

Note: Numbers may not add up due to rounding. See our full model at the back of this report.

**Cash balance (in USD millions)**

• 2021A	• \$8.1
• 2022A	• \$15.1
• 2023E	• \$20.7
• 2024E	• \$33.5

**Adj. EBITDA (in USD millions)**

• 2021A	• (\$22.6)
• 2022A	• (\$2.3)
• 2023E	• \$10.3
• 2024E	• \$15.6

**Risks/Valuation**

- Risks: dependence on network operators, a highly regulated industry, currently generating losses
- Our \$9 price target is derived from our discounted future earnings model

**Company description:** UCloudlink Group, Inc. is the world's first and leading mobile data traffic sharing marketplace. It pioneers the sharing economy business model for the telecommunications industry. The Company's products and services offer unique value propositions to mobile data users, handset and smart-hardware companies, mobile virtual network operators (MVNOs) and mobile network operators (MNOs).

Figure 1 – UCloudlink Group, Inc. – One-Year Trading snapshot



Source: CapitalIQ

## Quarterly Results

**Robust Sales Growth Offset by Shift in Product Mix and Rising Costs.** UCL reported 2Q23 revenue of \$22MM and an EPS of \$0.00 (\$0.02 loss per ADS). We had anticipated revenue of \$21.5MM and an EPS of \$0.00 (\$0.01 gain per ADS). The consensus was for revenue of \$21.65MM and an EPS gain of \$0.01. FactSet did not compile a consensus for EPS per ADS. Compared to our estimates (see Figure 2), the unfavorable \$0.03 per ADS EPS variance was primarily due to higher costs of products sold, increased sales and G&A expenses, reduced margins resulting from a greater product over service mix, and fair value losses on other investments.

Year over year, service revenues for Q2 2023 rose 25.2% to US\$14.1MM compared to Q2 2022. Costs for the same period increased 20.1% to US\$5.9MM. Product revenues in Q2 2023 grew 16.5% to US\$7.9MM, largely from terminal sales, with costs up 20.5% to US\$6.2MM. Overall gross profit increased by 24% to US\$9.9MM over Q2 2022.

Operational losses decreased to US\$0.9MM from US\$5.8MM in Q2 2022. Net loss was US\$0.9MM, compared to a net loss of US\$6.3MM in the second quarter of 2022. Adjusted EBITDA (Non-GAAP) was US\$2.1MM, improving from negative US\$1.0MM in the same period the previous year.

**Core data services continue to grow.** The volume of data moving through its platform has grown at a 25% CAGR for the last three years. Total data consumed through its platform in 2Q23 was 45,682 terabytes (5,530 procured by the company and 40,152 procured by its business partners), representing an increase of 4% from 43,936 terabytes in 1Q23.

**Revenue continues to rebound with international travel recovery.** The resurgence in international travel is one of the primary drivers behind the significant growth in sales. Average daily active terminals reached a new record of 318,778, up 4.8% from 304,121 in 1Q23 and 9.0% from 292,432 in 2Q22.

**New products and plans for further expansion.** In July 2023, UCL introduced the GlocalMe SIM card with patented cloud SIM technology. It offers multiple global data plans and is currently available in 10 key countries including Japan, the U.S., and Australia, with plans for further expansion. Additionally, UCLOUDLINK's Internet of Things (IoT) modules will be integrated into a major Japanese mobile operator's devices in 2023, diversifying revenue streams.

Revision to estimates. We are lowering our 2023 EPS but raising revenue. Our new 2023 revenue and EPS estimates are \$89.5MM and \$0.12, respectively compared to our previous estimates of \$87.5MM and \$0.14.

Figure 2 – UCloudlink Group, Inc. – Quarterly Variance Analysis (\$000)

Income Statement	FY23 Q2E	FY23 Q2A	Better / (Worse) Than Estimates
Revenue from services	\$14,500	\$14,096	(\$404)
Revenue from products	\$7,000	\$7,881	\$881
Total Revenue	21,500	21,977	\$477
Cost of services	6,235	5,927	\$308
Cost of products	5,180	6,185	(1,005)
Total cost of products sold	11,415	12,112	(\$697)
Gross profit from services	8,265	8,169	(\$96)
Gross profit from products	1,820	1,696	(124)
Total Gross Profit	10,085	9,865	(\$220)
Operating expenses:			
R&D	2,000	1,554	\$446
Sales and Marketing	3,000	3,516	(\$516)
G&A	3,500	3,866	(\$366)
Other expense, net	1,000	1,866	(866)
Total Expenses	9,500	10,802	(1,302)
Earnings (loss) from Operations	585	(937)	(1,522)
Total Other income/(expense)	(50)	51	\$101
Earnings before taxes	535	(886)	(\$1,421)
Tax expense/(benefit)	0	31	(31)
Net income	\$535	(\$917)	(\$1,452)
EPS	\$0.00	(\$0.00)	(\$0.00)
EPS per ADS	\$0.01	(\$0.02)	(\$0.03)
Share count	370,000	370,600	\$600

Source: Company filings and Litchfield Hills Research LLC

## Guidance and Financial Forecasts

The Company has provided guidance for its next quarter, forecasting 3Q23 revenue to range between \$23.5MM and \$24.5MM. This represents a YoY increase of 29.1% to 34.6%.

## Valuation and Price Target

### Valuation Methodology

We believe UCL is undervalued, and we support that belief with two valuation techniques. To determine our price target, we use a discounted future earnings model (see Figure 3) and then compare its valuation to that of its peers (see Figure 4).

### Discounted Future Earnings – Basis for Price Target

Our 12-month price target of \$9 is derived from a discounted earnings model. To determine this valuation, we aggregate all projected future earnings on a GAAP basis and discount them at a rate of 7.0%. We project that earnings will grow at a double-digit rate until 2027, after which growth is anticipated to decelerate to the rate of GDP. Our detailed valuation model can be found in Figure 3 below. It's important to note that this model likely understates potential earnings from new services, growth due to acquisitions, and possible tax benefits. However, as a counterbalance, our model also assumes consistent, uninterrupted yearly earnings growth. The calculated share price is \$9.32, which we've rounded down to \$9.00.

*Figure 3 – UCloudlink Group, Inc. – Price Target Calculation*

Implied Value of Future Discounted Earnings:		\$9.32
Year 1 is 2023		
Year	Forecast GAAP EPS	Discounted EPS
1	\$0.11	\$0.11
2	\$0.23	\$0.20
3	\$0.30	\$0.24
4	\$0.35	\$0.27
5	\$0.40	\$0.29
6	\$0.45	\$0.30
Terminal Value		\$7.91

Source: Litchfield Hills Research LLC

### Valuation Relative to Peers

Figure 4 provides a summary of our peer comparison for UCL. While these companies operate in similar sectors, none are direct comparables. If the shares were to match the average multiple of the group based on the 2024 Price to Sales or 2024 EV to Sales, the share price would surpass \$12, which is higher than our \$9 target. This, along with our discounted earnings model valuation, supports our belief that the shares are undervalued.

*Figure 4 – UCloudlink Group, Inc. – Valuation of Peers*

Ticker	Name	Price	Market Cap USD	EV USD	LTM Revenue USD	LTM Sales / Market Cap	2024 Price to Sales	2024 EV / Sales	2024 EV / EBITDA
CRM-US	Salesforce, Inc.	\$208.78	203,352	206,181	32,188	6.3x	5.2x	5.3x	14.9x
HUBS-US	HubSpot, Inc.	\$508.56	25,436	24,548	1,944	13.1x	9.9x	9.4x	52.2x
ZM-US	Zoom Video Communications, Inc. Class A	\$66.06	19,656	14,572	4,425	4.4x	4.1x	3.0x	7.8x
TWLO-US	Twilio, Inc. Class A	\$61.22	11,088	8,761	4,052	2.7x	2.5x	2.0x	
PCTY-US	Paylocity Holding Corp.	\$194.81	10,894	10,807	1,175	9.3x	7.8x	7.7x	23.3x
ZI-US	ZoomInfo Technologies Inc	\$18.23	7,319	7,979	1,199	6.1x	5.4x	5.9x	13.9x
FIVN-US	Five9, Inc.	\$71.39	5,155	5,248	848	6.1x	4.8x	4.9x	26.7x
EVCN-US	EverCommerce, Inc.	\$10.66	2,012	2,479	651	3.1x	2.6x	3.2x	14.7x
LVOX-US	LiveVox Holding, Inc. Class A	\$3.29	310	305	143		1.9x	1.9x	22.1x
Average						<b>6.4x</b>	<b>4.9x</b>	<b>4.8x</b>	<b>21.9x</b>
UCL-US	uCloudlink Group, Inc. Sponsored ADR	\$3.09	114	88	74	1.5x	1.1x	0.9x	5.6x
<b>UCL shares trading at a discount to peers:</b>						<b>-76%</b>	<b>-78%</b>	<b>-82%</b>	<b>-75%</b>

Source: Litchfield Hills Research LLC and FactSet

Figure 5– UCloudlink Group, Inc. – Income Statement (\$000 USD, except per share)

December ending year	2021A	2022A	2023E				2023E	2024E				2024E
	Year	Year	Q1A	Q2A	Q3E	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Year
Revenue from services	37,799	46,228	\$12,916	\$14,096	\$15,500	\$18,000	60,512	\$15,000	\$18,000	\$20,000	\$20,000	73,000
Revenue from products	36,026	25,233	5,090	7,881	8,500	7,000	28,471	7,000	8,000	8,000	7,000	30,000
<b>Total revenue</b>	<b>\$73,825</b>	<b>\$71,461</b>	<b>\$18,006</b>	<b>\$21,977</b>	<b>\$24,000</b>	<b>\$25,000</b>	<b>\$88,983</b>	<b>\$22,000</b>	<b>\$26,000</b>	<b>\$28,000</b>	<b>\$27,000</b>	<b>\$103,000</b>
<i>Growth</i>		-3%	15%	22%	32%	27%	25%	22%	18%	17%	8%	16%
<i>Cost of services</i>	21,556	20,346	5,102	5,927	6,975	8,100	26,104	6,750	8,100	9,000	9,000	32,850
<i>Cost of products</i>	30,434	18,581	4,303	6,185	6,120	5,040	21,648	5,040	5,760	5,760	5,040	21,600
Cost of Goods	51,990	38,927	9,405	12,112	13,095	13,140	47,752	11,790	13,860	14,760	14,040	54,450
<b>Gross Profit</b>	<b>21,835</b>	<b>32,534</b>	<b>8,601</b>	<b>9,865</b>	<b>10,905</b>	<b>11,860</b>	<b>41,231</b>	<b>10,210</b>	<b>12,140</b>	<b>13,240</b>	<b>12,960</b>	<b>48,550</b>
<b>Gross Margin</b>	<b>29.6%</b>	<b>45.5%</b>	<b>47.8%</b>	<b>44.9%</b>	<b>45.4%</b>	<b>47.4%</b>	<b>46.3%</b>	<b>46.4%</b>	<b>46.7%</b>	<b>47.3%</b>	<b>48.0%</b>	<b>47.1%</b>
R&D	13,697	8,430	1,303	1,554	2,100	2,000	6,957	1,368	1,632	2,205	2,100	7,305
Sales and Marketing	13,620	10,305	2,921	3,516	3,000	3,000	12,437	3,067	3,692	3,150	3,150	13,059
G&A	28,552	18,726	3,435	3,866	3,500	4,000	14,801	3,607	4,059	3,675	4,200	15,541
Other expense, net	11,876	14,265	(1,121)	1,866	1,000	1,000	2,745	1,000	1,000	1,000	1,000	4,000
Total Operating Expenses	67,745	51,726	6,538	10,802	9,600	10,000	36,940	9,042	10,383	10,030	10,450	39,905
Operating expense margins	92%	72%	36%	49%	40%	40%	42%	41%	40%	36%	39%	39%
<b>Operating Income</b>	<b>(45,910)</b>	<b>(19,192)</b>	<b>2,063</b>	<b>(937)</b>	<b>1,305</b>	<b>1,860</b>	<b>4,291</b>	<b>1,168</b>	<b>1,757</b>	<b>3,210</b>	<b>2,510</b>	<b>8,645</b>
<b>Operating Margin</b>	<b>-62.2%</b>	<b>-26.9%</b>	<b>11.5%</b>	<b>-4.3%</b>	<b>5.4%</b>	<b>7.4%</b>	<b>4.8%</b>	<b>5.3%</b>	<b>6.8%</b>	<b>11.5%</b>	<b>9.3%</b>	<b>8.4%</b>
Total Other Items	(174)	(572)	24	51	(50)	(50)	(25)	(50)	(50)	(50)	(50)	(200)
<b>Pre-Tax Income</b>	<b>(46,084)</b>	<b>(19,764)</b>	<b>2,087</b>	<b>(886)</b>	<b>1,255</b>	<b>1,810</b>	<b>4,266</b>	<b>1,118</b>	<b>1,707</b>	<b>3,160</b>	<b>2,460</b>	<b>8,445</b>
<b>Pre-Tax Margin</b>	<b>-62.4%</b>	<b>-27.7%</b>	<b>11.6%</b>	<b>-4.0%</b>	<b>5.2%</b>	<b>7.2%</b>	<b>4.8%</b>	<b>5.1%</b>	<b>6.6%</b>	<b>11.3%</b>	<b>9.1%</b>	<b>8.2%</b>
Taxes (benefit)	(43)	89	13	31	0	0	44	0	0	0	0	0
Tax Rate	0.1%	-0.5%	0.6%	-3.5%	0.0%	0.0%	1.0%	0.0%	0.0%	0.0%	0.0%	0.0%
<b>Net Income (loss)</b>	<b>(46,041)</b>	<b>(19,853)</b>	<b>2,074</b>	<b>(917)</b>	<b>1,255</b>	<b>1,810</b>	<b>4,222</b>	<b>1,118</b>	<b>1,707</b>	<b>3,160</b>	<b>2,460</b>	<b>8,445</b>
<b>Net Margin</b>	<b>-62.4%</b>	<b>-27.8%</b>	<b>11.5%</b>	<b>-4.2%</b>	<b>5.2%</b>	<b>7.2%</b>	<b>4.7%</b>	<b>5.1%</b>	<b>6.6%</b>	<b>11.3%</b>	<b>9.1%</b>	<b>8.2%</b>
EPS	(0.16)	(0.06)	0.01	(0.00)	0.00	0.00	0.01	0.00	0.00	0.01	0.01	0.02
EPS per ADS	(1.61)	(0.64)	0.06	(0.02)	0.03	0.05	0.11	0.03	0.05	0.09	0.07	0.23
Share count	285,979	312,485	369,438	370,600	370,000	370,000	370,010	370,000	370,000	370,000	370,000	370,000

Source: Company reports and Litchfield Hills Research LLC

Figure 6 – UCloudlink Group, Inc. – Balance Sheet (\$000 USD)

December ending year	2024E	2023E	2022A	2021A
<b>Balance sheet</b>				
<b>Current Assets</b>				
Cash and S.T.I.	\$33,552	\$21,157	\$15,118	\$8,064
Accounts receivable	6,800	6,200	5,961	14,923
Inventories	12,000	12,000	11,690	12,587
Other assets	<u>5,750</u>	<u>5,500</u>	<u>4,953</u>	<u>7,378</u>
<b>Total Current Assets</b>	<b>62,302</b>	<b>48,757</b>	<b>41,346</b>	<b>49,085</b>
Net PP&E	2,100	2,000	1,181	1,796
Other non-current assets	3,800	3,500	3,407	16,244
<b>Total Assets</b>	<b>\$68,202</b>	<b>\$54,257</b>	<b>\$45,934</b>	<b>\$67,125</b>
<b>Current Liabilities</b>				
Accounts payable	\$9,000	\$8,000	\$6,832	\$12,986
Accrued expenses	31,000	28,000	26,890	30,757
Other current liabilities	<u>3,500</u>	<u>3,000</u>	<u>2,717</u>	<u>3,028</u>
<b>Total current liabilities</b>	<b>43,500</b>	<b>39,000</b>	<b>36,439</b>	<b>46,771</b>
Notes	1,000	0	0	0
Other non-current	<u>300</u>	<u>300</u>	<u>204</u>	<u>262</u>
<b>Total Liabilities</b>	<b>44,800</b>	<b>39,300</b>	<b>36,643</b>	<b>47,033</b>
<b>Stockholders' Equity</b>				
Preferred stock				
Common stock	112	112	18	14
Additional paid-in-capital	240,000	240,000	236,774	230,048
Retained earnings	(216,710)	(225,155)	(229,377)	(209,524)
Cum. trans. adj. and treasury stock	<u>0</u>	<u>0</u>	<u>1,876</u>	<u>(446)</u>
Total stockholders' equity	<u>23,402</u>	<u>14,957</u>	<u>9,291</u>	<u>20,092</u>
<b>Total Liabilities and equity</b>	<b>\$68,202</b>	<b>\$54,257</b>	<b>\$45,934</b>	<b>\$67,125</b>

Source: Company reports and Litchfield Hills Research LLC

Figure 7 – UCloudlink Group, Inc. – Cash Flow (\$000 USD)

Statement of Cash Flows (\$000)	2024E	2023E	2022A	2021A	2020A	2019A
Net Income	\$8,445	\$4,222	(\$19,853)	(\$46,041)	\$257	\$9,738
Accounts receivable	(600)	(239)	8,962	29,738	7,276	(8,869)
Inventories	(300)	(276)	2,509	21,952	(305)	(13,613)
Other investments	0	(310)	897	1,410	(5,424)	12,717
Other assets	(250)	(547)	2,425	4,211	(5,828)	1,752
PP&E	(100)	(819)	615	15,115	344	(76)
Other non-current	(300)	(93)	12,837	6,696	3,001	(10,525)
Accounts payable	1,000	1,168	(6,154)	(19,009)	(3,610)	4,727
Accrued expenses	2,000	986	(3,566)	660	4,365	(3,309)
Short term borrowings	1,000	124	(301)	(18,695)	7,910	(5,338)
Other current liabilities	500	283	(311)	(10,155)	3,094	(337)
Notes	1,000	0	0	(8,142)	(1,520)	3,069
Other non-current	0	96	(58)	(8,746)	3,204	320
Preferred stock	0	0	0	0	0	0
Commons stock	0	94	4	(94)	0	0
Additional paid in capital	0	3,226	6,726	(584,235)	(859)	(1,230)
Accumulated other comp. loss and other	0	(1,876)	2,322	14,523	(2,233)	(131)
Dividend and/or tax adj.						5,623
Total Cash Flow	\$12,395	\$6,039	\$7,054	(\$600,812)	\$9,672	(\$5,482)

Source: Litchfield Hills Research LLC

**Disclosures:**

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**BUY:** We expect the stock to provide a total return of 15% or more within a 12-month period.

**HOLD:** We expect the stock to provide a total return of negative 15% to positive 15% within a 12-month period.

**SELL:** We expect the stock to have a negative total return of more than 15% within a 12-month period.

Total return is defined as price appreciation plus dividend yield.

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