Trickle Research

Every raging river, every great lake, every deep blue sea starts … with a trickle

Q3F22 Earnings Update

One Soft Solutions, Inc.

(OTC: OSSIF, TSX-V: OSS.V)

Report Date: 04/13/23

12- 24 month Price Target: US$.60

Allocation: 4

Closing Stock Price at Initiation (Closing Px: 09/27/22):US$.34

Closing Stock Price at This Update (Closing Px: 04/13/23):US$.33

Prepared By:
David L. Lavigne
Senior Analyst, Managing Partner Trickle Research

Disclosure: Portions of this report are excerpted from OneSoft's filings, website(s), presentations or other public collateral. We have attempted to identify those excerpts by *italicizing* them in the text.

One Soft reported year end numbers several days ago, and those numbers were better than we had anticipated both from our initiating coverage in September (2022) as well as from our update following Q3F22. Specifically, they reported revenues for fiscal 2022 of $6.9 million versus our initiating estimate of $5.5 million, an operating loss of $3 million versus $4.2 million, and eps of <$.02> vs. <$.03>. Clearly, they performed much better than we originally anticipated, and that included both revenue and expense items. In retrospect, in terms of our revisions following Q3 numbers, Q3 was a particularly strong quarter both YoY as well as sequentially. For instance, it was a markedly stronger quarter than Q1F22 and Q2F22, and we attributed to the lumpiness of the business, however, given that 4QF22 was even stronger than Q3F22, it is beginning to look more like a trend. We would add, by the time the Company reported earnings, none of this was particularly surprising because they provided detailed preliminary guidance in late January, which was largely spot on relative to reported audited results.

Looking ahead, the Company has again provided some detailed guidance into fiscal 2023, and that includes some granular information that we think further illustrates some of their momentum. First, on the high level, they are guiding to revenues of $10.1 million and net income of <$1.2 million> for fiscal 2023 and that compares to our *initiating* estimate of $10.4 million and <$2.2 million> respectively. Again, we revised that to $11.2 million and <$1.7 million> when we updated the model following 3QF22. Putting those comps into perspective, while our 3QF22 estimate for F2023 revenues was roughly $1 million higher than their current guidance, they are also guiding to a loss of about $500,000 *less than* our estimate at that time. Clearly, they are managing expenses much better than we anticipated, which frankly, is quite refreshing. Put another way, generally, we have no argument with better results on lower revenues. That noted, as a bit of insight into our thinking/modeling, to reiterate, we are still wrestling with quarter-to-quarter results in terms of what may be lumpiness and what may be sustainable momentum. To that end, there is some additional more granular guidance they provided with the year end numbers. They illustrated the guidance in a set of charts, and we found certain portions of these quite telling.

First, for reference, **Table 1.** reflects the guidance we addressed above. **Tables 2 & 3** reflect some cash issues we will address later in this update so we will skip to **Tables 4.**

Table 1.

Net income (loss) *$ 000's except percentages*	**Fiscal 2019 (Actual)**	**Fiscal 2020 (Actua)**	**Fiscal 2021 (Actual)**	**Fiscal 2022 (Actual)**	**Fiscal 2023 (Forecast)**	***% Change 2022 to 2021***	***% Change 2023 to 2022***
Revenue	$ 2,712	$ 4,056	$ 4,442	$ 6,889	$ 10,104	*55 %*	*47 %*
Direct costs	$ (702)	$ (921)	$ (1,125)	$ (1,978)	$ (2,526)	*76 %*	*28 %*
Gross Profit	$ 2,010	$ 3,135	$ 3,317	$ 4,910	$ 7,578	*48 %*	*54 %*
Salaries and employee benefits	$ (3,527)	$ (4,436)	$ (4,550)	$ (5,398)	$ (5,617)	*19 %*	*4 %*
Marketing expense	$ (460)	$ (563)	$ (735)	$ (1,008)	$ (911)	*37 %*	*(10) %*
General and administrative	$ (716)	$ (705)	$ (796)	$ (1,046)	$ (1,454)	*31 %*	*39 %*
Less costs capitalized	$ 102	$ 51	$ 289	$ 391	$ 275	*35 %*	*(30) %*
Operating expense, net of costs capitalized	$ (4,601)	$ (5,654)	$ (5,792)	$ (7,061)	$ (7,707)	*22 %*	*9 %*
Other expense	$ (1,015)	$ (737)	$ (1,414)	$ (821)	$ (1,168)	*42 %*	*42 %*
Net Loss	$ (3,606)	$ (3,256)	$ (3,889)	$ (2,972)	$ (1,297)	*24 %*	*56 %*

Table 2.

Adjusted EBITDA Reconciliation *$ 000's except percentages*	Fiscal 2019 (Actual)	Fiscal 2020 (Actua)	Fiscal 2021 (Actual)	Fiscal 2022 (Actual)	Fiscal 2023 (Forecast)	*% Change 2022 to 2021*	*% Change 2023 to 2022*
Net Loss	$ (3,606)	$ (3,256)	$ (3,889)	$ (2,972)	$ (1,297)	*24 %*	*56 %*
Add (subtract):							
Depreciation and amortization	$ 407	$ 416	$ 456	$ 461	$ 564		
Stock based compensation	$ 663	$ 589	$ 960	$ 619	$ 813		
Interest (income)	$ (147)	$ (115)	$ (24)	$ (67)	$ (108)		
Adjusted EBITDA	$ (2,683)	$ (2,366)	$ (2,497)	$ (1,959)	$ (28)	*22 %*	*99 %*

Table 3.

Cash and Deferred Revenue *$ 000's except percentages*	Fiscal 2019 (Actual)	Fiscal 2020 (Actua)	Fiscal 2021 (Actual)	Fiscal 2022 (Actual)	Fiscal 2023 (Forecast)	*% Change 2022 to 2021*	*% Change 2023 to 2022*
Cash and cash equivalents	$ 10,512	$ 7,223	$ 5,509	$ 4,392	$ 4,040	*(20) %*	*(8) %*
Deferred revenue	$ 1,640	$ 414	$ 1,184	$ 2,104	$ 1,815	*78 %*	*(14) %*

Table 4. provides a handful of interesting observations regarding the Company's momentum. In short, recognize that as they move (moved) forward, most of these line items reflect growth. While this is still not enough information for us to accurately reflect *exactly when* they will recognize revenues around the data, we think it is reasonable to suggest that they illustrate the trend. Further, we found the last (highlighted) line item particularly interesting, especially in the context of the narrative that follows the table, which we excerpted from the F2022 MD&A:

Table 4.

CIM Use & Revenue Generating Data-miles	Fiscal 2019 (Actual)	Fiscal 2020 (Actua)	Fiscal 2021 (Actual)	Fiscal 2022 (Actual)	Fiscal 2023 (Forecast)	*% Change 2022 to 2021*	*% Change 2023 to 2022*
Pipeline miles on SaaS subscription	38,631	38,793	91,266	98,839	151,195	*8 %*	*53 %*
Pipeline miles generating revenue	22,549	29,544	41,320	53,483	65,697	*29 %*	*23 %*
% of subscription miles generating revenue	*58%*	*76%*	*45%*	*54%*	*43%*	*n/a*	*n/a*
Revenue per mile for revenue generating miles (Note 1)	*$ 120.26*	*$ 137.29*	*$ 107.50*	*$ 105.34*	*$ 130.97*	*n/a*	*n/a*

Note 1: *The revenue per mile for revenue generating miles is different from the estimate in the January 24, 2023 guidance, recalculated for Fiscals 2022 and 2023 to reflect CIM revenue only and exclude IM Operations revenue.*

> *In Fiscal 2022 the Company added a pricing strategy based on ingested data-miles so new customers could ramp their CIM costs over a 5 or 7 year period, commensurate with their regulatory inline inspection schedule sfor liquid and gas pipelines, respectively. While some customers may onboard all of their pipeline assets over shorter or longer periods, we believe this consumption is generally reasonable to forecast revenue. For example, assuming a $100 per data-mile figure, revenue expectations for a customer with 10,000 miles of liquid pipeline would approximate $200,000 in year 1; $400,000 in year 2; $600,000 in year 3; $800,000 in year 4; and $1 million in the fifth and subsequent years. Readers are cautioned that this theoretical assumption will not be accurate for all customer scenarios and that pricing strategies may be changed, potentially affecting forecasted revenue generation timelines.*
>
> - *Two other factors are expected to result in increasing revenue over time. Most multi-year customer contracts now include annual price escalation terms, allowing the Company to increase pricing in accordance with either a stated percentage (usually 10% or less) or increases in the U.S. CPI index. Also, because customers will be charged for new SaaS modules they commence using, maximum annual revenue from customers will occur only after all pipeline asset data has been ingested and all additional functionality modules have been fully implemented.*

• "Pipeline miles generating revenue" in the above table approximates the cumulative data-miles ingested into CIM that are revenue generating. "% of subscription miles generating revenue" is the percentage of revenue generating data-miles compared to total miles operated, cumulatively for all customers. "Revenue per mile for revenue generating miles" is the calculation of total revenue divided by cumulative revenue generating data-miles. This calculation is only an approximation, as the revenue per data-mile figure will only be accurate when all customers' miles become revenue generating for the entire fiscal year and is subject to fluctuation due to customer pipeline maintenance schedules. Management uses this revenue per mile figure only as an approximation to determine trending analyses.

The anticipated (2023) increase in *"Revenue per mile for revenue generating miles"* provides a cogent data point, that we think supports some of our thesis from the initial coverage. First, the increase from $105.34 in F2022 (which incidentally represents a five year low for the period 2019 through the 2023 estimate) to $130.97 (the five-year high), is considerable. For the sake of comparison, if they had achieved the same revenue per mile in F2022, they would have ostensibly realized an additional $1.37 million in revenue. That leads us to the next obvious question, which is 'what is the basis for the increase in revenue per mile?". They addressed that in part in the highlighted narrative above. To unpack that narrative, some of the increase is better pricing but some of it is also the anticipation of customers beginning to add new modules to their protocols. Recall, our initiating coverage addressed the importance of these new modules as a basis for growth beyond the addition of new customers. Further, we believe there is considerable operating leverage in the addition of these new pieces of revenue, which we think explains the Company's guidance regarding gross margins which they expect to see back around 75% for fiscal 2023 (and likely beyond). As an aside, we are also inclined to think that the Company may be positioned for better pricing power as they continue to establish themselves and grab additional market share. Keep in mind, as we also pointed out in the initiating coverage, their solution represents better, faster and cheaper than legacy approaches, which we think may provide them with some added pricing power as they gain footing/recognition across the industry.

Revisiting **Tables 2 & 3** above, we submit the following narrative from their January 24, 2023, preliminary guidance:

*Brandon Taylor, Chief Operating Officer, added, "Beside questions about revenue growth expectations and its drivers, people who follow the Company commonly ask two other questions: (1) whether additional financing is imminently required by the Company; and (2) when the Company expects to operate cash positive. Regarding revenue growth, we believe Fiscal 2023 revenue will exceed $10 million, of which about 90% is forecast to come from increased use of our software-as-a-service ("**SaaS**") solutions as existing customers onboard more of their pipeline assets. We are forecasting cash to be $4 million at Fiscal 2023 year-end and cash from operations to be approximately breakeven near the end of the year**, thus we do not anticipate raising additional capital based on our current plan and budget."***

The past two years have been challenging for many small public companies, especially those burning cash and thus requiring additional equity capital to finance that burn. We have lamented that fact in some of our recent coverage terminations in terms of the extreme dilution that has created for some names. Succinctly, while One Soft continues to burn cash and remains unprofitable, that gap is closing, and they expect F2023 to be largely cash neutral. Moreover, recall, that notion is aided by the fact that they often collect cash from customers prior to provisioning the services (the deferred revenue component they often reference). The point is, the fact that they will likely not need to rely on the equity markets to finance burn is highly constructive in the current environment, and we think there is reasonable visibility to positive cash flow and profitability without the need for additional dilution.

To again revisit some of our original thesis, the need for monitoring assets with the potential for catastrophic failure remains heightened. Recent train derailments underscore that notion. As we pointed out in the initiating coverage, trains represent competition to pipelines when it comes to transporting energy, but the relative historic safety advantages of pipelines vs. rail are well documented and quite clear. While we submit that logic does not seem to be front and center these days, logic would dictate that perhaps we should build more pipelines (and use fewer trains) to transport hazardous materials, which would presumably be good for One Soft. That may or may not happen, however, we think the regulatory focus and frankly the shear economic calculus of hardening/monitoring these assets against catastrophic failure is likely to increase, which should most certainly benefit One Soft.

Lastly, we have recast our model to approximate the Company's guidance, but we must admit, those numbers represent a discount to our internal expectations for fiscal 2023, in part because they suggest that they will not be adding a great deal of new business (at least that contributes to the current year) and we are not sure we embrace scenario. That said, as we noted, the timing of adding new miles of pipe (either from new or existing customers) as well as adding new modules and their eventual contribution to revenues remains a bit elusive, so for now we will stand near the guidance.

We reiterate our allocation of 4, and our 12-24 month price target of US$.60. We will likely revisit our allocation (higher) if the stock experiences additional compression. We would reiterate, the more we learn about OneSoft, the more we are convinced that their opportunities remain open-ended, perhaps well beyond our current target assumptions.

Projected Operating Model

(Reflected in Canadian Dollars)

OneSoft Solutions Inc.						
Projected Operating Model						
(Reflected in Canadian Dollars)						
By: Trickle Research						
	(estimate)	(estimate)	(estimate)	(estimate)	(estimate)	(estimate)
	3/31/2023	6/30/2023	9/30/2023	12/31/2023	Fiscal 2023	Fiscal 2024
Revenue	**$ 2,002,819**	**$ 2,368,939**	**$ 2,648,351**	**$ 3,127,267**	**$ 10,147,376**	**$ 18,605,546**
Direct Costs	$ 525,564	$ 598,788	$ 654,670	$ 750,453	**$ 2,529,475**	**$ 4,221,109**
Gross Profit	**$ 1,477,256**	**$ 1,770,151**	**$ 1,993,681**	**$ 2,376,813**	**$ 7,617,901**	**$ 14,384,437**
Salaries and Employee Benefits	$ 1,340,423	$ 1,395,341	$ 1,437,253	$ 1,509,090	**$ 5,682,106**	**$ 6,950,832**
Sales and Marketing	$ 217,136	$ 233,901	$ 262,636	$ 300,842	**$ 1,014,516**	**$ 1,564,184**
General and Adminsitrative	$ 330,183	$ 353,981	$ 372,143	$ 403,272	**$ 1,459,579**	**$ 2,009,360**
Operating Expenses	$ 1,887,743	$ 1,983,223	$ 2,072,032	$ 2,213,205	**$ 8,156,202**	**$ 10,524,376**
Software Development Costs Capitalized	$ (58,471)	$ (61,226)	$ (63,329)	$ (66,933)	**$ (249,959)**	**$ (313,607)**
Operating Expenses, net of Captialized Costs	**$ 1,829,271**	**$ 1,921,997**	**$ 2,008,703**	**$ 2,146,272**	**$ 7,906,243**	**$ 10,210,770**
Loss Before Other Expenses	**$ (352,016)**	**$ (151,846)**	**$ (15,022)**	**$ 230,541**	**$ (288,342)**	**$ 4,173,667**
Stock Based Compensation	$ 100,000	$ 100,000	$ 100,000	$ 100,000	**$ 400,000**	**$ 800,000**
Amortization of Intangibles	$ 183,784	$ 185,621	$ 187,478	$ 189,352	**$ 746,235**	**$ 776,535**
Depreciation of Property and Equipment	$ 4,600	$ 4,600	$ 4,600	$ 4,600	**$ 18,400**	**$ 18,400**
Interest Income	$ (19,254)	$ (15,205)	$ (14,675)	$ (14,656)	**$ (63,790)**	**$ (79,953)**
Foreign Exchange Loss	$ -	$ -	$ -	$ -	**$ -**	**$ -**
Other	$ -	$ -	$ -	$ -	**$ -**	**$ -**
Total Other Expenses	**$ 269,130**	**$ 275,017**	**$ 277,403**	**$ 279,296**	**$ 1,100,846**	**$ 1,514,982**
Gain (Loss) Before Income Tax	**$ (621,146)**	**$ (426,862)**	**$ (292,424)**	**$ (48,755)**	**$ (1,389,187)**	**$ 2,658,685**
Income Tax						
Net Gain (Loss)	**$ (621,146)**	**$ (426,862)**	**$ (292,424)**	**$ (48,755)**	**$ (1,389,187)**	**$ 2,658,685**
Other Comprehensive Gain (Loss)	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**
Net Gain/(Loss) per share -Basic	**$ (0.01)**	**$ (0.00)**	**$ (0.00)**	**$ (0.00)**	**$ (0.01)**	**$ 0.02**
Net Gain/(Loss) per share - Diluted	**$ (0.01)**	**$ (0.00)**	**$ (0.00)**	**$ (0.00)**	**$ (0.01)**	**$ 0.02**
Basic Shares Outstanding	**120,791,939**	**120,916,939**	**121,041,939**	**121,166,939**	**120,979,439**	**121,791,939**
Diluted Shares Outstanding	**120,791,939**	**120,916,939**	**121,041,939**	**121,166,939**	**120,979,439**	**121,791,939**

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Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

- A Trickle rating of 1 thru 3 would best correspond to a "Speculative Buy" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.
- A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.
- A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.