

Update to Webcentral Shareholders: Webcentral's Investment in Cirrus

ASX Announcement, 29 September 2021



Takeover bid and Cirrus Shareholding

On 16 September 2021, Webcentral Group Limited's (**Webcentral**) on-market takeover bid for Cirrus Networks Holdings Limited (**Cirrus**) (**Takeover Bid**) closed. Upon close of the Takeover Bid, Webcentral had a holding in Cirrus of 155,666,592 shares equating to 16.74%. Since that time, Webcentral has increased its holding in Cirrus through on-market purchases to 156,349,355 shares equating to 16.81%.

In total, Webcentral has expended in excess of \$5 million to attain this 16.81% stake in Cirrus, and is now the largest shareholder in Cirrus.

Webcentral objectives with respect to Cirrus

As the largest shareholder in Cirrus, Webcentral now has a significant vested interest in the success and profitability of Cirrus.

Since the close of the Takeover Bid, Webcentral has attempted to engage with the Board of Cirrus on the potential for another control transaction, such as a further takeover bid. However, as at the time of this update, Cirrus and Webcentral have not been able to reach agreement on the terms on which due diligence information would be supplied to Webcentral.

Webcentral believes the Lonergan Report obtained by the Cirrus Board during the Takeover Bid effectively values Cirrus at 2.7 to 2.9 cents per share, well below Webcentral's bid price of 3.2 cents cash per share. Since the close of the Takeover Bid, Cirrus shares have generally traded in the range of 2.8 cents to 3.2 cents, a range reflective of that value.

Unless Webcentral is able to obtain due diligence information to support a higher valuation Webcentral does not consider it can justify entering into negotiations for a potential control transaction.

In light of this, Webcentral has decided to focus for the time being on taking steps to restore Cirrus to a proper level of profitability. For the benefit of Webcentral shareholders, its plan to do this is outlined later in this update.

The Webcentral executive team has confidence in the Cirrus business. As industry participants and investors in Cirrus for the long term, Webcentral knows and understands the IT services business undertaken by Cirrus and believes it can be turned around and operated more profitably.

As Webcentral shareholders know, the Webcentral executive team has an impressive track record of successfully turning around underperforming companies. At the time of 5G Networks (Webcentral's parent entity) launching its takeover of Webcentral in 2020, Webcentral was bordering on insolvency and had entered into a proposal for a takeover by way of a scheme of arrangement at a price of just 10 cents per share. A year later, Webcentral is consistently trading at beyond 50 cents per share.

Webcentral has spent in excess of \$5m to date acquiring its stake in Cirrus and intends to see through its turnaround plan. Webcentral has a clear plan to turn around Cirrus – this is briefly outlined below.

Board Spill

On 17 August 2021, Webcentral requisitioned a meeting of shareholders for the removal of certain current members of the Board of Directors (**Board**) of Cirrus and the appointment of new members to the Board. An extraordinary general meeting has been convened by Cirrus to be held on **Friday 15 October 2021**.

In this regard, Webcentral proposes:

- The appointment to the Cirrus Board of 2 experienced Webcentral nominees, Joe Demase and Michael Wilton.
- The removal of all of the incumbent Directors of Cirrus other than Paul Everingham:
 - Chairman Andrew Milner;
 - Managing Director Matthew Sullivan; and
 - Non-executive director Daniel Rohr.
- An immediate review of Cirrus operations with the benefit of Webcentral's experience and expertise. The review will focus on costs, margins and profitability.
- Initiatives in the short term to reinvigorate Cirrus and restore Cirrus to a suitable level of profitability.



Webcentral has written to all Cirrus shareholders putting forward its case for the appointment of its nominees. A copy of Webcentral's Letter to Cirrus Shareholders is available on Webcentral's website at <https://www.webcentral.com.au/corporate/investors/>.

The current state of Cirrus' business

On 11 August 2021, Cirrus released its FY21 results. After adjustments, its normalised EBITDA was \$2m. The key points from the Cirrus FY21 results are:

- revenue increased by approximately \$11m from the previous year, but the additional revenue was primarily in lower margin hardware sales, and the cost to deliver this revenue was in the order of \$16m;
- recurring revenue from business projects and managed services declined. In Webcentral's experience, this type of business typically results in higher margin sales compared to lower margin hardware sales; and
- the absence of any clear pathway or strategy to turn around the stagnating profitability of Cirrus and no discussion of potential growth areas or opportunities to increase its margins.

Webcentral considers this an unacceptably low level of profitability for a company with a turnover in the region of \$100m. As noted above, Webcentral proposes to implement a turn-around plan if its nominees are appointed at the Board spill meeting on 15 October 2021.

Webcentral's turn-around plans for Cirrus

Webcentral has a clear plan to identify the problems at Cirrus and restore the company to a proper level of profitability. This plan will be put into action if Webcentral is successful in having its nominees appointed to the Cirrus Board at the spill meeting on 15 October 2021. The Webcentral plan includes:

- an immediate review of Cirrus operations with the benefit of Webcentral's experience and expertise. The review will focus on costs, margins and profitability; and
- initiatives in the short term to reinvigorate Cirrus and restore Cirrus to a suitable level of profitability.

Webcentral offers Cirrus:

- access to an experienced management team and support staff with deep expertise in all aspects of the Cirrus businesses; and
- access to funding to support a turnaround strategy (5GN Networks provided a loan of \$47.5m to Webcentral to allow it to pay out its lenders).

Based on public information only, there are aspects of the business that Webcentral believes it can significantly improve upon. Webcentral is confident that it can implement an effective turn-around plan to unlock unrealised potential in the Cirrus business.

Sales and marketing

Cirrus has improved revenue in the enterprise sector in a difficult market but:

- there is evidence of sales, especially in hardware, on unsustainable margins;
- additional revenue amounting to approximately \$11m was primarily in lower margin hardware sales, and the cost to deliver this revenue was in the order of \$16m;
- recurring revenue from business projects and managed services has declined. In Webcentral's experience, this type of business typically results in higher margin sales compared to lower margin hardware sales;
- there has been instability in the sales function. The loss of Jason Smith – National Manager Sales / MIT (made redundant 2021) may have impacted the sales effort; and
- the sales team need to be refocussed and incentivised towards higher margin business and, in particular, managed services (this is declining) with less focus on less profitable hardware sales.

Cirrus appears to have a relatively low-level marketing function. Webcentral has a well-established marketing team with expertise and experience in managed services and professional services to support the existing Cirrus marketing team. Webcentral can and will provide that support.

As well as the initiatives to improve the sales and marketing functions at Cirrus, Webcentral can provide Cirrus with access to the existing Webcentral customer base for cross-sell and up-sell opportunities.

Operational efficiency

Webcentral thinks it likely that operational inefficiencies are affecting Cirrus' margins and profitability. In the context of a growing enterprise like Cirrus, operational inefficiencies can be magnified.

The Webcentral executive team are familiar with this type of problem and have addressed it before. Approaches to improving operational efficiency will likely include:

- improving speed to turning on revenue. Webcentral has over 350 employees who can assist with customer projects and delivery;



- improving efficiencies and reducing cost in the product delivery life cycle. The efficiency improvements will include automation where appropriate. Webcentral has 4 development teams currently working on internal automation projects; and
- improving back-end efficiencies so that Cirrus can focus on those aspects of the business they are good at, with Webcentral looking after cloud hosting and networks.

Managed services and professional services are core businesses of Webcentral and well understood by the Webcentral executive team.

Technical expertise

As a relatively small company, it is likely that Cirrus lacks some of the technical expertise necessary to reach full operational efficiency:

- it is not clear that Cirrus has a well-established CTO function. In contrast, the Webcentral CTO is highly credentialled, passionate about technology and deeply involved in all aspects of the business' product development process. Among other things, the Webcentral CTO delivers a monthly technology roadmap update to all staff; and
- Webcentral can provide technical support to Cirrus staff, especially in areas of Webcentral expertise to allow Cirrus staff to focus on their core strengths.

Webcentral will make its technical expertise available to Cirrus to help improve efficiencies and assist Cirrus in difficult projects.

Conclusion

Webcentral has made a substantial investment in Cirrus but considers the investment well justified.

As outlined above, Webcentral has clear strategic plans for Cirrus and firmly believes that it can turn the Cirrus business around. Its experienced executive team has shown in the past that it can effectively take small underperforming technology businesses and guide them towards profitability.

Webcentral will keep its shareholders and the market appropriately updated on developments with respect to its shareholding in Cirrus and any potential control transaction.

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About Webcentral

Webcentral is an Australian owned digital services company who empower more than 330,000 customers to grow and thrive in the online world. Our portfolio of digital services is extensive, with market leading offers across domain management, website development and hosting, office and productivity applications and online marketing.

Our customer focussed heritage has been built on expertise, innovation and personalised service; critical attributes delivered through our culture and embraced by our people. This is demonstrated through more than 25 years of online industry leadership across Australia's digital foundation brands such as Melbourne IT, Netregistry and WME.

The Webcentral mission is dedicated to leading online success for our customers. We achieve this by building trusted and valued client relationships which convert successful business outcomes at each milestone across the customers' digital journey.