

## CY19 updated for audited accounts and COVID-19

Shekel Brainweigh Limited (ASX:SBW) has released its audited accounts for CY19 and an update on the impact of/response to COVID-19. On the audited account front the group has for the first time provided segment results for the “traditional” and “new retail” divisions. The key point to note is that adjusting the “traditional” divisional EBIT for a bad-debt provision and “growth” R&D, the division recorded EBIT of US\$2.7m (A\$4.5m). A 6x multiple implies a valuation of A\$27m (\$0.195/share) against the current market cap of \$9.1m. The implied value in the current share price for the new retail division is therefore negative A\$18m (or zero and the traditional business 2.0x EBIT) despite impressive technology partners, early commercialisation success and significant R&D to date. On the COVID-19 front, the group has significantly reduced salaries for the next 60-90 days and applied for a US\$1.25m loan from the Israeli Government as part of that country’s COVID-19 package. Minimal impact has been felt to date with Q120 revenue similar to Q119 but the company is expecting potential near-term disruption in its medical division (~30% of revenue) for the duration of the pandemic (we assume 3-months). The self-checkout business (predominantly supermarkets) should continue to weather the storm (~70% of revenue) given the resilience we have seen in this sector thus far.

### Business model

SBW produces weighing scale hardware/software that is employed by OEMs for self-checkout and healthcare applications requiring speed and accuracy. Prices received from customers are typically fixed, and gross margins are in-line with that achieved by most OEM equipment suppliers. The group is looking to extend this market leading technology into new verticals, opening up larger market opportunities, potentially higher gross margins and some recurring SaaS style revenue from data analytics. One of the new verticals (Innovendi vending machines) is in commercialisation while others are nearing commercialisation (The Sorter smart shelving and the Micro-market Capsule).

### CY20 updated for COVID-19

Trading in Q120 has been similar to Q119 and the supply chain remains intact. That said the company expects some disruption from COVID-19, particularly in the medical division and has reduced costs accordingly in anticipation. We have reduced costs for 3-months in CY20 and added them back in CY21. The group had US\$1.9m cash at March 31 and has applied for a US\$1.25m loan from the Israeli Government as part of its COVID-19 support. A slowdown in sales would also release working capital (rec > pay by US\$4m).

### Base case valuation A\$0.40/share fully diluted

We have reduced our base case DCF valuation to A\$0.40/share (\$55m) from A\$0.48/share predominantly driven by a higher equity risk premium (7.0% vs 6.5%). Based on sustainable earnings from the “traditional” scales business we believe there is a significant negative valuation being applied to the New Retail Division. SBW continues to trade at a significant discount to small cap hardware/software peers despite achieving strong sales, modest PBT losses (incorporating higher R&D spend) and multiple new product options.

#### Historical earnings and RaaS Advisory estimates on a reported basis

Year end	Revenue (US\$m)	EBIT (US\$m)	NPAT (US\$m)	EPS (c)	PER (x)	EV/sales(x)
12/19a	18.8	(2.1)	(2.4)	(0.02)	(2.5)	0.19
12/20e	19.8	(1.3)	(1.4)	(0.01)	(7.6)	0.15
12/21e	25.8	1.9	1.1	0.01	3.0	0.12
12/22e	29.1	3.6	2.4	0.02	1.8	0.03

Source: Company Data, RaaS Advisory Estimates

## Technology – Hardware/software

6 April 2020

### Share details

ASX Code	SBW
Share price at 2nd Apr	\$0.068
Market Capitalisation	\$9.04M
Shares on issue	139M
Enterprise value	\$12.14M
Cash at 31 Mar '20	A\$3.1M
Free float	~20%

### Share performance (12 months)



### Upside Case

- Strong growth expected in the group's core self-checkout and healthcare markets
- New verticals have commenced commercialisation, with significant opportunities.
- Mix shift to recurring SaaS fees will increase gross margins and lower days receivables

### Downside Case

- Low liquidity with ~20% free float
- Currency translation from USD and AASB16 adds complexity for investors
- Near term ROE likely to be impacted by R&D expenditure

### Management

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Barak Nir	Chief Financial Officer
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\*The author holds shares

## FY19 result updated for audited accounts

There has been some modest movements at various line items between the unaudited accounts issued on February 28 and the audited accounts issued 31 March.

The key change relates to the treatment of a US\$698k bad debt provision to a shareholder group which was recorded at the interest line in the unaudited numbers and at the operating cost line in the audited numbers. This shareholder group has indicated a willingness to repay the loan when the share price returns to the IPO price (A\$0.35/share) but given the current share price a provision was recommended.

A raft of non-cash charges, the impacts of AASB16, varying treatment of R&D spend between halves (between the P&L and software capitalisation) and higher overall R&D spend relative to CY18 makes the result at the PBT line difficult to analyse.

To compare with CY18 and provide a logical base for future forecasts we have:

- Added actual rental expense back to General & Admin expense.
- Separated Share Based Payments from R&D expenses.
- Removed the AASB16 rental charge from depreciation.
- Separated all non-cash charges from the operating expenses including the shareholder loan provision and share based payments.

The table below looks at the SBW result by half-year incorporating audited results. In summary sales growth improved 2H over 1H and costs were higher over both halves as new products continued to be developed.

Exhibit 1: SBW operating performance by half-year – audited accounts						
Variable	1H18	1H19	% Chg	2H18	2H19	% Chg
Sales	8.8	8.4	-4%	9.9	10.4	5%
Gross Profit	3.3	3.8	17%	5.1	4.4	-13%
GP%	37%	45%		51%	42%	
Operating costs	2.8	5.1	83%	3.8	3.8	1%
R&D (ex SBP)	0.5	2.1	290%	1.1	0.8	-25%
Other	2.2	3.0	34%	2.6	3.0	12%
<b>EBITDA</b>	0.5	-1.3	-358%	1.3	0.6	-54%
Deprecation	0.1	0.1	-20%	0.1	0.1	-16%
Amortisation	0.0	0.0		0.0	0.0	
<b>EBIT</b>	0.4	-1.3	-440%	1.2	0.5	-57%
(EBIT margin)	4.5%	-15.9%		12.1%	5.0%	
Share based pay	0.3	0.4		0.8	0.2	0.3
Other	0.0	0.0		1.0	0.7	0.0
Reported EBIT	0.1	-1.7		-0.6	-0.4	

Source: Company financials and RaaS Analysis

Other key updates from the audited accounts include:

- **Cash at bank as at March 31 was US\$1.9m, down from US\$2.1m in December**, ironically should sales slow SBW may see a short-term release of funds as trade receivables were US\$4.7m higher than trade payables at December 31.
- **The company resumed capitalising software development in 2H19 (US\$1.3m)** following a break in 1H19 (US\$50k), with R&D spend for 2H19 predominantly related to the traditional business, and in particular, Edgify.  
Given revenues are expected from new products in CY20 we do not expect capitalised expenditure in CY20.
- **No amortisation** of capitalised software as we had expected but expect this to begin in CY20.

## Segment reporting

SBW has released further detail surrounding the “Traditional” and “New Retail” divisions which provides further colour on both R&D allocations and underlying operating earnings.

### R&D allocations

Adjusted for share based payments we estimate SBW spent US\$4.487m in R&D over CY19. This number includes an additional US\$290k in the New Retail division which was offset against sales in-line with accounting standards.

The table below splits out this spend by segment. We estimate a US\$2.966m spend for the New Retail division and US\$1.521m for the Traditional division.

Within the traditional business we estimate a significant increase in new product development, namely the Edgify product and some new product added to the Healthweigh® line towards CY2020 (estimated at US\$0.75m) which is looking to use AI to better identify product at the checkout and potentially be retro-fitted to all checkouts irrespective of whether SBW supplies the weighing systems.

<b>Exhibit 2: SBW R&amp;D breakdown</b>		
Line item	US\$	Comments
Reported	3,472,000	Per P&L
less Share based payments	569,000	Not treating as R&D
add New Retail revenue offset	290,000	Revenue which was offset by R&D
add capitalised software	1,294,000	In the cash flow and all relating to New Retail
<b>Underlying Spend</b>	<b>4,487,000</b>	
New Retail	2,966,000	All growth and up from ~US\$1.39m in FY18
Traditional	1,521,000	A combination of maintenance & growth and up from ~\$0.7m in FY18
Source: Company financial & RaaS estimates		

### Segmental EBIT & valuation implications

At current prices the most important analysis in this note is Exhibit 3 below. If we adjust the reported EBIT of the Traditional division for the provision of bad debts (US\$698k) and growth capex relating to R&D (US\$750k), and apply a 6.0x EBIT multiple then the value of this earnings stream in A\$ terms is between A\$20m and A\$27m. This implies a negative valuation of the New Retail division of between A\$11m and A\$19m, all else being equal.

<b>Exhibit 3: SBW Traditional Business Valuation</b>		
Line item	CY19 adjusted	CY19 adjusted for growth R&D
Reported EBIT (US\$)	1,325,000	1,325,000
Add bad debt provision	698,000	698,000
Add growth R&D	0	750,000
Underlying Traditional EBIT (US\$)	2,023,000	2,773,000
EBIT Multiple	6.0x	6.0x
Valuation (US\$)	12,138,000	16,638,000
Valuation (A\$) (@\$0.60)	20,230,000	27,730,000
Current Mkt Cap (A\$)	9,035,000	9,035,000
<b>Implied value of New Retail (A\$)</b>	<b>(11,195,000)</b>	<b>(18,695,000)</b>
Source: Company financial & RaaS estimates		

## COVID-19 update

The company has provided an update of current and expected impacts from COVID-19 which we have summarised below.

- **Q1CY20 trading.** Revenues in the traditional scales business were similar to last year, with little disruptions in the retail market (for self-checkout) but material disruptions in the medical market (for incubators).
- **Potential Q2CY20 disruptions.** The company is expecting a “large” reduction in sales for the medical segment (~30% of sales) “for the duration of the pandemic” which have assumed to be 3-months.
- **Operating cost savings implemented.** To offset potential sales weakness the company have 22% of employees on unpaid leave from March-19 (aided by a Government scheme), the remaining employees have taken a 20%-40% pay cut while Management and Board have taken a 30% pay cut.
- **US\$1.25m loan applied for.** As part of the Israeli Governments COVID-19 package SBW has applied for a US\$1.25m loan, with the decision expected late April.

As best we can, we have factored the above (with the exception of the loan) into our numbers.

## Unit sales assumptions

The table below highlights our current unit sales assumptions by key product category. For FY20 we have skewed expected sales to the second half but lowered Healthcare and Innovendi slightly.

This table does not include the expected increase in SaaS/data analytic fees which result from New Retail sales and accelerate as units increase in circulation.

Exhibit 4: SBW product sales by units					
Year-end	2019F	2020F	2021F	2022F	2023F
Self-checkout	34,587	35,874	38,027	40,308	42,727
Healthcare	16,500	14,850	16,038	17,321	18,707
Innovendi	110	270	850	900	900
Innovendi Kit	0	200	370	400	400
Smart Shelves	0	50	300	525	900
Capsule	0	0	25	50	100
Source: Company Financials & RaaS estimates					

## Peer comparison update

We consider listed peers to SBW to be:

- Small/micro-cap in size;
- Predominantly a technology hardware producer making a “one-time” unit sale;
- Supplying OEM’s with components to a branded end-product;
- Utilising their core technology to develop new products or push into new verticals;
- Dealing mainly with Blue-Chip customers.

While the technologies and potential market opportunities may vary by industry and product, these companies share similar challenges in terms of gross margins, brand recognition, balancing payables and receivables and funding growth requirements.

SBW continues to trade at a material discount to all selected peers including a 70% discount to the next lowest EV/sales (RVS). Like most small, loss making companies there has been some serious share price erosion across the peer group over the last month..

Considering SBW’s material sales, modest PBT losses and solid GP% the current discount in our view is unjustified.

### Exhibit 5: Peer financial comparison

Company Name	Ticker	Share price (cps)	Mkt Cap (\$m)	Dec-19 Debt/(cash) (A\$m)	CY19 Adj PBT (A\$m)	CY19 sales (A\$m)	CY19 GP%	CY19 WC/Sales	CY19 EV/Sales	CY19 R&D/sales
Pivotal Systems	PVS	0.79	95	-8.2	-15.0	23.2	11%	63%	3.7	45%
Atomos *	AMS	0.44	82	-16.0	-1.9	64.0	43%	20%	1.0	13%
Revasum	RVS	0.36	33	-10.3	-20.7	31.1	11%	43%	0.7	65%
Elsight	ELS	0.25	26	-1.4	-4.8	1.8	38%	11%	13.7	103%
MicroX *	MX1	0.13	20	-7.8	-11.0	1.6	67%	-5%	7.5	128%
Mobilicom	MOB	0.06	15	-4.7	-3.4	3.4	71%	11%	2.9	93%
Shekel Brainweigh	SBW	0.07	9	-3.9	-3.6	28.5	44%	37%	0.2	22%

Sources: Company financials, Thomson Reuters      \*June year-end, 1H20 number annualised

## DCF Valuation

Our base case DCF valuation now sits at \$0.40/share, down from our most recent update (A\$0.48), with a higher equity risk premium (now 7.0% from 6.5%) the key difference in the reduction.

### Exhibit 6: Base case DCF valuation

Parameters	
Discount Rate / WACC	11.5%
Terminal growth rate assumption (inflation adjusted)	2.0%
In A\$m	
Present value of cashflows	18
Present value of terminal value	32
PV of enterprise	50
Net value (\$m)	54
Net value per share	\$0.40
Source: RaaS estimates	

**Exhibit 7: Financial Summary**

Shekel Brainweigh (SBW.ASX)						Share price (3 April 2020)						A\$	0.07			
Profit and Loss (US\$m)						Interim (US\$m)		H118A	H218A	H119A	H219A	H120F	H220F			
Y/E 31 Dec	FY18A	FY19A	FY20F	FY21F	FY22F	Revenue	8.8	9.9	8.4	10.4	8.2	11.6				
Revenue	18.7	18.8	19.8	25.8	29.1	EBITDA	0.2	(0.5)	(1.6)	(0.3)	(0.8)	0.3				
Gross profit	8.3	8.2	9.2	12.3	14.3	EBIT	0.1	(0.6)	(1.7)	(0.4)	(1.2)	(0.1)				
GP margin %	44.5%	43.7%	46.5%	47.9%	49.1%	NPATA (normalised)	(0.0)	(1.1)	(1.6)	(0.9)	(0.8)	0.1				
EBITDA	(0.3)	(1.9)	(0.5)	2.7	4.4	Adjustments	0.0	0.0	(0.5)	(0.8)	(0.3)	(0.3)				
Depn	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	NPAT (reported)	(0.0)	(1.1)	(2.1)	(1.6)	(1.1)	(0.2)				
Amort	0.0	0.0	(0.7)	(0.7)	(0.7)	EPS (normalised)	(0.000)	(0.010)	(0.011)	(0.006)	(0.006)	0.001				
EBIT	(0.1)	(1.8)	0.3	3.6	5.3	EPS (reported)	(0.000)	(0.010)	(0.015)	(0.012)	(0.008)	(0.002)				
Interest	(0.7)	(0.3)	(0.2)	(0.2)	(0.3)	Dividend (cps)	0.000	0.000	0.000	0.000	0.000	0.000				
Tax	0.1	(0.0)	0.2	(0.5)	(0.9)	Imputation	0.0	0.0	0.0	0.0	0.0	0.0				
Minorities	0.0	0.0	0.0	0.0	0.0	Operating cash flow	na	na	na	na	na	na				
Equity accounted assoc	0.0	0.0	0.0	0.0	0.0	Free Cash flow	na	na	na	na	na	na				
NPAT pre significant items	(0.8)	(2.1)	0.3	2.8	4.1	Divisionals	H118A	H218A	H119	H219F	H120F	H220F				
Significant items	(0.4)	(1.2)	0.0	0.0	0.0	Traditional Scales	8.8	9.9	8.4	10.4	6.7	9.9				
NPAT (reported)	(1.2)	(3.3)	0.3	2.8	4.1	New Retail	-	-	-	-	1.4	1.7				
Cash flow (US\$m)						Total Revenue	8.8	9.9	8.4	10.4	8.2	11.6				
Y/E 31 Dec	FY18A	FY19A	FY20F	FY21F	FY22F											
Adj EBITDA inc. rent	0.8	(0.7)	(0.5)	2.7	4.4	Gross profit	3.3	5.1	3.8	4.4	3.7	5.5				
Interest	(0.2)	(0.2)	(0.2)	(0.2)	(0.3)	Gross Profit Margin %	37.2%	51.0%	45.5%	42.2%	45.9%	46.9%				
Tax	0.0	0.2	0.1	(0.2)	(0.7)											
Working capital changes	0.5	(0.9)	0.7	(2.0)	(1.0)	R&D	0.5	1.1	2.1	0.8	1.9	2.1				
Operating cash flow	1.2	(1.6)	0.0	0.3	2.5	General & Admin & Other	2.2	2.6	3.0	3.0	2.7	3.0				
Mtce capex	(0.1)	(0.2)	(0.2)	(0.3)	(0.3)	One-off costs & Non-cash	0.3	1.8	0.4	0.9	-	-				
Free cash flow	1.0	(1.8)	(0.2)	0.1	2.2	Total costs	3.1	5.6	5.4	4.7	4.6	5.1				
Capitalised Software	(0.8)	(1.3)	0.0	0.0	0.0											
Acquisitions/Disposals	(0.2)	(0.1)	0.0	0.0	0.0	EBITDA	0.2	(0.5)	(1.6)	(0.3)	(0.8)	0.3				
Other	0.0	0.0	0.0	0.0	0.0	EBITDA margin %	2.1%	(5.1%)	(19.2%)	(3.0%)	(10.1%)	2.7%				
Cash flow pre financing	0.0	(3.2)	(0.2)	0.1	2.2											
Equity	6.1	0.0	0.0	0.0	0.0	Margins, Leverage, Returns		FY18A	FY19A	FY20F	FY21F	FY22F				
Debt	(0.4)	0.0	0.0	0.0	0.0	EBITDA margin %		(1.7%)	(10.2%)	(2.6%)	10.6%	15.2%				
Net Dividends paid	0.0	0.0	0.0	0.0	0.0	EBIT margin %		(0.7%)	(9.4%)	1.6%	13.9%	18.2%				
Net cash flow for year	5.7	(3.2)	(0.2)	0.1	2.2	NPAT margin (pre significant items)		(4.2%)	(11.3%)	1.5%	11.0%	14.2%				
Balance sheet (US\$m)						Net Debt (Cash)	-	6.25	-	2.57	-	2.36	-	2.42	-	4.63
Y/E 31 Dec	FY18A	FY19A	FY20F	FY21F	FY22F	Net debt/EBITDA (x)	(x)	nm	nm	nm	nm	nm				
Cash	6.3	2.6	2.4	2.4	4.6	ND/ND+Equity (%)	(%)	33.8%	21.4%	22.6%	20.8%	28.5%				
Accounts receivable	5.6	5.8	5.3	6.6	7.2	EBIT interest cover (x)	(x)	n/a	n/a	74.6%	6.4%	4.7%				
Inventory	3.2	3.5	3.7	5.0	5.8	ROA		(0.6%)	(9.0%)	1.7%	17.9%	21.9%				
Other current assets	2.0	1.5	1.6	2.0	2.2	ROE		(9.4%)	(25.9%)	(16.9%)	12.2%	20.6%				
Total current assets	17.0	13.4	13.0	16.1	19.8											
PPE	0.5	0.6	0.6	0.7	0.8	NTA (per share)		0.11	0.07	0.05	0.05	0.06				
Intangibles	2.0	3.2	2.6	1.9	1.3	Working capital		6.9	7.8	7.1	9.2	10.1				
Right of Use Asset	0.0	2.4	1.5	0.6	2.1	WC/Sales (%)		37.0%	41.6%	36.0%	35.5%	34.9%				
Deferred tax asset	0.0	0.0	0.0	0.0	0.0	Revenue growth		2.4%	0.9%	5.3%	30.2%	12.7%				
Other non current assets	0.2	0.0	0.8	2.1	2.9	EBIT growth pa		nm	nm	nm	1017.0%	47.5%				
Total non current assets	2.7	6.2	5.5	5.4	7.0	Pricing		FY18A	FY19A	FY20F	FY21F	FY22F				
Total Assets	19.7	19.6	18.6	21.5	26.8	No of shares (y/e)	(m)	113	139	139	139	139				
Accounts payable	1.9	1.5	1.9	2.5	2.8	Weighted Av Dil Shares	(m)	113	139	139	139	139				
Short term debt	4.0	4.1	4.3	5.6	6.3											
Lease Liability	0.0	1.8	1.3	0.4	1.9	EPS Reported	US cps	(0.01)	(0.02)	(0.01)	0.01	0.02				
Other	1.4	2.6	2.7	3.5	4.0	EPS Normalised/Diluted	US cps	(0.01)	(0.02)	(0.01)	0.01	0.02				
Total current liabilities	7.2	9.9	10.2	12.0	15.0	EPS growth (norm/dil)		nm	nm	nm	nm	71%				
Long term debt	0.0	0.0	0.0	0.0	0.0	DPS	cps	0.000	0.000	0.000	0.000	0.000				
Other non current liabs	0.3	0.3	0.3	0.3	0.3	DPS Growth		n/a	n/a	n/a	n/a	na				
Total long term liabilities	0.3	0.3	0.3	0.3	0.3	Dividend yield		0.0%	0.0%	0.0%	0.0%	0.0%				
Total Liabilities	7.5	10.2	10.5	12.3	15.2	Dividend imputation		0	0	0	0	0				
Net Assets	12.3	9.5	8.1	9.2	11.6	PE (x)		9.5	-	2.5	-	7.6	3.0	1.8		
						PE market		12.0	12.0	12.0	12.0	12.0				
Share capital	7.7	7.7	7.7	7.7	7.7	Premium/(discount)			(120.9%)	(163.0%)	(74.6%)	(85.2%)				
Accumulated profits/losses	2.9	(0.5)	(1.9)	(0.8)	1.6	EV/EBITDA		nm	nm	(5.6)	1.1	0.7				
Reserves	1.3	1.8	1.8	1.8	1.8	FCF/Share	US cps	(0.007)	(0.022)	(0.002)	0.000	0.016				
Minorities	0.3	0.4	0.4	0.4	0.4	Price/FCF share		(7.0)	(2.1)	(29.7)	104.0	2.9				
Total Shareholder funds	12.3	9.5	8.1	9.2	11.6	Free Cash flow Yield		(14.4%)	(48.4%)	(3.4%)	1.0%	34.9%				

Source: RaaS Advisory

# FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

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Corporate Authorised Representative, number 1248415

of

BR SECURITIES AUSTRALIA PTY LTD

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Effective Date: 26<sup>th</sup> November 2018

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RaaS is the entity providing the authorised AFSL services to you as a retail or wholesale client.

**What Financial Services are we authorised to provide?** RaaS is authorised to

- provide general advice to retail and wholesale clients in relation to
  - Securities
- deal on behalf of retail and wholesale clients in relation to
  - Securities

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### Our general advice service

Please note that any advice given by RaaS is general advice, as the information or advice given will not take into account your particular objectives, financial situation or needs. You should, before acting on the advice, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If our advice relates to the acquisition, or possible acquisition, of a particular financial product you should read any relevant Prospectus, Product Disclosure Statement or like instrument. As we only provide general advice we will not be providing a Statement of Advice. We will provide you with recommendations on securities

### Our dealing service

RaaS can arrange for you to invest in securities issued under a prospectus by firstly sending you the offer document and then assisting you fill out the application form if needed.

### How are we paid?

RaaS earns fees for producing research reports. Sometimes these fees are from companies for producing research reports and/or a financial model. When the fee is derived from a company, this is clearly highlighted on the front page of the report and in the disclaimers and disclosures section of the report.

We may also receive a fee for our dealing service, from the company issuing the securities.

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If you have a complaint about our service you should contact your representative and tell them about your complaint. The representative will follow BR's internal dispute resolution policy, which includes sending you a copy of the policy when required to. If you aren't satisfied with an outcome, you may contact AFCA, see below. BR is a member of the Australian Financial Complaints Authority (AFCA). AFCA provide fair and independent financial services complaint resolution that is free to consumers.

Website: [www.afca.org.au](http://www.afca.org.au); Email: [info@afca.org.au](mailto:info@afca.org.au); Telephone: 1800931678 (free call)

In writing to: Australian Financial Complaints Authority, GPO Box 3, Melbourne, VIC, 3001.

### Professional Indemnity Insurance

BR has in place Professional Indemnity Insurance which satisfies the requirements for compensation under s912B of the Corporations Act and that covers our authorized representatives.





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