

**TZ Limited**

TZL AU

▶ **Market Cap**  
**A\$52m**

▶ **Free Float**  
**65%**

Current **A\$0.13**  
Target  **A\$0.17**  
Prev. Target  
Up/Downside **35.5%**

**STOCK RATING****ADD**

HOLD

REDUCE

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**TZL150205**

Morgans Financial Limited has been appointed by TZ Limited to manage its Share Purchase Plan (SPP) announced in February 2015 and may receive fees in this regard

## Securing a brighter future

*The last three years has seen TZL transform from an R&D house into a commercially focussed business with revenue growth and an impressive list of customers. Revenue nearly tripled in FY14 and should more than double in FY15 which puts TZL close to EBITDA profitability. TZL's world class product is now hitting its stride and sales momentum is strong. We initiate coverage with an Add and A\$0.17 price target.*

### What TZL do ▶

TZL has invested 13 years of research and development and has lodged over 180 patents to develop their world leading product which is a smart digital locking mechanism. TZL's globally unique smart electronic lock has been commercialised via two key products: 1) Smart Lockers (aka Packaged Asset Delivery) which is ~75% of revenue; and 2) Data Centre locks (aka Infrastructure Protection) which is ~25% of revenue. TZL has a number of world class customers including Fortune 500s, Governments, technology companies and leading Postal Agencies. Customers include: Microsoft, GE, Cisco, IBM, Savis, Singapore Post, Pos Indonesia, Poste Italiane and others.

### Investment risk vs reward ▶

We have monitored TZL closely over the last two-three years and believe that the story is now looking compelling as product and commercialisation risk has been minimised. Revenue momentum is strong as evidenced by ongoing upgrades to guidance. At the mid-point of guidance TZL's FY15 revenue will be \$19m which is up an impressive ~125% yoy. We believe business success and shareholder upside should come from securing more revenue (through larger rollouts of existing contracts and new products) which should make TZL self-funding within 24 months. TZL is not yet self-funding so the key downside risk relates to the possibility TZL will require additional funding. That said, we think any additional funding requirements are likely to be coupled with meaningful contract wins (TZL has a tender pipeline in excess of A\$300m and traditionally high win rates) so we expect some upside to our forecasts.

### Investment view – Initiate with an Add recommendation ▶

TZL has commercialised a world class electronic lock and delivered significant sales. Its enviable customer base indicates minimal product risk. Revenue has increased 6 fold in the last 2 years and places TZL within 24 months of break-even, in our view. Should TZL win 50% of its pipeline this could result in \$45m in EBITDA (over 4 years) which we think could justify a 26cps valuation. The TZL investment thesis primarily relates to accelerating sales to push TZL through the profitability inflection point. We initiate coverage on TZL with an Add recommendation and A\$0.17 price target.

Key forecasts	Jun-13A	Jun-14A	Jun-15E	Jun-16E	Jun-17E
Revenue (A\$m)	2.7	8.5	19.0	26.1	40.7
EBITDA (A\$m)	-17.4	-10.3	-2.9	-1.0	4.6
Reported NPAT	-22.1	-12.1	-4.1	-2.2	3.1
Cash NPAT	-17.0	-7.7	-4.1	-2.2	3.1
Net Profit Growth (%)	n.m.	54.6	47.0	45.8	241.5
Normalised Earnings Per Share (¢)	n.m.	-0.04	-0.01	-0.01	0.01
EPS Growth (%)	n.m.	n.m.	77%	49%	238%
EV/Revenue (x)	12.7	5.5	2.7	2.1	1.3
EV/EBITDA (x)	-2.0	-4.5	-17.3	-53.4	11.5

SOURCE: MORGANS, COMPANY REPORTS



#### Table of contents

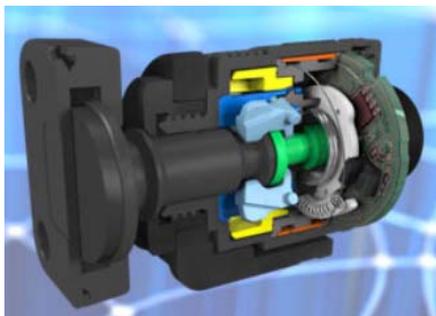
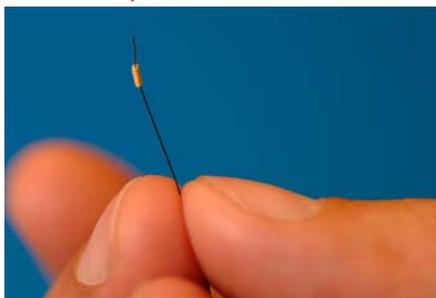
Brief commentary on our forecasts - page 3
Introducing TZL - page 3
SWOT analysis - page 7
The financials - page 8
Board and management - page 11
Key risks and rewards - page 12
Valuation & pipeline sensitivity analysts - page 14
Timeline of ASX releases - page 16

## BRIEF COMMENTARY ON OUR FORECASTS

While there is some significant revenue growth in our forecasts they do not include all of the potential work that TZL could receive over that period. TZL announced to the ASX a revenue pipeline of A\$306m over 4 years or roughly A\$75m pa (assuming 100% win rate and an even split over 4 years). Our peak revenue forecast is A\$60m in FY22 so our forecasts (and consequently our A\$0.17 price target) are not based on a high win rate. We have also assumed costs increase at a reasonably steady rate with a rise in FY16 to accommodate the next stage of expansion. It is possible costs remain more tightly controlled than our forecast.

We have opted for a more conservative approach and will look to increase our forecasts and price target should TZL continue to be successful in converting this pipeline, which we think is likely. Should TZL be successful in converting 50% of this pipeline we estimate TZL could generate between A\$7-25m in EBITDA per annum over four years which could justify a valuation of between 26 and 56 cents per share, in our view. Refer to page 14 - Valuation & pipeline sensitivity for the supporting information.

### TZL's key building blocks (the locking mechanism)



## INTRODUCING TZL

TZL's core business is based around its proprietary electronic locking and fastening devices. These devices use shape memory alloy actuation to drive a unique mechanical locking device. Shape memory alloy is a smart material which changes shape when stimulated by power. The change of shape is used to drive actuation (opening or closing). This seemingly simple idea is incredibly complicated in practice and has taken over a decade of research and development to perfect. Along the way, TZL has filed over 180 patent applications (with over 40 patents granted) to protect their IP and in doing so has developed substantial Intellectual Property.

This decades of work has recently been transitioned from R&D into commercial applications. Over the last three years TZL has moved from an R&D and technology licensing company to one with an enviable list of customers including both domestic and multinational Fortune 500 companies. Intriguingly TZL does not have any notable direct competitors offering similar products. Their competitors tend to be legacy providers of old fashion mechanical or electro-mechanical locks (i.e. key or solenoid controlled locks). TZL have a high tender win rate due to product and technology superiority. They position themselves as a fully integrated provider of logistic and security solutions. Their core business model is around selling their smart locks and the associated hardware and software for controlling and managing the locks.

In FY14 TZL generated A\$8.5m in revenue and the Board has guided to FY15 revenue of around A\$19m. We estimate that 75% of FY15 revenue will come from Smart Lockers (TZL call this division Packaged Asset Delivery). Data centre rack locks account for the remaining 25% of revenue (TZL call this division Infrastructure Protection). We explain these divisions in more detail on the follow pages but have attempted to categorise this in Figure 2.

## Our interpretation of TLZ's two key divisions ▶

Currently TZL has two main divisions being smart lockers and data centre locks. Overtime we expect the verticals within these divisions to expand and we also expect the number of divisions to expand as TZL leverages its electronic locks into new applications.

**Figure 2: TZL's products explained**

Verticle	What	Example	Typical sales model
<b>Packaged Asset Delivery (PAD) aka smart lockers</b>			
Third parties fabricate the metal lockers, TZL contract manufacture the locks, TZL build and integrate the software, a third party contractor installs and maintains the system			
PAD - Postal	E-commerce mail	Singapore Post's e-commerce parcel delivery network	TZL is the prime contractor for locker bank and software integration. TZL subcontract locker bank build to Dexion and installation to a local builder
PAD - Corporate	Accountable mail	Personal packages and confidential information	TZL supplies locks to prime contractor and integrates software
	Hot desk lockers	Audited storage, distribution and collection of work items (laptop & paperwork)	TZL supplies locks to prime contractor and integrates software
	Day lockers	Employee personal storage (gym clothes)	TZL supplies locks to prime contractor and integrates software
PAD - Retail / Click n Collect	Accountable mail	Hills afterhours parts collection, Apple in store collection of items ordered online	TZL supplies locks to prime contractor and integrates software
PAD - Government	Accountable mail	Audited distribution of legal documents (courier/receptionist replacement)	TZL supplies locks to prime contractor and integrates software
PAD - Universities	Accountable mail	Audited distribution of personal packages (concierge replacement)	TZL supplies locks to prime contractor and integrates software
PAD - Residential applications	Accountable mail	Audited distribution of personal packages (concierge replacement)	TZL is the prime contractor - for each locker bank and software integration. TZL subcontract locker bank build to Dexion and installation to a local builder
PAD - Automated Delivery Asset Management (ADAM)	Accountable mail	TZL has partnered with Australian providers for a prototype proof of concept Australian e-commerce parcel delivery network. N.B. this is a non-core proof of concept trial	TZL temporarily funding the capex
<b>Infrastructure Protection (IXP) aka data centre rack locks</b>			
TZL contract manufacture the locks and sell through distribution partners. TZL build and integrate the software, a third party contractor installs and maintains the system			
IXP - electronics DC locks	Electronic rack access and monitoring	TZL locks installed (at the DC) to replace to old fashion key locks	DC operator purchases and installs
IXP - legacy swing handle but upgradable DC locks	OEM rack access - upgradable	TZL upgradable locks installed (at the factory) to replicate old fash locks. While TZL locks are mechanical (when installed) they can be live upgraded to electronic	Rack manufacture purchases and installs

SOURCES: MORGANS; COMPANY REPORTS

**Electronic notification and unlocking of parcels**



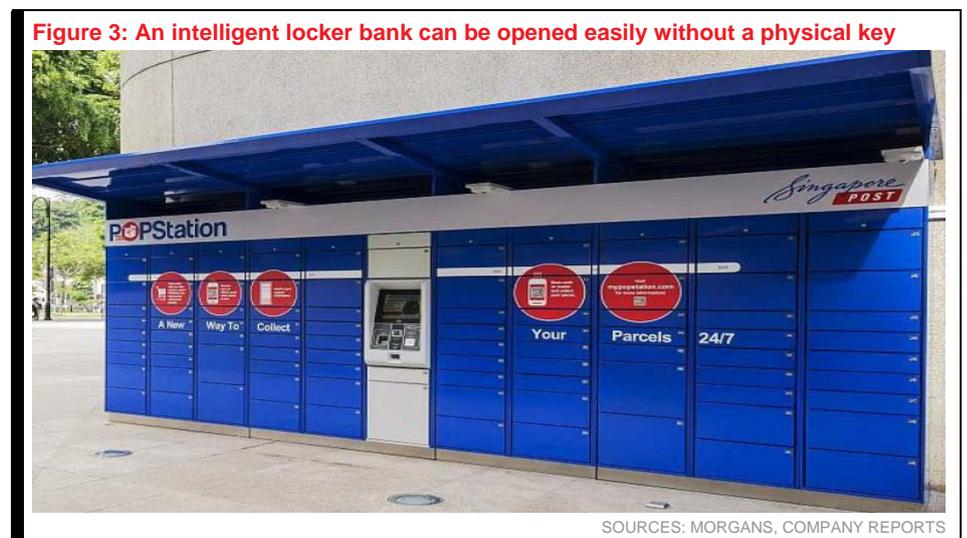
## A more detailed look at Smart Lockers aka Packaged Asset Delivery ▶

Smart Lockers by TZL are the smart version of traditional key lockers and they can be interacted with digitally. From an end customer perspective this means the user experience can be greatly enhanced as the person receiving the parcel receives an email/SMS notification that their parcel has arrived and they can collect it at virtually any hour of the day using an electronic access code.

From the logistic companies perspective this means they can improve operational efficiency and address the increasing costs associated with unsuccessful first try courier deliveries to households and improve the delivery experience for their customers. A prime example is for a postal organisation which uses lockers to provide an alternative and convenient parcel pick-up location for their customers. Because the lockers are interactive the postal organisation can direct last mile parcel deliveries to the lock and allow customers to pick-up their parcel using a unique access code to open that locker. The postal organisation has complete visibility on the chain of custody from when the parcel is dropped off, and when it is picked up.

TZL provides intelligent lockers for a number of applications. The lockers are manufactured by a 3<sup>rd</sup> party (metal lockers are supplied by Dexion and TZL also work with a large range other locker manufacturers) and TZL provides the locking mechanism, system hardware - and software for controlling the lockers. From an installation perspective they can be either the prime contractor (as is typical for postal agencies) whereby TZL manage the entire installation process; or alternatively TZL can be a technology supplier (as is typical for corporate locker builds like Westpac in Australia) where the builder assembles the lockers but is asked by the end customer to include TZL locks. The uniqueness of TZL's locks mean that they can be electronically controlled transforming the lockers from a simple storage unit into intelligent lockers. Examples include:

- 1) Singapore Post using TZL's lockers for the collection of e-commerce parcels;
- 2) Westpac in Australia using TZL's lockers for day lockers for temporary employee storage when hot-desking or for storage of gym clothes;
- 3) Accountable mail for audited distribution and collection of legal documents;
- 4) Hill Industries in Australia using lockers for after-hour collection of parts from its retail outlets (rather than extending store opening hours).



Singapore Post is at the cutting edge of technology for the delivery of parcels ordered on-line. Singapore Post use TZL's solution as part of the logistic component of e-commerce (for delivery to the end user).

**Reporting monitoring and control of cabinets/ racks within data centres**

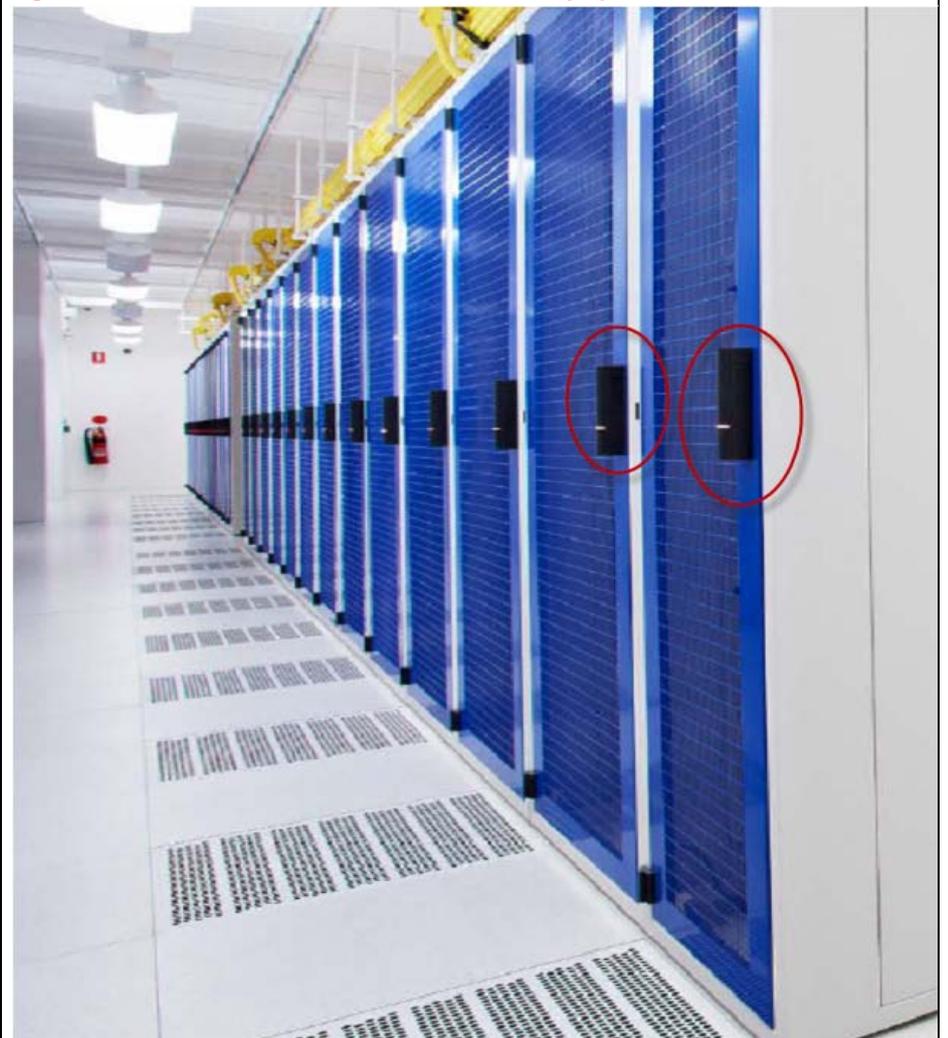


In corporate applications – what begins as a stand-alone electronic locking system eventually becomes a fully networked system which interfaces and integrates with the clients security and human database. New and leaving staff can be easily managed as can storage of staff's own personal items (e.g. files and laptops) and or delivery of accountable mail where the employer needs to know that the employee has collected sensitive documentation.

**A more detailed look at Data Centre rack locks aka Infrastructure Protection ▶**

The same auditing and control functionality that makes TZL lockers smart applies to TZL's data centre rack locks. The TZL lock protects servers within a rack (and more importantly the data within them) rather than protecting parcels within a locker. The ancillary benefits not typically included in Smart Lockers but in Data Centre locks include: Environmental monitoring – the locks can trigger alerts if the temperature or humidity is too high; and remote access. TZL's product allows the rack owner to quickly and remotely unlock their rack. For example a company could temporarily allow a third party technician to access their rack and replace a faulty part. Assuming the technician has arrived at the data centre and got through security they can call the companies IT person and ask them to unlock the rack (using a smart phone application as seen on the left hand side of this page) so the faulty hardware can be replaced.

**Figure 4: TZL rack locks are the black locks half way up each rack**



SOURCES: MORGANS, COMPANY REPORTS

**The new household letter box –  
capable of storing parcels**



## Other opportunities ▶

We see the **other product applications** (based around TZL's proprietary locking mechanism) as greatly expandable from here. That said, we believe TZL can become a profitable and successful company based purely on the two products it currently has. New products would further add to the upside.

As illustrated on the left hand side of this page, TZL have put some serious consideration into expanding their product range. While this new age letterbox is not currently in production it is an example of new areas that TZL can expand into while leveraging their existing IP. We think another obvious example is locks for poker machines (protecting coins not servers).

TZL's approach to building new products is a co-development approach. Rather than investing substantial capital and time into concepts, **TZL looks to partner with corporations looking for a solution to an existing problem.** Development of the letter box for example has been undertaken in collaboration with Singapore Post and they have placed orders for a small quantity of letter boxes to support initial commercialisation. This is important as it means the likelihood of commercial success is much greater.

## Manufacturing ▶

Historically TZL locks have been manufactured via a third party contract manufacturer in the US with plants in Mexico. This was partially a function of proximity to, and the US government's requirement for an approved manufacturer, and partially a function of not having enough production volume to warrant transitioning manufacturing to Asia. However as revenue has grown significantly over the last few years TZL have now added a second contract manufacturer in China. Full scale production from China is expected in earlier Q4 2015.

This new contract manufacturer allows TZL to scale production as required. It also has the benefit of adding redundancy to the business (there is no longer a single point of failure in manufacturing) and of improving gross profit margins as TZL's second supply source has implemented a new and improved manufacturing processes at a lower cost of labour.

As a result of the second facility which comes online in early 2015, TZL is targeting a 15% overall Gross Margin gain. All things being equal, TZL's blended gross profit margin should improve from around 50% in FY14 to ~65% in FY16.

## SWOT

### Strengths ▶

- World class technology with leading products in data centres and parcel lockers;
- Impressive customer base with a large number of Fortune 500 global companies; and
- Significant time and dollars sunk into development and commercialisation of the product range.

### Weaknesses ▶

- Currently a niche operator that is not yet profitable or self-funding so is likely to require additional funding; and
- TZL has small, highly committed team and Directors that are actively engaged in the business. However it currently has limited breadth of management and corporate governance may not be up to standard expected by some investors. We would expect that over time management is expanded to possibly include a global CEO and an experienced Chief Financial Officer.

### Opportunities ►

- Increasing sales to existing customers;
- Introduction of new products and new geographies; and
- Possible divestments, licensing or monetisation of specific products.

### Threats ►

- Competitive response from incumbents.

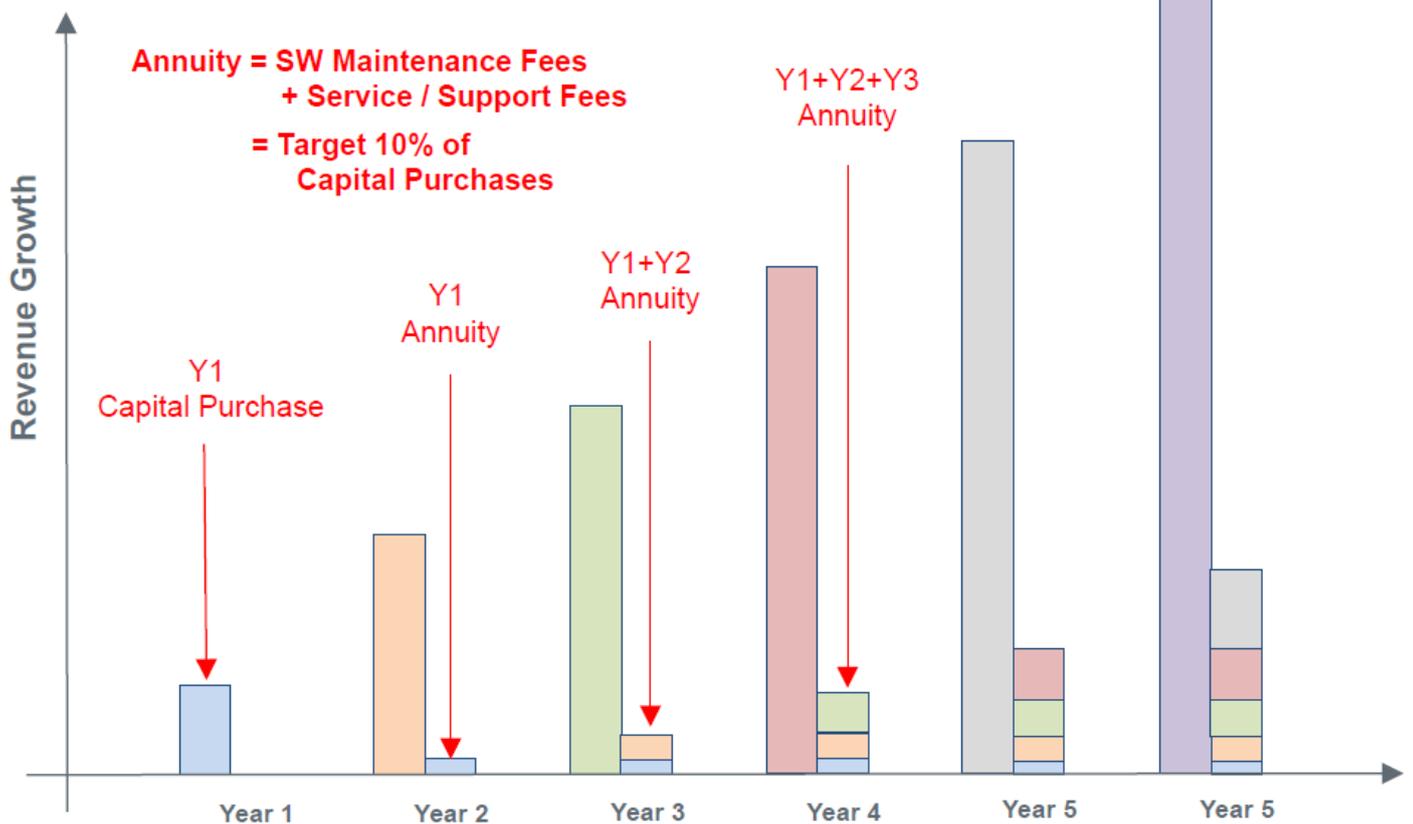
## THE FINANCIALS

### Revenue and what could accelerate it ►

In 2H14 TZL generated 25% of its revenue from Australia, 25% from Singapore, 40% from the USA and the balance from Canada and the UK. The evolution of the business has meant that TZL's data centre locks were first successful in Australia and from there have grown into new geographies.

Typically TZL target 10% of the upfront capital costs as an ongoing software and service maintenance fee (pa over the products life). This means TZL should have at least 10% of the prior year revenue as recurring revenue. Depending on the nature of the project revenue may be received over a number of phases. For example the Singapore Post Postal locker rollout began with a 5 lock trial in FY13 and was progressively rolled out to 50, then 100 and total lockers with the last 15 lockers being installed in 2H15. These larger projects give TZL good earnings visibility but also mean delays can be problematic in the short term.

Figure 5: Building a recurring revenue base



SOURCES: COMPANY REPORTS

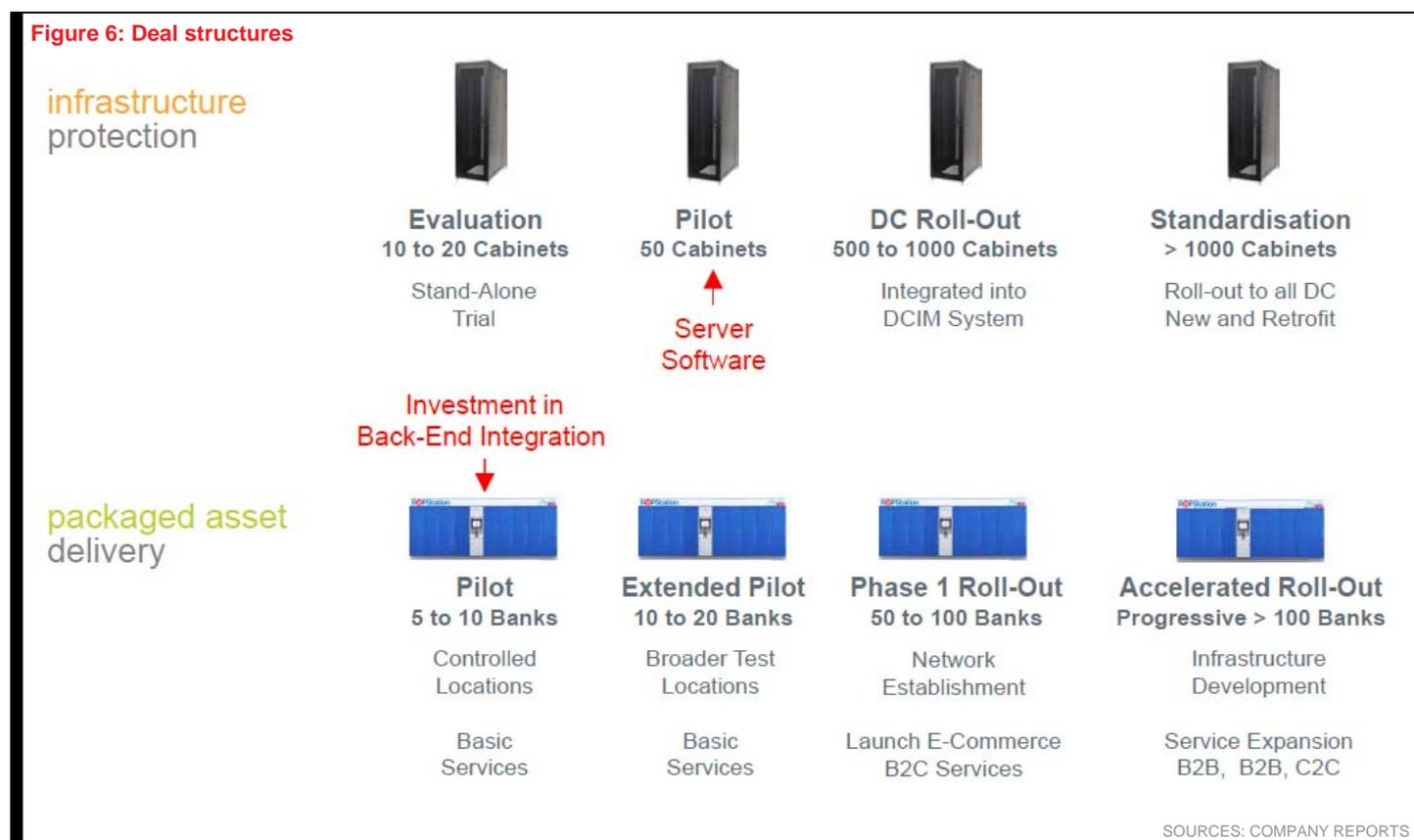
The United States is TZL's largest revenue contributor at 40% of 2H14 revenue. This is despite having the majority of TZL staff based out of Australia. We understand TZL co-founder, John Wilson, has recently moved to the United States to concentrate a greater amount of time on sales in the United States. Given the size of the market and TZL's success in the US already. **We think there are significant US opportunities in the postal and corporate arenas.**

### The revenue model ▶

TZL's sales are typically multi-year multi-site agreements. What tends to happen is that a customer makes a small initial purchase which it trials for 3-6 months before progressing to a larger staged rollout.

For example Singapore Post initially trialled 5 locker banks and eventually this increased to 100 live locker banks. We estimate the sales were staggered over 2 years with 5 locker banks sold in 1H13, none sold in 2H13, 10 locker banks sold in 1H14, 30 locker banks sold in 2H14, 40 locker banks sold in 2H15 and the final 15 locker banks to be sold in 2H15.

Figure 6: Deal structures



### Currency exposure ▶

TZL has somewhat of a natural currency hedge. Both **sale price and manufacturing costs are typically in US dollars**. A weaker AUD results in more revenue and gross profit (A\$ on translation). Operating cost are mostly in AUD so overall a weaker AUD and stronger USD is a positive to TZL. We estimate that every 1% decline in AUD:USD (a weakening of the AUD) results in 0.75% increase in gross profit to TZL (~75% of TZL's revenue is generated outside Australia and largely in USD).

## Research and development spend ▶

**Capitalised R&D** was A\$0.5m or ~6% of revenue in FY14. We forecast this number to increase to around A\$0.75m or 4% of revenue from FY15 onwards. We estimate that TZL invests around **15% of its revenue in total Research and Development** which is a healthy amount relative to industry standards (10-20% of revenue on R&D) and relative to the size of TZL's business.

Our total R&D calculations include development opex, development capex and work completed internally by TZL's infinity design (which bills its staff out 50% of the time and spends the other 50% of the time working on TZL products). We have not included employee costs in our R&D estimate but it could be easily argued a significant portion of this is R&D related. Employee costs are TZL's largest single cost at around 70% of revenue and 60% of total operational costs.

## Funding ▶

TZL has sufficient capital to fund the business plan to deliver FY15 revenue guidance. Should business activity accelerate beyond that or the company win material new contracts then additional growth capital may be required.

TZL has a strong product offering but a relatively small balance sheet. At 30 June 2014 TZL had A\$2.6m in cash and no debt. They recently raised A\$1m (8m new shares issued at 12.5cps). TZL has 393m shares on issue after the capital raising. In our view, the balance sheet remains reasonably tight and we expect that TZL will require additional equity funding to grow the business. The amount of funding that may be required is difficult to estimate. On our analysis, we expect that TZL needs an additional A\$10m in equity before the business is likely to be self-funding. This could vary materially depending on any number of outcomes so could be substantially higher or lower. We assume the equity base increases by ~10% to 442m shares by the end of FY16.

**We forecast TZL to reach profitability in FY17 and from this point onwards it should be a self-funding business.**

## Comments on TZL's latest quarterly update ▶

On 30<sup>th</sup> January 2015, TZL released its December 2014 quarterly information. 1H15 reported revenue is expected to be around A\$7m (which is in-line with our forecast and up 112% yoy). TZL reaffirmed FY15 revenue guidance of A\$18m which requires 2H15 revenue of A\$11m. This 1H/ 2H revenue split is in-line with FY14. Their quarterly revenue run-rate has increased to A\$5m (from A\$2m in Q2 FY14) which makes 2H revenue in excess of A\$10m look comfortably achievable.

TZL also noted a backlog of A\$4m. This is effectively orders in hand that have not yet been shipped. Given TZL typically have a 14 week lead time we expect all of this backlog to convert to revenue in Q3 FY15. Operating cash flow should also improve in Q3 FY15 as TZL's inventory that was built up for several larger customers in Q2 is shipped and converted into cash receipts.

## Share Purchase Plan to fund working capital ▶

On 4<sup>th</sup> February TZL announced a Share Purchase Plan to fund future growth. Morgans Financial Limited has been appointed by TZ Limited to manage its Share Purchase Plan (SPP) announced in February 2015 and may receive fees in this regard. The SPP is expected to close on 27<sup>th</sup> February with new shares listing on the ASX on 9<sup>th</sup> March 2015.

The funds raised under the SPP will:

- enable the Company to fund the delivery of further contract wins in its PAD and IXP businesses;

- allow the Company to expand its tender team in order to execute in response to new tender requests;
- fund the costs of marketing the Company's Day Locker offering which has been successfully launched and deployed in Australia, to existing accountable mail customers in the USA; and
- provide additional working capital.

## BOARD AND MANAGEMENT

### Management ►

Given its relatively small size TZL doesn't have much breadth to its Executive ranks. Mark Bouris is the Executive Chairman and there are two other directors but the company lacks a Chief Executive Officer and also lacks a Chief Financial Officer. From a corporate governance perspective this is a challenge but we'd expect that over time, as scale is built, these roles should be filled.

Figure 7: Board and management

Name	Role	Background	Qualifications	TZL ownership (inc options)
Mark Bouris	Executive Chairman	Has over 25 years' experience in the finance and property sectors. Mark is also the Executive Chairman of Yellow Brick Road, Non-Executive Chairman of Anteo Diagnostics Limited and a board member of the Sydney Roosters. He is an Adjunct Professor at the University of New South Wales Australian School of Business and he sits on boards for the University of NSW Business Advisory Council and the University of Western Sydney Foundation Council. Mark is also the author of three business and finance books.	BCom (UNSW), MCom (UNSW), HonDBus (UNSW), HonDLitt (UWS), FC	3.10%
Kenneth Ting	Executive Director and Company Secretary	Kenneth Ting has a background in accounting, law and investment banking with a focus on the commercialisation of technology and public and private equity raisings. Kenneth joined Deutsche Bank in 1997 after 4 years at PricewaterhouseCoopers Corporate Finance and Tax division. He was Vice President of Technology Investment Banking at Deutsche Bank and worked in Deutsche Bank's Sydney, San Francisco and London offices. Kenneth has a passion for technology and has worked with technology companies throughout his career. He has been involved in the completion of over \$5 billion in M&A, private equity and IPO assignments in Australia, USA and Europe. His industry specialisation is in the electronics manufacturing, software, IT services, telecommunication and Internet sectors.	BCom, BLaw, CA	3.10%
Paul Casey	Director	Paul Casey brings over 30 years' experience in international travel and tourism and early stage investing. Paul was President and Chief Executive Officer (CEO) of Hawaiian Airlines, a New York Stock Exchange (NYSE) listed company, from 1997 until 2002. Prior to that he led the Hawaii Visitors and Convention Bureau (HVCB) as President and CEO and he held a succession of senior management positions with Continental Airlines and Thomas Cook. Paul has run a travel software start-up in Bangkok, was the CEO of an investment firm focussed on rolling up travel-related businesses in China and was involved in restructuring a number of travel and tourism projects. He is also an investor and adviser to several Hawaii early stage companies and since 2011 has been on the board of PDT.		0%
John Wilson	Co-founder	John Wilson co-founded and built TZ from its inception in 1998 to when he left the Company in late 2006. He returned as a consultant to the Company in 2010 and today, continues to provide on-going operational and strategic business support. John has extensive global business experience, having spent most of his 25 year career in the development of international businesses in Asia, Europe and the US including establishment of major strategic alliances and partnerships, technology licenses and driving market entry strategies through new product innovation and commercialisation. Prior to starting TZ, he spent a decade working for a major multinational manufacturing corporation in senior executive positions across marketing, business development, strategy development, technology management and business unit general management. John specializes in the field of strategic business development, innovation management and product commercialisation. John has an engineering degree and post graduate qualifications in international marketing. He has also received significant skills development from graduate programs in the US and in Europe in the areas of value based management and innovation management.		n/a

SOURCES: COMPANY REPORTS

## KEY RISKS AND REWARDS

### Risks ▶

There are several people within TZL that we consider integral to the business. Given the currently limited resources and limited breadth of Executives this creates **key man risk**.

TZL is a loss making business so in our view the key risk relates to funding the business until it reaches profitability. We expect **further equity** is likely to be required and attempt to factor this into our forecasts with a 10% higher share count.

Overtime there are the **traditional technological and competitive response risks** that apply to all businesses. However, in our view, in the short term these are unlikely primarily due to the fact that TZL's is not yet a mass market product (its niche). More specifically TZL are not hurting the incumbents enough yet for them to respond. As TZL's revenue grows there is the risk that legacy competitors react to TZL's success by greatly improving their R&D effort in order to bridge the gap between their product and TZL's. TZL has invested decades of R&D to only recently achieve product success and they have accumulated losses of A\$175m along the way. Replicating the product would be much harder and more costly than simply acquiring the company, in our view.

### Rewards ▶

TZL have a large and growing pipeline with up to \$306m of potential work up until 2018. We believe TZL's product superiority and historic win rates place them well to win a large portion of this work.

We understand that to-date, and based on the work TZL has bid for as the prime-contractor, its win rates have been close to 100%. A lot of work is also handed to TZL directly (i.e. not through a tender process) but as a direct result of customers "specking in" the TZL product.

**If we arbitrarily assume TZL bid for and is successful in winning 50% of the total \$306m pipeline then this would equate to A\$153m worth of work.** Our forecast assumes TZL generates total revenue of A\$117m from FY16 to FY18 inclusive. Assuming the revenue is evenly spread across 4 years this equates to revenue of \$38 per annum in FY16, 17, 18 and 19.

This \$38m in potential annualised revenue should result in EBITDA of around A\$7m-25m which could justify a per share valuation of around 26cents (applying 10x EV/EBITDA). See page 14 for more details.

Obviously we expect there are many more revenue generating opportunities that will present themselves in the coming years so see risk to the upside.

While the most obvious opportunities relate to winning more work we also expect that TZL (as a whole) could become a corporate target as it builds scale and that the opportunity to license parts of the TZL business could also result in significant rewards/ monetisation.

TZL is currently nipping at the heels of several multinationals. As TZL's product continues to gain traction we believe this is likely to put them on the radar as a corporate target. For example in the data centre locking arena TZL currently competes with companies like APC/ Schneider Electric. Schneider is a multi-billion-dollar multinational company with global manufacturing and distribution networks and could easily acquire TZL's Data Centre locking business to complement its legacy data centre business.

TZL's ADAM network (Australian postal lockers) is also ripe for divestment, in our view. It has been built as a proof of concept and requires capital and scale to fulfil the vision. We expect that this is more likely to succeed in the hands of a well-funded multinational.

Pipeline ▶

Figure 8: \$23m pipeline over the next three years

## IXP New Projects / Existing Client Potential

2015 to 2018 Horizon

Project Description	Sales Potential
<b>IXP, NORTH AMERICA</b>	
Financial Institutions and Telco Projects	\$7M
North American Government Entities (Federal, State and City)	
Sales through Distribution, OEM's and Integrators	
<b>IXP, EUROPE</b>	
OEMs – SwingHandle Initiative	\$8M
Expansion from Datacentre Operators who have standardised on TZ	
<b>IXP, AUSTRALIA</b>	
OEMs –SwingHandle Initiative	\$3M
New Datacentres – planned infrastructure development	
<b>IXP, ASIA</b>	
Expansion into Asian Datacentre Operators	\$5M

SOURCES: COMPANY REPORTS

Figure 9: \$283m pipeline over the next three years

## PAD New Projects / Existing Client Potential

2015 to 2018 Horizon

Project Description	Sales Potential
<b>CORPORATE LOCKERS, USA</b>	
Expansion projects from existing Technology, IT and Financial Institution customers	\$10M
<b>RESIDENTIAL LOCKERS, USA</b>	
National expansion of leading Property Management firms	\$10M
<b>OTHER PAD BUSINESS, US AND AUSTRALIA</b>	
Higher Education Parcel Lockers	\$6M
Retail Click and Collect Parcel Lockers	
<b>DAY LOCKERS, AUSTRALIA</b>	
Banking, Insurance, Financial Services and New Corporate Clients	\$7M
<b>POSTAL LOCKERS</b>	
Expansion of existing SE Asia Network - Singapore Post, Pos Malaysia, Pos Indonesia	\$250M
Expansion of US Logistics Network	
European Postal Tender	
European Postal Business – Pos Italiane Expansion, New Postal Business	

SOURCES: COMPANY REPORTS

## VALUATION AND PIPELINE SENSITIVITY

Below we have attempted to quantify the potential outcomes from differing win rates and their impact on earnings and our valuation. Our base case 50% win rate could, in our view, justify a 26cps valuation. Details are explained below.

### Pipeline sensitivities ▶

TZL's listed pipeline is worth \$306m over 4 years. If we assume they are successful in winning 50% of this work this would generated EBITDA of A\$7.2m on revenue of A\$37.9m (annually for four years). At the base case we apply 10 EV/EBITDA to this valuation to establish a 26 cent per share valuation. It's difficult to separate the pipeline of work from current work TZL has as the two are intertwined. Regardless successful execution by TZL represents significant upside for shareholders.

Figure 9 below runs some sensitivities around this. To simply the process we assume the A\$306m pipeline of work (as announced by TZL) is evenly split over 4 years so the annualised revenue opportunity (point 4) is \$75.75m. We assume that TZL win 50% of this pipeline.

As figure 9 below shows, if we assume the **low case (A)** that the pipeline represents all of TZL revenue and therefore there is no operating leverage in the business (i.e. the pipeline revenue is directly attached to TZL fixed operating costs), then we end up with an EBITDA profit of A\$7.2m (a 19.1% EBITDA margin) justifying, in our view, a share price of 16 cents (applying 10x EV/EBITDA). If we apply an EV/EBITDA multiple of 6x (a bear case) then the valuation is 10cps while applying 14x (a bull case) the valuation lifts to 23cps.

If we assume the **base case (B)** that the pipeline represents upside to TZL's existing revenue base and therefore generates margin expansion because the operating cost don't expand as much as revenue (we assume the incremental operating costs are 75% of case A). Apply 10x EV/EBITDA to this generates a 26c valuation. If we apply an EV/EBITDA multiple of 6x (a bear case) then the valuation is 16cps while applying 14x (a bull case) the valuation lifts to 37cps.

If we assume the **High case (C)** that the pipeline represents upside to TZL existing revenue base and has no incremental operating costs associated with it; then the outlook is impressive. In our view this is a highly unlikely event but does indicate that business such as TZL should have strong operating leverage as all the gross profit falls to an EBITDA profit. If we apply an EV/EBITDA multiple of 6x (a bear case) then the valuation is 33cps while applying 14x (a bull case) the valuation lifts to 78cps.

**Figure 10: Pipeline sensitivity and valuation if we capitalised the earnings**

Details	Legend	A - Low case	B - Base case	C - High case
Total pipeline over 4 years	1	303	303	303
Total pipeline per annum	2 = 1 / 4 yrs	75.75	75.75	75.75
Assumed TZL win rate	3	50%	50%	50%
TZL Revenue	4 = 2 * 3	37.9	37.9	37.9
Gross profit	5	24.6	24.6	24.6
... Gross profit margin	6	65.0%	65.0%	65.0%
TZL opex	7 = Morgans F FY16 opex	17.4	13.0	0.0
EBITDA	8 = 5 - 7	7.2	11.6	24.6
... EBITDA margin	9	19.1%	30.6%	65.0%
Multiple applied to val	10	10	10	10
Enterprise value	11 = 8 * 10	72.4	115.9	246.2
Net Debt (1)	12	0.0	0.0	0.0
Equity value	13 = 11 - 12	72.4	115.9	246.2
Diluted shares on issue	14 = Morgans F FY16 shares	442.8	442.8	442.8
Valuation per share	15 = 13 / 14	0.16	0.26	0.56

SOURCES: MORGANS, COMPANY REPORTS

## TZL commentary on pipeline and win rates ▶

We have discussed the tender win rates and operational costs associated with the pipeline with TZL management. Their feedback is very positive. TZL typically win much greater than 50% of their tenders and expect limited increased in operating costs should revenue step-up strongly.

TZL is already operating with a relatively large fixed cost base as it had to set-up the business for 24-7 support of its Fortune 500 clients. This support base shouldn't change materially as the revenue base increases. More specifically the rule of thumb management work towards is that 25% of contract revenue should become EBITDA profit. For example a US\$40k contract typically comprise of US\$20k in COGS (locker components), US\$10k in labour associated with TZL's overheads (e.g. office and support costs) and the remaining US\$10k is profit.

## Impact of changed tender rates ▶

Adjusting the win rates has a strong impact on the valuation. Every 5% change in the win rate (e.g. moving from a 50% to 55% win rate) adds roughly 20% to EBITDA and the valuation.

**Figure 11: Impact of changing the tender win rate**

Our base case is illustrated below with a **50% win rate** (i.e. no change)

	Base	Revised	% change
Win rate	50%	50%	0.0%
EBITDA	11.6	11.6	0.0%
Valuation per share (at mid point or 10x)	0.26	0.26	0.0%

Illustrated below with a **30% win rate** (i.e. 20% reduction on our base case)

	Base	Revised	% change
Win rate	50%	30%	-40.0%
EBITDA	11.6	1.7	-85.0%
Valuation per share (at mid point or 10x)	0.26	0.04	-85.0%

Illustrated below with a **70% win rate** (i.e. 20% increase on our base case)

	Base	Revised	% change
Win rate	50%	70%	40.0%
EBITDA	11.6	21.4	85.0%
Valuation per share (at mid point or 10x)	0.26	0.48	85.0%

SOURCES: MORGANS

## TIMELINE OF ASX RELEASES

Below we've highlighted and grouped TZL's substantial ASX announcements for a history of the companies' progress over the last two years.

**Figure 12: Colour code**

DC rack locks
Parcel Lockers for retailers or distributor
Parcel Locks for corporate hot desks
ADAM - Australian Automated Delivery Asset Management

SOURCES: MORGANS, COMPANY REPORTS

**Figure 13: Timeline around key ASX releases part 1 or 2**

19-Nov-14	Poste Italiane's Paccomat Parcel Locker Network officially opened		Locker
18-Nov-14	TZL signs multi-million dollar supply contract with Fredon Industries for Day Lockers at Westpac's new Baragaroo office in Sydney. To be completed early 2015.		Locker
11-Nov-14	PO from Hills Limited (HIL:ASX) for parcel lockers for Hills' Click and Collect (after hours pick up at Hills Lidcombe NSW & Hills Hendra QLD)		Locker
4-Nov-14	TZL parcel lockers commissioned with US Logistics and Transportation Corporation (see 28 May 14 announcement)		Locker
27-Oct-14	Pos Malaysia (Malaysian Post) awards a TZL a conditional order of Parcel Lockers (conditional on Pos Malaysia Berhad and TZL to contracting)		Locker
12-Sep-14	TZL gets PO (through Integrator Appsilan Asia Pte Ltd a Lantrovision subsidiary) from European finance company for DC locks in its Singaporean DC. Deal relates to the Monetary Authority of Singapore (MAS) issues new legal requirements for critical It system security.		DC
4-Sep-14	PO for ACG Fire and Security for another set of Day Lockers for a major bank in Brisbane.		Locker
24-Jul-14	TZL patents in Australian and Japan granted. This is for a micro fastening mechanism called TZL's Beam Clip.		
16-Jun-14	Pos Indonesia (Indonesian Post) officially launched e-Post Lockers. Three month trial starting this month and could progress to 40 locker banks		Locker
28-May-14	Master Supply Agreement with US Logistics and Transportation Corporation for Parcel Lockers. TZL awarded several locker banks after 9 month tender process.		Locker
27-May-14	PO for Day Lockers for Westpac (through ACG Fire & Security) announced (150 Collins St Melbourne and 275 Kent St Sydney)		Locker
30-Apr-14	Quarterly update		
11-Apr-14	Day Locker deal with Westpac in Au announced. Supply for mid 2014 to early 2015 as new offices become available.		Locker
9-Apr-14	Master Supply Agreement with "Global Consumer Electronics corporation headquartered in California".	A\$250k, 7 locker banks in 3 locations	Locker
31-Mar-14	TZL announces its extending PAD from parcel collection into day lockers (hot-desk style). Order size can be few millions dollars and typically Day Locks cater for 70-120% of FTEs		Locker
25-Mar-14	PO from Singapore Post for 55 additional locker banks to be installed by the end of CY 2014.		
30-Jan-14	Quarterly update		Locker
20-Jan-14	Pos Indonesia (Indonesian Post) awards TZL (through its integrator Gunnebo Indonesia c/o PT) Smart locker trial for deployment in March 2014.		Locker
9-Jan-14	TZL receives largest IXP order today in the US and announces its SwingHandle (retrofit able lock) will be released this month.	A\$0.8m	DC
7-Jan-14	Poste Italiane (Italian Post) awards TZL (through its Integrator FBA) Smart Parcel Locker rollout. Pilot plans for early 2014 with 5 locker banks including software and integration.	5 lockers	Locker
30-Oct-13	TZL presentation on "The Future of E-Commerce Delivery" in London		
30-Oct-13	Cooperations agreement signed with major European System Integrator do DC locks to DC and Defence projects. Progressive deployments up until 2015.		DC
23-Oct-13	All convertible notes now converted to ordinary shares. \$24m of debt converts to 137m TZL shares at 14-18c per share		
8-Oct-13	Quarterly update		
4-Oct-13	IXP update - now installed in over 2,300 cabinets in America for Government, Defence, Banking, Finance & Insurance. Expanding into new geographies. Appointed BGW Group as an Australian distributor		DC
28-Aug-13	Singapore Post PO for 30 locker banks with 80-120 lockers per bank. To be installed by end of CY13.	Seven figure o	Lockers
9-Aug-13	Waters Australia (subsidiary of NYSE:WAT) to use ADAM as a temporary staging point for distributing spare parts to its field personnel. Allowing for parts collection within 24 hours of order. Trialled in VIC and they pay per parcel delivered		Lockers
6-Aug-13	Locker agreement to supply East Tennessee State University and a second US college. This allows for 20 hour per day parcel collection vs currently 7 hours allowed.		Lockers

SOURCES: MORGANS, COMPANY REPORTS

**Figure 14: Timeline around key ASX releases part 2 or 2**

Date	Description	Scale
2-Aug-13	TZL acquires its supplier Infinity Design Development (Industrial designer) for A\$.5m.	
31-Jul-14	Quarterly	
10-Jul-13	ADAM enters agreement with Secure Parking (1,400 car parks in Au and Asia Pacific). Trial now with phase 2 expected in October	250 sites in Au Lockers
3-Jun-13	TZL sells its PDT division - Product Development Technologies for US\$5m. Bring capital to TZL and removes the capital drain as this was a loss making division	
23-May-13	ADAM adds TNT Express (domestic and international couriers) to Teaming agreement.	ADAM
22-May-13	ADAM update - to go live in the next few weeks at MLC Centre in Martin Place Sydney, Melbourne Central Shopping Centre (CBD), BP Petrol Station at Church St Richmond VIC and 3 more in MLB, SYD & BNE to be confirmed shortly	ADAM
21-May-13	Singapore Post signs PO for Phase 2	Lockers
21-May-13	Teaming agreement with Fastway Couriers in Au to work in ADAM Parcel Locker System. TZL comments that Fastway + Toll agreements get them to 60% of parcel delivered in Australia.	ADAM
30-Apr-14	Quarterly update -	
22-Apr-13	Singapore Post Smart Locker (POPStation) network officially opened. Each station has about 115 lockers with four different dimensions for different parcel sizes. Sing Post signals it will proceed to phase 2 which includes new features such as direct integration to e-commerce retailers so they can use POPStation Network.	Lockers
11-Apr-13	Enters master supply agreement with global financial services corporation for smart lockers in some US locations and potentially world wide for secure delivery of accountable mail and packages. Pilot is US\$250k (deployment at the end of May) and success could add to more contracts. TZL also comments its received >1k SlideHandles orders from SRA/ Server Racks Australia for the Au government for mid May deployment.	US\$250k + ongoing Lockers
8-Apr-13	Toll agreement for ADAM. Toll will add ADAM to its "extensive collection network" inc Parcel newsagency parcel collection service.	ADAM
11-Mar-13	Site agreement for Adam. Automated Delivery Asset Management agreements with major petrol station franchisee in VIC and also Au's largest independent & fully integrated oil company. VIC with AA holding which has 50 BP stations. AU with Australian Fuel Distributors / AusFuel which have 80 Gull petrol stations in WA, SA, QLD & NT. TZL has a 12 month exclusivity agreement inc pilot to convert to a deal. Trials in SYD x2, MLB x2, Bx1, Px1 from beginning of May 2013	Pilot 6 sites with up to 130 sites on offer ADAM
7-Mar-13	First phase on Singapore Post smart-lockers completed with 5 locker banks deployed. Lockers per bank ranged from 80-120. This phase includes integration of TZL solution into Singapore Post's IT infrastructure (courier/workflow management). Phase 2 should be another 50 lockers progressively rolled out over the next 12 months. Total project could be upto 100 locker banks deployed.	Lockers
31-Dec-12	ASX correction issued due to symantecs - Sing Post saying until they official open the lockers Phase 1 not complete.	Lockers
18-Dec-12	TZL & QVT (convertible note holder) agree to convert debt to equity at 14cps	
18-Dec-12	Confirmed first Au smart-locker has been manufactured and will be trialled in Sydney CBD in January 2013 re "Adam" smart-locker parcel delivery network	ADAM
31-Oct-12	PAD - Q1 had 5 trial deployments to US Fortune 100 companies. This should lead to rolling out 50 new locations in 24 months and US\$2.4m rev. Also secured 20 banks of lockers for 2 prominent tech leaders - should be delivered end FY13. 2 Integrator Partners appointed in Europe which are targeting pilot programs in early CY13	Lockers
31-Oct-12	IXP secured 2 large contracts from US government agencies with 2 more sizeable contracts expected in Q2. Winning work in Latin America, Middle East, Nordics, Europe and Au (AU = NXT, MAQ and SRA for government work).	DC
31-Oct-12	Quarterly update - now 25 TZL certified partners supporting IXP & PAD in North America, EMEA and Australia.	
22-Oct-12	Rack locking system contract with "two major DC deployments in the Middle East and South America". Potential for 1,600 racks of the next two years	1,600 racks DC
24-Sep-12	GPT Trial Deployment - of parcel locker network - plans around carrier agnostic parcel network in Australia	ADAM
14-Sep-12	Singapore Post tender awarded for Smart locker network. Singapore Post also owns e-commerce sites vPOST and Clout Shoppe.	Locker
13-Aug-12	ADAM Teaming agreements with Temando Pty Limited (e-commerce delivery system provider) & ParcelPoint (has lockers in 500 AU locations) for streamlined parcel collection.	ADAM
4-Jul-12	Redwood Systems Partnership - for LED energy efficient lighting guiding clients to their racks	DC
22-Jun-12	MOU signed with UCIT Online Security for "Remote Concierge systems". "Hoping to integrate a few dozen condos in the first 18 months"	Lockers
6-Jun-12	ControlCircle data cabinet security locking supply agreement signed	600 cabinets DC
30-May-12	Loss of Au Post tender due to Pitney Bowes Au. "TZL expects to achieve its first break even month in terms of cash flow during the last quarter of the financial year ending 30 June 2013."	ADAM
4-Apr-12	TZL releases "certified Integrator Program". New Sales channels to be established in June 2012 with the sign up of 20 businesses. Each partner committed to delivering \$100k pa in sales	
2-Mar-12	DC locks for "at least 95%" of Macquarie Telecom's IC2 DC	9,500 racks DC
1-Mar-12	Supplier agreement with Dexion for locker fabrication	
1-Feb-12	LOI - with leading global shopping centre for locker deployment.	
1-Feb-12	Trail deployment expected by June 2012	ADAM

SOURCES: MORGANS, COMPANY REPORTS

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