

(In million)		FY2016	FY2017	FY2018
Revenue		126.7	139.6	160.0
Net loss		(9.4)	(15.6)	(138.4)
Loss per share (HKD cent)		(0.3)	(0.4)	(3.5)
Share outstanding (million shares)	4,070	Share price (HKD)	1.76	
Market Capitalization (HKD'm)	7,160	12-month high/low (HKD)	2.50/0.58	

Major shareholders Chairman Mr. Raymond Ting Pang Wan (51.85%), Ding lu (7.35%), Diginex Limited (5.24%)

Source: Annual report 2017, Mason securities

Madison Holdings Group Limited (8057.HK) is a company incorporated in Hong Kong in the retail sales and wholesales of a wide spectrum of wine products and other alcoholic beverages in Hong Kong with a focus on premier wine and fine wine as well as the provision of a range of customer-centric value-added services. Successfully listed on GEM in October 2015, the adjusted IPO price was HK\$ 0.075 (share subdivision of every 1 share into 10 shares in October 2016). Since 2017, the company began to carry out financial services business. In 2018, the company set foot in the blockchain industry, and began to acquire and invest in cryptocurrency exchange and cryptocurrency mining company. Madison Holdings is currently the only company directly involved in the actual blockchain technology and cryptocurrency among all Hong Kong listed companies. The company is beneficially owned and controlled by the chairman and executive director of the company, Mr. Ting Pang Wan Raymond, who directly or indirectly holds 51.85% of the shares, while the remaining shareholders holding more than 5% include Mr. Ding Lu (7.35%) and Diginex Limited (5.24%).

Figure 1: Company's Milestones



Source: Bloomberg, Mason Securities

1. Financial Performance

As a general review, the revenues for the company's 2016 financial year (2016FY), 2017 financial year (2017FY) and 2018 financial year (2018FY) (ended 31 March 2018) were HK\$127 million, HK\$140 million and HK\$160 million, with a net loss of HK\$9.45 million, HK\$14.6 million or HK\$138 million. In 2018FY, its losses increased substantially due to changes in the fair value of the exchangeable bonds which generated a loss of HK\$124 million. Its gross margin were 26.0%, 20.2% and 24.4%, respectively. In 2018FY, the wine business generated a revenue of HK\$151 million, which accounted 95% of the total revenue.

2. Blockchain market layout new impetus

Blockchain technology is a distributed database system that acts as an “open ledger” to store and manage online transactions. The information of transaction is simultaneously recorded over multiple, distributed database systems across the globe. Each validated record in the database is called a “block” which contains details, such as identities of transacting parties, transaction amount and timestamp, etc. Since each “block” is linked to the previously validated “block”, it is nearly impossible for anyone to alter information about the records retrospectively. Since Blockchain is immutable – information remains in the same state for as long as the network exists, Blockchain can be considered as a trustworthy “big database”. Its decentralized features can totally eliminate the middleman, such as government and banks, in a transaction. According to a report from an industry intelligence advisory firm, the market size of Blockchain is expected to increase from US\$219.9 million from 2016 to US\$7,688.3 million in 2022, representing a compound annual growth rate (CAGR) of 79.6%. The main growth drivers of the blockchain industry include the ability to lowering the total costs, simplifying business processes, demonstrating greater transparency and stability, performing faster transaction speed and applying “Blockchain-as-a-service” in different areas (including but not limited to, payment system, financial services, cloud computing, networking, network security and encryption currency, etc.). As one of the applications of blockchain technology, cryptocurrency has received wide attention.

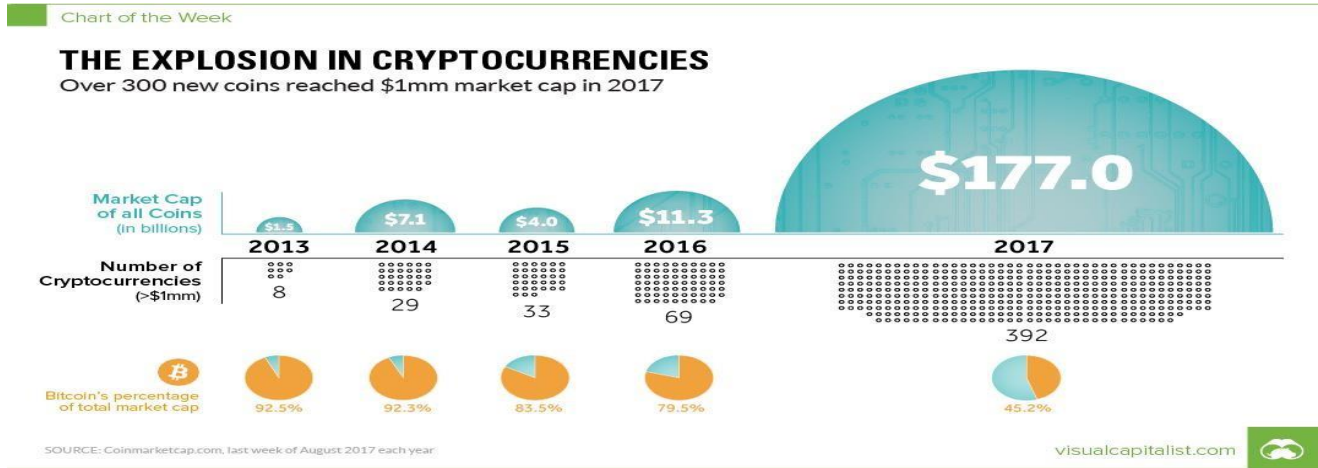
Figure 2: Bitcoin and major players in the industry value chain



Source: Frost & Sullivan

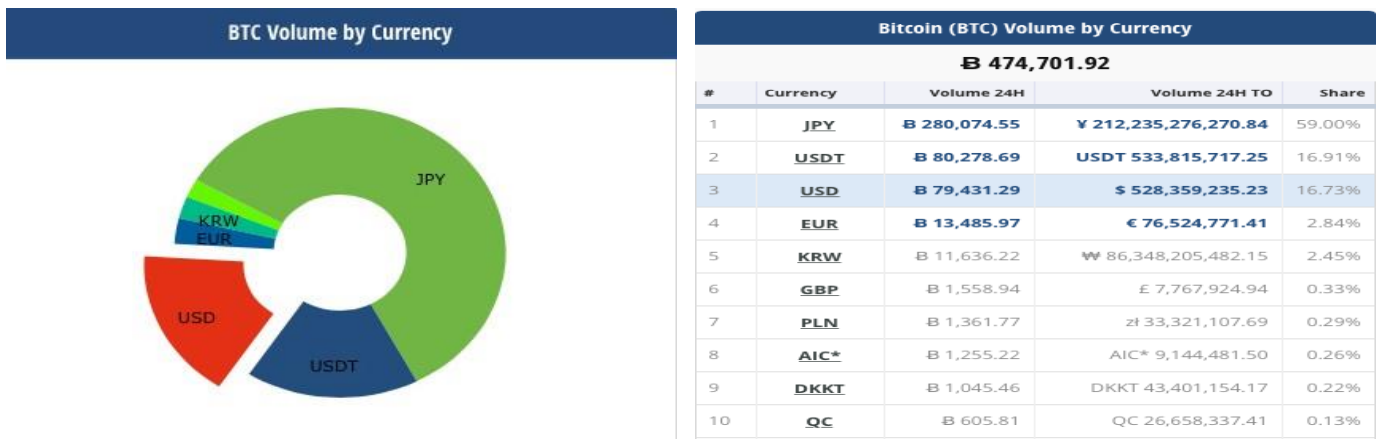
In 2017, the total market value of the cryptocurrency has been increased to US\$17.7 billion, representing nearly 15 times the amount in 2016. Japan is the world's most active virtual goods and cryptocurrency market. In 2017, by introducing legalized cryptocurrency trading license system in Japan, cryptocurrency settlement became Japan's one of the accredited legal settlement method. As of March 2018, the FSA (Financial Services Agency in Japan) had issued 16 cryptocurrency trading platform licenses. By far, Japan is currently the largest Bitcoin exchange market.

Figure 3: Types of cryptocurrency and the explosive growth in the total market value of cryptocurrencies



Source: Visual Capitalist

Figures 4 and 5: the distribution of Bitcoin volume in different currency



Source: CoinMarketCap

2.1 The 20% acquisition of Japan cryptocurrency trading platform, Bitpoint

Given the rising demand for cryptocurrency, the Directors are optimistic about the development of the cryptocurrency trading platform. On 30 March 2018, Madison Holdings entered into an agreement with the vendor, Remixpoint.Inc to acquire 20% stake in Bitpoint for a consideration of JPY 5 billion (equivalent to HK\$362 million) which will be fully paid in cash upon completion of the acquisition. Established in March 3, 2016, Bitpoint Japan is one allowed to engage in cryptocurrency trading platform. It supports the transaction currency, Bitcoin (BTC), Bitcoin cash (BCH), Ethernet currency (ETH), LTC and XRP, earning trading platform services (mainly cryptocurrency and fiat currency transactions with a bid-ask spread on the market of about 5%-7%). As for FY2018, the platform obtained an income of JPY 4.55 billion (approximately HK\$323 million), which was 182 times the income of the previous year, and generated net profit of JPY 3.73 billion (approximately HK\$278 million), turning losses to profit. The profit was mainly attributable to 1) a significant increase in the number of clients upon successfully obtaining the cryptocurrency trading; and 2) the upgrade of the trading system by the end of 2017 to meet the demand in the increased trading volume and reduce the delay time of the transaction and settlement. As of May 2018, the platform had more than 50,000 members. As shown in the Madison Holdings' announcement, the vendor delegated a Japanese business valuation company to issue a valuation report of the target company, and it is expected that the target company is expected to generate revenue and net profit of over JPY 21.6 billion (approximately HK\$1.534 billion) and JPY 13.9 billion (approximately HK\$987 million) for the 2019 financial year, respectively. Madison Holdings' purchase price was about 6.5 times the FY2018 earnings. Madison Holdings expects the acquisition will be completed in July, and we expect the acquisition will bring Madison Holdings a net profit of about HK\$100 million in the 2019 financial year.

2.2 The 51% acquisition of cryptocurrency mining company, Diginex

On 27 April 2018, Madison Holdings announced the acquisition of 51% stake in Diginex (a distributed classification DLT technology service provider) for a total consideration of US\$60 million of which US\$10 million will be paid by cash (Paid), and the remaining US\$50 million (approximately HK\$392 million) will be paid by 213 million new shares (representing approximately 4.98% of the enlarged issued share capital) to be issued by Madison Holdings upon the completion of the acquisition. Diginex was established on 21 December 2015 and started its operation on 1 June 2017. The target company currently has 2.2 megawatts of datacenters under management located across Asia and Europe. The target company mines predominately Ethereum (ETH) using high performance graphics processing units (“GPU”) Mining. The target company chose Sweden as the main cryptocurrency mining location as it is a favorable region (low temperature, low electricity cost and low taxes). Such acquisition is in line with Madison Holdings’ expansion plans in cryptocurrency blockchain related fields, and virtual currency mining is integral to fill the upstream business chain. As of 31 March 2018, Diginex achieved revenue of HK\$12.12 million and had a net loss of HK\$1.25 million. According to the Diginex’ survey, it can breakeven if the market price of Ethereum price is higher than US\$200. When Ethereum price reaches a year average of US\$640, it is expected the net profit would be US\$40 million in the financial year 2019. Madison expects the acquisition to be completed by July, and we expect that Diginex will bring Madison Holdings a net profit of US\$10 million (HK\$78.5 million) for the financial year 2019.

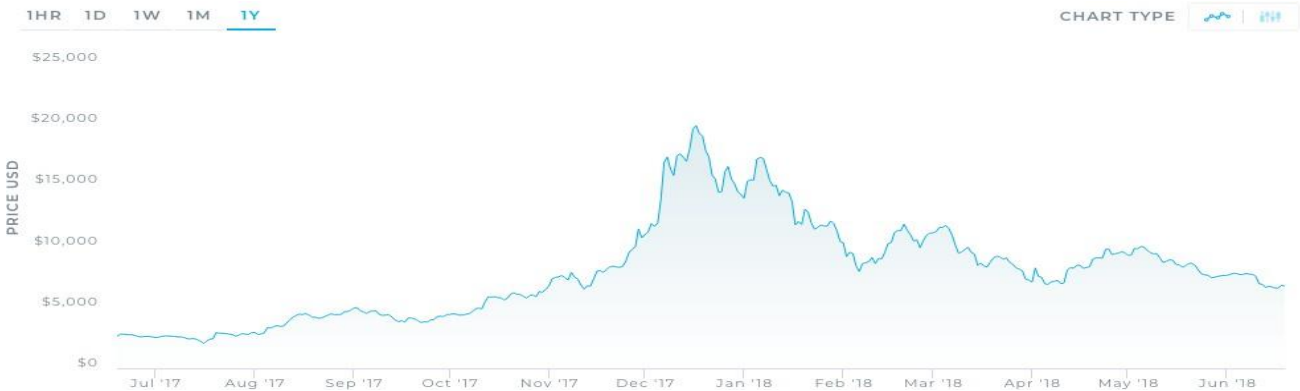
2.3 The acquisition of 100% stake in Three Bear Technologies (The transaction was terminated on June 19, 2018)

On 5 May, 2018, Madison Holdings announced the acquisition of 100% stake in China Shenzhen Three Bear Technology, Inc., for a total consideration of HK\$1.131 billion, of which 20% (HK\$226 million) will be settled by cash, and 80% by issuing new shares at an issue price of HK\$1.8 by installments (accounted for by the allotment and issue of the Consideration Shares after all the enlarged issued share capital of about 11%). The target company is mainly engaged in mobile internet technology and blockchain application software products. The gaming industry are generally plagued by a number of problems, such as uncertain ownership rights of members’ virtual props on the platform, insecure accounts being easily stolen, the operation is less transparency, and difficulty in recovering core data errors. The aforesaid problems have perplexed gaming industry participants of different scale for the long period of time. The target company has strived for various solutions for the aforesaid problems. Recently, the target company has researched, developed and applied blockchain technology in the gaming industry to effectively ensure the security and authenticity of ownership of virtual props, while improving the fairness and playability of games on the platform. The target company, through its research and development process, has accumulated pragmatic blockchain technology and trained up core staff in mastering blockchain technology. Safeguarded by the blockchain technology, the target company is able to provide a fair and transparent entertainment community for its registered members. The target company itself also provides all kind of self-developed mobile games. The target company has 50-60 blockchain technology R&D team, the directors of Madison Holdings consider that Blockchain technology has a potential to become the major underlying technology applicable to financial services industry in the future. Furthermore, the target company is working on to build a cryptocurrency discussion platform for professionals to boost the number of users. As of 31 December 2017, the target company achieved a revenue of HK\$109 million and a net profit of HK\$7.065 million. The purchase price is 16 times of its 2017’s PE. Moreover, the seller guarantees Madison Holdings that the net profit for 2018 fiscal year will be not less than HK\$70 million. The seller and buyer agreed to terminate the acquisition agreement on 19 June 2018. The Board considers to terminate the acquisition agreement is in the interests of Madison Holdings and its shareholders as a whole, and there was no material adverse impact on the existing business or financial position of the Madison Group.

3. Relevant risks

3.1 Volatility risk in cryptocurrency

The changes in policies and regulations on holding, using and mining cryptocurrency may result in high volatility in cryptocurrency price which may greatly impact the profitability of the company. For instance, on 4 September 2017, the People's Bank of China announced that initial coin offering (ICO) is an illegal public financing activity and imposed an immediate ban on all ICO. The price of all major cryptocurrencies plummeted after the announcement.



Source: Blockchain.info

3.2 Liquidity risk and value dilution effect of equity financing

The two recent acquisitions of Madison Holdings involved JPY500 million (equal to HK\$362 million) and US\$60 million (equals to HK\$471 million) where JPY 500million (equals to HK\$362 million) and US\$10 million (equals to HK\$78.5 million) will be settled in cash respectively. The payments will be made upon the completion of the acquisitions in July 2018. Madison Holdings raised HK\$120 million by placing 70.06 million new shares to not less than 6 placees at the price of HK\$1.7 per share in April 2018. The net fund raised from the share placing will be used on acquiring 20% stake of Bitpoint. As of 31 March 2018, Madison Holdings had HK\$43.27 million of cash which was insufficient to complete the acquisitions. This implies that Madison Holdings may seek extra capital by further placing new shares, issuing convertible bonds or other debt financing arrangements. Noteworthy, since the acquisitions would be funded by issuing new shares, the voting rights of the major shareholder would be diluted from 51.85% to 49.27% upon the completion of the acquisitions.

Appendix: Balance Sheet

(In million)	FY2016	FY2017	FY2018
Inventory	41.5	51.4	50.6
Held-for-trading financial assets	-	-	7.0
Trade and other receivables	34.9	47.4	32.9
Tax recoverable	1.2	1.5	0.0
Bank balances and cash	46.4	52.2	43.2
Current assets	124.0	152.5	133.8
Plant and equipment	5.6	7.6	8.0
Exchangeable bonds	-	-	147.1
Deposits	0.6	1.7	2.6
Deferred tax asset	0.3	0.7	0.6
Non-current assets	6.5	10.0	158.3
Trade and other payables	5.1	8.7	15.7
Amount due to a shareholder	-	-	0.2
Loan from a shareholder	-	-	0.8
Convertible bonds	-	-	101.8
Derivative financial instrument	-	-	14.9
Other	0.4	-	-
Current liabilities	5.5	8.7	133.4
Promissory note payable	-	-	11.3
Non-current liability	-	-	11.3
Equity attributable to owners of the Company	124.5	148.7	154.0
Non-controlling interests	0.5	5.5	(6.5)
Total equity	125.0	154.2	147.6
Current ratio	2255%	1753%	100%
Debt/Asset ratio	4%	5%	50%

Income Statement

(In million)	FY2016	FY2017	FY2018
Revenue	126.7	139.6	160.0
Cost of sales	(93.7)	111.6	121.0
Gross profit	33.0	28.0	39.0
Other income	12.7	1.5	0.5
Selling and distribution expenses	(13.5)	(14.4)	(18.1)
Administrative expenses	(39.2)	(31.8)	(47.0)
Net trading loss			(2.0)
Change in fair value of exchangeable bonds			(124.2)
Change in fair value of derivative			5.2
Impairment loss recognised on goodwill			(3.8)
Finance costs			(6.6)
Loss before tax	(7.1)	(16.4)	(157.0)
Income tax (expense) credit	(2.2)	0.4	(0.1)
Loss for the year and total comprehensive expense for the year	(9.3)	16.0	(157.1)
Non-controlling interests	0.1	(0.4)	(18.8)
Profit/ (Loss) attribute to owners of the company	(9.4)	(15.6)	(138.4)

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BUY	Based on a current 12-month view of total shareholder return (change in share price from current price + projected dividend yield), we expect a positive return of over 10%.
HOLD	Based on a current 12-month view of total shareholder return, we expect the return to range between +10% to -10%.
SELL	Based on a current 12-month view of total shareholder return we expect a negative return of over 10%.

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