

Fundamental Research Corp.

Investment Analysis for Intelligent Investors

May 12, 2016

Shoal Games Ltd. (TSXV: SGW / OTCQB: SGLDF) – Q1 Strong / Trophy Bingo Gaining Traction

Sector/Industry: Mobile Games

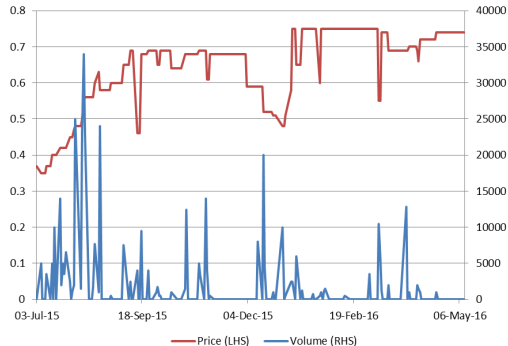
www.shoalgames.com

Market Data (as of May 11, 2016)

| | |
|---------------|-------------------|
| Current Price | C\$0.75 |
| Fair Value | C\$1.60 |
| Rating* | BUY |
| Risk* | 5 (Highly Spec) |
| 52 Week Range | C\$0.35 – C\$0.75 |
| Shares O/S | 57,702,303 |
| Market Cap | C\$43.28 mm |
| Current Yield | N/A |
| P/E (forward) | N/A |
| P/B | N/A |
| YoY Return | N/A |
| YoY TSXV | -23.1% |

*see back of report for rating and risk definitions

*All the figures are in US\$ unless otherwise specified.



Highlights

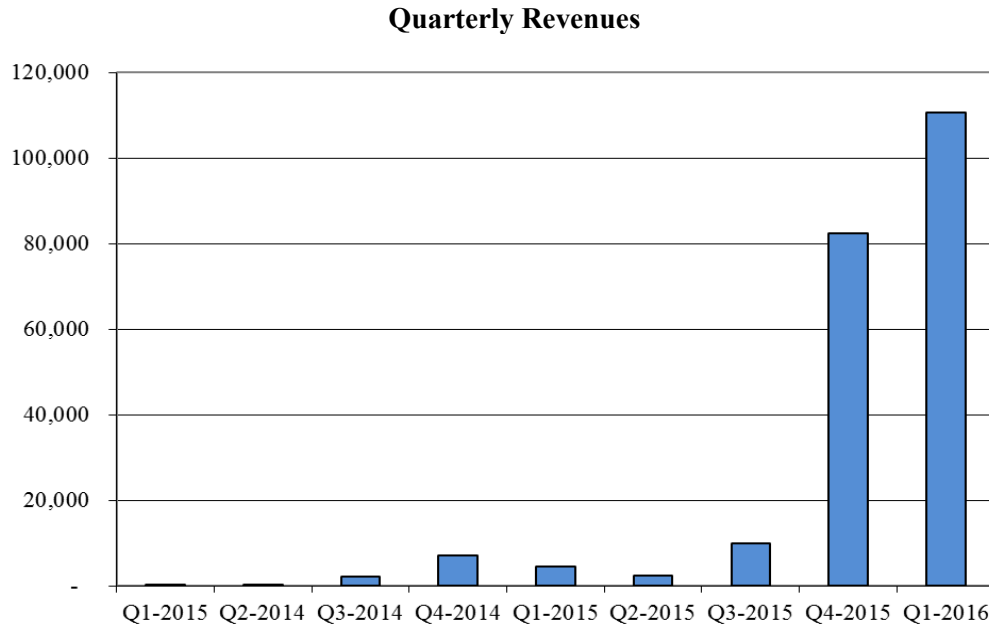
- Shoal Games Ltd. (“company”, “Shoal”, “SGW”) reported strong results in Q1-2016 (quarter ended March 31, 2016) this Monday.
- In Q1-2016, revenues grew by 34% QOQ to \$110,559, up from \$82,540 in Q4-2015. The full launch of Trophy Bingo was in Q3-2015.
- All of the Key Performance Indicators (“KPIs”) showed strong improvements. Daily Active Users (“DAUs”) increased from 13,870 in Q4-2015, to 18,122 in Q1-2016. The Monthly Gross Average Bookings per Paying User (“MGABPPU”) increased QOQ from \$17.51 to \$22.38. Player acquisition cost also dropped QOQ. All these metrics, we believe, clearly indicate that Trophy Bingo is gaining traction.
- In April 2016, the company announced that it has secured brand rights to produce Garfield Bingo. This deal allows Shoal to launch a new bingo game, using the same platform as Trophy Bingo, and capture the attention of the 17 million Facebook fans of Garfield. We believe this is a very pragmatic strategy as it allows the company to capture a wide range of players with two games. Management estimates the new Garfield Bingo game will be launched in late 2016.
- Shoal recently announced that it has closed the first tranche of a C\$2 million financing by issuing 1.50 million units for gross proceeds of C\$0.90 million. Management expects to close the second tranche by the end of May, followed by a rights offering in June.
- We reiterate, the company has a strong management team, led by Mr. T.M. (Tarrnie)Williams – Ex President and CEO of Electronic Arts (Canada) Inc. (Nasdaq: EA). Shoal is the only publicly listed micro/small company in Canada offering investors the opportunity to participate in the growing mobile games market in the social casino segment.

Key Financial Data (FYE - Dec 31)

| (US\$) | 2015 | 2016E | 2017E |
|--------------------|-------------|-------------|-----------|
| Cash | 570,086 | 988,225 | 2,171,557 |
| Working Capital | 454,447 | 779,636 | 2,527,867 |
| Total Assets | 1,129,526 | 1,155,664 | 3,020,179 |
| LT Debt to Capital | 0.0% | 0.0% | 0.0% |
| Revenues | 111,521 | 1,739,955 | 6,930,438 |
| Net Income | (2,965,307) | (2,015,613) | 1,748,717 |
| EPS | -0.05 | -0.03 | 0.03 |

Key Performance Indicators

In Q1-2016, Trophy Bingo’s revenues were \$110,559, up from \$82,540 in Q4-2015, and \$9,914 in Q3-2015. The following chart shows the company’s revenues since Trophy Bingo’s launch.



Trophy Bingo has been downloaded over 440,000 times from the Apple iOS and Google Play app stores, up from 325,000 times at the time of our initiating report in March 2016.

All of the key KPIs improved QOQ in Q1-2016, as shown in the chart below.



Source: Company

- DAUs increased from 13,870 in Q4 to 18,122 in Q1-2016
- Monthly Gross Average Bookings per Paying User (“MGABPPU”) increased QOQ from \$17.51 to \$22.38.
- Effective cost per install (“eCPI”) decreased from \$1.54 to \$0.96. Management’s goal is to bring this cost down to \$0.80 by December 2016, and to \$0.60 by December 2017.

**Development
Plans**

The company's key areas of focus at this time are the following:

- Deliver content & feature expansions
- Release social & viral feature set (Q1 release)
- Release 20 new levels every month (commencing in Q2)
- Develop tools for build-your-own content (Q3 release)
- Develop innovative multi-player game play (Q3 release)

By achieving the milestones above, Shoal believes they will be able to:

- Increase the average ARPDau by 100% by December 2017.
- Increase long-term player retention beyond 180 days.
- Increase LTV by 100% – 200%
- Reduce UAC by 50% through increased virality by December 2017.
- Significantly increase the number of DAUs from the current 18,000 to 140,000+ by December 31, 2016.
- Start paying dividends to investors upon achieving profitability.

**Secures brand
rights to
produce
Garfield Bingo**

On April 18, 2016, Shoal announced that it licensed the rights to Garfield, the iconic cartoon cat and the protagonist of the Garfield comic strips. Paws Inc. is the sole owner of the copyrights and trademarks of Garfield.

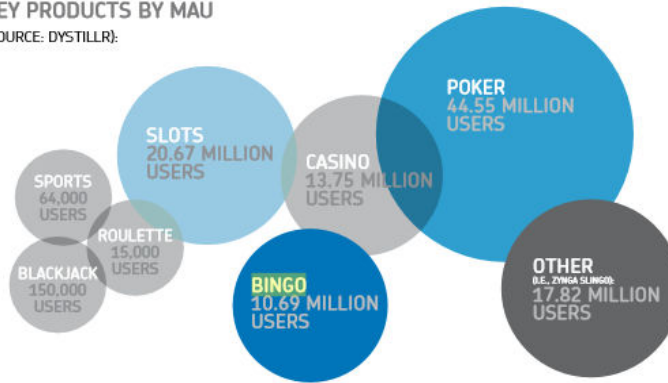
This deal allows Shoal Games to launch a mobile game that will feature Garfield and the rest of the famous Garfield cast. **Shoal estimates that the new Garfield Bingo game will be launched in late 2016.** According to management, the game will instantly appeal and capture the attention of the 17 million Facebook fans of Garfield. As a result, management expects a much lower player acquisition cost for the new game. They estimate that Garfield mobile apps have generated over 30 million downloads since inception.

As per the company's press release, Paws Inc. the VP Digital Marketing of Paws Inc. commented that *"We chose Shoal Games to be the developer of Garfield Bingo because of their success with Trophy Bingo and commitment to quality software development and unique game design."* **This is a very encouraging sign and is a testament to the quality of Shoal's team.**

**Review of the
Bingo Gaming
Market**

The social bingo market is estimated to have approximately 11 million MAUs. **The market is currently dominated by two games – Bingo Bash and Bingo Blitz, each with more than 1 million DAUs, and 4.5 million MAUs.** These two games, we estimate, account for over 90% of the total market.

KEY PRODUCTS BY MAU
(SOURCE: DYSTILLR):



PAYVISION

Caesars Interactive Entertainment (Nasdaq: CZR) acquired Buffalo Studios (owner of Bingo Blitz) for approximately \$53 million in December 2012. GSN Games acquired Bash Gaming (owner of Bingo Bash) for approximately \$160 million in 2014. GSN Games is a joint venture between Sony (NYSE: SNE) and AT&T Inc. (NYSE: T). **Using the estimates of 11 million MAUs and 3.5 million DAUs, we estimate the social bingo market is worth approximately \$150 million per annum.**

Shoal’s plan with Trophy Bingo is to offer an innovative product that engages bingo players in new and challenging ways. Management’s objective is to attract users by offering an innovative new type of bingo game that is fun, challenging, and most importantly, requires players to act strategically to win. Management believes that these traits will allow them to attract players away from Bingo Bash and Bingo Blitz, which are built in a more traditional format and are becoming dated (both launched in 2010). Market research firm, Newzoo indicates that social casino gamers play an average of 5.6 titles in a genre. Given the advanced marketing techniques, and the narrow demographic profile of bingo players, we believe, the company will be able to target the players of other social bingo games (including Bash & Blitz) with precision.

Trophy Bingo is a 120-level puppy themed social bingo game. The game is free to download and generates revenue when players make in-app purchases and through advertisements.



Shoal’s team is currently focussed on enhancing game play, expanding content, and delivering innovative game modes so that players will become immersed in Trophy Bingo. The game is currently live in three languages – English, Spanish and French. Management plans to add Swedish, Dutch, Portuguese, and Italian once the content plans for Trophy Bingo are completed in the third quarter of 2016.

Q1-2016 Performance

In Q1-2016, the company’s revenues, net of fees to Google (GOOGL), Apple (AAPL) and Amazon (AMZN), were \$110,559, up by 34% QOQ. EBITDA was -\$0.63 million in Q1-2016 versus -\$0.70 million in Q1-2015. Operating expenses were \$0.62 million in Q1. Management estimates operating expenses to be approximately \$4 million in 2016 (subject to the availability of capital), which includes \$1.7 million in marketing (player acquisition) costs.

The net loss in Q1-2016 was \$0.63 million (EPS: -\$0.01) versus \$0.72 million (EPS: -\$0.01) in Q1-2015.

The following table shows a summary of the company's cash flows. Free cash flows were -\$0.42 million in Q1-2016 versus -\$0.62 million in Q1-2015.

| Summary of Cash Flows | 2015 (3M) | 2016 (3M) |
|----------------------------|------------------|------------------|
| Cash Flows from Operations | (617,330) | (418,389) |
| Cash Flows from Investing | (272) | - |
| Cash Flows from Financing | - | - |
| Net Change | (617,602) | (418,389) |
| Free Cash Flows | (617,602) | (418,389) |

At the end of Q1-2016, the company had \$0.15 million in cash, with no debt. Working capital and the current ratio were -\$0.06 million, and 0.8x, respectively.

| Liquidity Analysis | 2015 | Q1-2016 |
|--------------------|-----------|-----------|
| Cash | \$570,086 | \$151,697 |
| Working Capital | \$454,447 | -\$59,042 |
| Current Ratio | 3.56 | 0.79 |
| Debt / Capital | 0.0% | 0.0% |
| LT Debt / Capital | 0.0% | 0.0% |

Financing – The company is currently pursuing a C\$2 million private placement by issuing up to 3.33 million common shares at C\$0.60 per share. Upon completing this financing, the company plans to pursue a rights offering to holders of the common shares, wherein shareholders will receive one right for each common share held. Ten rights will entitle the shareholder to purchase one common share at a specified exercise price within a fixed time period. The time period and pricing will be announced by the company within one month of closing of the current financing. The rights are expected to be listed on the TSX Venture Exchange. To further sweeten the offering to investors, shareholders who exercise all their rights will have the option to purchase additional shares at the same price without requiring the purchase of additional rights.

On May 5, 2016, the company announced that it has closed the first tranche by issuing 1.50 million units for gross proceeds of C\$0.90 million. Management expects to close the second tranche by the end of May, followed by the rights offering in June.

Stock options and warrants: At the end of 2015, the company had no options or warrants outstanding.

As the company’s marketing budget and user acquisition strategy are contingent on the proposed financings, to be conservative, we have slightly adjusted downwards our near-term EPS estimates as shown below. As a result, our Discounted Cash Flow valuation dropped slightly from C\$1.60 to C\$1.56 per share.

Valuation

| STATEMENTS OF OPERATIONS | | | | | | |
|------------------------------------|-------------------|-------------------|------------------|-------------------|-------------------|-------------------|
| (in US\$)- YE Dec 31st | 2015 | 2016E | 2017E | 2018E | 2019E | 2020E |
| Net Revenues | 111,521 | 1,739,955 | 6,930,438 | 15,234,188 | 24,687,688 | 34,013,438 |
| Cost of Sales | 482,012 | 482,013 | | | | |
| Gross Profit | -370,491 | 1,257,942 | 6,930,438 | 15,234,188 | 24,687,688 | 34,013,438 |
| Expenses | | | | | | |
| Selling & Marketing | 549,726 | 1,188,828 | 2,138,723 | 4,403,253 | 6,667,783 | 8,932,313 |
| Trophy Bingo development | 1,230,216 | 1,086,915 | 1,195,607 | 1,315,167 | 1,446,684 | 1,591,352 |
| Compensation & Consulation | 438,572 | 548,215 | 603,037 | 663,340 | 729,674 | 802,642 |
| G & A | 356,647 | 445,809 | 490,390 | 539,429 | 593,371 | 652,709 |
| EBITDA | -2,945,652 | -2,011,824 | 2,502,682 | 8,312,999 | 15,250,175 | 22,034,422 |
| Amortization | 3,467 | 3,788 | 4,515 | 4,806 | 4,922 | 4,969 |
| EBIT | -2,949,119 | -2,015,613 | 2,498,167 | 8,308,192 | 15,245,252 | 22,029,453 |
| Interest & Bank Charges | 1,089 | | | | | |
| Exchange rate and Unusual items | -33,582 | | | | | |
| EBT | -2,981,612 | -2,015,613 | 2,498,167 | 8,308,192 | 15,245,252 | 22,029,453 |
| Gain from sale of domain name | 16,305 | | | | | |
| Income Taxes | | - | 749,450 | 2,492,458 | 4,573,576 | 6,608,836 |
| Net Earnings for the period | -2,965,307 | -2,015,613 | 1,748,717 | 5,815,735 | 10,671,677 | 15,420,617 |
| EPS | -0.05 | -0.03 | 0.03 | 0.10 | 0.18 | 0.26 |

We reiterate our BUY rating and maintain our fair value estimate at C\$1.60 per share.

Risks

The following risks, though not exhaustive, may cause our estimates to differ from actual results:

- The social games sector is highly competitive. There are over one million apps each available on both the App Store and Google Play stores.
- The social bingo gaming market is currently dominated by two established players.
- Keeping players engaged is critical and requires continuous development and innovation.
- Trophy Bingo is in its early stages and has yet to start to generate significant revenues.
- The company may have to pursue equity financings, which may dilute existing shareholders.
- The social games sector is not subject to any material regulations. Any unfavorable changes in regulations in the future may impact the company’s business.
- Management and insiders own 81% of the outstanding shares. Therefore, the liquidity and the average daily trading volume of SGW’s shares are low at this time.

We assign a risk rating of 5 (Highly Speculative).

APPENDIX

| STATEMENTS OF OPERATIONS | | | | | | |
|------------------------------------|-------------------|-------------------|------------------|-------------------|-------------------|-------------------|
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| G & A | 356,647 | 445,809 | 490,390 | 539,429 | 593,371 | 652,709 |
| EBITDA | -2,945,652 | -2,011,824 | 2,502,682 | 8,312,999 | 15,250,175 | 22,034,422 |
| Amortization | 3,467 | 3,788 | 4,515 | 4,806 | 4,922 | 4,969 |
| EBIT | -2,949,119 | -2,015,613 | 2,498,167 | 8,308,192 | 15,245,252 | 22,029,453 |
| Interest & Bank Charges | 1,089 | | | | | |
| Exchange rate and Unusual items | -33,582 | | | | | |
| EBT | -2,981,612 | -2,015,613 | 2,498,167 | 8,308,192 | 15,245,252 | 22,029,453 |
| Gain from sale of domain name | 16,305 | | | | | |
| Income Taxes | | - | 749,450 | 2,492,458 | 4,573,576 | 6,608,836 |
| Net Earnings for the period | -2,965,307 | -2,015,613 | 1,748,717 | 5,815,735 | 10,671,677 | 15,420,617 |
| EPS | -0.05 | -0.03 | 0.03 | 0.10 | 0.18 | 0.26 |

| BALANCE SHEET | | | | | | |
|---|------------------|------------------|------------------|------------------|-------------------|-------------------|
| (in US\$)- YE Dec 31st | 2015 | 2016E | 2017E | 2018E | 2019E | 2020E |
| Assets | | | | | | |
| Cash | 570,086 | 988,225 | 2,171,557 | 7,239,991 | 17,028,802 | 31,584,448 |
| Accounts receivable | 44,948 | 125,794 | 693,044 | 1,523,419 | 2,468,769 | 3,401,344 |
| Prepaid expenses | 17,205 | 25,159 | 138,609 | 304,684 | 493,754 | 680,269 |
| Current Assets | 632,239 | 1,139,178 | 3,003,209 | 9,068,093 | 19,991,325 | 35,666,061 |
| Property and equipment | 6,314 | 7,526 | 8,010 | 8,204 | 8,282 | 8,313 |
| Other Assets | 482,013 | - | - | - | - | - |
| Security Deposits | 8,960 | 8,960 | 8,960 | 8,960 | 8,960 | 8,960 |
| Total Assets | 1,129,526 | 1,155,664 | 3,020,179 | 9,085,257 | 20,008,566 | 35,683,333 |
| Liabilities & Shareholders' Equity | | | | | | |
| Accounts payables & accrued liabilities | 145,226 | 326,977 | 442,776 | 692,119 | 943,751 | 1,197,902 |
| Related parties | 32,566 | 32,566 | 32,566 | 32,566 | 32,566 | 32,566 |
| Current Liabilities | 177,792 | 359,543 | 475,342 | 724,685 | 976,317 | 1,230,468 |
| Loans payable | | | | | | |
| Shareholder's Equity | | | | | | |
| Share Capital | 19,334,290 | 21,194,290 | 21,194,290 | 21,194,290 | 21,194,290 | 21,194,290 |
| Foreign Currency Translation | 24,580 | 24,580 | 24,580 | 24,580 | 24,580 | 24,580 |
| Deficit | -18,407,136 | -20,422,749 | -18,674,032 | -12,858,298 | -2,186,621 | 13,233,996 |
| Total Liabilities & Shareholders' Equity | 1,129,526 | 1,155,664 | 3,020,179 | 9,085,257 | 20,008,566 | 35,683,333 |

| STATEMENTS OF CASH FLOWS | | | | | | |
|--|-------------------|-------------------|------------------|------------------|-------------------|-------------------|
| (in US\$)- YE Dec 31st | 2015 | 2016E | 2017E | 2018E | 2019E | 2020E |
| Operating Activities | | | | | | |
| Net earnings for the period | -2,965,787 | -2,015,613 | 1,748,717 | 5,815,735 | 10,671,677 | 15,420,617 |
| Items not involving cash | | | | | | |
| Depreciation | 3,467 | 3,788 | 4,515 | 4,806 | 4,922 | 4,969 |
| Trophy Bingo Amortization | 482,012 | 482,013 | | | | |
| Gain on sale of domain name | -16,305 | | | | | |
| | -2,496,613 | -1,529,811 | 1,753,232 | 5,820,541 | 10,676,599 | 15,425,586 |
| Accounts Receivable | 77,213 | -80,846 | -567,250 | -830,375 | -945,350 | -932,575 |
| Other Assets | 1,682 | | | | | |
| Prepaid Expenses | -2,838 | -7,954 | -113,450 | -166,075 | -189,070 | -186,515 |
| Accounts payable and accrued expenses | 37,518 | 181,751 | 115,799 | 249,343 | 251,632 | 254,150 |
| Changes in working capital | 113,575 | 92,951 | -564,901 | -747,107 | -882,788 | -864,940 |
| Cash from (used in) operations | -2,383,038 | -1,436,861 | 1,188,331 | 5,073,434 | 9,793,811 | 14,560,646 |
| Financing activities | | | | | | |
| Private Placement | | 1,860,000 | | | | |
| Exercise of Stock Options | 77,250 | | | | | |
| Cash provided by financing activities | 77,250 | 1,860,000 | - | - | - | - |
| Investing activities | | | | | | |
| Acquisition of Equipment | -512 | -5,000 | -5,000 | -5,000 | -5,000 | -5,000 |
| Cash used in investing activities | -512 | -5,000 | -5,000 | -5,000 | -5,000 | -5,000 |
| Increase (decrease) in cash | -2,306,300 | 418,139 | 1,183,331 | 5,068,434 | 9,788,811 | 14,555,646 |
| Cash beginning of period | 2,876,386 | 570,086 | 988,225 | 2,171,557 | 7,239,991 | 17,028,802 |
| Cash end of period | 570,086 | 988,225 | 2,171,557 | 7,239,991 | 17,028,802 | 31,584,448 |

Fundamental Research Corp. Equity Rating Scale:

Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk

Hold – Annual expected rate of return is between 5% and 12%

Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk

Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

Fundamental Research Corp. Risk Rating Scale:

1 (Low Risk) - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company’s capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.

Disclaimers and Disclosure

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