Zacks Small-Cap Research

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Tapinator, Inc. (TAPM-OTC)

TAPM: 2Q15 Results Driven by Expanding Games Portfolio and Strong User Metrics

Current Recommendation	**Buy**
Prior Recommendation Date of Last Change	07/9/2015
Current Price (8/26/15)	$0.54
Target Price	**$0.65**

OUTLOOK

Tapinator's user metrics reflect rising traction with gamers, we believe. Cumulative downloads reached roughly 97M at the end of 2Q15, up roughly 50% from 65M at the end of 1Q15. The company's games had 47M average daily active users at 2Q15, which represents a 236% y/y improvement and 75% sequential advance. Average monthly active users of 7.73M increased 188% compared to 2Q14 and 68% compared to 1Q15.

SUMMARY DATA

52-Week High	**$2.20**
52-Week Low	**$0.15**
One-Year Return (%)	**N/A**
Beta	**-0.71**
Average Daily Volume (sh)	**83,514**
Common Shares Out (mil)	**56.9**
Market Capitalization ($mil)	**$31**
Short Interest Ratio (days)	**0.4**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**50**
Annual Cash Dividend	**N/A**
Dividend Yield (%)	**N/A**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2015 Estimate	**N/A**
P/E using 2016 Estimate	**N/A**

Risk Level	**High**
Type of Stock	**Small-Growth**
Industry	**Software/ Gaming**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013					0.1 A
2014	0.1 A	0.2 A	0.3 A	0.4 A	0.9 A
2015	0.4 A	0.6 A	0.7 E	0.8 E	2.6 E
2016					4.1 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013					-$0.00 A
2014	-$0.00 A	$0.00 A	$0.00 A	-$0.00 A	$0.00 A
2015	$0.00 A	-$0.09 A	-$0.08 E	$0.00 E	-$0.17 E
2016					$0.00 E

Quarters might not sum reflecting rounding, share count changes

Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

Disclosures begin on page 9

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KEY POINTS

- Last week, Tapinator reported 2Q15 revenue of $615,358, up 172% compared to 2Q14 and 49% compared to 1Q15, reflecting the company's expanding portfolio of both rapid-launch and full-featured games. On the higher revenue base, the company generated adjusted EBITDA of $187,591 versus $111,675 registered in 1Q15 and $12,589 registered in 2Q14.

- As a result of a $2.0 million note issuance, Tapinator's cash balance was $1.85 million at June 30, 2015 compared to $121,740 at December 31, 2014. This gives the company greater financial flexibility, we believe, as it continues to invest in new game development. The company introduced 19 new games during the quarter, bringing its portfolio to 112 titles that, in the aggregate, have achieved over 100 million downloads.

- Tapinator's rising traction with gamers is reflected in its user metrics, we believe. Cumulative downloads reached roughly 97 million at the end of 2Q15, up roughly 50% from 65 million at the end of 1Q15. The company's games had 47 million average daily active users at 2Q15, which represents a 236% year-over-year improvement and 75% sequential advance. Average monthly active users of 7.73 million increased 188% compared to 2Q14 and 68% compared to 1Q15.

- The company is optimistic about its licensed IP and franchise opportunities. Management believes that *Dice Mage* and *Combo Quest* both have franchise potential. With the update of *Deadliest Catch* to version 1.1, the game – which has been featured as a *Best New Game* on iOS – has expanded to the Android platform and Kindle devices. In addition to *Deadliest Catch*, Tapinator intends to develop a game based on a well-known movie franchise slated for 2Q16 release.

2Q15 RESULTS

Last week, Tapinator (OTC:TAPM) reported 2Q15 financial results. Revenue of $615,358 advanced 172% compared to 2Q14 and 49% compared to 1Q15, reflecting the company's expanding portfolio of both rapid-launch and full-featured games. On the higher revenue base, the company generated adjusted EBITDA of $187,591 versus $111,675 registered in 1Q15 and $12,589 registered in 2Q14. This represents a nearly 15-fold year-over-year increase and 68% sequential advance. The company attributes the significant improvement in adjusted EBITDA primarily to operating leverage, as it scales and grows its business.

Tapinator recorded an operating loss of $143,319 for 2Q15 versus operating income of $12,399 generated in 2Q14. This swing to an operating loss primarily reflects increased amortization of capitalized software costs.

Tapinator recorded a net loss of $4,993,561 for 2Q15, which included a $4,694,571 non-cash charge related to the mark-to-market of the company's derivative liability, as well as the above-noted increase in amortization of capitalized software costs. Tapinator registered net income of $12,399 in the same period of 2014. We have revised our 2015 forecast to reflect year-to-date trends. We have also raised our price target to $0.65. This equates to a lofty roughly 8.8x our 2016 revenue forecast, which we believe is attainable at this early stage of the company's development, given its anticipated continued growth. TAPM shares are trading above our prior $0.30 price target.

Liquidity and Balance Sheet

At the end of 1Q15, Tapinator had cash and equivalents of $70,753. In 2Q15, the company raised $2.0 million through the issuance of a $2.24 million 8% senior convertible note due January 1, 2017, with five-year warrants to purchase 10.9 million shares and five-year callable warrants to purchase 10.9 million shares. The company used a portion of the capital to eliminate debt. As a result of this financing, Tapinator's cash balance was $1.85 million at June 30, 2015 compared to $121,740 at December 31, 2014.

GROWING PORTFOLIO OF GAMES; IMPROVING PLAYER METRICS

Tapinator continues to invest in new game development. The company introduced 19 new games during the quarter, bringing its owned and operated portfolio to 112 mobile gaming titles. In the aggregate, these games have achieved over 100 million cumulative downloads to-date. At the end of 2Q15, 20 titles had reached the one million download mark, up from 15 at the end of 1Q15.

A number of titles have ranked at the top of the mobile leaderboard charts and have been featured by the Apple, Google, and Amazon App Stores. The company strives to release one to two new Rapid Launch games every week. Its business model on its Rapid Launch games is to make the games free-to-play to gamers and monetize them primarily through advertising. To minimize disruption to players, ads occur between levels as players move up in the game and when the game ends. Users can also purchase new levels of play in order to progress within the game, which represents another revenue source.

Expanding Full-Featured Games Portfolio; Growing Focus on Franchise, In-App Purchases

In addition to Rapid Launch mass-appeal games, Tapinator also offers original, full-featured premium games. Management’s strategy with regard to full-featured titles is to focus on those that it believes have franchise potential. With Full Featured games, Tapinator relies primarily on in-app purchases. Tapinator continues to expand its full-featured game portfolio, adding two new games during summer 2015 and updating three others. By the end of 2Q15, the company had four full-featured titles that had been designated as *Best New Games* on iOS.

Key Summer 2015 Full-Featured Game Launches or Upgrades

Title	Version
Rotatio	1.0
Dice Mage	1.0
Combo Quest	1.2
Video Poker VIP	2.0
Deadliest Catch: Seas of Fury	1.1

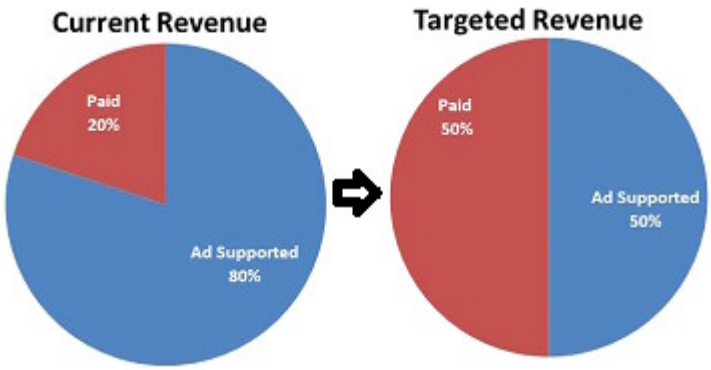
Source: Company reports

The company introduced two new full featured games in summer 2015: *Rotatio* and *Dice Mage*. This week, Tapinator announced that *Dice Mage* has been featured as a *Best New Game* on Apple's iOS platform and has climbed to the #2 position in Free Dice games within the leaderboards, ranking among the top-10 grossing dice games.

In addition, the company also updated *Combo Quest, Video Poker* and *Deadliest Catch*. The company believes that *Dice Mage* and *Combo Quest* both have franchise potential. The *Combo Quest* update was designed to expand the game's appeal in international markets by adding localization support for Spanish, French, Italian, and German. The latest version of *Combo Quest* was featured as a *Best New Game Update* earlier this month, which marks the third time that the title has been featured in the App Store. Tapinator added several new in-app purchase opportunities with the latest *Combo Quest* entry.

Historically, most social games have been free-to-play, generating revenue through in-game sales of virtual goods, according to VentureBeat. In general, free-to-play games tend to attract a wider audience of players who, in turn, could potentially be converted to paying users through purchases of in-app virtual goods or by paying to progress to more challenging game levels. The worldwide market for sales of virtual goods was estimated at roughly $15 billion in 2014, according to market research provider In-Stat.

Until recently, the company had been almost exclusively focused on free-to-play mobile games, with roughly 80% of the games have historically been ad supported free-to-play, with the other roughly 20% monetized through in-app purchases. In the early days of mobile gaming, players had gravitated more heavily toward free-to-play games. However, with the increase in time spent on mobile games, consumers' willingness to spend on mobile games has also increased. With the market shift towards in-app purchases, the company hopes to transition its revenue mix over the next 12-24 months from 80% advertising to 50% advertising and 50% micro transactions.



Source: Company reports

Licensed and Social Games

Towards this goal, Tapinator's business model has also recently expanded to include a greater focus on licensed game titles that leverage well-known brands. Management believes the successful launch of two recent celebrity games – *Nik Wallenda in Sky Balance* and *Melissa Etheridge* in a song-based game – support its decision to pursue this strategy. The *Nik Wallenda* game was released in November 2014 to coincide with a special broadcast on the Discovery Channel.

Tapinator has also released a game inspired by Discovery's show *Deadliest Catch.* The show portrays the difficulties and adventures of the captains and crews of four crab-fishing ships on the Bering Sea. The company is optimistic about the prospects for this title, particularly given the marketing support that the game will receive from Discovery and the popularity of the *Deadliest Catch* show itself, which has been renewed for the upcoming 2016 television season.

The *Deadliest Catch: Seas of Fury*™ game allows players to simulate the experience through 20 levels of consecutive difficulty. Compared to original IP titles, the company believes the existing brand awareness of a licensed game enables lower gamer acquisition costs and will allow the company to accelerate its user installations. The company is also optimistic that the game will monetize at better rates than its proprietary non-branded genres. With the update to version 1.1, the company expanded *Deadliest Catch: Seas of Fury* – which has been featured as a *Best New Game* on iOS – to the Android platform and Kindle devices.

The company is also optimistic about other licensed IP opportunities. In addition to *Deadliest Catch*, Tapinator intends to develop a game based on a well-known movie franchise. This title is slated for 2Q16 release.

Growing Focus on Social Casino Gaming

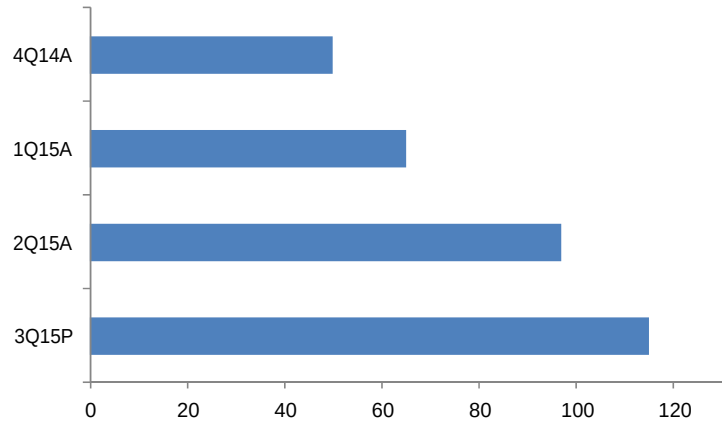
Another way Tapinator hopes to shift its revenue mix is through its recent decision to enter the social casino gaming niche. Social casino games are casino-style games such as blackjack, poker, slots and others that monetize through virtual currency purchases instead of real money payouts, according to VentureBeat. Social casino games generate over $2.5 billion annually, with the lion's share of revenue from mobile users. There is some concern that the social casino gaming market has matured and that growth has slowed, although Tapinator believes that video poker is less competitive than other social casino categories on mobile platforms and represents a strong growth opportunity.

In May 2015, Tapinator launched its first social casino game, *Video Poker VIP*, on the iOS platform for iPads. *Video Poker VIP* combines popular video poker gameplay with mobile slot machine-like mechanics, according to management. The company intends to broaden *Video Poker VIP* distribution to the iPhone, Google Play and the Amazon Appstore. The company recently introduced *Video Poker VIP* version 2.0, expanding the game to the iPhone platform. Based on initial player retention metrics, user feedback from the game and monetization thus far, the company is optimistic about its prospects.

Rising User Metrics

Tapinator's rising traction with gamers is reflected in its user metrics and growing base of user downloads, we believe. Tapinator's cumulative downloads had reached roughly 97 million at the end of 2Q15, up approximately 50% from 65 million at the end of 1Q15.

Tapinator - Growing Installations



Source: Company reports

The company also announced that its games had 47 million average daily active users at 2Q15, which represents a 236% year-over-year improvement and 75% sequential advance. Average monthly active users of 7.73 million increased 188% compared to 2Q14 and 68% compared to 1Q15.

Tapinator Player & Game Metrics

	Metric	Y/Y %Chg	Q/Q %Chg
Average DAUs	47	236%	75%
Average MAUs	7.73	188%	68%
Average New Daily Downloads	0.35	268%	139%
Cumulative Downloads*	96.91	298%	50%
Cumulative Game Library Titles*	112	180%	20%

Metrics millions except game library *As of June 30, 2015
DAUs Daily active users MAUs Monthly active users
Source: Company reports

RECENT NEWS

On May 12, 2015, the company announced the planned release of its *Deadliest Catch* game based on a license with Discovery Communications (DISCA-not rated).

Tapinator launched its first social casino game, *Video Poker VIP,* on May 7, 2015.

On July 23, 2015, Tapinator unveiled its slate of full-featured summer 2015 games.

Tapinator announced that its games portfolio had reached 100 million users on July 28, 2015.

The company announced the results for its second quarter of 2015 on August 20, 2015.

Tapinator launched its *Dice Mage* role-playing game on August 25, 2015.

RISKS

- TAPM is not cash flow positive and may need to seek additional short-term funding that could dilute shareholders.
- Competition continues to increase, which could make it difficult for TAPM to execute its growth strategy.
- Industry spending on player acquisitions and marketing could push Tapinator to increase its spending, as well, which could have a negative impact on the company's results and cash position.
- The company is not fully reporting.
- The social casino gaming sector could prove more competitive and difficult to penetrate than management anticipates.

PROJECTED INCOME STATEMENT AND BALANCE SHEET

Tapinator, Inc. Income Statement & Projections ($)

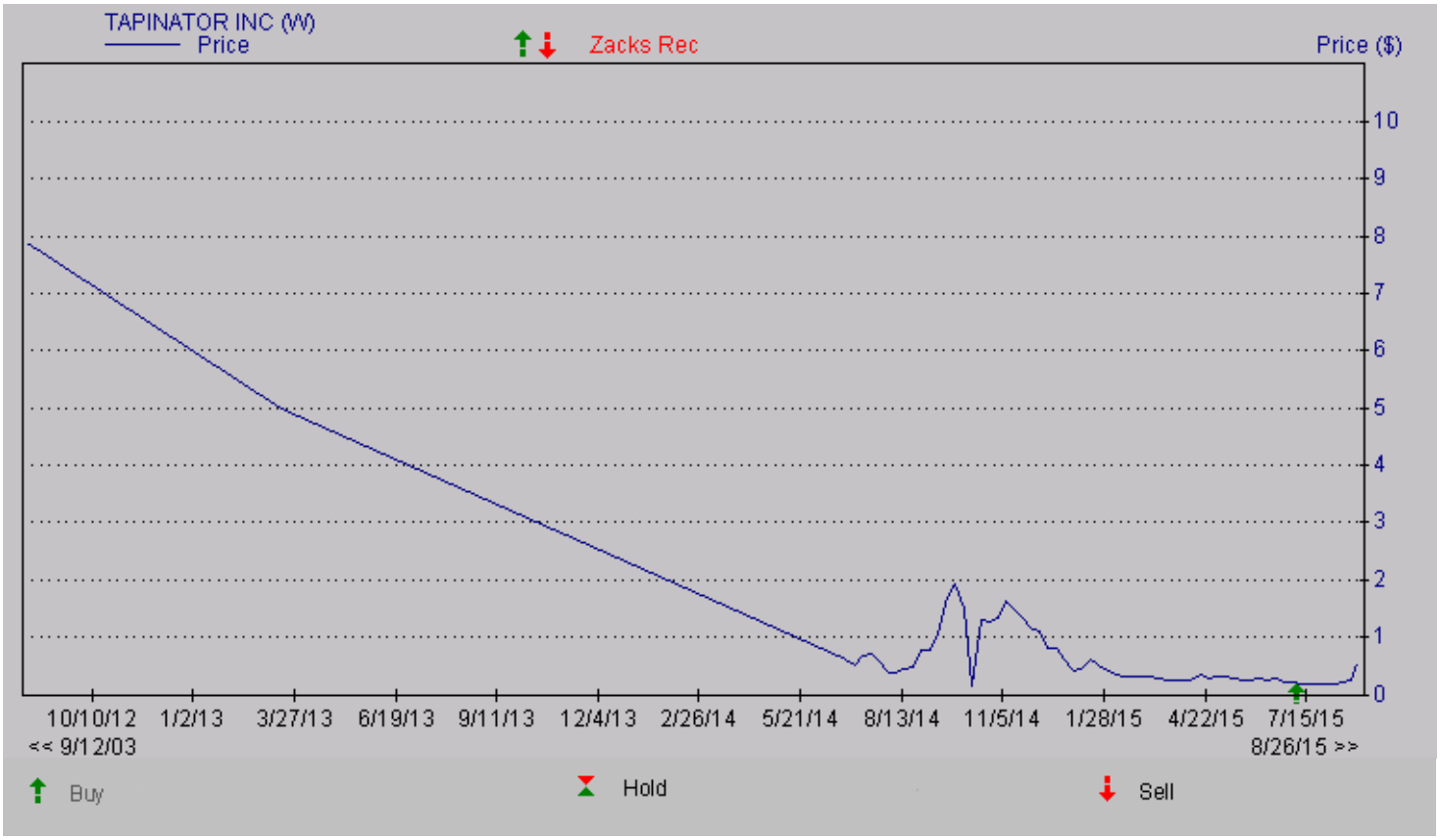
	1Q14	2Q14	3Q14	4Q14	2014	1Q15A	2Q15A	3Q15E	4Q15E	2015E
Revenue	$95,984	$226,320	$250,339	$370,806	$943,449	$411,883	615,358	$725,983	$815,773	$2,568,997
Expenses										
Platform fees	28,763	67,736	73,322	110,867	280,688	132,000	184,311	217,795	244,732	778,838
R&D	55,300	125,939	79,172	80,754	341,165	91,307	141,543	137,937	154,997	525,784
Marketing							41,795	45,000	50,000	136,795
General and administrative	20,029	20,246	64,009	192,865	297,149	163,836	391,028	394,938	396,913	1,346,715
Total expenses	104,092	213,921	216,503	384,486	919,002	387,143	758,677	795,670	846,642	2,788,132
Operating income (loss)	(8,108)	12,399	33,836	(13,680)	24,447	24,740	(143,319)	(69,687)	(30,869)	(219,135)
Loss on chg derivative liabs							4,694,571	4,000,000	2,000	8,696,571
Debt discount amort							114,146	114,000	114,000	342,146
Interest expense	-			15,941	15,941	15,754	40,899	41,000	41,000	138,653
Pretax income (loss)	(8,108)	12,399	33,836	(29,621)	8,506	8,986	(4,992,935)	(4,224,687)	(187,869)	(9,396,505)
Income taxes	25				614	3,146	626	500	500	4,772
Net income (loss)	(8,133)	12,399	33,836	(29,621)	7,892	5,840	(4,993,561)	(4,225,187)	(188,369)	(9,401,277)
Per share data:										
LPS	($0.00)	$0.00	$0.00	($0.00)	$0.00	$0.00	($0.09)	($0.08)	($0.00)	($0.17)
Avg. shares out	36,700,000	45,874,372	55,498,545	55,570,208	55,641,871	55,819,919	55,285,873	55,285,873	55,285,873	55,419,385

Tapinator, Inc. Consolidated Balance Sheets ($)

	31-Dec-13	30-Jun-14	30-Sep-14	31-Dec-14	31-Mar-15	30-Jun-15
Cash & equivalents	12,418	24,415	213,072	121,740	70,753	1,845,462
Accounts receivable	34,198	139,371	116,366	130,681	137,682	261,934
Prepaid expenses						13,470
Due from related parties	9,790	57,160	117,168	-	-	-
Total current assets	56,406	220,946	446,606	252,421	208,435	2,120,866
Property and equipment	2,158	1,777	1,587	17,500	6,213	7,841
Software development costs	-	3,078	176,954	1,260,865	1,367,249	1,207,045
Capitalized financing costs						108,135
Investments	-	12,500	14,086	19,086	19,086	19,086
Security deposits	5,690	5,800	5,800	19,840	14,040	14,040
Total assets	**64,254**	**244,102**	**645,033**	**1,569,712**	**1,615,023**	**3,477,013**
Accounts payable	9,750	10,535	3,442	6,596	961	4,171
Accrued expenses	7,000			50,329	35,235	-
Due to related parties	25,811	130,107	205,374	129,327	112,273	67,177
Total current liabilities	42,561	140,642	208,816	186,252	148,469	71,348
Notes payable	-	-	-	203,954	281,208	-
Senior convertible debenture						57,253
Derivative liabilities	-	-	-	-	-	6,694,571
Total liabilities	**42,561**	**140,642**	**208,816**	**390,206**	**429,677**	**6,823,172**
Redeemable Preferred Stock				773,499	773,499	-
Total stockholders' equity	21,693	103,459	436,217	406,007	411,847	(3,346,159)
Total liabilities and stockholders'	**64,254**	**244,102**	**645,033**	**1,569,712**	**1,615,023**	**3,477,013**

Source: Company reports, Zacks

HISTORICAL ZACKS RECOMMENDATIONS



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Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters.
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