Zacks Small-Cap Research

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The Pulse Network, Inc. (TPNI-OTCBB)

TPNI: *Shares are a Way to Play the Expanding Digital Marketing Sector*; *Reiterate Buy.*

Current Recommendation	**BUY**
Prior Recommendation	Neutral
Date of Last Change	12/13/2013
Current Price (3/3/14)	$0.08
Target Price	**$0.54**

OUTLOOK

The Pulse Network operates in the rapidly growing digital market space. It is a cloud based platform focused on content marketing and event solutions designed to improve clients' engagement with customers and generate leads for new opportunities. Secular trends are likely to be a positive tailwind for Pulse's growth, in our view, as the internet transforms the way buyers gather information and engage with vendors. The company recently announced that its flagship IMS event was so successful that Pulse would expand it to 10 cities in 2014, which we believe will help to grow the brand and, in turn, boost revenue.

SUMMARY DATA

52-Week High	**$0.60**
52-Week Low	**$0.05**
One-Year Return (%)	**N/A**
Beta	**N/A**
Average Daily Volume (sh)	**114,547**
Shares Outstanding (mil)	**90.7**
Market Capitalization ($mil)	**$7.3**
Short Interest Ratio (days)	**0.02**
Institutional Ownership (%)	**N/A**
Insider Ownership (%)	**91%**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
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 2013 Actual	**N/A**
P/E using 2014 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Business Svcs**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Jun)	Q2 (Sep)	Q3 (Dec)	Q4 (Mar)	Year (Mar)
2012					4.2A
2013	1.0A	0.7A	1.5A	0.6E	3.8A
2014	0.9A	0.6A	1.0A	1.0E	3.6E
2015					4.1E

FY ends March 31.

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

	Q1 (Jun)	Q2 (Sep)	Q3 (Dec)	Q4 (Mar)	Year (Mar)
2012					-$0.41A
2013	-$0.00A	-$0.00A	-$0.00A	-$0.01E	-$1.55A
2014	-$0.00A	-$0.01A	-$0.00A	-$0.00E	-$0.01E
2015					-$0.02E

Disclosures begin on page 8

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

* Quarters may not = annual due to shr count chgs /rounding

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KEY POINTS

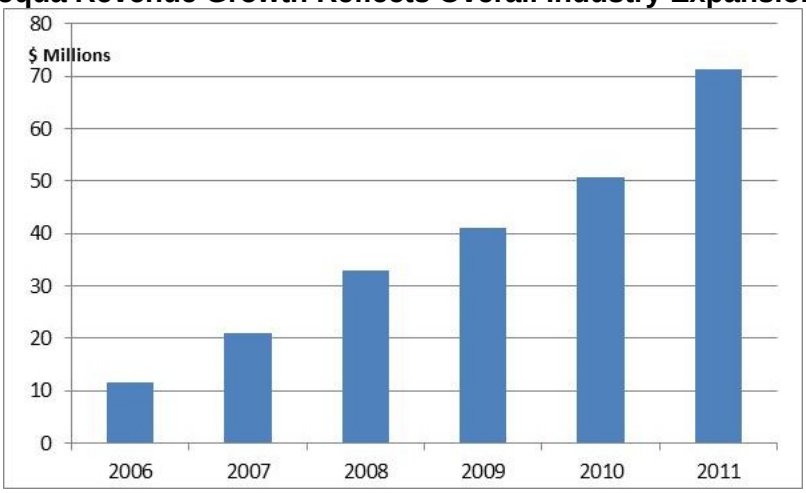
- We believe TPNI shares offer a means of gaining exposure to the rapidly growing digital marketing sector. In our view, with the shares at this level, the **risk / reward ratio is attractive**.
- Rapid sector growth has been driven by an increasing number of companies implementing digital marketing and content strategies, we believe.
- At the same time, larger technology companies looking to gain entry into the sector have fueled significant M&A activity.
- Pulse is in a transition phase, as it winds down a legacy business and drives growth at its digital marketing and content business, which advanced 34% in the quarter ended December 2013.
- We believe the company's recent decision to expand its flagship IMS (Inbound Marketing Summit) event to several U.S. cities in 2014 could facilitate the growth of Pulse's digital marketing and content operation.

INDUSTRY ENJOYING RAPID GROWTH

Pulse operates in a dynamic industry, in our view, with growing interest from potential customers and potential acquirers, we believe. There are a number of secular trends driving this interest, in our view**.** The Internet has changed the way consumers and businesses make decisions about which products and services to purchase. In turn, this has boosted the importance of online interaction with potential customers, making digital marketing increasingly more germane. The significant rise in the number of social media sites and their usage, as well as rising penetration of mobile devices, is also changing the way companies market their products and services. As a result, the nascent digital marketing industry has grown substantially over the past several years.

What is digital marketing? Digital marketing enables companies to leverage various electronic channels including social media to promote products, services or brands. Digital marketing also allows marketers to analyze their marketing campaigns to determine which aspects are generating positive responses. The analysis can occur much more quickly than with traditional marketing campaigns. In addition to the Internet, digital marketing also leverages emerging channels such as mobile text messaging, mobile apps, podcasts, electronic billboards and digital television, among others.

Eloqua Revenue Growth Reflects Overall Industry Expansion



Source: Company reports

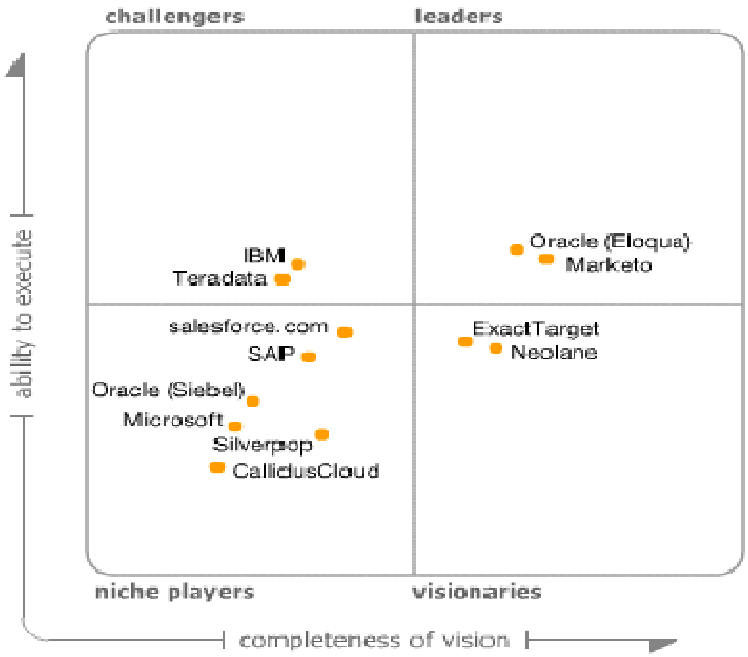
When it was founded in 1999, Eloqua was one of the pioneers in the space. Eloqua's growth underscores how rapidly the sector expanded from 2006 to 2011, in our view. Over that period, Eloqua's revenue grew to $71 million, up from $11.5 million in 2006. That represents a CAGR of over 44%. Eloqua was acquired by Oracle (ORCL-not rated).in 2013. Similarly, revenue for another leading digital marketing player, Marketo (MKTO-not rated), reached $95.9 million in 2013, up from $14.0 million in 2010, representing a CAGR of 90%.

Despite the recent growth, the sector remains relatively new, with prospects for substantial upside, we believe. According to a recent article in *Venture Beat Magazine*, "In spite of years of 50 percent annual growth, marketing automation is still the *new* new thing for almost all companies in America." Forrester Research predicts that domestic spending on interactive marketing will reach $76.6 billion in 2016. This equates to an estimated 26% of total U.S. marketing spend and represents a 122% increase from $34.5 billion spent in 2011.[12] Forrester estimates that spending on email, mobile and social media marketing will grow from $4.8 billion in 2011 to $15.7 billion in 2016, which equates to a CAGR of 27%.

At the same time, enterprise spending on automating, analyzing and optimizing marketing and sales is also projected to grow. IDC predicts that the marketing automation market will grow from $3.7 billion in 2011 to $5.5 billion in 2016. IDC also predicts that the CRM analytics market, which includes marketing and sales analytics, will grow from $2.2 billion in 2010 to $3.4 billion in 2015.

GROWTH ATTRACTS NEW PLAYERS, ORGANICALLY AND VIA M&A

Digital Marketing Four Quadrants



Source: Gartner

[1] *Fast-growing marketing automation still has only 3% penetration in non-tech companies,* VB Magazine, January 8, 2014
[2] That metric represented 16% of total spend.

We believe these metrics underscore the rapid growth and significant upside potential for the overall digital marketing industry. This anticipated growth is likely to benefit many of the current and prospective players, in our view. According to Gartner, Oracle, by virtue of its acquisition of Eloqua, and Marketo are the leaders in the space. As market leaders, they are likely to enjoy first mover advantage, we believe. We also believe that several other new entrants have significant opportunities, given how young the industry still is. Many of these newer entrants, including the Pulse Network, occupy niche roles within the broader digital marketing segment, in our view.

INDUSTRY CONSOLIDATION

Within the industry, including among what Gartner calls "Challengers, Visionaries and Niche Players," there has been considerable consolidation. Larger technology companies, interested in entering the market, have acquired many of the leading digital marketing companies over the past 18 months. Eloqua was acquired by Oracle, as noted. Silverpop acquired CoreMotives, Manticore Technology merged with Sales Engine International, Aprimo acquired eCircle, LoopFuse merged with Nearstream, ExactTarget acquired Pardot and was subsequently acquired by Salesforce.com (CRM-not rated) and Adobe (ADBE-not rated) acquired privately held Neolane for an estimated roughly $600 million.

Many of these transactions have come at fairly elevated valuations. For example, Oracle's purchase of Eloqua was at an estimated 8x TTM revenue and Salesforce.com's acquisition of ExactTarget was at an estimated 9x. Following this significant consolidation, there are only a handful of other independent companies engaged in digital content marketing, including Marketo, HubSpot, Act-On and Pulse Network. Many are privately-held.

Recent Consolidation Among Digital Marketing Enablers

Acquiror	Acquisition Target	Date	Price Paid ($M)
Salesforce.com	Radian6	Mar-11	$340
Silverpop	CoreMotives	Apr-12	NA
Teradata / Aprimo	eCircle	May-12	NA
Manticore Technology*	Sales Engine Inter'l	Jun-12	NM
ExactTarget	Pardot	Oct-12	$95.5
Oracle	Eloqua	Dec-12	$871
LoopFuse*	Nearstream	Jan-13	NM
Salesforce.com	ExactTarget	Jun-13	$2,500
Adobe	Neolane	Jul-13	$600

* Merger
Source: Company reports, WSJ, TechCrunch

We believe this consolidation has positive implications for the remaining independent companies. In our view, it indicates strong interest from larger companies wanting to gain entry into the sector. Moreover, there are not many public companies remaining in the sector. The few that are still independent include Pulse, Marketo and Responsys (MKTG-not rated).

NICHE PLAYER IN THE SPACE

Pulse is a smaller player, at this point. However, its **key digital marketing operation is growing rapidly, achieving 34% year-over-year revenue expansion** in the December quarter. This growth is masked, we believe**,** by negative year-over-year total revenue trends, as the company winds down a legacy business**.** We believe the metrics noted above suggest that the addressable market for Pulse's platform is large and growing rapidly. The company's growth strategy includes acquiring new customers either organically or through integration with other players. This is where the Pulse's annual conferences play a strategic role, we believe.

Pulse's cloud-based content marketing platform consists primarily of:

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- **Event Management** Pulse's cloud-based platform enables event groups to store data related to tradeshows and conferences they organize. Customers can leverage the Pulse platform to manage their leads databases for new business prospects, interact with customers and provide online and onsite registration functions. The company believes its solution helps event groups promote their events, boost and verify attendance and drive attendee satisfaction.

- **Online Broadcast** Pulse's interactive webinar player allows webinar participants to ask questions and chat with the host. The platform also collects data from the webinar, including the questions participants ask and the length of time they spend on the webinar. Marketers can analyze this data for lead generation.

- **Content Marketing Tools** The company provides content marketing tools, including content curation distribution, syndication and analytics. These tools are designed to help marketers share content related to their products and services and interact with potential customers.

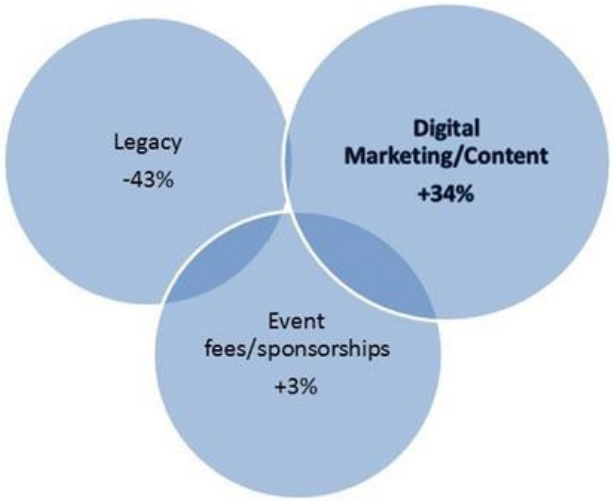
RECENT NEWS

In September 2013, Pulse borrowed $110,100 from Saber Insurance Trust. The loan and interest are to be repaid by June 1, 2014. On December 13, 2013 the Company issued a convertible promissory note for $52,500, payable 12- months from the date of issuance. On January 29, 2014, Pulse issued a promissory note for up to $335,000. On February 5, 2014, Pulse sold a $335,000 convertible promissory note to JMJ Financial through a private placement. Through Dec, the company had borrowed $60,000 under it.

Third Quarter Results

On February 13, 2014, the company reported results for its third fiscal quarter ended December 31, 2013. Pulse continues to transition to a digital marketing and content company and is winding down its legacy business. Total revenue declined 28.9% year-over-year to $1,042,708. This decline was driven primarily by a 42.7% drop in Sales from the legacy business and the loss of clients related to that segment. Pulse continues to focus its efforts on growing its digital marketing and content business. Importantly, revenue at this segment advanced 34% year-over-year, as the company continues to expand its client base. In addition, revenue from Sales to sponsors and attendees for Pulse-hosted conferences increased by 3.2%. Over time, as the digital marketing and content business grows, we expect it to offset declines at the company's legacy business.

Pulse Revenue Streams



Source: Company reports

Against the aforementioned 28.9% revenue decline, cost of sales declined 35.1%, while S,G&A increased by 20.3%. Total expenses declined by 8.2%. The company recorded an operating loss of $123,458 compared to operating income of $196,109 registered in the third quarter of fiscal 2013. Our full year estimates for fiscal 2014 change by the variances from our projections in the third fiscal quarter.

VALUATION

Because the company has not yet attained positive net income and because the sales-to-revenue appears to be a metric widely used in the recent acquisitions in the sector, our valuation methodology is based on market capitalization-to-revenue. Determining Pulse s revenue growth level is somewhat challenging at this early stage of the company's transition. As the company's transition continues, we believe total revenue will begin to grow.

We forecast revenue of $4.1 million for fiscal 2015. It appears that many of the transactions in the sector were done at over 8X-9X revenue. Our $0.54 price target implies an 11.8 multiple, on a basic market capitalization-to-revenue basis.

The company's growth strategy includes acquiring new customers either organically or through integration with other players. If management can execute this strategy successfully, it implies – we believe – that the medium-term outlook for revenue growth could be more robust.

RISKS

- Revenue could take longer than we expect to ramp and there may be continued revenue lumpiness from quarter to quarter.
- The Pulse Network is under-capitalized and may continue to access short term financings.
- Competition could increase. Although expertise and experience within the digital marketing sector are likely drivers of success, in our view, we believe barriers to entry are low.
- The shares are illiquid and controlled largely by insiders.
- Insiders own series B preferred shares that are each convertible into five common shares, which could be dilutive to public shareholders if converted. However, insiders own the majority of shares at this point and would be diluted, as well.

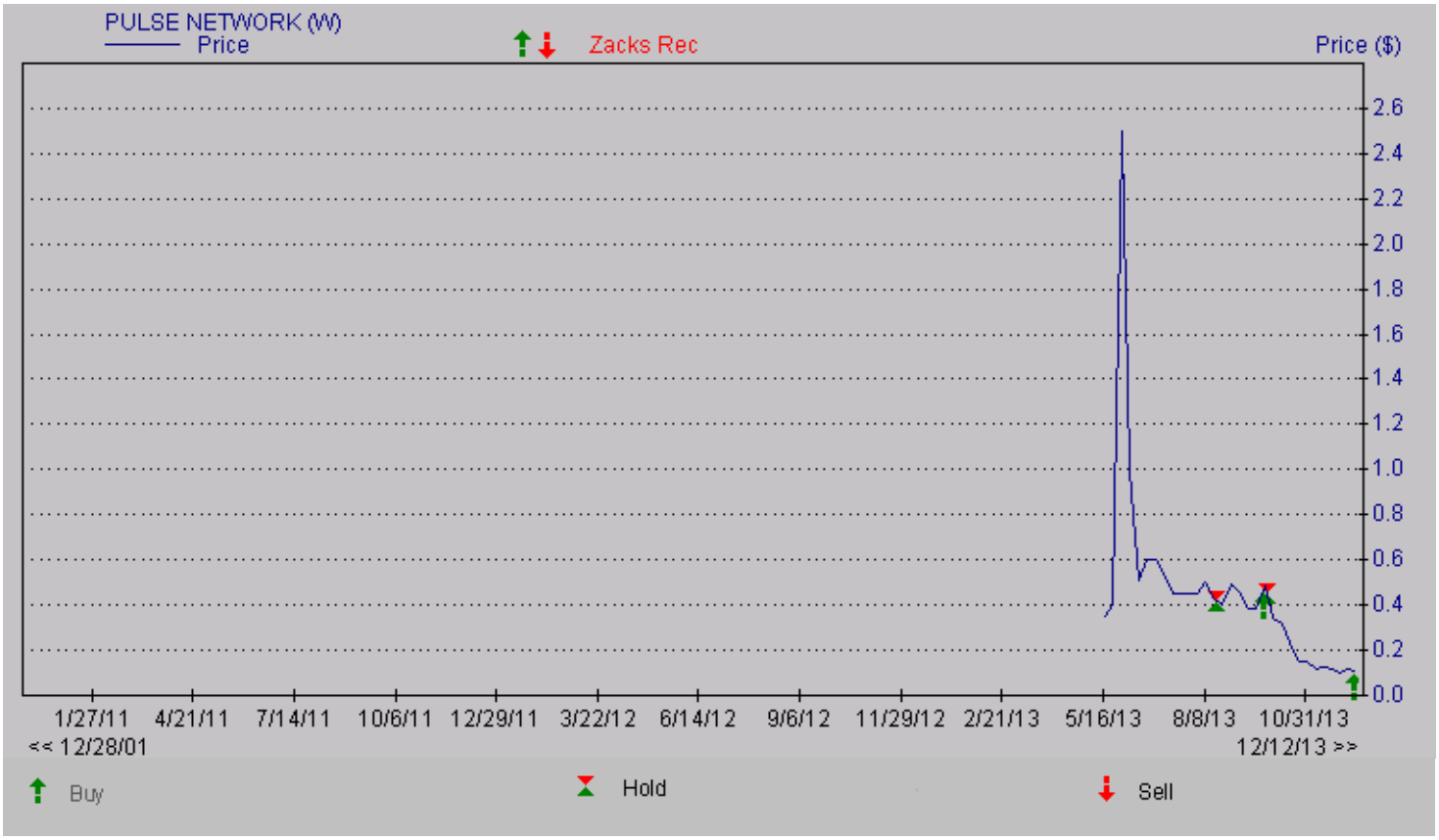
PROJECTED INCOME STATEMENT

The Pulse Network Income Statement and Projections ($)

Fiscal year ends March 31		Jun-12	Sep-12	Dec-12	Mar-13		Jun-13	Sep-13	Dec-13	Mar-14		
	FY2012	1Q13A	2Q13A	3Q13A	4Q13A	FY2013A	1Q14A	2Q14A	3Q14A	4Q14E	FY2014E	FY2015E
Revenue	**$4,157,757**	**$1,045,694**	**$650,457**	**$1,466,224**	**$595,096**	**$3,757,471**	**$934,222**	**$624,917**	**$1,042,708**	**$1,003,708**	**$3,605,555**	**$4,142,612**
Cost of sales	1,231,897	549,483	228,723	496,968	121,247	1,396,421	228,982	195,766	322,698	412,420	1,159,866	1,532,223
Gross profit	2,925,860	496,211	421,734	969,256	473,849	2,361,050	705,240	429,151	720,010	591,288	2,445,689	2,610,389
Gross profit margin	70.4%	47.5%	64.8%	66.1%	79.6%	62.8%	75.5%	68.7%	69.1%	58.9%	67.8%	63.0%
Selling expenses	655,851	134,941	109,786	114,159	97,229	456,115	121,186	181,148	137,441	119,245	559,020	495,204
G&A	2,274,193	589,235	593,616	658,988	1,285,812	3,127,651	698,101	705,250	706,027	861,978	2,971,356	3,448,235
Operating loss	(4,184)	(227,965)	(281,668)	196,109	(909,192)	(1,222,716)	(114,047)	(457,247)	(123,458)	(389,935)	(1,084,687)	(1,333,050)
Interest expense	33,159	2,591	2,875	4,271	47,969	57,706	19,288	32,271	25,247	13,768	90,574	61,803
Net loss	(37,343)	(230,556)	(284,543)	191,838	(957,161)	(1,280,422)	(133,335)	(489,518)	(148,705)	(403,703)	(1,175,261)	(1,394,854)
LPS	**($0.41)**	**($0.00)**	**($0.00)**	**$0.00**	**($0.01)**	**($1.55)**	**($0.00)**	**($0.01)**	**($0.00)**	**($0.00)**	**($0.01)**	**($0.02)**
Weighted avg shares out	90,900	90,000,000	90,000,000	90,000,000	90,000,000	823,855	90,114,286	90,436,667	90,700,000	90,400,000	90,412,738	90,400,000

Source: Company reports, Zacks SCR estimates

HISTORICAL ZACKS RECOMMENDATIONS



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