Zacks Small-Cap Research

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# Tapinator, Inc. (TAPM-OTC)

## TAPM: Anticipation Builds for the Q2 Launch Of ROCKY

| | |
|---|---|
| **Current Recommendation** | **Buy** |
| Prior Recommendation | N/A |
| Date of Last Change | 07/07/2015 |
| Current Price (03/31/16) | $0.25 |
| **Target Price** | **$0.50** |

## OUTLOOK

Tapinator continues to grow rapidly and in 2016 will accelerate its efforts with the launch of a number of high profile games: ***ROCKY*** based on the movie, the follow on to its biggest hit yet--- ***Big Sport Fishing 2*** and ***Combo Quest 2***, this time as a freemium version. These particular launches, in combination with its usual strategy, could propel the company over $4 million in sales this year. With the ability to generate positive 22% EBITDA margins, the company could reach a stock price of $0.32 this year and $0.50 by 2017.

## SUMMARY DATA

| | |
|---|---|
| **52-Week High** | **$0.54** |
| **52-Week Low** | **$0.16** |
| **One-Year Return (%)** | **N/A** |
| **Beta** | **N/A** |
| **Average Daily Volume (sh)** | **37,142** |
| **Common Shares Out (mil)** | **57** |
| **Market Capitalization ($mil)** | **$14** |
| **Short Interest Ratio (days)** | **N/A** |
| **Institutional Ownership (%)** | **0** |
| **Insider Ownership (%)** | **50** |
| **Annual Cash Dividend** | **$0.00** |
| **Dividend Yield (%)** | **0.0** |
| **5-Yr. Historical Growth Rates** | |
| **Sales (%)** | **N/A** |
| **Earnings Per Share (%)** | **N/A** |
| **Dividend (%)** | **N/A** |
| **P/E using TTM EPS** | **NM** |
| **P/E using 2015 Estimate** | **NM** |
| **P/E using 2016 Estimate** | **NM** |

| | |
|---|---|
| **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) |
|---|---|---|---|---|---|
| 2014 | 0.1 A | 0.2 A | 0.3 A | 0.4 A | 0.6 A |
| 2015 | 0.4 A | 0.6 A | 0.7 A | 0.7 A | 2.4 A |
| 2016 | 0.7 E | 0.9 E | 1.2 E | 1.2 E | 4.0 E |
| 2017 | | | | | 5.6 E |

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

| | Q1 (Mar) | Q2 (Jun) | Q3 (Sep) | Q4 (Dec) | Year (Dec) |
|---|---|---|---|---|---|
| 2014 | -$0.00 A | $0.00 A | $0.00 A | -$0.00 A | $0.00 A |
| 2015 | $0.00 A | -$0.09 A | -$0.01 A | -$0.00 A | -$0.01 A |
| 2016 | -$0.01 E | -$0.01 E | -$0.01 E | $0.01 E | -$0.03 E |
| 2017 | | | | | -$0.01 E |

**N/A**

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## KEY POINTS

- For the year ending December 31, 215, Tapinator reported revenues of $2.4 million versus $0.9 million a year ago, up 159%. EPS was reported as loss of $0.03, but was a non-GAAP loss of $0.01 once one-time charges and stock-based compensation is eliminated. The company achieved adjusted EBITDA of $523,000 and paid cash interest of $106,000 and no taxes.

- Tapinator reported Q4 2015 revenue of $692,268, up 87% over Q4 2014, but down sequentially from the $728,128 in Q3 2015. Despite lower revenues adjusted EBITDA was $149,000 versus $73,914 in Q3 2105.

- The company took a significant hit to earnings in the quarter by writing down its entire mini-game software development assets of $584,000. This one-time loss was responsible for $0.01 of EPS.

- Tapinator continues to invest in new game development. The company introduced 30 new games in Q4 up from 26 in Q3 2015. This brought its owned and operated portfolio to 183 active titles. By the end of 2015, 42 titles had been downloaded more than 1 million times.

- Tapinator's business model has also recently expanded to include a greater focus on licensed titles that leverage well-known brands. Tapinator has released games inspired by Discovery's *Deadliest Catch* and *Nik Wallenda in Sky Balance* and its biggest opportunity this year is ***ROCKY* to be launched in June** in coordination with MGM and the 40th anniversary of the original movie and it should benefit from the *Creed 2* movie in 2017.

- The company is currently valued at a fully diluted enterprise value of $16.4 million. The company has given guidance that EBITDA in 2016 should be near $900,00. Using an industry average of 19.6 EV/EBITDA, the stock would be worth $0.32 per share, and by looking at 2017 EBITDA estimates that could increase to $0.50, up 100% from today's price.

## Q4 2015 RESULTS

Tapinator reported Q4 2015 revenue of $692,268, up 87% over Q4 2014, but down sequentially from the $728,128 in Q3 2015. The decline in revenues was the result of softness early in the quarter but business picked up later in Q4 and is strong until today. There does not appear to be any particular reason for this softness. Despite lower revenues adjusted **EBITDA was $150,000** versus $73,914 in Q3 2105.

A large one-time item affected results. Reported results showed operating expenses (ex the platform fees) were $1.1 million versus $235,000 last year and $688,000 in Q3 2015. The operating loss in Q4 was $602,000 versus a loss of $14,000 a year ago. However included in this year's operating loss was a write down its entire mini-game software development assets of $584,000. These assets were from an acquisition in 2014 of a B2B casino platform that management decided required too many resources outside its core business to be cost effective and it would not be marketed any longer. There are however some small revenues still being generated from legacy customers. This one-time loss was responsible for $0.01 of EPS. Without this charge, **the operating loss would have been only $18,000.**

The company reported debt discount amortization from the converts of $365,000 and interest expense of $81,000 resulting in a net loss of $1 million versus a loss of $23,000 last year. Without the write off of assets, the loss would have been $464,000. Loss per share was reported as $0.02 versus

breakeven last year but the non-GAAP EPS loss excluding one-time charges and stock-based compensation rounds to $0.00 in Q4 2015. More importantly EBITDA in Q4 was a positive $149,000 versus $52,000 last year and $74,000 in Q3 2015.

### Liquidity and Balance Sheet

Tapinator's cash balance was $1.49 million at year-end down from $1.79 at September 30, 2015. In June 2015, the company raised $2.0 million through the issuance of a $2.24 million 8% senior convertible note due January 1, 2017 (convertible at $0.205), with five-year warrants to purchase 10.9 million shares and five-year callable warrants to purchase 10.9 million shares (exercise price of $0.30). The note is convertible into 10.9 million shares and total warrants outstanding could add 29.1 million additional shares.

### Q1 2016 Games



While the fast track business launched 25 new games again in Q1, the full-featured business was less active with only *Miss the Moose* launching late in Q1. It was featured as a best new game in Apple's App store and has been doing well with a five star rating from 73 commenters. It is simple and addictive and consists only of a car driving around a track that can speed up to miss hitting a moose running by.



In simulation games, a new title launch two weeks ago *Multi-Storey Parking 3-D* seems to be getting a very good reception.

## GAMES

Tapinator continues to invest in new game development. The company introduced 30 new games during the fourth quarter. This brought its owned and operated portfolio to 183 mobile gaming titles. These games have cumulatively achieved over 100 million cumulative downloads to-date. At the end of Q4 2015, 42 titles had reached the one million download mark. To date no game has been responsible for over 10% of revenues, and the company has not suffered the boom bust of other hits driven businesses.

Tapinator's rising traction with gamers is reflected in its user metrics and growing base of user downloads, we believe. Tapinator's cumulative downloads reached 166 million, up 245% from the previous year. Average monthly active users of 8.8 million increased 104% year over year but was down 14% sequentially from Q3.

**Tapinator Q4 2015 Metrics**

| | Q4 2015 | Q3 2015 | Y/Y % Change | Q/Q % Change |
|---|---|---|---|---|
| Average DAUs | 0.532 | 0.591 | 149% | -10% |
| Average MAUs | 8.8 | 10.2 | 104% | -14% |
| Average New Daily Downloads | 0.338 | 0.424 | 144% | -20% |
| Cumulative Downloads | 166 | 135 | 245% | 23% |
| Cumilative Game Titles | 183 | 153 | 95% | 20% |

## LAUNCH TIMELINE

Second Quarter:

- ***Multiplayer VIP Poker*** was expected in Q1 but should launch early in Q2. We are also looking for more games launched in the casino category possibly later in the year.

- ***ROCKY***: game based on the legendary franchise should launch in June in anticipation of the movie 40th anniversary November 21. It should also benefit from he theatre launch of *Creed 2* the next movie in the Rocky sequel. We believe the company is hoping for "seven figures" in revenue from this game alone and believe is has evergreen staying power. It will be on the OIS, Google Play and Amazon platforms.

- ***Combo Quest 2***: a freemium sequel to the original paid version hit, *Combo Quest.* It should launch mid-quarter.

- ***Big Sport Fishing 2***: a freemium sequel to the 14+ million downloaded, *Big Sport Fishing*. It has been the company's biggest title to date. Expect the launch mid-quarter.

Third Quarter:

- ***Turn Left***: quick fix game

- ***Pavlov's Puppy***: quick fix game

- To Be Announced: game based on an upcoming major motion picture

Fourth Quarter:

- ***Fusion Heroes***: strategy game with match-3 elements

| Q1 2016 | Q2 2016 | Q3 2016 | Q4 2016 |
|---|---|---|---|
| MISS THE MOOSE | ROCKY | TURN LEFT | FUSION HEROES |
| VIDEO POKER VIP MULTIPLAYER | COMBO QUEST 2 | PAVLOV'S PUPPY | |
| | BSF 2 BIG SPORT FISHING II | Major motion picture based game. To be announced. | |

## RISKS

- 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.
- Its increased emphasis on licensed product could pressure overall margins as well as pose a bigger risk to earnings as development costs increase.

## VALUATION

In valuing Tapinator we look to the valuations of others in the industry. Most of the public companies are very large and range from Activision at $25B enterprise value to Glu Mobile at $175 million. Even the companies that are growing in this group grow much more slowly than Tapinator and thus Tapinator deserves a higher multiple to its peers. If we look at enterprise value to EBIDTA and eliminate the companies that have negative EBITDA we see they are valued at an average of 19.6 times. If we apply that number to TAPM's estimated 2016 EBITA of $900,000 we calculate a stock price of $0.32 per share. Looking ahead to 2017 estimates that price rises to $0.50 per share due to its rapid revenue growth and expanding margins.

| | Ticker | Revenue | | TTM | Enterprise Value / Sales | | EV/ | Included | Enterprise |
|---|---|---|---|---|---|---|---|---|---|
| Company | | 2016E | LTM | EBITDA | 2016E | LTM | EBITDA | in Average? | Value |
| Activision | ATVI | $6,290 | $4,660 | $1,420 | 4.1x | 5.5x | 18.2x | y | 25,810 |
| Electronic Arts | EA | $4,632 | $4,270 | $942 | 3.7x | 4.0x | 18.2x | y | 17,100 |
| Gameloft | GLOFY | $272 | $273 | $8 | 2.4x | 2.4x | 83.0x | n | 653 |
| Glu Mobile | GLUU | $261 | $250 | $8 | 0.7x | 0.7x | 22.5x | y | 174 |
| Take Two | TTWO | $1,729 | $1,340 | -$211 | 1.3x | 1.7x | -10.6x | n | 2,230 |
| Zynga | ZNGA | $728 | $765 | -$49 | 1.2x | 1.2x | -18.2x | n | 894 |
| **Average** | | | | **789.9** | **2.8x** | **3.4x** | **19.6x** | | **$14,361** |

## INCOME STATEMENT

| | March Q1 15 | June Q2 15 | Sept Q3 15 | Dec Q4 15 | March Q1 16E | June Q2 16E | Sept Q3 16E | Dec Q4 16E | 2014 | 2015 | 2016E | 2017E |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **REVENUE** | 0.412 | 0.615 | 0.728 | 0.693 | 0.700 | 0.900 | 1.200 | 1.200 | 0.943 | 2.448 | 4.000 | 5.600 |
| Yr-to-yr Gr. | 329% | 172% | 191% | 87% | 70% | 46% | 65% | 73% | | 159% | 63% | 40% |
| **OPERATING EXPENSES** | | | | | | | | | | | | |
| Platform Fees | 0.133 | 0.186 | 0.233 | 0.193 | 0.210 | 0.270 | 0.360 | 0.360 | 0.283 | 0.745 | 1.200 | 1.680 |
| Net revenues | 0.279 | 0.429 | 0.495 | 0.500 | 0.490 | 0.630 | 0.840 | 0.840 | 0.660 | 1.703 | 2.800 | 3.920 |
| % of Sales | 67.6% | 69.8% | 68.0% | 72.2% | 70.0% | 70.0% | 70.0% | 70.0% | 70.0% | 69.6% | 70.0% | 70.0% |
| R&D | 0.042 | 0.038 | 0.030 | 0.025 | 0.035 | 0.050 | 0.060 | 0.070 | 0.303 | 0.136 | 0.215 | 0.400 |
| Marketing & PR | 0.013 | 0.042 | 0.108 | 0.054 | 0.055 | 0.055 | 0.150 | 0.160 | 0.023 | 0.216 | 0.420 | 0.500 |
| G&A | 0.112 | 0.167 | 0.299 | 0.286 | 0.300 | 0.320 | 0.350 | 0.360 | 0.233 | 0.864 | 1.330 | 1.700 |
| **Impairment of cap software** | 0.000 | 0.000 | 0.000 | 0.584 | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 | 0.584 | 0.000 | 0.000 |
| Amortization of cap software | 0.049 | 0.323 | 0.212 | 0.170 | 0.200 | 0.210 | 0.210 | 0.210 | 0.038 | 0.754 | 0.800 | 0.900 |
| Depreciation and amortization | 0.000 | 0.003 | 0.019 | 0.019 | 0.019 | 0.019 | 0.019 | 0.019 | 0.001 | 0.042 | 0.050 | 0.070 |
| Tot Operating Exp. | 0.216 | 0.573 | 0.668 | 1.139 | 0.609 | 0.654 | 0.789 | 0.819 | 0.598 | 2.596 | 2.815 | 3.570 |
| **Operating Income** | 0.062 | (0.143) | (0.173) | (0.640) | (0.119) | (0.024) | 0.051 | 0.021 | 0.062 | (0.894) | (0.015) | 0.350 |
| **Operating Margin** | 15% | -23% | -24% | -92% | -17% | -3% | 4% | 2% | 7% | -37% | 0% | 6% |
| Yr-to-yr Gr. | -275% | -525% | -276% | -1525% | -213% | -89% | -118% | -102% | | | | |
| Debt discount amortization | 0.038 | 0.114 | 0.327 | 0.327 | 0.325 | 0.325 | 0.325 | 0.325 | 0.038 | 0.806 | 1.300 | 0.650 |
| Interest expense | 0.016 | 0.041 | 0.082 | 0.081 | 0.081 | 0.081 | 0.081 | 0.081 | 0.016 | 0.220 | 0.324 | 0.350 |
| **Pretax Income** | 0.009 | (0.298) | (0.582) | (1.048) | (0.525) | (0.430) | (0.355) | (0.385) | 0.009 | (1.920) | (1.639) | (0.650) |
| | 2.2% | -48.5% | -80.0% | -151.4% | -75.0% | -47.8% | -29.6% | -32.1% | 0.9% | -78.4% | -41.0% | -11.6% |
| Taxes | 0.003 | 0.001 | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 | 0.000 | 0.001 | 0.004 | 0.004 | 0.004 |
| Tax Rate | 35.0% | -0.2% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 7.2% | -0.2% | -0.2% | 0.0% |
| **Net Income** | 0.006 | (0.299) | (0.582) | (1.048) | (0.525) | (0.430) | (0.355) | (0.385) | 0.008 | (1.924) | (1.643) | (0.654) |
| Yr-to-yr Gr. | -170% | -2516% | -1821% | 3396% | -9090% | 44% | -39% | -63% | | -24482% | -15% | -60% |
| EPS | $0.00 | ($0.01) | ($0.01) | ($0.02) | ($0.01) | ($0.01) | ($0.01) | ($0.01) | $0.00 | ($0.03) | ($0.03) | ($0.01) |
| Yr-to-yr Gr. | -146% | -2105% | -1773% | 3301% | -8890% | 39% | -39% | -63% | | -23600% | -15% | -61% |
| Stock-based compensation | - | 0.006 | 0.015 | 0.015 | 0.015 | 0.015 | 0.015 | 0.015 | - | 0.036 | 0.062 | 0.080 |
| Non-GAAP net income | 0.006 | (0.293) | (0.567) | (0.449) | (0.510) | (0.415) | (0.340) | (0.370) | 0.008 | (1.303) | (1.581) | (0.574) |
| Non-GAAP EPS | $0.00 | ($0.00) | ($0.00) | ($0.00) | ($0.01) | ($0.01) | ($0.01) | ($0.01) | $0.00 | ($0.01) | ($0.03) | ($0.01) |
| Yr-to-yr Gr. | | | | | NM | 124% | 42% | 205% | | -6166% | 218% | -64% |
| Share Out | 55.8 | 55.3 | 57.1 | 57.1 | 57.1 | 57.1 | 57.1 | 57.1 | 55.0 | 57.1 | 57.1 | 57.6 |
| Fully diluted shares | | | 68.0 | 68.0 | 68.0 | 68.0 | 68.0 | 68.0 | 55.7 | 89.9 | 89.9 | 89.9 |
| | | | | | | | | | | 4% | 0% | 1% |
| EBITDA | 0.112 | 0.188 | 0.074 | 0.149 | 0.115 | 0.220 | 0.295 | 0.265 | 0.102 | 0.523 | 0.897 | 1.400 |
| Margin % | 27% | 31% | 10% | 22% | 16% | 24% | 25% | 22% | 11% | 21% | 22% | 25% |

## BALANCE SHEET

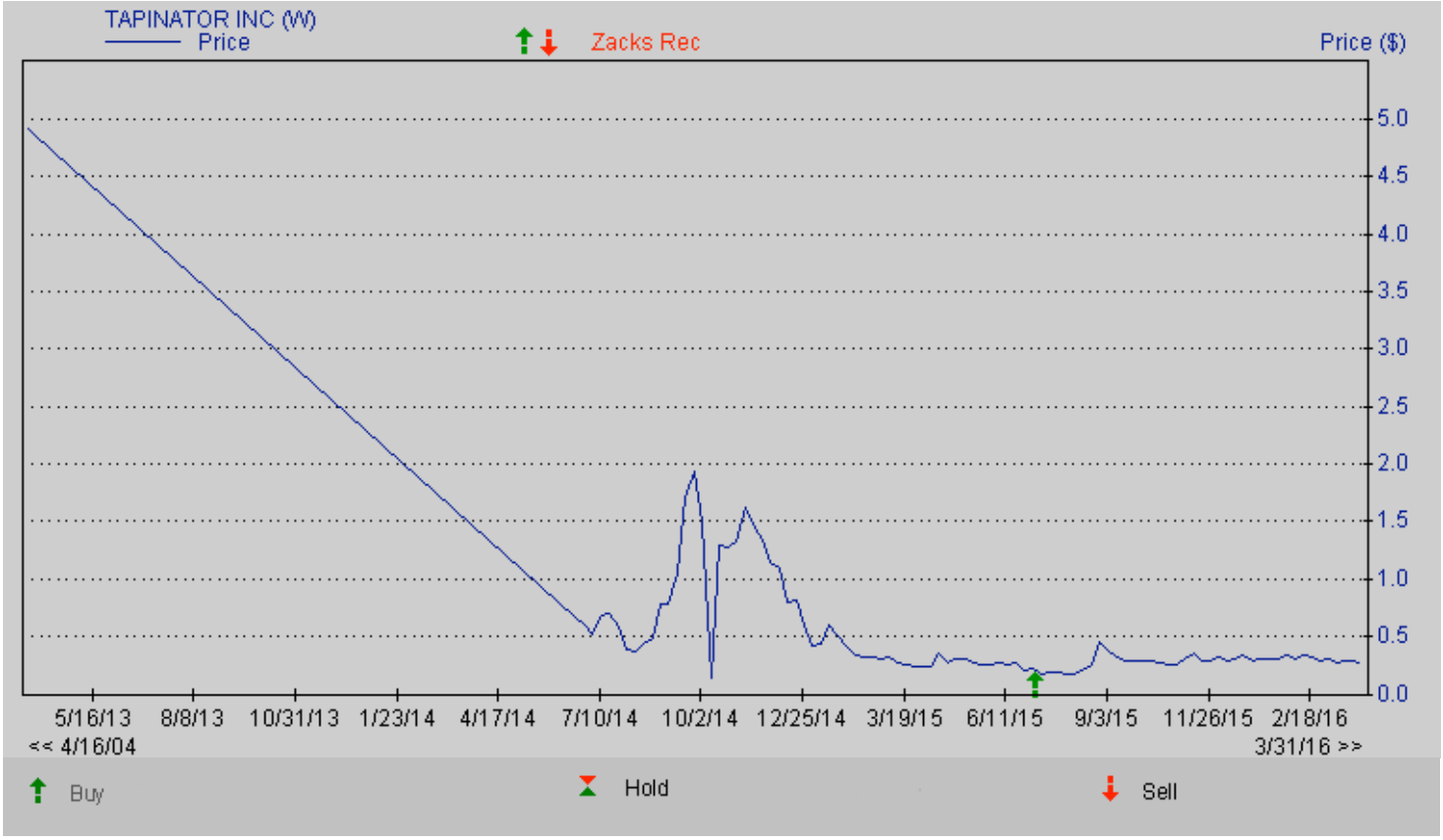
| | Dec. 31, 2015 | Sept. 30, 2015 | % Change |
|---|---|---|---|
| Cash and equivalents | 1,487,196 | 1,792,224 | -20.5% |
| Accounts receivable | 429,565 | 302,114 | 29.7% |
| Prepaid expenses | 54,589 | 59,836 | -9.6% |
| Total Current Assets | 1,971,350 | 2,154,174 | -9.3% |
| | | | |
| Property & Equipment | 13,714 | 12,416 | 9.5% |
| Software development costs | 746,936 | 1,200,920 | -60.8% |
| Capitalized financing costs | 71,959 | 90,047 | -25.1% |
| Investments | 19,086 | 19,086 | 0.0% |
| Security deposit | 14,052 | 14,040 | 0.1% |
| | | | |
| Total assets | 2,837,097 | 3,490,683 | -23.0% |
| | | | |
| Accounts payable | 197,031 | 95,299 | 51.6% |
| Due to related parties | 100,640 | 104,605 | -3.9% |
| Sr convertible debentures, net | 391,186 | 116,940 | 70.1% |
| | | | |
| Total current liabilities | 688,857 | 316,844 | 54.0% |
| | | | |
| Sr convertible debenture | 391,186 | 350,819 | 10.3% |
| | | | |
| Total liabilities | 1,080,043 | 667,663 | 38.2% |
| | | | |
| Total stockholder's equity | 1,757,054 | 2,823,020 | -60.7% |
| | | | |
| Total liab & stockholder's equity | 2,837,097 | 3,490,683 | -23.0% |
| | | | |
| Current ratio | 2.9 | 6.8 | |
| Working Capital | 1,282,493 | 1,837,330 | |
| Debt | 883,012 | 572,364 | |
| Debt as a % of assets | 31.1% | 16.4% | |
| Cash as % of total assets | 52.4% | 51.3% | |

## CASH FLOW

**2015 Quarterly Cash Flow**

| | 3 Mo Mar | 3 Mo June | 3 Mo Sept | 3 Mo Dec |
|---|---|---|---|---|
| **Cash flows from operating activities** | | | | |
| Net income (loss) | 5,840 | (298,989) | (582,392) | (1,048,467) |
| | | | | |
| Adjustments to reconcile net income (loss) to net cash prov | | | | |
| Depreciation and amortization | 49,441 | 323,729 | 233,465 | 189,039 |
| Amortization of debt discount | - | 151,646 | 327,402 | 327,402 |
| Amortization of original issue discount | 6,403 | 11,704 | 83,103 | (12,788) |
| Stock-based compensation | - | 5,175 | 15,489 | 15,792 |
| Impairment of capitalized software | - | - | - | 584,479 |
| | | | | |
| Cash flow | 61,684 | 193,265 | 77,067 | 55,457 |
| Free cash flow | (82,853) | 28,470 | (134,760) | (247,285) |
| | | | | |
| **Changes in operating assets & liabilities:** | | | | |
| Accounts recievable | (7,001) | (124,252) | (40,180) | (127,451) |
| Due from related parties | - | - | (110,494) | 110,494 |
| Prepaid expenses | - | (5,145) | (4,855) | (44,589) |
| Security deposits | 5,800 | - | - | (12) |
| Accounts payable & accrued expenses | (20,729) | 100,076 | 91,129 | (30,370) |
| Due to related parties | (17,055) | (45,095) | 37,428 | (3,965) |
| Capitalized financing costs | - | (110,494) | 110,494 | - |
| Interest on promissary notes | 9,351 | (9,351) | - | 148,644 |
| | | | | |
| Net cash provided by operating activities | 32,050 | (42,178) | (177,447) | 108,208 |
| | | | | |
| **Cash flows from investing activities** | | | | |
| Capitalized software development costs and other fixed ass | (144,537) | (164,795) | (211,827) | (303,270) |
| Purchase of property, plant and eqt. | | | | (10,272) |
| Reimbursement of leasehold improvements | | | | 10,800 |
| Net cash used in investing activities | (144,537) | (164,795) | (211,827) | (302,742) |
| | | | | |
| **Cash flows from financing activities** | | | | |
| Issuance of promissory notes | 24,000 | **1,976,000** | - | - |
| Beneficial conver feature on prom. Notes | 37,500 | (37,500) | - | - |
| Capitalized financing costs | - | - | - | (110,494) |
| Net cash provided by financing activities | 61,500 | 1,938,500 | - | (110,494) |
| | | | | |
| Net change to cash and cash equivalents | (50,987) | 1,774,889 | (389,274) | (305,028) |
| Cash and cash equivalents at beginning of period | 121,740 | 70,753 | 1,845,642 | 1,456,368 |
| Cash and cash equivalents at end of period | 70,753 | 1,845,642 | 1,456,368 | 1,487,196 |
| | | | | |
| **Non-cash investing and financing activities** | | | | |
| Redeemable preferred stock conversion | - | - | - | - |
| Common stock issued for convertible notes payable | - | - | - | 393,556 |
| issuance of red pref and assump of prom notes to acw sw | 876,718 | (876,718) | - | - |

## HISTORICAL ZACKS RECOMMENDATIONS


TAPINATOR INC (W)
Price
Zacks Rec
Price ($)
5.0
4.5
4.0
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
5/16/13
8/8/13
10/31/13
1/23/14
4/17/14
7/10/14
10/2/14
12/25/14
3/19/15
6/11/15
9/3/15
11/26/15
2/18/16
<< 4/16/04
3/31/16 >>
Buy
Hold
Sell

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