Zacks Small-Cap Research

August 17, 2017

Lisa Thompson
312-265-9154
lthompson@zacks.com

scr.zacks.com

10 S. Riverside Plaza, Chicago, IL 60606

# Net Element Inc. (NETE-NASDAQ)

## NETE: Russian Restructuring Should Reduces Losses

Using an industry average of EV to trailing GM of 6.9X we believe the stock could be worth $4.19 per share if NETE could reach profitability.

| | |
|---|---|
| Current Price (08/16/17) | $0.38 |
| **Valuation** | **$4.19** |

## OUTLOOK

Net Element is a software and services company for global online and mobile payments. It operates a merchant processor in the US with an attractive merchant offering with its Aptito front-end solution, and a mobile payment processor, PayOnline, operating primarily in Russia but expanding worldwide. PayOnllne was just certified in the US this month. NETE has shown extraordinary growth in the US, but needs to reach cash flow break even to stop equity dilution.

## SUMMARY DATA

| | |
|---|---|
| **52-Week High** | **$2.14** |
| **52-Week Low** | **$0.36** |
| **One-Year Return (%)** | **-80.1** |
| **Beta** | **1.0** |
| **Average Daily Volume (sh)** | **100,100** |
| **Shares Outstanding (mil)** | **19.0** |
| **Market Capitalization ($mil)** | **$7.2** |
| **Short Interest Ratio (days)** | **3.1** |
| **Institutional Ownership (%)** | **3** |
| **Insider Ownership (%)** | **28** |
| **Annual Cash Dividend** | **$0.00** |
| **Dividend Yield (%)** | **0.00** |
| **5-Yr. Historical Growth Rates** | |
| **Sales (%)** | **127** |
| **Earnings Per Share (%)** | **N/M** |
| **Dividend (%)** | **0** |
| **P/E using TTM EPS** | **N/M** |
| **P/E using 2017 Estimate** | **N/M** |
| **P/E using 2018 Estimate** | **N/M** |

| | |
|---|---|
| **Risk Level** | **High** |
| **Type of Stock** | **Small-Blend** |
| **Industry** | **Internet Commerce** |

## ZACKS ESTIMATES

**Revenue**
(in millions of $)

| | Q1 (Mar) | Q2 (Jun) | Q3 (Sep) | Q4 (Dec) | Year (Dec) |
|---|---|---|---|---|---|
| 2015 | 5.5 A | 6.9 A | 12.7 A | 15.1 A | 40.2 A |
| 2016 | 11.3 A | 13.7 A | 14.0 A | 15.3 A | 54.3 A |
| 2017 | 13.6 A | 16.1 A | 16.6 E | 18.2 E | 64.5 E |
| 2018 | | | | | 76.4 E |

**Earnings per Share**
(Non-GAAP EPS before non-recurring items)

| | Q1 (Mar) | Q2 (Jun) | Q3 (Sep) | Q4 (Dec) | Year (Dec) |
|---|---|---|---|---|---|
| 2015 | -$0.36 A | -$0.64 A | -$0.42 A | -$0.22 A | -$1.54 A |
| 2016 | -$0.13 A | -$0.10 A | -$0.11 A | -$0.16 A | -$0.64 A |
| 2017 | -$0.11 A | -$0.08 A | -$0.05 E | -$0.02 E | -$0.26 E |
| 2018 | | | | | -$0.16 E |

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

© Copyright 2017, Zacks Investment Research. All Rights Reserved.

## WHAT'S NEW

### Net Element Reports Smallest Quarterly Loss From Operations Since 2014

Net Element reported its smallest quarterly adjusted operating loss since 2014 at $1.3 million as revenues continue to grow. It grew total revenues 17.9% year over year in Q2 2017, with both North America and PayOnline showing growth in the low 30 percents. The company reported revenues of $16.1 million in 2017 versus $13.7 million in 2016. The North American Unified Payments division grew 30.8% and added $2.6 million to revenues. PayOnline grew 33.2%, adding $270,000 to revenues. The Mobile payments division declined 71% to just $518,000 despite the strength in the Ruble.

### Russian Restructuring Should Reduce Losses

The company took steps during the quarter to reduce expenses in Russia by consolidating the two separate offices for Mobile and PayOnline into one, and eliminating redundant and excess staff. The company also cancelled its lease on a Russian apartment. The total expense reduction for these actions has not yet been evidenced, as they happened late in Q2 and throughout Q3. We expect their full effect to be realized in Q3 and result in a restructuring charge taken in this September quarter. At this point, we expect G&A to be reduced in Q3 from Q2 levels, but are not sure by how much nor the magnitude of the restructuring charge. The Russian operations are already cash flow positive and this reduction in expense can only help margins going forward.

### Gross Margin Reaches Two Year High

Gross margin expanded in Q2 to 17.1% from 16.1% in Q1 2016 and from 15.5% in Q1 2017. This was the highest quarterly reported gross margin since June 2015. The 19% growth in sequential revenues added 34% in gross margin dollars. We expect gross margin to continue to improve in Q3 with volume. PayOnline was certified in the US on August 7$^{th}$, and we expect Unified Payments to ultimately save some money using PayOnline rather than a third party, but this may take until Q4 to cut over to the in-house system. The company believes as much as 15% of Unified's transactions could benefit from integration resulting in perhaps as much as $100,000 a quarter. Both online transactions and those that are API-based (such as those coming from Poynt's terminals via the internet, rather than telephone-based transactions) would able to use PayOnline. More importantly is that with its own front-end, Net Element will be able to offer a product with more features than it would using a third party solution and will ultimately make it more competitive.

Total expenses decreased to $4.2 million from $5.0 million primarily due to a reduction in stock-based compensation. The operating loss decreased to $1.3 million from $2.8 million. With the consolidation in Russia, using PayOnline in the US, and increased volumes, the company should be able to continue to reduce losses.

Interest expense decreased to $322,000 from $429,000 in Q2 2016 due to more favorable lending terms. Of that $150,000 was cash interest.

This quarter there were 17.7 million average primary shares outstanding, while last year there were only 11.6 million, or 52% more than last year. The company is not in compliance to retain its listing and is in the process of requesting an extension. Management is getting prepared to reverse split the stock in order to regain compliance if needed. If it were to do so, it plans to wait as long as possible before taking this action.

The adjusted non-GAAP operating loss was $1.5 million versus $1.2 million a year ago. On a per share basis however, the **adjusted non-GAAP loss per share declined slightly to $0.09 per share versus a loss of $0.10 per share** in 2016 due the increased number of shares rather than a reduction in losses. The company reported it had 19.0 million primary shares outstanding on August 11, 2017.

**The Cash Burn Continues as Net Element Invests In Growth**

The company is still burning about $400,000-500,000 a month. This quarter it financed losses by borrowing an additional $2.6 million. In Q2, $563,000 was invested in client acquisition. After October, the company will be done paying for PayOnline, which now costs $200,000 per month. The company is still planning to launch its Aptito front-end system in Russia to be sold by PayOnline and is waiting on the Russian government to finalize new regulations. The company believes Aptito will be very competitive in the restaurant market versus the alternatives now available in Russia.

While the company continues to grow at high rates, it will continue to be cash flow negative. Net Element is focused on growing revenues and is willing to sacrifice short-term profits to generate revenues with a long tail, future profitability and higher margins. If it were to slow down growth it could be cash flow neutral. As long as public markets are willing to fund the company through equity, this strategy may play out in future years.

## INVESTMENT THESIS

- Net Element is growth company in the payments industry that should benefit from the adoption of mobile and online payments in the US, Russia, and the Middle East and ultimately globally.
- Its Aptito product line provides differentiation and value-added services to its generic card processing business.
- This business should increase margins as well as aid sales efforts by improving price/performance and customer stickiness as well as bring the PayOnline payment gateway in-house to the US.
- The company has an increasingly robust platform to create a global payment system complete with merchant from end and should be able to expand geographically.
- We believe the company could grow to 25% to $65 million in revenues in 2017 through internal growth. It is trading at a market value of $7.2 million, and an enterprise value of $9.8 million or 0.1Xs enterprise value to forecasted 2017 sales.
- If NETE achieves our forecasts without further common stock dilution than that already predicted and no incremental debt, we believe its common stock could be worth $4.19 per share by next year based on an industry average valuation of approximately 6.9xs enterprise value to gross margin.

## RISKS

- The company has financial arrangements that are dilutive to common shareholders. It is uncertain if the company will be able to make accretive investments with these funds and shareholders may suffer further dilution.
- The company is losing money and may not be able to reach profitability or positive cash flow.
- The company is involved in a number of lawsuits.

- The mobile and online payment market is still in its infancy and there is no assurance countries will adopt this method to pay for goods and services.

- The company is somewhat dependent on Russia and due to oil prices, political turmoil, and sanctions, and this could affect payment volumes and the ability to do business there.

- Future acquisitions may not be successfully integrated operationally or technologically. Purchased portfolios may not yield expected profits.

- The merchant acquirer market in the US is competitive and larger companies have an advantage due to economies of scale and access to capital.

- Operations in Russia and the United Federation and the Middle East face considerable political risk and the company may be prohibited from certain financial transactions by government regulation and restrictions.

- Currency, particularly the ruble, has fluctuated dramatically and could affect reported earnings and operations.

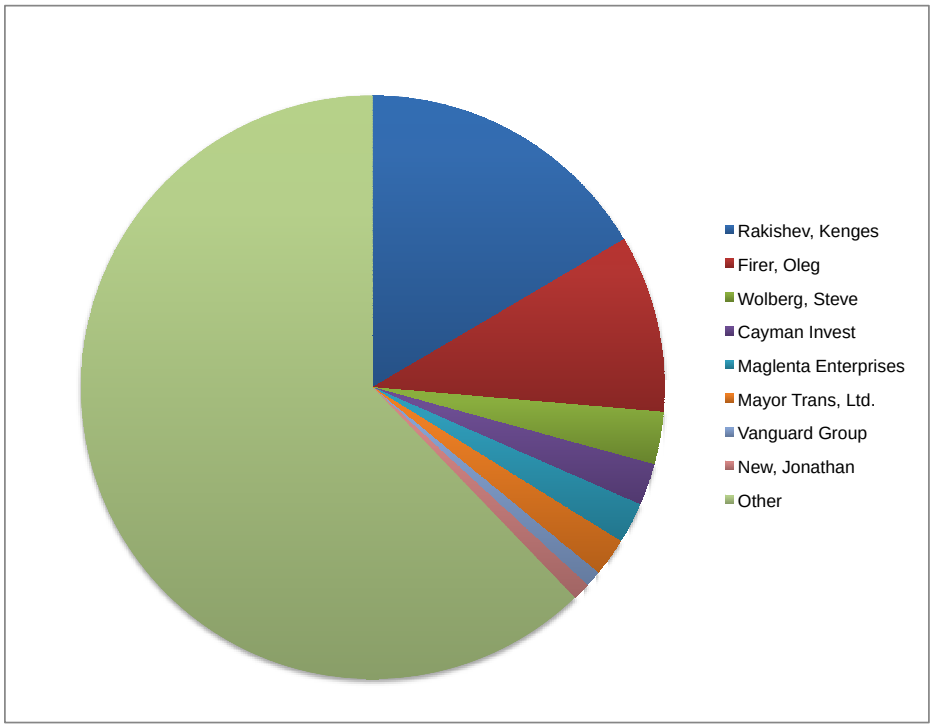
## VALUATION

Due the variation in reporting of revenues of the various competitors of Net Element, we have chosen to use gross margin contribution as a more accurate way to value the companies. Using Net Element's peer group we find an average valuation of 6.9 times the enterprise value to trailing twelve-month gross margin. If we use that multiple and apply it Net Element's trailing 12-month gross margin of $9.4 million, we see that the company could be worth $65 million enterprise value or $59 million market value if it were profitable. This equates to a stock price of $4.19 using 19.0 million shares outstanding.

**Merchant Acquring/Processing**

| Company | Ticker | EBITDA | Gross Margin | % | Revenue LTM | EV/GM | EV/EBITDA | Included in Average? | Enterprise Value |
|---|---|---|---|---|---|---|---|---|---|
| Cielo | CIOXY | 1,670 | 1,940 | 51% | 3,780 | 11.3 | 13.2 | n | 21,970 |
| Earthport | EPO.L | (10) | 15 | 43% | 35 | 7.9 | -12.2 | y | 119 |
| EVERTEC | EVTC | 158 | 214 | 53% | 401 | 8.5 | 11.5 | y | 1,810 |
| First Data | FDC | 2,790 | 4,650 | 59% | 7,910 | 7.1 | 11.8 | y | 33,040 |
| Global Payments | GPN | 1,150 | 1,750 | 42% | 4,190 | 9.6 | 14.6 | y | 16,800 |
| JetPay | JTPY | 4 | 19 | 30% | 64 | 2.3 | 12.0 | y | 43 |
| PayPal | PYPL | 2,260 | 10,840 | 92% | 11,760 | 4.6 | 22.3 | y | 50,380 |
| Qiwi | QIWI | 180 | 151 | 26% | 591 | 3.7 | 3.1 | y | 558 |
| Total System Services | TSS | 942 | 1,180 | 25% | 4,690 | 11.4 | 14.3 | y | 13,430 |
| Vantiv | VNTV | 880 | 1,900 | 50% | 3,800 | 6.9 | 14.9 | y | 13,080 |
| **Average** | | | | 47% | | 6.9 | 13.1 | | 14,362 |

## OWNERSHIP




## CASH FLOW

| | Mar. 31, 2015 | June 30, 2015 | Sept. 30, 2015 | Dec. 31, 2015 | Mar. 31, 2016 | June 30, 2016 | Sept 30, 2016 | Dec. 31, 2016 | Mar. 31, 2017 | June 30, 2017 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Cash flows from operating activities** | | | | | | | | | | |
| Net loss | $ (2,239,208) | $ (1,764,285) | $ (4,513,202) | $ (4,736,917) | $ (1,847,719) | $ (5,346,448) | $ (3,469,541) | $ (2,823,829) | $ (2,487,498) | $ (1,640,339) |
| **Adjustments to reconcile net loss to net cash provided by (used in) operating activities:** | | | | | | | | | | |
| Non controlling interest | $ (8,747) | $ (3,398) | $ (30,705) | $ (31,459) | $ (37,876) | $ (38,792) | $ (33,682) | $ (18,189) | $ (50,701) | $ (75,081) |
| Share based compensation | $ 601,371 | $ 601,371 | $ 601,371 | $ 2,502,191 | $ 360,984 | $ 2,014,589 | $ 732,701 | $ 355,161 | $ 596,404 | $ 0 |
| Deferred revenues | $ (34,858) | | | | $ (171,908) | $ (245,979) | $ 552,890 | $ (135,003) | $ (445,953) | $ (470,945) |
| Depreciation and amortization | $ 438,769 | $ 626,498 | $ 851,634 | $ 596,261 | $ 888,118 | $ 844,534 | $ 764,886 | $ 968,972 | $ 657,363 | $ 573,018 |
| Non cash interest | $ 0 | $ 349,146 | $ (349,146) | $ 0 | $ 0 | $ 297,434 | $ 444,423 | $ 110,551 | $ 46,135 | $ 48,113 |
| Amortization of deferred revenue | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ (1,221,177) | $ 0 | $ 0 |
| (Recovery of ) provision for loan losses | $ 0 | $ (94,770) | $ 94,770 | $ 0 | $ 0 | $ 0 | $ 0 | $ 500,000 | $ 0 | $ 192,895 |
| Amorization of prepaid costs | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 967,313 | $ 0 | $ 0 |
| **Changes in assets and liabilities, net of acquisitions and the effect of consolidation of equity affiliates** | | | | | | | | | | |
| Account receivable | $ 131,020 | $ 135,509 | $ (1,469,958) | $ (298,776) | $ 436,453 | $ (768,019) | $ (278,818) | $ (2,140,760) | $ 510,498 | $ 1,402,637 |
| Deferred revenue | $ 0 | $ (310,241) | $ 273,477 | $ 308,192 | $ 0 | $ 0 | $ 0 | $ 1,833,239 | $ 0 | $ 0 |
| Prepaid expenses and other assets | $ 278,319 | $ (104,721) | $ (263,433) | $ 381,466 | $ 334,291 | $ (63,359) | $ (602,430) | $ (239,084) | $ (231,755) | $ 516,416 |
| Accounts payable and accrued expenses | $ 668,175 | $ (621,264) | $ 1,727,439 | $ 1,796,957 | $ (909,344) | $ 2,786,305 | $ (1,876,961) | $ (368,025) | $ 449,284 | $ (2,294,445) |
| Net cash (used in) provided by operating | $ (165,159) | $ (2,305,489) | $ (1,034,911) | $ 417,324 | $ (947,001) | $ (817,169) | $ (4,210,955) | $ (2,210,831) | $ (956,223) | $ 129,230 |
| **Cash flows from investing activities** | | | | | | | | | | |
| Purchase of portfolio and client acquisition | $ 0 | $ (303,775) | $ (119,475) | $ (454,835) | $ 0 | $ 0 | $ 0 | $ (1,319,820) | $ (403,585) | $ (562,562) |
| Purchase of fixed and other assets | $ (6,849) | $ (58,202) | $ (419,086) | $ (95,072) | $ (396,819) | $ (558,741) | $ (391,158) | $ 1,159,629 | $ 355 | $ 180,068 |
| Net cash used in investing activities | $ (6,849) | $ (3,557,429) | $ (265,174) | $ (549,907) | $ (396,819) | $ (558,741) | $ (391,158) | $ (160,191) | $ (403,230) | $ (382,494) |
| **Cash flows from financing activities** | | | | | | | | | | |
| Proceeds from indebtedness | $ 650,000 | $ 0 | $ 0 | $ 0 | $ 75,000 | $ 1,140,000 | $ 1,453,500 | $ 502,040 | $ 92,000 | $ 3,206,792 |
| Repayment of indebtedness | $ (8,710) | $ 8,710 | $ 0 | $ 0 | $ 0 | $ 0 | $ (110,434) | $ 38,734 | $ (92,680) | $ (532,238) |
| Cash received from issuance of shares and | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 300,000 | $ 1,437,132 | $ 0 |
| Related party advances (payments) | $ 125,000 | $ (40,744) | $ 565,744 | $ (318,727) | $ 910,045 | $ 0 | $ (792,266) | $ 910,095 | $ 57,159 | $ (57,159) |
| Net cash provided by (used in) financing | $ 766,290 | $ 5,467,966 | $ 565,744 | $ (318,727) | $ 985,045 | $ 1,140,000 | $ 661,234 | $ 1,750,869 | $ 1,493,611 | $ 2,617,395 |
| Effect of exchange rate changes on cash | $ (331,346) | $ 303,903 | $ 375,021 | $ (262,929) | $ 57,537 | $ (741,514) | $ 192,807 | $ (143,498) | $ 57,288 | $ (25,972) |
| Net increase in cash | $ 91,048 | $ (91,048) | $ (359,320) | $ (714,239) | $ (301,238) | $ (90,918) | $ (3,748,072) | $ (763,651) | $ 191,446 | $ 2,338,159 |
| Cash at beginning of period | $ 675,231 | $ 766,279 | $ 675,231 | $ 315,728 | $ 1,025,747 | $ 724,509 | $ 633,591 | $ 1,385,286 | $ 621,635 | $ 813,081 |
| Cash at end of period | $ 766,279 | $ 675,231 | $ 315,728 | $ 1,025,747 | $ 724,509 | $ 633,591 | $ 1,385,286 | $ 621,635 | $ 813,081 | $ 3,151,240 |
| **Cash paid during the period for:** | | | | | | | | | | |
| Interest | $ 118,910 | $ 2,343 | $ 275,933 | $ 151,158 | $ 150,438 | $ 150,438 | $ (127,741) | $ 149,952 | $ 166,394 | $ 150,438 |
| Taxes | $ 30,505 | $ 59,706 | $ (15,794) | $ 146 | $ 86,770 | $ 86,770 | $ 0 | $ 0 | $ 64,314 | $ 86,770 |

## INCOME STATEMENT

| | Q1 2016 31-Mar | Q2 2016 30-Jun | Q3 2016 30-Sep | Q4 2016 31-Dec | Q1 2017 31-Mar | Q2 2017 30-Jun | Q3 2017E 30-Sep | Q4 2017E 31-Dec | 2015 | 2016 | 2017E | 2018E |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| North America Transaction | $7.9 | $10.4 | $11.2 | $12.7 | $11.0 | $13.6 | $14.1 | $15.5 | $27.4 | $42.1 | $54.2 | $65.0 |
| Yr-over-yr Growth | 51.7% | 65.9% | 42.9% | 56.4% | 39.6% | 30.8% | 26.0% | 22.2% | 41.7% | 53.8% | 44.0% | 20.0% |
| Credit card cost of service | 6.7 | 9.0 | 9.6 | 11.1 | 9.5 | 11.5 | 11.9 | 13.1 | 23.5 | 36.3 | 45.9 | 55.3 |
| Gross margin | 1.2 | 1.4 | 1.6 | 1.6 | 1.5 | 2.1 | 2.2 | 2.4 | 3.9 | 5.8 | 8.3 | 9.8 |
| Gross margin % | 15.3% | 13.8% | 14.3% | 12.2% | 13.7% | 15.7% | 15.7% | 15.7% | 14.2% | 13.7% | 15.3% | 15.0% |
| Mobile payments | 2.0 | 1.8 | 1.2 | 0.9 | 0.9 | 0.518 | 0.5 | 0.6 | 9.0 | 5.9 | 2.5 | 2.7 |
| Yr-over-yr Growth | 448.9% | 437.6% | -56.1% | -83.2% | -57.0% | -70.9% | -57.7% | -35.8% | 385.5% | -34.4% | -38.0% | 10.0% |
| Cost of Service | 1.8 | 1.6 | 1.0 | 0.9 | 0.8 | 0.5 | 0.5 | 0.6 | 8.1 | 5.3 | 2.4 | 2.4 |
| Gross Margin | 0.178 | 0.2 | 0.2 | 0.1 | 0.040 | 0.0 | 0.0 | 0.0 | 0.9 | 0.6 | 0.1 | 0.3 |
| Gross margin % | 8.9% | 12.0% | 14.7% | 7.9% | 4.7% | 3.0% | 3.0% | 3.0% | 10.2% | 10.9% | 3.6% | 11.9% |
| PayOnline | 1.4 | 1.5 | 1.6 | 1.7 | 1.7 | 2.0 | 2.0 | 2.1 | 3.8 | 6.2 | 7.8 | 8.6 |
| Yr-over-yr Growth | NA | NM | -22.2% | 17.6% | 23.0% | 33.2% | 25.2% | 23.4% | NA | 63.6% | 42.8% | 10.0% |
| Online Solutions Cost of Service | 0.9 | 1.0 | 1.1 | 1.1 | 1.2 | 1.3 | 1.3 | 1.4 | 2.4 | 4.1 | 5.3 | 5.5 |
| Gross Margin | 0.5 | 0.6 | 0.5 | 0.6 | 0.558 | 0.7 | 0.7 | 0.7 | 1.4 | 2.1 | 2.6 | 3.1 |
| Gross margin % | 35.1% | 37.0% | 33.4% | 35.0% | 32.1% | 33.2% | 33.2% | 33.5% | 38.1% | 34.5% | 33.0% | 36.0% |
| **Total revenues** | 11.3 | 13.7 | 14.0 | 15.3 | 13.6 | 16.1 | 16.6 | 18.2 | **40.2** | **54.3** | **64.5** | **76.4** |
| Yr-to-yr Growth | 103.2% | 98.2% | 10.5% | 1.4% | 20.4% | 17.9% | 18.6% | 18.8% | 89.8% | 34.9% | 25.4% | 18.4% |
| **Costs and expenses:** | | | | | | | | | | | | |
| Cost of revenues | 9.4 | 11.5 | 11.7 | 13.1 | 11.5 | 13.3 | 13.7 | 15.0 | 34.0 | 45.7 | 53.5 | 63.2 |
| Gross Margin | 1.875 | 2.2 | 2.3 | 2.2 | 2.1 | 2.8 | 2.9 | 3.2 | 6.3 | 8.6 | 11.0 | 13.2 |
| % of Sales | 16.7% | 16.1% | 16.5% | 14.2% | 15.5% | 17.5% | 17.4% | 17.3% | 15.6% | 15.8% | 17.0% | 17.3% |
| G&A | 2.1 | 2.0 | 2.3 | 2.4 | 2.8 | 2.6 | 2.6 | 2.5 | 9.3 | 8.8 | 10.5 | 11.6 |
| Stock-based compensation | 0.4 | 2.0 | 0.7 | 0.4 | 0.6 | 0.1 | 0.6 | 0.8 | 4.3 | 3.5 | 2.1 | 2.1 |
| Provision for loan losses | 0.3 | 0.1 | 0.3 | 1.0 | 0.3 | 0.9 | 0.3 | 0.2 | 0.6 | 1.7 | 1.6 | 1.8 |
| Depreciation and amortization | 0.9 | 0.8 | 0.8 | 1.0 | 0.7 | 0.6 | 0.6 | 0.6 | 2.5 | 3.5 | 2.4 | 2.4 |
| Total operating expenses | 3.6 | 5.0 | 4.1 | 4.8 | 4.4 | 4.2 | 4.1 | 4.1 | 16.8 | 17.4 | 16.7 | 17.9 |
| **Loss from operations** | (1.7) | (2.8) | (1.8) | (2.6) | (2.3) | (1.3) | (1.2) | (0.9) | (10.5) | (8.8) | (5.7) | (4.7) |
| Interest expense, net | (0.150) | (0.4) | (0.6) | (0.3) | (0.270) | (0.3) | (0.3) | (0.3) | (3.6) | (1.5) | (1.2) | (1.0) |
| Other expense | (0.0) | (0.0) | 0.4 | (0.0) | (0.0) | (0.0) | 0.0 | 0.0 | (0.1) | 0.4 | (0.1) | (0.1) |
| Gain on asset disposal | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Gain on change in conversion derivative | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | (26.9) | 0.0 | 0.0 | 0.0 |
| Loss from stock value guarantee | 0.0 | (2.2) | (1.6) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | (3.7) | 0.0 | 0.0 |
| One-time charges | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | (0.2) | 0.0 | 27.7 | 0.0 | (0.2) | (0.2) |
| Total non-operating expenses | (0.2) | (2.6) | (0.2) | (0.3) | (0.3) | (0.4) | (0.5) | (0.3) | (2.8) | (4.8) | (1.5) | (1.3) |
| Pretax operating income (loss) | (1.9) | (5.4) | (3.5) | (2.8) | (2.5) | (1.7) | (1.7) | (1.2) | (13.3) | (13.6) | (6.9) | (5.7) |
| Income tax provision | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Tax rate | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% | 0% |
| **Operating Loss** | (1.9) | (5.4) | (3.5) | (2.8) | (2.5) | (1.7) | (1.7) | (1.2) | (13.3) | (13.6) | (6.9) | (5.7) |
| Minority interest | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 |
| Net loss | (1.8) | (5.3) | (3.5) | (2.8) | (2.5) | (1.6) | (1.7) | (1.2) | (13.3) | (13.5) | (6.9) | (5.7) |
| Preferred dividend | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | (1.6) | 0.0 | 0.0 | 0.0 |
| Net loss to common stock | (1.8) | (5.3) | (3.5) | (2.8) | (2.5) | (1.6) | (1.7) | (1.2) | (14.8) | (13.5) | (6.9) | (5.7) |
| Foreign currency translation gain (loss) | (0.0) | (0.5) | (0.1) | (0.3) | 0.0 | (0.1) | 0.0 | 0.0 | (0.3) | (0.9) | (0.1) | 0.0 |
| Comprehensive loss | (1.9) | (5.8) | (3.6) | (3.1) | (2.5) | (1.8) | (1.7) | (1.2) | (15.2) | (14.4) | (6.9) | (5.7) |
| Earnings ex-one time charge | (1.8) | (3.2) | (2.3) | (2.8) | (2.5) | (1.6) | (1.5) | (1.2) | (15.7) | (11.4) | (6.9) | (5.7) |
| Stock-based compensation | 0.4 | 2.0 | 0.7 | 0.4 | 0.6 | 0.1 | 0.6 | 0.8 | 4.3 | 3.5 | 2.1 | 2.1 |
| Adjusted Non-GAAP Earnings | (1.5) | (1.2) | (1.6) | (2.5) | (1.9) | (1.5) | (0.9) | (0.4) | (9.8) | (7.9) | (4.8) | (3.6) |
| Yr-to-yr Growth | -9.7% | -63.4% | -44.6% | 19.4% | 27.1% | 29.3% | -46.2% | -82.3% | 42% | -20% | -51% | -25% |
| GAAP EPS | ($0.16) | ($0.46) | ($0.25) | ($0.19) | ($0.15) | ($0.10) | ($0.09) | ($0.06) | ($2.32) | ($1.03) | ($0.37) | ($0.26) |
| **Non-GAAP EPS** | **($0.13)** | **($0.10)** | **($0.11)** | **($0.16)** | **($0.11)** | **($0.09)** | **($0.05)** | **($0.02)** | **($1.54)** | **($0.60)** | **($0.26)** | **($0.16)** |
| Yr-to-yr Growth | -63% | -84% | -73% | -26% | -13% | -15% | -60% | -87% | -17% | -60.7% | -57.5% | -57.9% |
| Share outstanding | 11.3 | 11.6 | 14.0 | 15.3 | 16.5 | 17.7 | 19.0 | 21.6 | 6.4 | 13.1 | 18.7 | 22.0 |
| Yr-to-yr Growth | 145% | 134% | 105% | 61% | 46% | 52% | 35% | 41% | 72% | 104.3% | 43.3% | 30.2% |
| Fully diluted shares | 12.8 | 13.2 | 15.6 | 17.6 | 18.8 | 20.1 | 21.4 | 24.0 | 8.7 | 14.8 | 21.1 | 24.4 |
| Yr-to-yr Growth | 110% | 95% | 74% | 38% | 48% | 52% | 37% | 36% | 87% | 62.8% | 42.1% | 15.6% |
| Adjusted EBITDA | (0.449) | 0.088 | (1.846) | (1.258) | (1.009) | (0.642) | (0.006) | 0.455 | (3.751) | (3.509) | (1.202) | (0.206) |

## BALANCE SHEET

| | June 30, 2017 | Mar. 31, 2017 | Qtr-Qtr % Change | June 30, 2016 | Yr- Yr % Change |
|---|---|---|---|---|---|
| **Current assets:** | | | | | |
| Cash | **$1,274,279** | **$813,081** | 57% | **$633,591** | 101% |
| Accounts receivable, net | 6,007,143 | 6,724,985 | -11% | 5,827,586 | 3% |
| Prepaid expenses and other assets | 1,219,524 | 1,686,126 | -28% | 806,202 | 51% |
| Total current assets | 8,500,946 | 9,224,192 | -8% | 7,267,379 | 17% |
| | | | | | |
| Fixed assets, net | 103,239 | 113,908 | -9% | 142,409 | -28% |
| Intangible assets, net | 3,308,229 | 3,466,408 | -5% | 4,513,823 | -27% |
| Goodwill | 9,643,752 | 9,643,752 | 0% | 9,643,752 | 0% |
| Other long term | 417,574 | 536,512 | -22% | 553,302 | -25% |
| Total assets | 21,973,740 | 22,984,772 | -4% | 22,120,665 | -1% |
| | | | | | |
| **Current liabilities:** | | | | | |
| Accounts payable | $7,516,761 | $8,337,673 | -10% | $6,075,259 | 24% |
| Deferred revenue | 439,074 | 910,019 | -52% | 326,023 | 35% |
| Accrued expenses | 4,437,601 | 5,366,887 | -17% | 4,205,599 | 6% |
| Notes payable (current portion) | **984,720** | **719,564** | 37% | **384,209** | 156% |
| Due to related parties | **366,636** | **356,200** | 3% | **329,921** | 11% |
| Total current liabilities | 13,744,792 | 15,690,343 | -12% | 11,321,011 | 21% |
| | | | | | |
| Notes payable (non-current portion) | **6,253,513** | **3,844,115** | 63% | **3,823,921** | 64% |
| Total liabilities | 19,998,305 | 19,534,458 | 2% | 15,144,932 | 32% |
| | | | | | |
| **STOCKHOLDERS' DEFICIT** | | | | | |
| Common stock | 1,797 | 1,753 | 3% | 1,336 | 35% |
| Paid in capital | 166,220,080 | 165,833,480 | 0% | 160,092,967 | 4% |
| Accumulated other comp income (loss) | (2,620,615) | (2,474,513) | 6% | (2,091,604) | 25% |
| Accumulated deficit | (161,570,423) | (159,930,083) | 1% | (151,149,215) | 7% |
| Noncontrolling interest | (55,404) | 19,677 | -382% | 122,249 | -145% |
| Total stockholders' deficit | 1,975,435 | 3,450,314 | -43% | 6,975,733 | -72% |
| | | | | | |
| Total liabilities and stockholders' deficit | 21,973,740 | 22,984,772 | -4% | 22,120,665 | -1% |
| | | | | | |
| Net Cash | (77,077) | (262,683) | -71% | (80,539) | -4% |
| Current and Quick Ratio | 0.6 | 0.6 | 5% | 0.6 | -4% |
| Working Capital | (5,243,846) | (6,466,151) | -19% | (4,053,632) | 29% |
| Total Debt | 7,604,869 | 4,919,879 | 55% | 4,538,051 | 68% |
| Debt/TA | 35% | 21% | 62% | 21% | 69% |
| DSO | 34.0 | 45.3 | -25% | 38.8 | -13% |
| Enterprise value | 4,974,365 | 12,567,605 | -60% | 25,672,279 | -81% |

## HISTORICAL STOCK PRICE

### 1 Year Chart




**Source: E*TRADE Securities**

# DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, Lisa Thompson, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESTMENT BANKING AND FEES FOR SERVICES

Zacks SCR does not provide investment banking services nor has it received compensation for investment banking services from the issuers of the securities covered in this report or article.
Zacks SCR has received compensation from the issuer directly or from an investor relations consulting firm engaged by the issuer for providing non-investment banking services to this issuer and expects to receive additional compensation for such non-investment banking services provided to this issuer. The non-investment banking services provided to the issuer includes the preparation of this report, investor relations services, investment software, financial database analysis, organization of non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per-client basis and are subject to the number and types of services contracted. Fees typically range between ten thousand and fifty thousand dollars per annum. Details of fees paid by this issuer are available upon request.

POLICY DISCLOSURES

This report provides an objective valuation of the issuer today and expected valuations of the issuer at various future dates based on applying standard investment valuation methodologies to the revenue and EPS forecasts made by the SCR Analyst of the issuer's business.
SCR Analysts are restricted from holding or trading securities in the issuers that they cover. ZIR and Zacks SCR do not make a market in any security followed by SCR nor do they act as dealers in these securities. Each Zacks SCR Analyst has full discretion over the valuation of the issuer included in this report based on his or her own due diligence. SCR Analysts are paid based on the number of companies they cover.
SCR Analyst compensation is not, was not, nor will be, directly or indirectly, related to the specific valuations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports and articles are based on data obtained from sources that it believes to be reliable, but are not guaranteed to be accurate nor do they purport to be complete. Because of individual financial or investment objectives and/or financial circumstances, this report or article should not be construed as advice designed to meet the particular investment needs of any investor. Investing involves risk. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports or articles or tweets are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.