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Zacks Small-Cap Research

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Innovus Pharmaceutical (INNV-OTC)

INNV: 3Q18 preliminary revenues in-line with guidance but slightly below our estimate.

We base our $0.42/share value for INNV on a ten-year DCF with a WACC of 15%. Our WACC reflects current high financing costs as well as its relatively recent transition from start up to true operating status. On a P/S basis, INNV trades at 0.9x 2018E, while its peers trade anywhere from 1.2-29x 2018 sales, averaging 12.6x.

Current Price (11/14/18)	$0.11
Valuation	**$0.42**

OUTLOOK

On November 5, 2018, Innovus Pharmaceutical released preliminary 3Q18 revenues of $7.0-7.1 million. This is largely flat to slightly down from 2Q18 revenues of $7.4 million (including $6.9 million from product sales).

We believe the slowdown in revenue growth reflects a smaller marketing investment in 3Q18 versus 2Q18 when marketing spend exceeded $5.5 million, compared with $3.3 million in the 1Q18.

INNV expects to release 3Q18 results on November 14.

SUMMARY DATA

52-Week High	**$0.21**
52-Week Low	**$0.08**
One-Year Return (%)	**22.2**
Beta	**4.93**
Average Daily Volume (sh)	**693,000**
Shares Outstanding (mil)	**207**
Market Capitalization ($mil)	**$23**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**16**
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 2018 Estimate	**N/A**
P/E using 2019 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**High,**
Type of Stock	**N/A**
Industry	**Med-Drugs**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	2.2 A	2.0 A	2.2 A	2.4 A	8.8 A
2018	4.5 A	7.3 A	7.7 E	8.1 E	27.3 E
2019	8.9 E	9.7 E	10.4 E	10.2 E	38.7 E
2020					46.0 E

Earnings per share

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	-$0.02 A	-$0.01 A	-$0.01 A	-$0.01 A	-$0.04 A
2018	-$0.01 A	-$0.01 A	-$0.01 E	-$0.01 E	-$0.04 A
2019	-$0.01 A	-$0.00 A	-$0.00 E	-$0.00 E	-$0.01 E
2020					$0.01 E

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

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INVESTMENT UPDATE – 3Q18 preliminary revenues in line with guidance

The importance of consistent marketing campaigns

Innovus Pharamceutical announced preliminary 3Q18 revenues of $7.0 - $7.1 million, up over 200% from $2.2 million in the year earlier period, but down sequentially from $7.3 million posted in 2Q18. We were looking for a slight sequential improvement to $7.6 million (including $7.3 million in product sales).

In our initiation report (October 2, 2018), we noted that the supplements business differs from traditional pharmaceutical business. The supplements market relies more on customer interest than disease incidence. There are few blockbuster perennial products in the supplements market – particularly at a brand level. It is a marketing-driven business, where demand can wax and wane. As a result, marketing investment in the supplements market is not as "sticky" as in OTC and prescription drugs.

Innovus spent $5.5 million in 2Q18 largely on a 200k+ piece direct mail campaign. This represented a $2 million sequential increase in marketing expense, which caught us off guard. So while INNV reported stronger than expected revenue results in 2Q18, much of the upside surprise was offset by the increased marketing spend.

We understand that INNV did not make the same level of marketing investment this quarter and instead will focus on smaller, more frequent campaigns to determine which programs are most effective and with which customers. We believe that this marketing strategy will provide more meaningful metrics and improve operating cash flow – both keys to improving investor confidence in the shares.

Innovus is scheduled to release 3Q18 results on November 14.

Sensitivities and risks: Execution is key

It is still early to know how successful INNV's multi-pronged marketing program, with its emphasis on growing subscription-based revenues to leverage marketing expenditures, will be. Early trends are quite favorable. In our view, INNV needs to show that it can maintain its strategic focus and meet clear, pressure-tested, operating targets in order to reduce financing costs and gain a stable, buy-and-hold investor base. Sensitivities in our financial and valuation outlook are largely execution dependent including:

- New product acquisitions/launches
- Addressable market and product lifecycle
- Subscription persistency
- Marketing spend
- Financing costs
- Regulatory changes

FINANCIALS AND VALUATION

Our 2018 revenue estimate stays at $27.6 million, slightly ahead of guidance at $23 million. We expect the Company to make another marketing push in 4Q18 to target customers who include “improving health” in their new year’s resolutions and we anticipate that some of these revenues may book before year-end. Additionally, the Company appears close to releasing its GlucoGorx product/test strip bundle, which along with several other pipeline products may give the Company a 4Q revenue boost.

We value Innovus Pharmaceutical primarily using DCF techniques in large part because we expect much of the value in the Company will be unlocked over the next three to five years. The Company’s recent results suggest a strong recent track record of product introductions and healthy gross margins of 80%+.

A 10-year DCF with a WACC of 15% on our forecast compound average annual revenue growth of 71% from 2017-2020 fading to terminal growth of 2% and a terminal EBIT margin of 15% yields a value of $0.42 per share.

HISTORICAL STOCK PRICE



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