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Zacks Small-Cap Research

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Inuvo Inc. (INUV-AMEX)

Inuvo to Be Acquired by ConversionPoint Technologies for $2.22 in Cash and Stock

Inuvo has accepted an offer to be acquired for $2.22 paid with both cash and stock by ConversionPoint Technologies, a private company that plans to list on NASDAQ.

Current Price (11/07/18)	$1.25
Valuation	**$2.22**

OUTLOOK

Inuvo, a digital publishing, and advertising technology company, capitalizing on its newly enhanced ad platform, *INUVO Exchange*, and its expanded sales and marketing team. It has accepted an offer to be acquired which should close in Q1 2019.

SUMMARY DATA

52-Week High	**$1.36**
52-Week Low	**$0.40**
One-Year Return (%)	**50.6**
Beta	**0.7**
Average Daily Volume (sh)	**1,583,254**
Shares Outstanding (mil)	**32.4**
Market Capitalization ($mil)	**$40.5**
Short Interest Ratio (days)	**6.8**
Institutional Ownership (%)	**21**
Insider Ownership (%)	**18**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**12.3**
Earnings Per Share (%)	**8.5**
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	**Above Average**
Type of Stock	**Small Blend**
Industry	**Internet-Services**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2016	18.7 A	15.6 A	17.5 A	19.7 A	71.5 A
2017	17.2 A	18.3 A	20.3 A	23.8 A	79.6 A
2018	20.5 A	19.0 A	16.8 A	18.0 E	74.3 E
2019					84.0 E

Earnings Per Share
(Non-GAAP EPS from continuing operations)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2016	$0.03 A	-$0.01 A	-$0.00 A	-$0.00 A	-$0.01 A
2017	-$0.04 A	-$0.02 A	-$0.02 A	-$0.00 A	-$0.09 A
2018	-$0.04 A	-$0.03 A	-$0.04 A	-$0.02 E	-$0.11 E
2019					-$0.04 E

Zacks Projected EPS Growth Rate - Next 5 Years % **10**

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WHAT'S NEW

Inuvo to Be Acquired By ConversionPoint for $2.22 Per Share

Inuvo's management has long stated that it would seek buyers of the company once it hit a size to be of interest, which it deemed to be at a $100 million revenue run rate. In advance of reaching that run rate, the company has announced plans to be acquired. It has entered into a definitive agreement to be acquired by privately held ConversionPoint Technologies, Inc. for cash-and-stock valued at approximately $2.22 per share or $75.7 million, well above its previous market price of $0.41 per share. Inuvo shareholders will receive $0.45 per share in cash, and stock valued at an estimated $1.77 per share, or approximately $75.5 million in total consideration. ConversionPoint plans to file a Form S-4 with the SEC to register the shares of common stock to be issued in the acquisition and intends to file listing applications for its stock with the NASDAQ Capital Market and the Toronto Stock Exchange. We expect a seamless tax-free transition for INUV shareholders with INUV ending trading on one day and ConversionPoint opening trading the next day under a new ticker.

The reason for the merger is not only synergies between the two company's technologies and capabilities which complement each other and create additional revenue at minimal cost, but an arbitrage on valuation between the two. Here we encounter the difference in private and public company valuations and positioning. Inuvo is being purchased by ConversionPoint for approximately one times sales, while ConversionPoint has been valued at many times that due to its growth rate and its market positioning as an eCommerce platform compared with high flyers like Shopify (SHOP), LiveRamp (RAMP) and The Trade Desk (TTD.)

We know little about ConversionPoint Technologies' financials at this point we do know it was recently valued at $146 million in a $15 million private company round and it generated $50 million in sales in 2017 and is rapidly growing. If we guesstimate it is doing $75 million this year that is twice sales and twice the valuation metric used for Inuvo which has been offered approximately one times it sales. The combined company hopes to emerge on the public markets repositioned as a comp to Shopify, LiveRamp and The Trade Desk, all of which trade over ten times enterprise value to estimated 2018 sales. Should the merger be successful, there should be considerable upside for investors. Even at two times sales, at a $300 million enterprise value and 22 million shares outstanding, that would be a $13.64 per share. Keep in mind that as part of the transaction the combined company seeks to raise $36 million which is a requirement for the deal to close and will slightly dilute current shareholders. Inuvo will do a filing in the next few weeks that will provide financials on ConversionPoint including pro formas. The deal is expected to close in Q1 of 2019.

ConversionPoint describes itself as an eCommerce technology company changing how brands, advertisers, and agencies connect with, acquire, and retain customers. Powered by AI-enabled media optimization, CRM, and robust post-purchase platforms that automate product delivery and remarketing, ConversionPoint offers proprietary technologies to increase conversions, lifetime customer value, and return on ad spend. ConversionPoint focuses on the non-Amazon channels, including Walmart.com, Shopify.com, and BigCommerce.com. Management has identified a number of specific near-term opportunities by combining with Inuvo, including upselling Inuvo's high-margin AI powered IntentKey media to ConversionPoint's existing enterprise customers and online retail partners, as well as integrating ValidClick and creating a new traffic acquisition source for them.

Q3 2018 Results Show Sharp Decline in its Publisher Business

Q3 revenue disappointed as the company saw a sharper drop off in the supply, or publisher side of its business than it expected. The company has been deemphasizing this segment as it is not important to its long-term strategy, especially in light of the pending acquisition and has instead been directing

resources to grow its higher-margin demand business with the IntentKey. In addition, the prices paid per click by Yahoo have fallen off in the quarter and have not recovered. The company reported revenues of $16.8 million down 17% from the $20.3 million reported a year ago.

Margins improved versus last year with gross margin before marketing expense again at 63% the same as in Q2 and up from 52.5% a year ago. After marketing spend, the margin declined significantly to 13.8% versus 17.3% and 18.8% last quarter.

Expenses increased to $12.0 million versus $11.6 million a year ago, and operating losses increased to $1.3 million versus $0.9 million. Head count increased to 68 from 64 last quarter and 92 at the end of March.

The GAAP net loss for the quarter was $1.4 million versus $1.0 million a year ago. GAAP EPS loss was $0.04 vs. $0.03, but on a non-GAAP basis the loss was $0.04 versus $0.02 last year.

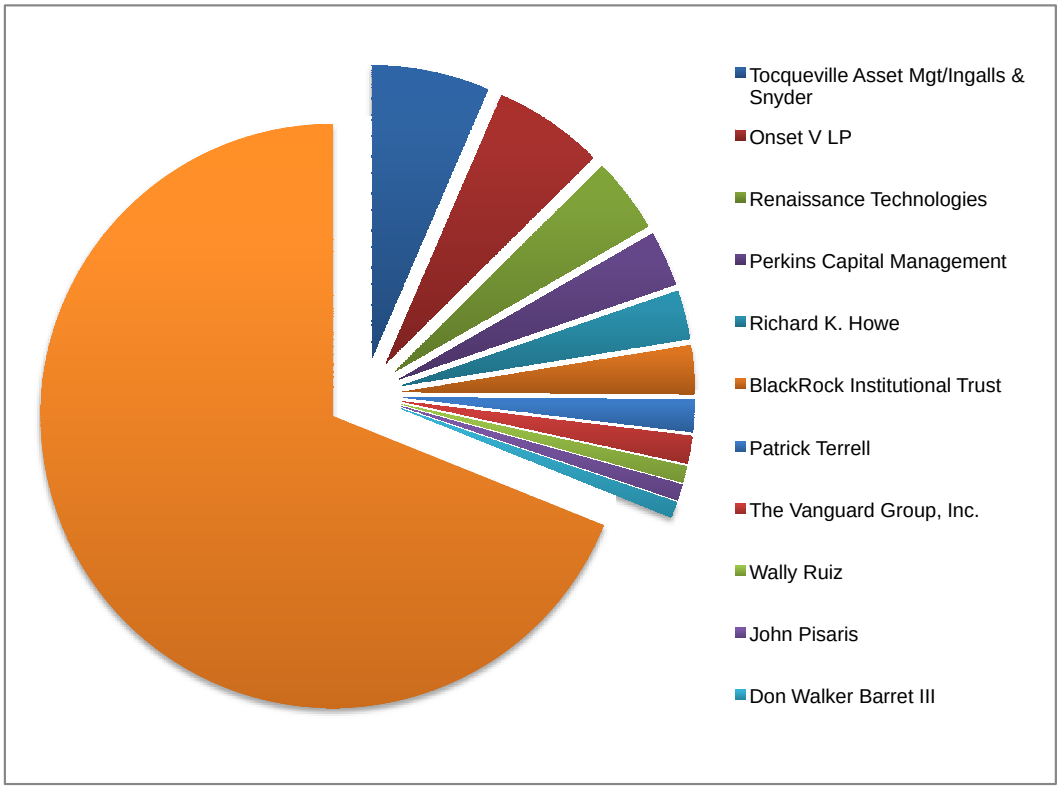
EBITDA for the quarter was a loss of $386,000 versus a positive $253,000 a year ago. For the first nine months of the year EBITDA was a loss of $195,000 versus a loss last year of $243,000.

RISKS

- While Inuvo has accepted an offer to be acquired, it is contingent upon the ability of the combined company to raise $36 million in conjunction with the merger as well as other approvals.
- There are few barriers to entry in the advertising network business and it typically operates with slim margins with competition mainly on price. Recently the industry has been consolidating.
- Prices paid to Inuvo by Yahoo! dropped in September and have not yet recovered. Yahoo is responsible for 70% of Inuvo's revenues.
- The company's growth is dependent on the success of new products that may not be adopted by new customers as well as integration with its merger partner.
- The digital ad business is very competitive and there is far more inventory of ad space than is needed. There could be continued price pressure that would lower click rates going forward. Much of the ad inventory in the US goes unsold; more inventory could exacerbate this supply-demand imbalance. Thus, Inuvo may have to increase volume of ads sold just to maintain revenues.
- Privacy regulations keep changing, especially in Europe and the company and its competitors have had to adapt to changes, which alters the competitive landscape and how it does business.

OWNERSHIP

Charles D. Morgan owns 2 million of the shares of the Tocqueville Asset Management position that at Ingalls and Snyder. Onset V was the venture capitalist owner of NetSeer, and still owns 2.2 million shares of Inuvo.



INCOME STATEMENT

Inuvo	Q1 2017 31-Mar	Q2 2017 30-Jun	Q3 2017 30-Sep	Q4 2017 31-Dec	Q1 2018 31-Mar	Q2 2018 30-Jun	Q3 2018 30-Sep	Q4 2018E 31-Dec	2016	2017	2018E	2019E
Total revenue	**$17.2**	**$18.3**	**$20.3**	**$23.8**	**$20.5**	**$19.0**	**$16.8**	**$18.0**	**$71.5**	**$79.6**	**$74.3**	**$84.0**
Yr-to-yr Growth	-8%	17%	16%	21%	19%	4%	-17%	-24%	2%	11%	-7%	13%
Total Cost of services	7.9	7.6	9.6	11.5	8.8	7.0	6.2	6.7	21.4	36.7	28.6	31.5
Gross profit	9.3	10.7	10.7	12.2	11.7	12.0	10.6	11.3	50.2	42.9	45.7	52.5
Gross Margin %	54%	58%	52.5%	51.6%	57%	63%	63%	63%	70%	54%	61%	63%
Operating expenses:												
Marketing	6.5	7.5	7.2	7.5	8.3	8.4	8.3	8.6	39.2	28.6	33.6	40.0
Profit after marketing of Digital Publishing	2.9	3.2	3.5	4.8	3.4	3.6	2.3	2.7	6.2	14.3	12.1	12.5
Margin %	16.6%	17.3%	17.2%	20.2%	16.7%	18.8%	13.8%	15.2%	14%	18%	16%	15%
Compensation	2.4	2.3	2.4	3.1	2.6	2.3	1.8	1.8	6.8	10.2	8.5	7.2
SG&A	2.1	2.2	2.0	2.0	2.1	2.0	1.9	1.9	5.0	8.3	7.8	7.5
Total operating expenses	11.0	12.0	11.6	12.6	13.0	12.8	12.0	12.3	51.0	47.1	50.0	54.7
Operating income:	(1.6)	(1.3)	(0.9)	(0.4)	(1.3)	(0.7)	(1.3)	(0.9)	(0.9)	(4.2)	(4.3)	(2.2)
Operating margin	-9.6%	-7.2%	-4.4%	-1.6%	-6.4%	-3.9%	-8.0%	-5.2%	-1.2%	-5.3%	-5.8%	-2.6%
Other income:												
Interest expense, net	(0.0)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.3)	(0.4)	(0.4)
Total other income	(0.0)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.3)	(0.4)	(0.4)
Income before income taxes	(1.7)	(1.4)	(1.0)	(0.5)	(1.4)	(0.8)	(1.4)	(1.0)	(1.0)	(4.6)	(4.7)	(2.6)
Pretax Margin	-9.8%	-7.6%	-4.9%	-2.1%	-6.9%	-4.4%	-8.6%	-5.8%	-1.3%	-5.7%	-6.4%	-3.1%
Income tax benefit	-	-	-	(1.5)	(0.0)	(0.0)	-	-	(0.0)	(1.5)	(0.0)	-
Tax rate	0%	0%	0%	9%	1%	0%	0%	9%	3.1%	32.9%	0.0%	0.0%
Net income from continuing operations	(1.7)	(1.4)	(1.0)	1.0	(1.4)	(0.8)	(1.4)	(1.0)	(0.9)	(3.1)	(4.7)	(2.6)
Net income from discontinued operations	(0.0)	-	-	-	-	-	-	-	0.2	(0.0)	-	-
Net income	(1.7)	(1.4)	(1.0)	1.0	(1.4)	(0.8)	(1.4)	(1.0)	(0.8)	(3.1)	(4.7)	(2.6)
Stk based compensation	0.3	0.3	0.3	0.4	0.4	0.3	0.3	0.4	1.3	1.3	1.3	1.3
One-time expenses	0.4	0.4	-	(1.5)	-	-	-	-	(0.0)	(0.8)	-	-
Non-GAAP Income from continuing	(1.0)	(0.6)	(0.6)	(0.1)	(1.0)	(0.5)	(1.2)	(0.7)	0.3	(2.6)	(3.4)	(1.3)
Net income per share:												
Basic EPS	(0.06)	(0.05)	(0.03)	0.04	(0.05)	(0.03)	(0.04)	(0.03)	(0.04)	(0.11)	(0.15)	(0.08)
Fully diluted EPS	(0.06)	(0.05)	(0.03)	0.03	(0.05)	(0.03)	(0.04)	(0.03)	(0.04)	(0.11)	(0.15)	(0.08)
Non-GAAP Diluted	**(0.04)**	**(0.02)**	**(0.02)**	**(0.00)**	**(0.04)**	**(0.02)**	**(0.04)**	**(0.02)**	**0.01**	**(0.09)**	**(0.11)**	**(0.04)**
	-233.3%	125.5%	368.9%	300.2%	-6.7%	-21.5%	58.1%	340.7%	-88%	-766%	21%	-64%
Shares												
Basic	27.0	28.5	28.6	28.6	28.7	30.6	32.3	32.4	24.6	28.2	31.0	32.4
Diluted	27.2	28.7	28.8	28.7	28.7	30.6	32.3	32.4	24.7	28.3	31.0	32.4
	10.8%	16.8%	16.4%	15.1%	5.2%	6.7%	12.4%	13.0%	0.6%	14.8%	9.4%	4.6%

BALANCE SHEET

	Sept 30, 2018	June 30, 2018	Qtr-Qtr % Change	Sept 30, 2017	Yr-Yr % Change
Current assets					
Cash	$4,190,274	$4,117,338	2%	$2,901,965	44%
Accounts receivable, net	5,614,031	7,587,429	-26%	9,976,903	-44%
Prepaid expenses and other current assets	307,256	380,075	-19%	347,707	-12%
Total current assets	10,111,561	12,084,842	-16%	13,226,575	-24%
Property and equipment, net	2,260,967	2,359,696	-4%	2,233,183	1%
Other assets					
Goodwill	9,853,342	9,853,342	0%	9,773,842	1%
Intangible assets, net of accumulated amortization	9,779,307	10,116,933	-3%	11,319,044	-14%
Other assets	35,171	35,170	0%	96,070	-63%
Total other assets	19,667,820	20,005,445	-2%	21,188,956	-7%
Total assets	32,040,348	34,449,983	-7%	36,648,714	-13%
Current liabilities					
Accounts payable	9,021,255	10,262,768	-12%	11,761,983	-23%
Accrued expenses and other current liabilities	2,456,831	2,973,153	-17%	2,936,116	-16%
Revolving credit line - current portion	4,825,000	**4,000,000**	21%	5,000,000	-4%
Total current liabilities	16,303,086	17,235,921	-5%	19,698,099	-17%
Long-term liabilities					
Deferred tax liability	2,331,900	2,331,900	0%	3,738,500	-38%
Other long-term liabilities	250,959	306,163	-18%	485,405	-48%
Total long-term liabilities	2,582,859	2,638,063	-2%	4,223,905	-39%
Total Liabilities	18,885,945	19,873,984	-5%	23,922,004	-21%
Stockholder's equity					
Total stockholders' equity	13,154,403	14,576,049	-10%	12,726,710	3%
Total liabilities and stockholders' equity	$32,040,348	$34,450,033	-7%	$36,648,714	-13%
Quick Ratio	0.6	0.7	-12%	0.7	-8%
Working Capital	(6,191,525)	(5,151,079)	20%	(6,471,524)	-4%
Net cash	(634,726)	117,338	-641%	(2,098,035)	-70%
Net cash as % of assets	-2%	0%	-682%	8%	-125%
Net cash per share	-$0.02	$0.00	-611%	$0.12	-117%
Debt % of assets	16%	12%	36%	15%	6%

CASH FLOW

	Year 2016	3 Mo. Ended 3/31/17	3 Mo. Ended 6/30/17	3 Mo. Ended 9/30/17	3 Mo. Ended 12/31/17	Year 2017	3 Mo. Ended 3/31/18	3 Mo. Ended 6/30/18	3 Mo. Ended 9/30/18
Operating activities:									
Net income	(772,584)	(1,693,054)	(1,382,371)	(986,170)	1,003,895	(3,057,700)	(1,408,024)	(832,697)	(1,441,650)
Adjustments to reconcile net income to net cash provided by operating activities:									
Settlement of tax liability	-	-	-	-	-	-	-	-	-
Depreciation and amortization	2,209,738	693,175	741,692	804,631	790,303	3,029,801	791,644	785,416	794,898
Deferred income taxes	(61,100)	-	-	-	(1,406,600)	(1,406,600)	-	-	-
Amortization of financing fees	25,600	6,400	6,400	6,400	6,400	25,600	6,400	6,400	6,400
Adjustment of European liabilities related to discontinued operations	(176,988)	1,109	-	-	-	1,109	-	-	-
Provision of doubtful accounts	5,800	-	141,000	(2,211)	(78,000)	60,789	-	(10,062)	(30,000)
Stock based compensation	1,264,266	292,334	293,825	336,913	356,735	1,279,807	377,847	289,950	159,798
Write-off of publisher payable	-	-	-	-	315,137	315,137		-	-
Change in operating assets and liabilities:									
Accounts receivable and unbilled revenue	(583,082)	2,740,326	(680,496)	(2,296,908)	(979,533)	(1,216,611)	3,300,989	(120,808)	2,003,398
Prepaid expenses and other assets	219,656	109,577	(124,826)	96,734	(28,798)	52,687	98,015	(89,799)	66,418
Accounts payable	(622,548)	(2,844,928)	(583,470)	2,328,706	1,536,933	437,241	(2,498,865)	(923,249)	(1,170,684)
Accrued expenses and other liabilities	(420,875)	(989,738)	434,059	(411,874)	298,012	(669,541)	(38,910)	111,515	(518,462)
Other, net	(34,864)	-	-	-	-	-	-	-	-
Net cash used by operating activities	1,053,019	(1,684,799)	(1,154,187)	(123,779)	1,814,484	(1,148,281)	629,096	(783,334)	(129,884)
Investing activities:									
Purchases of equipment and capitalized development costs	(1,116,371)	(151,424)	(469,274)	(442,113)	(495,882)	(1,558,693)	(514,065)	(427,571)	(358,543)
Net cash from NetSeer Asset Acquisition	-	235,763	-	-	-	235,763	-	-	-
Net cash used in investing activities	(1,116,371)	84,339	(469,274)	(442,113)	(495,882)	(1,322,930)	(514,065)	(427,571)	(358,543)
Financing activities:									
Proceeds from sale of common stock	-	-	-	-	-	-	-	2,134,162	(133,579)
Payoff of NetSeer debt acquired	-	(2,015,577)	-	-	-	(2,015,577)	-	-	-
Payments on capital leases	-	-	-	-	(158,782)	(158,782)	(53,839)	(51,747)	105,586
Deposit to collateralize letter of credit	-	-	-	-	-	-	-	-	-
Prepaid financing fees and other	25,600	-	-	-	25,600	25,600	-	-	-
Net taxes paid on RSU grants exercised	(203,836)	-	-	(97,376)	-	(97,376)	-	-	(77,044)
Proceeds from revolving line of credit	7,950,000	3,600,000	1,400,000	-	(100,000)	4,900,000	-	-	(75,000)
Payments on revolving line of credit	(7,950,000)	-	-	-	-	-	-	(900,000)	900,000
Payments on term note payable and capital leases	(46,313)	(7,250)	(19,345)	(70,705)	97,300	-	-	-	(158,650)
Treasury stock repurchase	(22,499)	-	-	(44,772)	-	(44,772)	-	-	-
Net cash used in financing activities	(247,048)	1,577,173	1,380,655	(212,853)	(135,882)	2,609,093	(53,839)	1,182,415	589,306
Effect of exchange rate changes	-	-	-	-	-	-	-	-	-
Net change - cash	(310,400)	(23,287)	(242,806)	(778,745)	1,182,720	137,882	61,192	(28,490)	100,879
Cash, beginning of quarter	3,974,793	3,946,804	3,923,517	3,680,711	2,901,966	3,946,804	4,084,686	4,145,878	4,117,388
Cash, end of period	3,664,393	3,923,517	3,680,711	2,901,966	4,084,686	4,084,686	4,145,878	4,117,388	4,218,267
Supplemental information:									
Interest paid	72,751	25,317	79,745	75,734	88,164	268,960	94,428	89,466	103,480
NetSeer stock issuance	-	4,459,244	-	-	-	4,459,244	-	-	-
Writedown of domain names and cont. liab.	-	222,477	-	-	147,029	369,506	-	-	-
Income taxes paid	26,000	-	-	-	-	-	-	-	-
Purchase of property and equipment under capital lease	-	-	-	523,518	6,889	530,407	-	-	-
Purchase of intangible assets through a contingent liability	-	-	-	-	-	-	-	-	-
Stock issuance for partial settlement of cont. liability *	300,001	-	-	-	-	-	-	-	-
Write down of domain names due to partial settlement of cont. liability	46,367	-	-	-	-	-	-	-	-
Operating Cash Flow	2,494,732	(700,036)	(199,454)	159,563	987,870	247,943	(232,133)	239,007	(510,554)
Free cash flow	1,378,361	(851,460)	(668,728)	(282,550)	491,988	(1,310,750)	(746,198)	(188,564)	(869,097)
Adjusted EBITDA	2,622,669	(663,000)	166,847	252,690	758,130	1,069,601	(145,348)	336,245	(385,786)

HISTORICAL STOCK PRICE



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