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Zacks Small-Cap Research

Sponsored – Impartial - Comprehensive

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Net Element Inc. (NASDAQ: NETE)

LOI to Reverse Merge With Mullen Technologies

Using the lowest peer valuation of 1.2x EV/2020 estimated sales, the stock would be worth $15.80 per share.

Current Price (06/15/20)	$6.90
Valuation	**$15.80**

OUTLOOK

Net Element signed a LOI for a reverse merger with Mullen Technologies, distributor of Qiantu Motors' EV cars, and plans to divest its payment processing businesses. These businesses provide software and services to merchants for global online and mobile payments. NETE operates a merchant processor in the US with an attractive merchant offering using its Aptito front-end solution and its Netevia payments platform. It is also an international payment processor, operating primarily in Russia. NETE has been greatly effected by the shut down of restaurants and storefronts as more than half of customers come from these industries.

SUMMARY DATA

52-Week High	**$6.90**
52-Week Low	**$1.56**
One-Year Return (%)	**77.8**
Beta	**1.6**
Average Daily Volume (sh)	**2,630,300**
Shares Outstanding (mil)	**4.1**
Market Capitalization ($mil)	**$29**
Short Interest Ratio (days)	**1.2**
Institutional Ownership (%)	**7**
Insider Ownership (%)	**19**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**16.1**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/M**
P/E using 2020 Estimate	**N/M**
P/E using 2021 Estimate	**N/M**

Risk Level	**Above Average**
Type of Stock	**Small Growth**
Industry	**Internet Commerce**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2018	16.0 A	16.5 A	17.2 A	16.1 A	65.8 A
2019	15.0 A	16.5 A	16.8 A	16.6 A	65.0 A
2020	15.8 A	10.7 E	12.8 E	15.0 E	54.4 E
2021					68.0 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2018	-$0.40 A	-$0.23 A	-$0.23 A	-$0.22 A	-$1.07 A
2019	-$0.28 A	$0.11 A	-$0.24 A	-$0.35 A	-$0.76 A
2020	-$0.32 A	-$0.94 E	-$0.45 E	-$0.19 E	-$1.72 E
2021					-$0.87 E

Zacks Projected EPS Growth Rate - Next 5 Years % **5.0**

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WHAT'S NEW

Net Element Announces LOI for Reverse Merger with Mullen Technologies, Maker of Electric Vehicles

This morning Net Element announced a Letter of Intent (LOI) for a triangular reverse merger with Mullen Technologies a private company based in California. The survivor company will be named Mullen Technologies, the ticker will be changed, and the payment processing business is to be sold. Mullen was expected to be a highly anticipated IPO but management decided that the cost of, and the time it would take to IPO, was too much compared with a reverse merger solution. This proposed transaction would allow Mullen to be public this year and then raise capital in a secondary transaction to support its plans. Mullen Technologies plans to sell Qiantu Motors' electric vehicles. Qiantu is a Chinese manufacturer that is a subsidiary of CH Auto based in Beijing. It already sells vehicles in China. Mullen has an agreement to sell those vehicles in the US and plans to assemble them here. It needs capital to pay for an assembly plant. Mullen is expected to deliver its first vehicle, the Dragonfly K50, in Q2 2021.

Figure 1. Dragonfly K50 at the NY International Auto Show 2019



Source: Shutterstock

Last year Mullen announced plans to assemble its Qiantu K50 electric sports car on the West Plains in Washington State, but that agreement expired on March 31. According to S3R3 Solutions, the public development authority that recruited Mullen Technologies to the region, Mullen needs $56 million for a deposit but expects to raise a total of about $1.3 billion in capital for the project. It believes Mullen hopes to be granted a $450 million loan from the Department of Energy, raise $450 million in private funding, and is exploring tax credits and opportunity zone funding as well.

The management of the remaining company will be from Mullen but Oleg Firer, CEO of Net Element, would remain on the board. Should this move forward after due diligence, and upon reaching a definitive agreement, the company will file a proxy statement and S-4 to gain approval from shareholders.

Mullen Technologies was founded in 2014 and is based in Brea, California. David Michery formerly of music production fame runs it. It currently sources cars from its Chinese OEM partner Qiantu Motor. Mullen currently has eight car dealerships in California and another in Arizona where it sells a variety of cars and showrooms its K50. It also owns CarHub, a platform that leverages AI for a solution for buying, selling, and owning a car. Early in 2020, the company launched Mullen Funding Corp. to provide direct auto financing and lease options for new and pre-owned Mullen vehicles. In April, Mullen Technologies began making portable ventilators out of its battery R&D center in Monrovia, CA. These units are expected to be available for delivery shortly to fulfill contracts already won.

Mullen Technologies is rumored to be highly valued based both on its business prospects and it intellectual property. It has valuable lithium battery patents to create batteries rivaling Tesla's technology. It has a joint venture with Ukrainian company NextMetals Ltd. to create a solid-state battery under a new division called "Mullen Next."

Net Element shareholders are expected to own 15% of the surviving company. If Mullen can reach revenues of $100 million in the next 24 months, it is entitled to another 5% of the shares leaving Net Element shareholders with 10%. If revenue is less than $80 million, then the Net Element shareholders will get another 5% leaving Mullen shareholders with 80% of the fully diluted common shares of the company.

At Net Element's current enterprise value of $37 million (using a $6.90 stock price) this puts the entire valuation of Mullen Technologies at $248 million, far less than we expect it is currently valued in the private market. We will get financial information on the privately held Mullen once the S-4 is filed.

We expect this transaction to be completed at the earliest in Q3 2019, and will update investors when more information is provided when the upcoming the S-4 is filed or when Q2 is reported.

INVESTMENT THESIS

- Net Element is in the process of a reverse merger and has plans to sell off its payment processing business. If the deal goes according to plan, Net Element shareholders will own 15% of the survivor company.

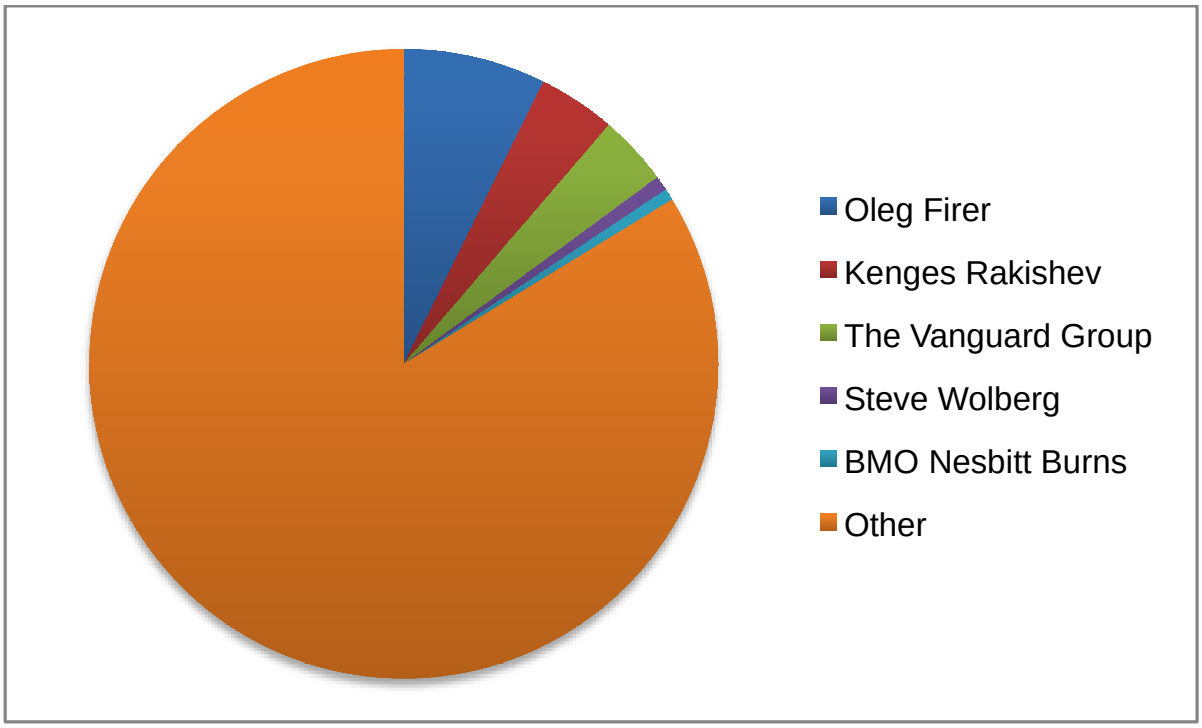
- Mullen Technologies is an electric car vendor that is raising money to build an assembly plant in the US for cars that are already being produced and sold in China. Its first model is expected to be delivered in the US in the first half of 2021. This transaction should make the required capital raising process faster, less costly, and require less regulatory approval.

- The S-4 will provide more information allowing investors to see the inherent value of Mullen and could compel the stock price higher.

RISKS

- The proposed transaction may not occur as neither company has yet done due diligence. Nor have shareholders approved the deal.
- The survivor company may not be valued very highly by investors due to the high risk in the venture.
- If the deal does not go through, the stock may fall to pre-deal levels and given the affect of the pandemic on Net Elements' business, the stock may even decline from those levels.
- US relations with China could impede the success of Mullen Technologies given its reliance on a China based company. Tariffs with China have changed and could change again.

OWNERSHIP



Source: Zacks Investment Research, SEC filings

INCOME STATEMENT

	Q1 2019 31-Mar	Q2 2019 30-Jun	Q3 2019 30-Sep	Q4 2019 31-Dec	Q1 2020 31-Mar	Q2 2020E 30-Jun	Q3 2020E 30-Sep	Q4 2020E 31-Dec	2018	2019	2020E	2021E
North America Transaction	$14.4	$15.7	$15.9	$15.8	$15.2	$10.0	$12.0	$14.0	$59.1	$61.8	$51.16	$63.00
Yr-over-yr Growth	2.8%	9.1%	2.1%	3.9%	5.5%	-36.5%	-24.6%	-11.1%	15.6%	4.5%	-17.2%	23.1%
Cost of service	11.8	13.4	13.4	13.8	12.8	8.7	10.4	11.9	50.5	52.4	43.8	53.6
Gross margin	2.6	2.3	2.5	2.0	2.3	1.3	1.6	2.1	8.6	9.4	7.3	9.5
Gross margin %	18.1%	14.6%	15.8%	12.6%	15.4%	13.0%	13.3%	15.0%	14.5%	15.2%	14.3%	15.0%
International	0.684	0.7	0.9	0.9	0.7	0.7	0.8	1.0	6.6	3.2	3.2	5.0
Yr-over-yr Growth	-66.1%	-63.4%	-45.8%	-4.5%	0.0%	-3.9%	-10.7%	12.0%	-25.5%	-51.5%	-0.6%	56.1%
International Cost of Service	0.5	0.5	0.7	0.7	0.5	0.5	0.6	0.7	5.1	2.3	2.3	3.4
Gross Margin	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.3	1.6	0.9	0.9	1.7
Gross margin %	28.1%	39.0%	25.8%	20.2%	30.3%	30.6%	25.0%	28.0%	23.7%	27.8%	28.3%	33.0%
Total revenues	**15.0**	**16.5**	**16.8**	**16.6**	**15.8**	**10.7**	**12.8**	**15.0**	**65.8**	**65.0**	**54.4**	**68.0**
Yr-to-yr Growth	-5.9%	0.1%	-2.5%	3.4%	5.3%	-35.0%	-23.9%	-9.9%	9.5%	-1.2%	-16.4%	25.1%
Costs and expenses:												
Cost of revenues	12.3	13.9	14.1	14.5	13.3	9.2	11.0	12.6	55.6	54.7	46.1	56.9
Gross Margin	2.8	2.6	2.7	2.2	2.5	1.5	1.8	2.4	10.2	10.3	8.2	11.1
% of Sales	18.5%	15.7%	16.3%	13.0%	16.0%	14.2%	14.1%	15.9%	15.5%	15.8%	15.2%	16.3%
SG&A	2.4	2.3	2.4	2.3	2.3	2.0	2.0	2.1	9.8	9.3	8.4	10.0
Stock-based compensation	0.0	2.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	2.1	0.1	1.0
Provision for loan losses	0.3	0.1	0.4	0.4	0.4	2.0	1.0	0.2	2.1	1.4	3.6	1.2
Depreciation and amortization	0.9	0.7	0.8	0.8	0.8	0.7	0.7	0.7	2.5	3.1	2.9	2.8
Total operating expenses	3.6	5.2	3.6	3.5	3.6	4.7	3.7	3.0	14.5	15.9	15.1	15.0
Loss from operations	(0.8)	(2.6)	(0.9)	(1.3)	(1.0)	(3.2)	(1.9)	(0.6)	(4.3)	(5.6)	(6.8)	(3.9)
Loss from operations ex-one time	(0.8)	(0.6)	(0.9)	(1.3)	(1.0)	(3.2)	(1.9)	(0.6)	(4.3)	(5.6)	(6.8)	(3.9)
Interest expense, net	(0.2)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)	(0.8)	(1.1)	(1.4)	(1.4)
Other expense	(0.1)	1.3	0.1	0.2	0.0	0.0	0.0	0.0	0.8	1.5	0.0	0.0
One-time charges	0.0	0.0	0.0	(1.3)	0.0	0.0	0.0	0.0	(0.6)	(1.3)	0.0	0.0
Total non-operating expenses	(0.3)	1.0	(0.2)	(1.5)	(0.3)	(0.3)	(0.3)	(0.3)	(0.7)	(1.0)	(1.4)	(1.4)
Pretax operating income (loss)	(1.1)	(1.6)	(1.0)	(2.8)	(1.4)	(3.6)	(2.3)	(1.0)	(5.0)	(6.6)	(8.2)	(5.3)
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	(1.1)	(1.6)	(1.0)	(2.8)	(1.4)	(3.6)	(2.3)	(1.0)	(5.0)	(6.6)	(8.2)	(5.3)
Minority interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1
Net loss to common stock	(1.1)	(1.5)	(1.0)	(2.8)	(1.4)	(3.5)	(2.3)	(0.9)	(4.9)	(6.5)	(8.2)	(5.3)
Foreign currency translation gain (loss)	(0.0)	(0.0)	0.0	(0.0)	0.1	0.0	0.0	0.0	0.3	(0.0)	0.1	0.0
Comprehensive loss	(1.1)	(1.5)	(1.0)	(2.8)	(1.2)	(3.5)	(2.3)	(0.9)	(4.6)	(6.5)	(8.2)	(5.3)
Earnings ex-one time charge	(1.1)	(1.5)	(1.0)	(1.5)	(1.4)	(4.6)	(2.3)	(0.9)	(4.3)	(5.1)	(8.2)	(5.3)
Stock-based compensation	0.0	2.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	2.1	0.1	1.0
Adjusted Non-GAAP Earnings	(1.1)	0.5	(1.0)	(1.4)	(1.3)	(4.6)	(2.2)	(0.9)	(4.2)	(3.1)	(8.2)	(4.3)
Yr-to-yr Growth	-27.7%	-153.2%	12.1%	68.3%	20.1%	-1089.7%	124.9%	-35.1%	-40%	-26%	164.9%	-47.4%
GAAP EPS	($0.29)	($0.37)	($0.24)	($0.68)	($0.33)	($0.71)	($0.45)	($0.19)	($1.28)	($1.60)	($1.73)	($1.07)
Non-GAAP EPS	**($0.28)**	**$0.11**	**($0.24)**	**($0.35)**	**($0.32)**	**($0.94)**	**($0.45)**	**($0.19)**	**($1.07)**	**($0.76)**	**($1.72)**	**($0.87)**
Yr-to-yr Growth	-29%	-149%	5%	58%	13.5%	-938.4%	88.4%	-46.2%	-69.7%	-29.1%	125.3%	-49.6%
Share outstanding	3.9	4.2	4.2	4.1	4.1	5.0	5.0	5.0	3.9	4.0	4.8	5.0
Yr-to-yr Growth	1%	9%	6%	6%	5.8%	18.0%	19.4%	20.6%	96.6%	4.5%	17.6%	4.3%
Fully diluted shares	3.9	4.2	4.2	4.1	4.1	4.1	4.1	4.1	4.8	4.0	4.1	4.1
Yr-to-yr Growth	-19%	-13%	-15%	-16%	0.0%	0.0%	0.0%	0.0%	120.1%	-16.7%	0.0%	17.5%

BALANCE SHEET

	Mar 31, 2020	Dec 31, 2019	Qtr-Qtr % Change	Mar. 31, 2019	Yr- Yr % Change
Current assets:					
Cash	**$606,672**	**$486,604**	25%	**$476,989**	27%
Accounts receivable, net	4,021,585	6,560,928	-39%	5,134,505	-22%
Prepaid expenses and other assets	1,300,316	1,621,144	-20%	1,426,214	-9%
Total current assets	5,928,573	8,668,676	-32%	7,037,708	-16%
Equipment, net	0	3,773	-100%	21,853	-100%
Intangible assets, net	5,348,652	5,678,649	-6%	6,330,652	-16%
Goodwill	7,681,186	7,681,186	0%	9,007,752	-15%
Operating lease right-of-use asset	349,036	380,986	-8%	471,307	-26%
Other long term	654,897	629,651	4%	654,754	0%
Total assets	19,962,344	23,042,921	-13%	23,524,026	-15%
Current liabilities:					
Accounts payable	$4,509,311	$6,041,606	-25%	$5,301,425	-15%
Deferred revenue	2,001,091	1,401,117	43%	972,650	106%
Accrued expenses	930,912	1,800,344	-48%	2,753,464	-66%
Notes payable (current portion)	**909,086**	**909,086**	0%	**330,749**	175%
Operating lease liability (current portion)	101,777	133,727	-24%	90,321	13%
Due to related parties	**75,355**	**126,662**	-41%	**271,972**	-72%
Total current liabilities	8,527,532	10,412,542	-18%	9,720,581	-12%
Operating lease liability (net of current)	247,259	247,259	0%	380,986	-35%
Notes payable (non-current portion)	**8,352,627**	**8,342,461**	0%	**5,960,361**	40%
Total liabilities	17,127,418	19,002,262	-10%	16,061,928	7%
STOCKHOLDERS' DEFICIT					
Common stock	412	410	0%	386	7%
Paid in capital	185,337,965	185,297,069	0%	183,261,238	1%
Accumulated other comp income (loss)	(2,143,374)	(2,274,187)	-6%	(2,246,724)	-5%
Accumulated deficit	(180,116,849)	(178,750,634)	1%	(173,413,099)	4%
Noncontrolling interest	(243,227)	(231,999)	5%	(139,703)	74%
Total stockholders' deficit	2,834,927	4,040,659	-30%	7,462,098	-62%
Total liabilities and stockholders' deficit	19,962,345	23,042,921	-13%	23,524,026	-15%
Net Cash	606,672	486,604	25%	476,989	27%
Current and Quick Ratio	0.7	0.8	-16%	0.7	-4%
Working Capital	(2,598,959)	(1,743,866)	49%	(2,682,873)	-3%
Total Debt	9,337,068	9,378,209	0%	6,563,082	42%
Debt/TA	47%	41%	15%	28%	68%
DSO	23.2	36.1	-36%	31.1	-25%

CASH FLOWS

	YR 2018	Mar. 31, 2019 3 month	June 30, 2019 3 month	Sept 30, 2019 3 month	Dec. 31, 2019 3 month	YR 2019	Mar. 31, 2020 3 month
Cash flows from operating activities							
Net loss	$ (4,936,182)	$ (1,120,847)	$ (1,537,445)	$ (1,010,629)	$ (2,789,461)	$ (6,458,382)	$ (1,366,216)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:							
Non controlling interest	(86,551)	(13,966)	(40,225)	(28,783)	(23,287)	(106,261)	(11,228)
Share based compensation	142,017	15,006	2,005,841	15,008	15,007	2,050,862	38,400
Deferred revenues	(216,742)	(523,199)	(523,199)	494,832	456,834	(94,732)	(470,205)
Net non cash items in other income	(1,202,201)	-	-	-	-	-	-
Impairment for goodwill	636,000	-	-	-	1,326,566	1,326,566	-
Depreciation and amortization	2,454,637	851,220	747,347	755,985	765,691	3,120,243	779,443
Non cash interest	73,442	14,314	7,397	14,972	20,192	56,875	12,294
(Recovery of) provision for loan losses	16,238	10,013	(18,940)	8,927	(9,226)	(9,226)	485
Changes in assets and liabilities, net of acquisitions and the effect of consolidation of equity affiliates							
Account receivable	(1,503,755)	1,151,285	13,976	(423,880)	(1,005,139)	(263,758)	2,520,395
Prepaid expenses and other assets	384,403	253,634	415,012	(442,293)	(358,571)	(132,218)	364,019
Accounts payable and accrued expenses	971,202	(875,266)	(1,429,936)	(182,855)	3,058,618	(1,642,618)	(1,419,019)
Net cash (used in) provided by operating	(3,267,492)	(237,806)	(360,172)	(798,716)	(755,955)	(2,152,649)	448,368
Cash flows from investing activities							
Purchase of portfolio and client acquisition	(5,413,264)	(651,365)	(558,913)	(412,204)	(691,180)	(2,313,662)	(427,031)
Purchase of fixed and other assets	(114,931)	(413,132)	(55,155)	4,659	325,628	(138,000)	6,049
Net cash used in investing activities	(5,528,195)	(1,064,497)	(614,068)	(407,545)	(365,552)	(2,451,662)	(420,982)
Cash flows from financing activities							
Proceeds from indebtedness	2,131,500	-	1,116,500	920,184	997,816	3,034,500	155,206
Repayment of indebtedness	(2,785,134)	(102,700)	(106,384)	(110,204)	156,841	(162,447)	(145,040)
Lease liability	-	471,307	(29,213)	(30,098)	-	380,986	(31,950)
Related party advances (payments)	-	(171,615)	338,176	85,942	(50,032)	202,471	133,743
Net cash provided by (used in) financing	(653,634)	196,992	1,319,079	865,824	1,073,615	3,455,510	111,959
Effect of exchange rate changes on cash	(34,399)	(12,497)	18,768	(6,555)	15,789	15,505	5,969
Net increase in cash	(9,483,720)	(1,117,808)	363,607	(346,992)	(32,103)	(1,133,296)	145,314
Cash at beginning of period	11,733,271	2,249,551	1,131,743	1,495,350	1,148,358	2,249,551	1,116,255
Cash at end of period	2,249,551	1,131,743	1,495,350	1,148,358	1,116,255	1,116,255	1,261,569
Cash paid during the period for:							
Interest	773,737	230,789	245,135	255,069	-	730,993	336,120
Taxes	61,871	46,932	56,909	16,703	-	120,544	-
Operating cash flow	(3,119,342)	(767,459)	640,776	250,312	(237,684)	(114,055)	(1,017,027)
Free cash flow	(8,647,537)	(1,831,956)	26,708	(157,233)	(603,236)	(2,565,717)	(1,438,009)

HISTORICAL STOCK PRICE



Source: Zacks Investment Research

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