Zacks Small-Cap Research

September 14, 2015

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

scr.zacks.com

10 S. Riverside Plaza, Chicago, IL 60606

Inuvo Inc. (INUV-NYSE)

INUV: Increasing Revenue and Price Target as Business Continues Strong

Current Recommendation	**Buy**
Prior Recommendation	Buy
Date of Last Change	02/25/2015
Current Price (09/11/15)	$2.73
12-Month Target Price	**3.77**

OUTLOOK

Inuvo is digital publishing and advertising technology company. The business is composed of a network of website and app partners and a network of owned and operated websites and apps. Revenue is earned from ads served by the company's proprietary technologies into those websites and apps. Its new native ad product "SearchLinks" could accelerate growth and increase valuation. Management's goal is to reach a revenue run rate of $100 million by the end of 2017.

SUMMARY DATA

52-Week High	**$3.45**
52-Week Low	**$1.09**
One-Year Return (%)	**75.0**
Beta	**1.03**
Average Daily Volume (sh)	**73,061**
Shares Outstanding (mil)	**24**
Market Capitalization ($mil)	**$66**
Short Interest Ratio (days)	**2.56**
Institutional Ownership (%)	**29**
Insider Ownership (%)	**17**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**4.4**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**21.0**
P/E using 2015 Estimate	**24.8**
P/E using 2016 Estimate	**21.0**
Zacks Rank	**3**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Internet-Services**
Zacks Rank in Industry	**31 of 41**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013	16 A	13 A	15 A	11 A	55.0 A
2014	10.1 A	10.9 A	13.0 A	15.5 A	49.6 A
2015	13.4 A	16.7 A	17.5 E	19.0 E	66.8 E
2016					80.0 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013	-$0.01 A	$0.01 A	$0.04 A	-$0.02 A	$0.03 A
2014	$0.03 A	$0.03 A	$0.03 A	$0.04 A	$0.13 A
2015	$0.03 A	$0.03 A	$0.03 E	$0.04 E	$0.11 E
2016					$0.13 E

Zacks Projected EPS Growth Rate - Next 5 Years % **20**

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KEY POINTS

- Inuvo is an emerging player in the digital advertising space a market that is growing over 16% per year and should benefit from this market growth.

- After transitioning out of a money-losing toolbar business, the company just reported its third quarter in a row of over 30% growth. Inuvo should be able continue to grow revenues at over 30% again this quarter and possibly beyond.

- The company has stated its goal is to reach a $100 million in revenue run rate by the end of 2017. This could happen even faster were the company to grow through acquisition as well as organically. It is adding more content to its company-owned sites, as well as strategically adding content through the acquisition of content-based web sites.

- The company just introduced a new advertising product, “SearchLinks”, that is finding success with its ad network partners and create more customer retention. It should create a barrier to entry for its ad business, as it is complex and possibly unique in the industry. This native advertising product is in a very high growth space and companies in that space have higher valuations.

- Since launching coverage of the company, the stock has moved up from $1.34 in February to its current price of $2.76. If the company is valued on enterprise value to sales (since many competitors operate at a loss), the stock is still priced below its peers who trade at an average of 1.4 times sales. With our increased revenues estimate, we are raising our target price to $3.77 if the company achieves $80 million in revenue in 2016, the price could move to $4.27. However, if SearchLinks is successful, investors should look to others in the native advertising space that are currently valued at closer to 3.5x revenues which would reflect a valuation more than double that.

WHAT’S NEW

Company Affirms that Growth Has not Slowed; Raising Estimates

Last week at a conference Inuvo’s management indicated that despite concerns that the auto vertical had appeared to be giving revenues a one-time boost, overall revenue growth for the company had not slowed as any auto slow down had been made up for by other sectors. So rather than the 19% year over year revenue growth we had been expected we know think that revenue growth should continue over 30% for another quarter at least. As a result we are raising revenues to $17.5 million for the quarter from $15.5 million. We are keeping EPS the same as we expect any incremental profit will continue to be reinvested in operations. Q4 we are raising to $19 million, which yields $67 million for the year. The result is raising the price target to $3.77 near term.

SearchLinks is still in test mode and the company is working with 30 customers to fine tune it and figure out how much back office support each customer needs in order to staff properly and to assure that the publisher are successful with their campaigns. The great majority of these customers has been working with Taboola and/or Outbrain and are now comparing and contrasting results. One promise Inuvo makes publishers is that they will safeguard their brands by refusing to show some of the more unpleasant content articles as links—for example the ones with the pictures of sores or other deformities. This will allow brands to control their image in an area they may not have even thought about.

VALUATION

Since we are increasing our revenue estimate, we are also increasing our price target. Inuvo is hybrid ad technology platform/ad network and website publisher. Since the company is almost spilt 50/50, we are using a combination of these types of pubic companies to create a blended valuation. Should SearchLinks, a native ad tech product be successful, we would look to higher revenue multiples as that business is much more attractive.

We applied average multiples to Inuvo's historical and projected revenues based on the comparable companies in the table below. Based purely on public company comps, the result is a market value of $93 million or $3.77 per share. Using this multiple and applying it to 2016 estimated revenues of $80 million, we believe the stock price could move to $4.27, up 7%.

	Ticker	Revenue		TTM	Enterprise Value / Sales		EV/	Included	Enterprise
Company		2015E	LTM	EBITDA	2015E	LTM	EBITDA	Average?	Value
Autobytel	ABTL	$129	$110	$9	1.6x	1.8x	22.0x	y	203
Bluecora	BCOR	$474	$517	$78	1.0x	0.9x	6.1x	y	472
Criteo	CRTO	$476	$1,070	$87	4.3x	1.9x	23.3x	n	2,030
Demand Media	DMD	$131	$147	-$6	0.4x	0.4x	-9.1x	y	57
Rocket Fuel	FUEL	$504	$466	-$53	0.5x	0.6x	-4.9x	y	258
Marchex	MCHX	$144	$159	$7	0.4x	0.4x	8.6x	y	58
Millennial Media Inc.*	MM	$272	$285	-$41	0.8x	0.8x	-5.2x	y	217
The Rubicon Project	RUBI	$242	$164	-$10	2.2x	3.2x	-53.3x	y	528
MaxPoint Interactive	MXPT	$90	$129	-$13	1.1x	0.8x	-32.0x	y	99
SITO Mobile	SITO	$18	$14	-$1	5.6x	6.8x	-77.5x	y	98
Travelzoo	TZOO	$132	$136	$9	0.6x	0.6x	9.5x	y	83
Average				**-2.2**	**1.4x**	**1.6x**	**-13.6x**		**$207**

* Bought by AOL

	Revenue		TTM	Enterprise Value / Sales		Valuation Range	
	2015E	LTM	EBITDA	2015E	LTM	Low	High
Inuvo	**$67**	**$59**	**4.7**	**1.4x**	**1.6x**	**$95**	**$95**
YoY growth							
Conclusion of Enterprise Value			**$95,085,462**				
Market Value			**$93,016,309**				
Shares Outstanding			24,700,000				
Price per Share			**$3.77**				

	Revenue		2015E	Enterprise Value / Sales		Valuation Range	
	2016E	2015E	EBITDA	2016E	2015E	Low	High
Inuvo	**$80**	**$67**	**0.0**	**1.4x**	**1.6x**	**$108**	**$113**
YoY growth							
Conclusion of Enterprise Value			**$110,758,154**				
Market Value			**$108,689,001**				
Shares Outstanding			25,428,412				
Price per Share			**$4.27**				

RISKS

- There are few barriers to entry in the advertising network business and it typically operates with slim margins with competition mainly on price.

- The company is almost entirely dependent upon Yahoo! and Google for revenues.

- Some of the company's growth is dependent on the success of a new product that is virtually untested in the market and may not be adopted by new customers.

- 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.

- Inuvo has limited resources with which to compete against much larger companies and this could hinder its growth.

- SearchLinks, a new native advertising product, may not gain traction and its advertising results may not outperform competitors, which may decrease growth and certainly future valuation.

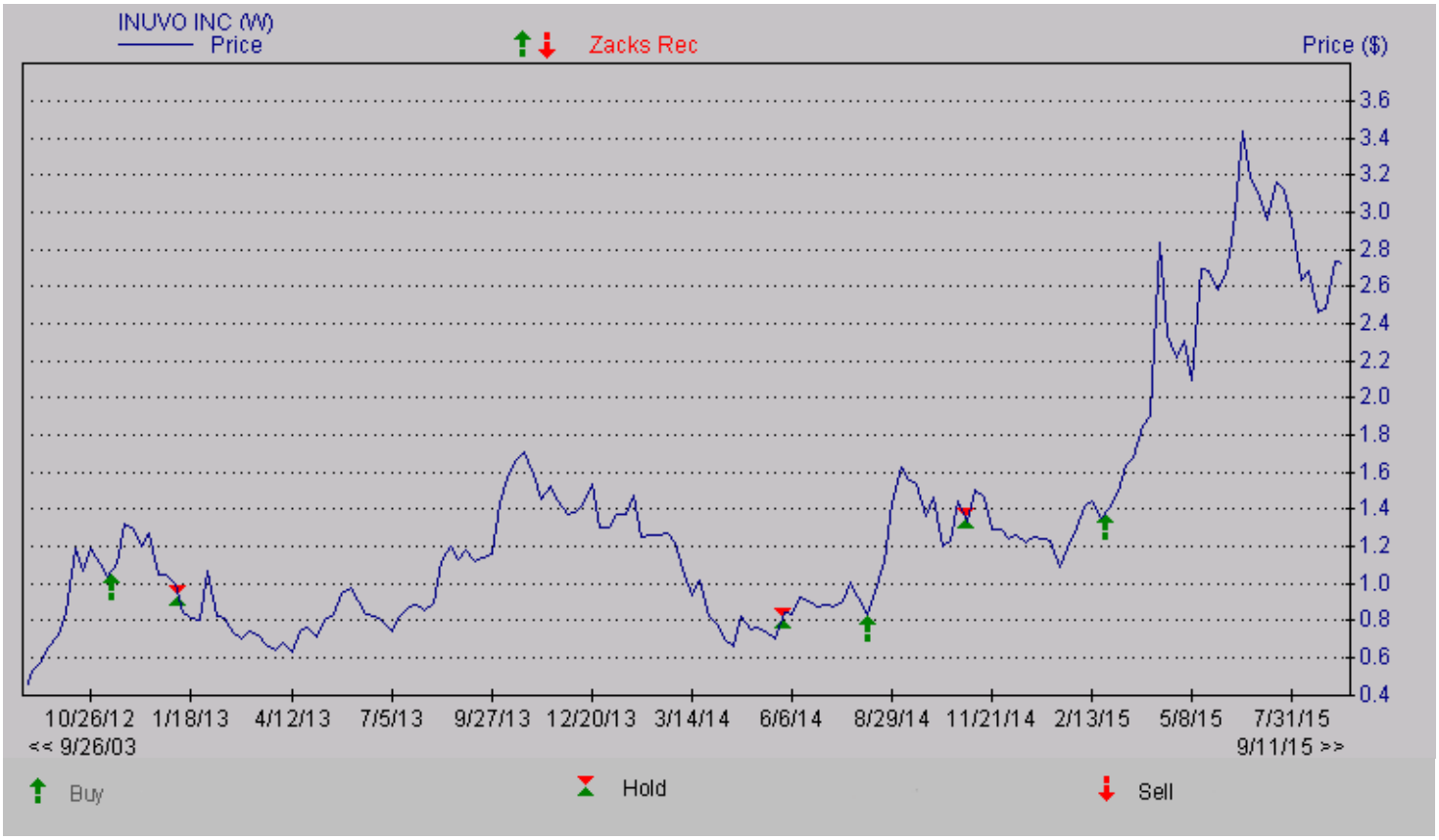
PROJECTED INCOME STATEMENT

Inuvo	Q1 2014 31-Mar	Q2 2014 30-Jun	Q3 2014 30-Sep	Q4 2014 31-Dec	Q1 2015 31-Mar	Q2 2015 30-Jun	Q3 2015E 30-Sep	Q4 2015E 31-Dec	2013	2014	2015E	2016E
Partner Network Revenue	5.5	5.6	7.1	7.6	7.6	$9.3	$9.7	$10.0	36.0	25.7	36.6	42.1
Yr-to-yr Growth	-39%	-35%	-34%	-1%	39%	67%	37%	32%	39%	-29%	42%	15%
Owned and operated, excluding Appbar	3.7	4.8	5.6	7.7	5.8	7.3	7.8	9.0	8.5	21.8	30.0	37.5
Yr-to-yr Growth	68%	156%	187%	200%	59%	52%	40%	17%	107%	157%	38%	25%
Appbar	1.0	0.5	0.3	0.2	$0.1	$0.1	$0.0	$0.0	10.5	2.1	0.2	0.0
	-80%	-80%	-80%	-81%	-90%	-83%	-100%	-100%	-55%	-80%	-91%	-100%
Total revenue	**10.1**	**10.9**	**13.0**	**15.5**	**13.4**	**16.7**	**17.5**	**19.0**	**55.0**	**49.6**	**66.8**	**79.6**
Yr-to-yr Growth	-36%	-17%	-10%	36%	32.6%	53%	35%	23%	3.0%	-9.8%	34.7%	19.2%
Cost of services	3.7	4.7	5.9	6.2	6.1	7.1	7.7	7.9	28.8	20.4	28.7	34.1
Partner network gross margin	1.9	1.0	1.2	1.4	1.5	2.2	2.0	2.1	8.0	5.5	7.9	8.0
% GM partner network	34%	17%	17%	19%	20%	24%	21%	21%	22%	21%	22%	19%
Owned and Operated GM	4.6	5.3	5.9	7.9	5.8	7.4	7.8	9.0	18.2	23.7	30.1	37.5
% GM owned and operated	98%	99%	100%	100%	100%	100%	100%	100%	98%	99%	100%	100%
Gross profit	6.4	6.3	7.1	9.3	7.4	9.6	9.9	11.1	26.2	29.2	38.0	45.5
Gross Margin	63.7%	57.4%	54.6%	60.2%	54.8%	57.6%	56.3%	58.4%	47.7%	58.8%	56.8%	57.2%
Operating expenses:					84%	89%						
Marketing	3.7	3.6	4.3	5.9	4.9	6.6	6.4	7.4	14.4	17.5	25.3	31.3
Compensation	1.1	1.1	1.2	1.4	1.2	1.3	1.6	1.6	6.0	4.8	5.7	6.3
SG&A	1.0	1.1	1.2	1.2	1.0	1.2	1.2	1.1	5.8	4.4	4.4	4.9
Total operating expenses	5.8	5.8	6.7	8.4	7.1	9.1	9.2	10.1	26.2	26.7	35.5	42.4
Operating income:	0.7	0.5	0.5	0.9	0.251	0.5	0.7	1.0	0.0	2.5	2.5	3.1
Operating margin	6.6%	4.3%	3.6%	5.8%	1.9%	3.2%	3.9%	5.4%	0.0%	5.0%	3.7%	3.9%
Other income:												
Interest expense, net	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.0)	(0.0)	(0.0)	(0.4)	(0.4)	(0.2)	-
Total other income	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.0)	(0.0)	(0.0)	(0.4)	(0.4)	(0.3)	(0.2)
Income before income taxes	0.6	0.4	0.4	0.8	0.2	0.5	0.7	1.0	(0.3)	2.1	2.2	2.9
Pretax Margin	5.7%	3.3%	2.9%	5.3%	1.5%	3.0%	3.7%	5.2%	-0.6%	4.3%	3.4%	3.6%
Income tax benefit	(0.1)	0.00	0.00	(0.1)	(0.4)	(0.0)	(0.0)	-	(0.3)	(0.2)	-	-
Tax rate	-13%	0%	0%	-9%	-204%	-7%	-5%	0%	92%	-7.1%	0.0%	0.0%
Net income from continuing operations	0.6	0.4	0.4	0.8	0.6	0.5	0.7	1.0	(0.0)	2.3	2.2	2.9
Net income from discontinued operations	0.0	0.0	0.0	(0.1)	0.0	(0.0)	-	-	0.5	(0.0)	-	-
Net income	0.7	0.4	0.4	0.6	0.6	0.5	0.7	1.0	0.5	2.3	2.2	2.9
Foreign currency valuation	-	-	-	-	-	-	-	-	(0.0)	0.0	0.0	0.0
Comprehensive income	0.7	0.4	0.4	0.6	0.6	0.5	0.7	1.0	0.5	2.3	2.2	2.9
Stk based compensation	0.1	0.2	0.3	0.3	0.1	0.1	0.1	0.1	0.7	1.0	0.5	0.5
One-time expenses	-	-	-	0.1	-	-	-	-	-	0.1	0.0	0.0
Non-GAAP Income from continuing	0.8	0.6	0.7	1.2	0.7	0.7	0.8	1.1	0.7	3.3	2.7	3.4
Yr-over-Yr									-110.9%	393.3%	-17.3%	25.7%
Net income per share:												
Basic from continuing	0.03	0.02	0.02	0.03	0.03	0.02	0.03	0.04	(0.00)	0.10	0.10	0.12
Diluted from continuing	0.03	0.02	0.02	0.03	0.03	0.02	0.03	0.04	(0.00)	0.09	0.09	0.11
Non-GAAP Diluted from continuing	**0.03**	**0.03**	**0.03**	**0.04**	**0.03**	**0.03**	**0.03**	**0.04**	**0.03**	**0.13**	**0.11**	**0.13**
					-18.3%	5.5%	21.3%	12.2%	-110%	358%	-14%	20%
Shares												
Basic	23.4	23.4	23.4	23.6	24.1	24.3	24.4	24.5	23.3	23.5	23.5	24.7
Diluted	23.5	24.1	24.1	24.5	24.2	24.7	24.8	24.9	23.3	24.0	24.2	25.4
	1.0%	3.1%	3.0%	5.0%	3.2%	2.7%	2.7%	1.8%	10.8%	3.2%	0.8%	5.0%
Adjusted EBITDA	1.34	1.19	1.18	1.78	0.67	1.09	1.25	1.58	3.75	5.48	4.60	5.30
	-2%	39%	-19%	2138%	-50%	-9%	6%	-11%		46%	-16%	15%

BALANCE SHEET

	June 30, 2015	March 31, 2015	
Current assets			
Cash	$3,779,339	$1,923,617	96%
Accounts receivable, net of allowance for doubtful accounts of $87,733 and $62,845, respectively	6,348,993	7,398,031	-14%
Unbilled revenue	29,038	19,629	48%
Prepaid expenses and other current assets	286,577	232,727	23%
Total current assets	10,443,947	9,574,004	9%
Property and equipment, net	1,201,858	999,267	20%
Other assets			
Goodwill	5,760,808	5,760,808	0%
Intangible assets, net of accumulated amortization	9,789,539	9,331,821	5%
Other assets	210,050	200,032	5%
Total other assets	15,760,397	15,292,661	3%
Total assets	27,406,202	25,865,932	6%
Current liabilities			
Accounts payable	8,368,632	7,001,628	20%
Accrued expenses and other current liabilities	4,175,373	3,052,266	37%
Term and credit notes payable - current portion	666,667	959,942	-31%
Total current liabilities	13,210,672	11,013,836	20%
Long-term liabilities			
Deferred tax liability	3,552,500	3,552,500	0%
Term and credit notes payable - long term	833,334	2,500,000	-67%
Other long-term liabilities	581,052	98,711	489%
Total long-term liabilities	4,966,886	6,151,211	-19%
Total Liabilities	18,177,558	17,165,047	6%
Stockholdersâ€™ equity			
Total stockholders' equity	9,228,644	8,700,885	6%
Total liabilities and stockholders' equity	$27,406,202	$25,865,932	6%
Quick Ratio	0.8	0.9	-9%
Working Capital	(2,766,725)	(1,439,832)	92%
Cash as % of assets	14%	7%	85%
Debt % of assets	8%	14%	-45%

HISTORICAL ZACKS RECOMMENDATIONS



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