



Net Element, Inc.
(Nasdaq CM: NETE, Target Price: \$25.00)

Net Element, Inc. (Nasdaq CM: NETE, "Net Element") is a global financial technology and value-added solutions company that supports payment technology solutions, online payments and value-added transactional services in emerging countries and in the United States. The company is headquartered in Miami Beach, Florida.

Investment Highlights

Net Element reported full year 2017 results on April 2, 2018, during which the company recapped recent performance and provided an update to its strategic initiatives. Highlights of the announcement are as follows:

- *2017 revenues surpass \$60mn.* Net Element reported 2017 full year revenues of \$60.1mn, which represented an increase of approximately 11% versus \$54.3mn in 2016.
- Revenue growth was driven by strong execution in the company's North America Transactions Solutions business segment, which grew by 21.3% YoY.
- *Transaction volume grows.* The company reported transactions processed on its platform increased by 14% to reach \$2.8 billion in 2017, versus \$2.45 billion during 2016. Transaction dollars processed in the company's North American markets grew by 18% and reached \$2.3 billion.
- NETE reported a Net Loss of (\$9.9mn), versus a loss of (\$13.5mn) in 2016. NETE reported GAAP EPS of (\$5.04) in 2017, with average shares outstanding of 2.0mn.
- *Balance Sheet Improves.* NETE ended the year with cash on hand of \$11.3mn, and total financial debt of \$7.0mn. The company raised \$7.6mn of new capital during 4Q17, which is pegged for investments in new blockchain and organic growth initiatives.
- In the announcement, NETE noted that the company was able to maintain Nasdaq CM listing compliance and also that the company was named as one of the fastest growing companies in North America on Deloitte's 2017 Technology Fast 500™.
- Net Element launched its new multi-channel payments platform, Netevia, which the company stated connects and simplifies payments across a number of channels through a single integration point – including POS, e-commerce, and mobile devices. The company is also integrating new technology into Netevia, which will make it a decentralized blockchain technology solution.
- NETE also named two new members to its Board of Directors, CNBC host Jon Najarian as well as Bank of America veteran and fintech executive Jonathan Fichman. Both new members will serve on the company's Audit, Nominating and Corporate Governance, and Compensation Committees.

No change to target following results

The price target remains unchanged for Net Element, with NETE showing from double-digit growth and an improved balance sheet, with further growth potential from its new blockchain initiatives. We would look to re-evaluate the target as the company updates investors on its progress and expectations for blockchain in 2018-2019.

Stock Details (4/9/18)

Nasdaq CM:	NETE
Sector / Industry	Financial Tech / Mobile Payments
Price target	\$25.00
Recent share price	\$7.35
Shares o/s (mn)	3.9
Market cap (in \$mn)	28.7
52-week high/low	\$33.50 / 2.60

Source: Thomson Reuters, SeeThruEquity Research

Key Financial (\$mn, unless specified)

	FY16A	FY17A	FY18E
Revenues	54.2	60.1	72.1
EBITDA	(8.7)	(6.1)	(4.8)
Operating Inc. (Loss)	(8.8)	(8.6)	(7.2)
Net Income	(13.5)	(10.0)	(8.4)
EPS (\$)	(10.33)	(5.04)	(2.13)

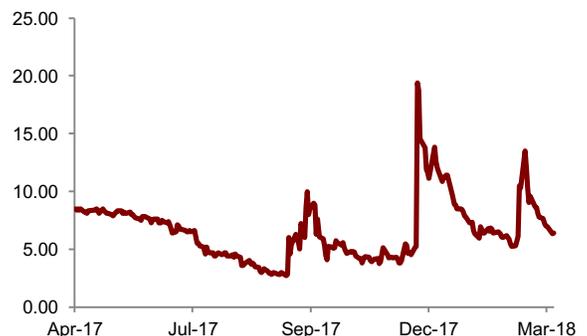
Source: SeeThruEquity Research

Key Ratios

	FY16A	FY17A	FY18E
Operating Margin (%)	(16.3)	(14.3)	(10.0)
EBITDA margin (%)	(16.0)	(10.1)	(6.7)
Net margin (%)	(24.8)	(16.7)	(11.7)
P/Revenue (x)	0.5	0.5	0.4
EV/EBITDA (x)	NM	NM	NM
EV/Revenue (x)	0.4	0.4	0.3

Source: SeeThruEquity Research

Share Performance, LTM



Source: Thomson Reuters

ANNUAL FINANCIAL SUMMARY

Figure 1. Income Statement Summary

Figures in \$, unless specified	FY2017	FY2016	FY2015
Total Revenue	60,064,824	54,286,859	40,235,362
YoY Change %	10.6%	34.9%	
Service Fees	58,723,908	48,784,855	31,204,871
% Revenue	97.8%	89.9%	77.6%
Branded Content	1,340,896	5,502,004	9,030,491
% Revenue Mix	2.2%	10.1%	22.4%
Cost of Service Fees	49,934,371	40,521,236	25,858,098
Cost of Branded Content	1,302,841	5,187,005	8,119,117
Gross Profit	8,827,612	8,578,618	6,258,147
Gross Margin (%)	14.7%	15.8%	15.6%
General and Administrative	10,629,773	8,797,883	9,310,477
Non-cash compensation	2,940,424	3,463,435	4,306,304
Bad debt Provisions	1,320,848	1,688,237	649,571
Depreciation & Amortization	2,533,985	3,466,511	2,513,162
Operating Expenses	17,425,030	17,416,066	16,779,514
Operating Income (Loss)	-8,597,418	-8,837,448	-10,521,367
Operating Margin (%)	-14.3%	-16.3%	-26.2%
Interest & Other Items	-1,425,631	-4,778,628	-2,806,559
Pre-Tax Income	-10,023,049	-13,616,076	-13,327,926
Minority Interest	109,564	128,539	74,314
Net Inc. (loss) attributable to stockholders	-9,913,485	-13,487,537	-13,253,612
Foreign Currency & Preferred Dividends	-43,623	-920,794	-1,899,453
Comprehensive Income (loss)	-9,957,108	-14,408,331	-15,153,065
EPS	(\$5.04)	(\$10.33)	(\$23.22)
Avg Shares outstanding in period	1,967,676	1,305,801	639,112

Source: company results release

Net Element revenues and transaction volume grow by double-digits in 2017

- **2017 revenues rise by 11% to reach \$60.1mn.** On April 2, 2018, Net Element reported 2017 full year results, with revenues coming in at \$60.1mn, which represented an increase of approximately 11% versus \$54.3mn in 2016.
- **Transaction volume grows.** Net Element reported that transactions processed on its platform increased by 14% to reach \$2.8 billion in 2017, versus \$2.45 billion during 2016. Transactions processed in the company's North American markets grew by 18% and reached \$2.3 billion. International transaction processing volume was flat year-over-year.
- **NA Transactions leads growth.** Net Element experienced healthy 21.4% revenue growth in its North American Transactions Solutions segment, which generated \$51.1mn in revenues in 2017. Growth was driven by organic sales to small and medium sized business merchants and value-added offerings.
- The International Transactions Solutions segment declined, due to the impact of the consolidation of the company's Mobile Solutions and Online Solutions segments.

NETE Segment Mix	2017	FY17 Mix %	2016	FY16 Mix %
NA Transaction Solutions	\$51,138	85%	\$42,131	78%
Intl Transaction Solutions	\$8,926	15%	\$12,156	22%
Total	\$60,065	100%	\$54,287	100%

Source: Company release

- 2017 gross profit increased modestly to 8.8mn, or 14.7% of revenues, versus \$8.6mn, or 15.8% of revenue in 2016. Management attributed the narrowing gross margins to revenue mix, citing the decrease in Digital Provider segment revenues and an increase in lower margin North American Transaction revenues.
- **GAAP EPS of (\$5.04).** NETE reported a Net Loss of (\$9.9mn), versus a loss of (\$13.5mn) in 2016. NETE reported GAAP EPS of (\$5.04) in 2017, with average shares outstanding of 2.0mn. The company had 3.9mn shares outstanding as of April 2, 2018.
- **Balance Sheet improves with year-end investment.** Net Element ended 2017 with a significantly improved balance sheet. The company ended the year with cash on hand of \$11.3mn, and \$7.0mn of financial debt. Current assets were \$19.0mn, with current liabilities of \$14.7mn and net shareholders' equity of \$13.1mn.
- The company raised \$7.55mn during the fourth quarter, which management characterized as growth funds in order to support the company's organic growth programs and new blockchain initiatives. On the company's call with investors, CFO Jonathan New noted that the going concern opinion had been removed from the company's audited financial statements, reflecting this success in capital raising.

Net Element launches Netevia platform, continues to develop blockchain initiative

- Net Element recently launched its new multi-channel payments platform, Netevia. According to the announcement, Netevia connects and simplifies payments across a number of channels through a single integration point – including POS, e-commerce, and mobile devices.
- The company is also integrating blockchain technology into Netevia, which will allow the company to offer a decentralized payments ecosystem that developers and application providers can integrate into, giving them access to Net Element's merchant partner network, and ultimately enabling Net Element to offer a suite of blockchain-focused value-added services. The company joined the Enterprise Ethereum Alliance ("EEA"), a large open-source blockchain initiative with over 250 member companies.
- Management characterized progress made on the blockchain initiative as remaining in the development stage on its update call with investors, and we look forward to hearing further updates throughout the year given the high interest in this sector, and what appears to be a strong strategic fit with Net Element's core transaction processing business. According to notes in its 10K filing, Net Element appears to have discontinued its partnership with Bunker Capital in this area.

- We note that Net Element's existing services include value-added electronic payment solutions in a multi-channel environment covering point-of-sale (POS), e-commerce and mobile devices. Therefore the addition of blockchain technology would be a natural extension of these core capabilities, and may facilitate an avenue by which Net Element can capture market share in the digital payments market versus incumbents who may take longer to embrace cryptocurrency.

Price target unchanged at this time

- We updated our price target for Net Element in December 2017 following the company's announcement that it would enter the high growth blockchain market, and that Net Element had succeeded in raising substantial new capital, reducing the risk of being de-listed from the Nasdaq CM or issuing shares in a discounted high dilution offering. While we still expect Net Element to invest in growth, and raise external capital in the future to invest in growth opportunities and/or acquisitions, the company has improved its financial position to the point where the going concern opinion has been removed from its 2017 audited financial statements.
- Net Element has an existing business with scale and growth from its multi-channel digital payment and transaction processing technologies, which supports more than 20mn e-commerce customers and more than \$60mn in annual company revenues.
- Blockchain and cryptocurrency should be a natural extension of the company's strategy. Further, while the company is clearly in the beginning stages of integrating blockchain into its platform, Net Element may indeed be positioned to capture share from larger online payment processing vendors with the disruptive impact of cryptocurrency, and the company's experience cultivating value-added services in its existing markets.
- **Valuation:** The target suggests a market valuation of \$97.5mn, which represents 1.6x 2017A revenues and would still place Net Element in the lower portion of the peer group based on this metric.

Company	Mkt cap (\$ mn)	EV/Revenue(x)		P/E Ratio	
		TY	NY	TY	NY
Global Payments Inc	17,491	5.6x	5.1x	21.7x	18.7x
Vantiv	24,289	4.9x	4.5x	21.7x	18.1x
Net 1	540	1.0x	0.9x	5.7x	5.1x
PayPal Holdings	89,472	5.7x	4.9x	32.7x	27.0x
WEX	6,810	6.1x	58.5x	20.8x	18.0x
Bottomline Technologies	1,582	1.7x	1.5x	33.5x	27.8x
EuroNet Worldwide	3,716	1.6x	1.5x	13.8x	12.1x
VeriFone Systems	1,744	1.4x	1.4x	10.7x	9.1x
Planet Payment (acquired)	257	3.7x	3.3x	26.4x	21.4x
Average		3.5x	9.1x	20.8x	17.5x
Net Element Inc	28.7	0.6x	0.4x	N/A	N/A
Premium (discount)		(82.8%)	(95.5%)	N/A	N/A

* STE Research, Yahoo!Finance estimates for peer companies as of 4/3/18
Planet Payment acquired by Fintrax for \$257mn in 12/2017

- We continue to see NETE as an intriguing high risk / high reward growth company in the financial technology space. We would look to revisit the target following further details on the potential impact of the blockchain initiative on company-specific growth, guidance for 2018E, or evidence of NETE approaching recurring free cash flow breakeven – any of which may potentially justify a narrowing valuation gap versus peers in the industry.

About Net Element, Inc.

Net Element, Inc. (NETE) operates a payments-as-a-service transactional and value-added services platform for small to medium enterprise ("SME") in the U.S. and selected emerging markets. In the U.S. it aims to grow transactional revenue by innovating SME productivity services using blockchain technology solutions and Aptito, our cloud-based, restaurant and retail point-of-sale solution. Internationally, Net Element's strategy is to leverage its omni-channel platform to deliver flexible offerings to emerging markets with diverse banking, regulatory and demographic conditions. Net Element was ranked as one of the fastest growing companies in North America on Deloitte's 2017 Technology Fast 500™. In 2017 we were recognized by South Florida Business Journal's as one of 2016's fastest growing technology companies. Further information is available at www.NetElement.com.

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