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## Pareteum (NYSE American/TEUM)

**BUY**

**Q2/18 results very positive**

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*Pareteum provides mobility cloud platform and software solutions*

### Investment Highlights

1) Pareteum reported very positive quarterly financial results for their Q2/2018 earlier this month, including revenue growth year-over-year of 85% to \$6.0 million and net income of \$1.7 million or \$0.03 per share, as compared to a net loss of \$1.3 million or (\$0.10) per share for the same period one year ago. Revenue growth this year was led by increased connections (or users) of 225% year-over-year to over 2.7 million. While the Company's more established monthly service revenue category grew solidly (by 42%) to \$4.3 million in Q2, its newer source of revenues from installation and software development jumped to \$1.7 million from only \$235,000 the prior year. Pareteum was also able to diversify its revenues in new geographic territories outside of Europe by nearly 8X in Q2/18, such that these represent nearly 41% of total, up from a little less than 10% one year ago. After level gross margins of 70%, higher overhead expenses, but less than revenue increases, and a gain of \$1.6 million for derivative liabilities revaluation, Pareteum was able to turn around its recent history of quarterly losses with positive net income this year. Adjusted EBITDA for the quarter was a very solid \$1.3 million, helping the Company increase its cash balance to \$19.2 million at the end of Q2/18, up from \$13.5 million at the start of the year.

2) The Company also provided improved financial guidance for fiscal 2018, included revenue growth of 80% over 2017 and gross margins in the 70%-75% range. Thus, we are increasing our revenue estimates for Pareteum for 2018E to \$24.5 million, or 80.8% above revenues of \$13.5 million in 2017, up from \$21.7 million forecasted previously. We are also assuming gross margins of 73% overall for 2018E for Pareteum, slightly higher overhead expenses this year of \$18.8 million as compared to \$17.7 million in 2017, positive other income gains, and higher shares outstanding to bring our estimate to \$0.01 in positive EPS for 2018E, as compared to a loss of (\$0.84) in 2017. For the upcoming third quarter, we are estimating that Pareteum will post revenues of \$7.0 million and net income of

**Current Price \$2.56**

**Price Target \$3.10**

Estimates	F2016A	F2017A	F2018E
Revenue(\$000s)	\$12,856	\$13,548	\$24,500 E
1Q March	3,274	2,795	4,113 A
2Q June	3,267	3,239	6,003 A
3Q September	3,171	3,499	7,000 E
4Q December	3,144	4,015	8,487 E

EPS	(\$4.67)	(\$0.84)	\$0.01 E
1Q March	(0.66)	(0.14)	(0.04) A
2Q June	(0.43)	(0.10)	0.03 A
3Q September	(0.08)	(0.16)	0.01 E
4Q December	(3.50)	(0.44)	0.01 E
P/E (x)	N/A	N/A	N/A

EBITDA/Share	\$0.20	\$0.13	\$0.10
EV/EBITDA (x)	11.0	17.2	22.3 X

<b>Stock Data</b>	
52-Week Range	\$0.54-\$3.59
Shares Outstanding (mil.)	60.3
Market Capitalization (mil.)	\$154.4
Enterprise Value (mil.)	\$134.9
Debt to Capital (6/18)	2.9%
Book Value/Share (6/18)	\$0.43
Price/Book	6.0 X
Average Trading Volume (3-month) Mill	1.36
Insider Ownership	9.6%
Institutional Ownership	16.3%
Short interest (mil.)	6.9
Dividend / Yield	\$0.00/0.0%



**Price target and ratings changes over the past 3 years:**  
 Update - September 22, 2017 – Buy - Target \$2.10  
 (from Target of \$2.25 or \$56.25 after 1-25 reverse split)  
 Update – BUY – April 4, 2018 – Target increased \$3.10

**Please find Important Disclosures beginning on Page 5.**

\$0.01 per share. Growth in contract revenue backlog and associated backlog conversion this year is expected to fuel growth at Pareteum in the second half of 2018E, and indeed in Q2/18 the Company signed 13 new contracts adding \$55 million to its 36-month backlog, which hit \$300 million by the end of July.

**3) Meanwhile, Pareteum's pending merger with Artilium, first announced in June, is proceeding, with an estimated closing date of late September 2018.** To date, the plan has been approved by both the Pareteum Board of Directors and all of the independent Artilium Directors, and in early August Pareteum filed its definitive proxy with the US SEC which included certain pro forma financial data and projections for the combined companies, along with other information.

## Conclusion/Stock Valuation

With a new, experienced management team, growing revenues and increased backlog stressing recurring revenue and higher-margin contracts, an improved balance sheet and successful cost-reduction program, long-term investors have much to like about Pareteum. Short-term, however, recent and pending share dilution has held back TEUM share price appreciation to some extent. For example, this includes 7.1 million shares behind the exercise of warrants issued to investors in a private placement offering in December 2017 registered for resale in late July, and approximately 37.9 million shares to be issued to existing Artilium shareholders later this fall when the proposed acquisition closes. All-in-all, though, we are maintaining our BUY rating on Pareteum and our 12-18 month price target of \$3.10 per share. (For a more complete analysis of our stock valuation methodology on TEUM shares please refer to our Company Updates on TEUM dated September 22, 2017 and April 4, 2018, including comparison with stocks such as GTT Communications (GTT, NR), Level 3 Communications (Acquisition by CenturyLink), Cogent Communications (CCOI, NR) and Lumos Networks (Acquisition by Private Equity)).

## Risk Factors

**In addition to normal economic and market risk factors that impact most equities and the common risks shared by Pareteum with other companies in the industry, we believe an investment in TEUM involves the following risks:**

- **Reliance on key management** – At present, TEUM relies on several key members of its management team who have been in key executive positions for an extended period of time. Should one or more of these key executives leave the Company, TEUM could find it difficult to replace their long-standing knowledge of operations and industry expertise.
- **Reliance on partnerships** – To date, TEUM has signed a number of distribution and joint venture partnerships for its technologies and services. Thus, in the future certain factors related to sales and new product development may be determined by third parties and out of the control of Company management.
- **Limited stock liquidity** – Trading volume in TEUM stock is comparatively light and these shares have a relatively limited history of trading on major US stock exchanges compared with other technology stocks. As such, news regarding TEUM, its target market, partners and/or competitors could lead to significant volatility in the stock price.
- **Competitive Markets** – The Company and its partners compete in its target mobile telecom services market with a number of companies, many of which are considerably larger than the Company. There can be no assurance that the Company and its partners will be able to successfully compete and launch new products into these competitive markets in the future.

- **Regulatory risks** – TEUM and its partners are subject to regulatory review for its ongoing service and new market development activities, both in the US and internationally. Any negative correspondence from US or other regulatory agencies could have an adverse effect on the ongoing operations of the Company.
- **Lack of historic profitability** - TEUM did not achieve operating profitability on a quarterly basis for several years, and according to our forecasts is expected to do so in the near future but only on a relatively modest basis. Although the Company maintains adequate cash reserves at the present time, there can be no assurance the Company will not need to raise additional working capital in the future should operating losses resume.
- **Need to defend patents and other intellectual property** – TEUM currently holds a number of US and International patents on its services and related technologies, some of which expire in the near future. The Company may be required to defend its patents in the US and overseas in the future, and there can be no assurance these defenses will be successful.

Robert M. Wasserman

**Pareteum**  
**Consolidated Statements of Operations and Comprehensive Loss**  
 (In 000s, except per share data)

FYE December	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018F
Revenues	\$47,361	\$44,359	\$43,651	\$37,168	\$32,233	\$29,202	\$19,452	\$20,356	\$31,015	\$12,856	\$13,548	\$24,500
Cost of service	45,609	43,336	41,453	35,121	28,723	23,003	9,389	6,689	5,926	3,659	3,684	6,620
Gross Profit	1,752	1,023	2,198	2,047	3,510	6,199	10,063	13,668	25,089	9,197	9,864	17,880
Operating Expenses:												
Product development						6,804	6,091	7,229	4,543	3,544	1,480	3,000
Sales and marketing						3,707	3,139	2,394	2,634	1,341	1,575	2,750
General and administrative						11,492	15,063	12,603	11,650	11,708	10,097	9,000
Depreciation and amortization						5,710	6,601	8,220	6,624	4,247	4,533	4,000
Total operating expenses	13,105	15,470	12,738	20,521	29,186	27,713	30,894	30,445	25,451	20,839	17,685	18,750
Income (loss) from operations	(11,353)	(14,447)	(10,540)	(18,474)	(25,676)	(21,514)	(20,832)	(16,777)	(362)	(11,642)	(7,821)	(870)
Other Income												
Interest income	101	42	161	240	107	248	104	128	106	112	172	200
Interest expense	(849)	(499)	(939)	(1,803)	(201)	(1,870)	(3,135)	(5,176)	(1,488)	(1,228)	(5,063)	(400)
Other expense (gain)	1,470	(1,602)	(5,790)	(74,102)	(164)	704	(843)	(3,216)	(3,279)	(17,945)	(864)	2,000
Income (loss) before tax	(10,631)	(16,506)	(17,108)	(94,138)	(25,935)	(22,432)	(24,705)	(25,042)	(5,023)	(30,703)	(13,576)	930
Provision for income taxes	1	1	1	1	0	289	(200)	217	(17)	38	107	0
Net income (loss)	(10,631)	(16,507)	(17,109)	(94,139)	(25,935)	(22,721)	(24,505)	(25,259)	(5,006)	(30,741)	(13,683)	930
Basic income per share	(\$27.89)	(\$13.64)	(\$7.99)	(\$33.30)	(\$6.21)	(\$5.19)	(\$5.05)	(\$3.70)	(\$0.79)	(\$4.67)	(\$0.84)	\$0.02
Diluted income per share	(\$27.89)	(\$13.64)	(\$7.99)	(\$33.30)	(\$6.21)	(\$5.19)	(\$5.05)	(\$3.70)	(\$0.79)	(\$4.67)	(\$0.84)	\$0.01
Basic shares outstanding	381	1,211	2,142	2,827	4,173	4,453	5,050	5,908	6,328	6,739	16,338	57,000
Diluted shares outstanding	381	1,211	2,142	2,827	4,173	4,453	5,050	5,908	6,328	6,739	16,338	68,000
Key ratios:												
Revenue growth		-6.3%	-1.6%	-14.9%	-13.3%	-9.4%	-33.4%	4.7%	52.4%	-58.6%	5.4%	80.8%
Gross margin	3.7%	2.3%	5.0%	5.5%	10.9%	21.2%	51.7%	67.1%	80.9%	71.5%	72.8%	73.0%
S G & A/sales						52.0%	93.6%	73.7%	46.1%	101.5%	86.2%	48.0%
Depreciation, amort, non-cash comp						\$12,544	\$15,365	\$12,615	\$13,000	\$13,011	\$9,951	\$7,500
Operating margin	-24.0%	-32.6%	-24.1%	-49.7%	-79.7%	-73.7%	-107.1%	-82.4%	-1.2%	-90.6%	-57.7%	-3.6%
Cash Flow/share	(\$27.89)	(\$13.64)	(\$7.99)	(\$33.30)	(\$6.21)	(\$2.29)	(\$1.81)	(\$2.14)	\$1.26	(\$2.63)	(\$0.23)	\$0.09
EBITDA/share	(\$29.78)	(\$11.93)	(\$4.92)	(\$6.54)	(\$6.15)	(\$2.01)	(\$1.08)	(\$0.70)	\$2.00	\$0.20	\$0.13	\$0.10

**Balance Sheets**

	12/31/17	6/30/18
<b>Assets:</b>		
Cash and equivalents	\$13,538	\$19,205
Restricted cash	200	229
Accounts receivables, net	2,058	3,853
Prepaid expenses & other current	900	1,175
Total current	16,696	24,462
Other long term assets	91	89
Note receivable	595	596
Property and equipment	4,714	4,680
Long-term Investments	3,230	3,230
<b>TOTAL ASSETS</b>	<b>\$25,326</b>	<b>\$33,057</b>

**Quarterly Earnings Comparisons**

	March	June	Sept	Dec	Total
<b>Revenues (in \$Mill)</b>					
2010	\$9,944	\$9,674	\$9,040	\$8,510	\$37,168
2011	8,508	7,791	7,797	8,137	32,233
2012	8,581	7,085	6,699	6,837	29,202
2013	6,240	3,564	4,124	5,524	19,452
2014	5,384	5,072	7,299	7,870	25,625
2015	5,013	19,244	3,486	3,272	31,015
2016	3,274	3,267	3,171	3,144	12,856
2017	2,795	3,239	3,499	4,015	13,548
2018E	4,113	6,003	7,000	8,487	24,500

**Earnings per Share**

2010	(\$0.17)	(\$0.18)	(\$0.25)	\$0.20	(\$33.30)
2011	0.04	0.01	(0.01)	0.00	(6.21)
2012	(0.05)	(0.04)	(0.05)	0.28	(5.19)
2013	(0.04)	(0.07)	(0.03)	(4.91)	(5.05)
2014	(0.04)	(0.04)	(0.04)	(0.03)	(3.70)
2015	(0.01)	0.06	(0.03)	(0.81)	(0.79)
2016	(0.66)	(0.43)	(0.08)	(3.50)	(4.67)
2017	(0.14)	(0.10)	(0.16)	(0.44)	(0.84)
2018E	(0.04)	0.03	0.01	0.01	0.01

  

<b>Liabilities:</b>		
Accounts payable	\$1,979	\$2,569
Current lease obligations	0	0
Net billings in excess of revenues	243	259
Accrued expenses	5,250	3,698
9% unsecured Sub Note	66	134
Senior secured loan - short-term	0	0
Total current	7,538	6,659
Derivative liabilities	1,598	
Other long-term liabilities	151	118
Convertible note	618	622
Senior loan - long-term	0	0
Net billings - long-term	0	0
<b>TOTAL LIABILITIES</b>	<b>9,905</b>	<b>7,400</b>
Stockholders' equity	15,422	25,657
<b>TOTAL LIAB &amp; EQ</b>	<b>\$25,326</b>	<b>\$33,057</b>

Source: Dawson James Securities, Inc. estimates; Company documents

## Important Disclosures:

### Price Chart:



### Price target and ratings changes over the past 3 years:

Updated – Buy – September 22, 2017 – Price Target \$2.10  
(from Price Target of \$2.25 or \$56.25 after 1-25 reverse split)  
Update – BUY – April 4, 2018 – Price Target increased to \$3.10

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<b>Ratings Distribution</b>	<b># of Companies</b>	<b>% of Total</b>	<b># of Companies</b>	<b>% of Totals</b>
Market Outperform (Buy)	23	88%	7	30%
Market Perform (Neutral)	3	12%	0	0%
Market Underperform (Sell)	0	0%	0	0%
<b>Total</b>	<b>26</b>	<b>100%</b>	<b>7</b>	<b>27%</b>

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