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Research Note

Investors should consider this report as only a single factor in making their investment decision.

Pareteum Corporation

Speculative Buy

John Nobile
February 20, 2019

TEUM $3.64 — (NASDAQ)

	2016A	2017A	2018E	2019E
Revenues (millions)	$12.9	$13.5	$31.3	$113.0
Earnings (loss) per share	$(4.56)	$(0.84)	$(0.10)	$0.15

52-Week range	$3.75 – $0.54	Fiscal year ends:	December
Common shares out as of 11/13/18	97.8 million	Revenue per share (TTM)	$0.44
Approximate float	90.2 million	Price/Sales (TTM)	8.3X
Market capitalization	$356 million	Price/Sales (FY2019)E	3.6X
Tangible book value/share	$0.46	Price/Earnings (TTM)	NMF
Price/tangible book value	7.9X	Price/Earnings (FY2019)E	24.3X

Pareteum Corporation, headquartered in New York, NY, is a cloud communications platform company. Cloud communications involves the integration of multiple communication methods and services that can be accessed over the Internet and are handled and hosted by a third-party (such as Pareteum) through the cloud.

Key investment considerations:

Reiterating Speculative Buy rating and raising our twelve-month price target to $7.50 per share from $5.00 based on our increased 2019 revenue projection.

On February 13, 2019, Pareteum announced it acquired iPass in an all-stock transaction. This acquisition resulted in a significant increase to our 2019 revenue forecast due to the impact over the final 10 months of the year.

A day after the iPass acquisition was announced, the company announced that its 36-month backlog more than quadrupled to over $600 million from $147 million at December 31, 2017. Pareteum's 36-month contractual backlog and synergies (through cross selling, market expansion, and cost savings) created by the acquisition of iPass should support our revenue growth forecasts.

We project strong revenue growth should result in EBITDA of $24.6 million in 2019, up from a projected loss of $2.2 million in 2018.

For 2018, we maintain our revenue forecast of $31.3 million and net loss forecast of $6.9 million or $(0.10) per share.

For 2019, we project revenue more than tripling to $113 million and net income of $17.1 million or $0.15 per share. We previously forecasted revenue of $82 million and net income of $18.9 million or $0.18 per share. Our revised forecast reflects the acquisition of iPass.

****Please view our disclosures on pages 9 - 11.***

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Recommendation and Valuation

We are reiterating our Speculative Buy rating on Pareteum Corporation and raising our twelve-month price target to $7.50 per share from $5.00 based on our increased 2019 revenue projection stemming from the acquisition of iPass.

Our rating should be supported by worldwide spending on public cloud services and infrastructure, which is forecasted to achieve a five-year compound annual growth rate (CAGR) of 21.9% with public cloud services spending totaling $277 billion by 2021. One of the industries projected to grow the fastest is the telecommunications industry with a 23.3% CAGR to 2021. Software as a Service (such that Pareteum offers) is projected to be the largest cloud computing category, capturing nearly two thirds of all public cloud spending in 2018.

The acquisition of iPass resulted in a significant increase to our 2019 revenue forecast due to the sales impact over the final 10 months of the year. A day after the iPass acquisition was announced, the company announced that its 36-month backlog more than quadrupled to over $600 million from $147 million as of December 31, 2017. Pareteum's 36-month contractual backlog and synergies (through cross selling, market expansion, and cost savings) created by the acquisition of iPass should support our revenue growth forecasts.

We project strong revenue growth should result in EBITDA of $24.6 million in 2019, up from a projected loss of $2.2 million in 2018.

TEUM trades at a TTM multiple of 8.3X sales while industry (telecommunications software and services) peers trade at a trailing multiple of 1.7X sales. We believe Pareteum's premium compared to the industry is due to its substantial growth prospects. We project sales growth of over 260% for TEUM in 2019 compared to 6.3% for the industry. As the company's sales growth accelerates, we believe investors are likely to accord TEUM a higher multiple. We applied a multiple of 8.5X (up from 7X previously) reflecting the acquisition of iPass to our FY19 sales per share projection of $1.00, discounted for execution risk, to derive a year-ahead value of approximately $7.50 per share.

Significant Developments

Pareteum Completes Acquisition of iPass – On February 13, 2019, Pareteum announced it accepted for exchange all validly tendered iPass Inc. shares for the agreed consideration of 1.17 shares of Pareteum stock for each share of iPass. The shares accepted represent approximately 66.8% of iPass's outstanding shares of common stock. Pareteum acquired the remaining outstanding shares of iPass's common stock through a merger of a wholly-owned subsidiary of Pareteum with and into iPass immediately following expiration of the tender offer and acceptance of the iPass shares on February 12, 2019.

36-Month Backlog Grows to $615 Million – On February 14, 2019, Pareteum announced that it closed 2018 with six new three-year agreements with new and existing customers, worth a total of $15 million. Combined with previously announced contracts, Pareteum's 36-month contractual revenue backlog totaled $615 million.

Projections

2018 – We are maintaining our revenue forecast of $31.3 million and net loss forecast of $6.9 million or $(0.10) per share.

Gross profit should more than double to $21.3 million due primarily to sales growth, offset in part by gross margins decreasing to 67.9% from 72.8%. Our gross margin projections account for the lower blended margins with Artilium.

We project SG&A expenses of $20.3 million or 64.9% of sales compared to $11.7 million or 86.2% of sales. The significant increase in SG&A expenses is primarily the result of nonrecurring stock compensation in 3Q18. Product development costs are projected to grow $1.9 million to $3.3 million as the company continues to expand its service offerings. Depreciation and amortization expense is projected to decrease to $3.9 million from $4.5 million due primarily to lower depreciable fixed assets. We project the operating loss narrowing to $8.3 million from $8.8 million as the increase in revenue more than offsets the growth in operating expenses.

Interest expense should decrease to $700,000 from $5.1 million on a significantly lower average debt level. We project minimal taxes being paid in 2018 given the company's large amount of net operating loss carryforwards ($109 million as of December 31, 2017).

2019 – We project revenue more than tripling to $113 million and net income of $17.1 million or $0.15 per share. We previously forecasted revenue of $82 million and net income of $18.9 million or $0.18 per share. Our revised forecast reflects the acquisition of iPass.

We anticipate gross profit more than tripling to $68 million, offset in part by gross margin compression to 60.2% from 67.9% in 2018. The decrease in gross margins reflects a full year of lower blended margins with Artilium and iPass.

We project SG&A expenses increasing 67.3% to $34 million or 30.1% of sales due primarily to the inclusion of iPass. Product development costs should grow $6.3 million to $9.6 million due primarily to implementation of strategic growth initiatives to expand business opportunities. Depreciation and amortization expense should increase to $4 million from $3.9 million due primarily to greater depreciable fixed assets. We project a swing to operating income of $20.4 million versus an operating loss of $8.3 million as the increase in revenue more than offsets the growth in operating expenses. We project operating margins of 18.1% compared to (26.6)%.

Interest expense should increase to $1 million from $700,000 due to the debt acquired from the Artilium acquisition. We project the company paying $2.5 million in taxes for a rate of 13%.

Risks

In our view, these are the principal risks underlying the stock.

Economic – The economic climate, especially in Europe, may have an adverse effect in the markets in which Pareteum operates. Many of the company's customers' business is consumer driven, and to the extent there is a decline in consumer spending, Pareteum's customers could experience a reduction in the demand for their services.

International markets – Pareteum has significant international operations in Europe, and to a lesser extent in the US, Middle East and elsewhere. There can be no assurance that the company will be able to obtain the permits and operating licenses required for it to operate

Technological obsolescence - The telecommunications industry is subject to rapid and significant changes in technology, frequent new service introductions and evolving industry standards. If Pareteum fails to adapt successfully to technological advances, it could lose customers.

Integration of acquisitions - Strategic acquisitions are a part of the company's growth strategy. Acquisitions of businesses and customer lists involve operational risks, including the possibility that an acquisition may not ultimately provide the benefits originally anticipated by management.

Foreign currency exchange rates - Because most of Pareteum's business is conducted outside the US, fluctuations in foreign currency exchange rates versus the US dollar could adversely affect its financial results.

Competition – Pareteum is substantially smaller than its major competitors, whose marketing and pricing decisions, and relative size advantage, could adversely affect the company's ability to attract and retain customers and are likely to continue to cause significant pricing pressures that could adversely affect Pareteum's financial results.

Customer dependency **-** For the year ended December 31, 2017, Pareteum had one significant customer which accounted for 88% of its revenue. The loss or reduction in services to this significant customer could have an adverse impact on the company's business and financial condition.

Regulations – Pareteum operates in a heavily regulated industry. As a provider of communications technology, the company is subject to varying degrees of regulation in each of the jurisdictions in which it provides services. There can be no assurance that future regulatory changes will not have a material adverse effect on the company or that regulators will not raise issues with regard to Pareteum's compliance with applicable regulations.

Liquidity risk **-** Shares of Pareteum Corporation have risks common to those of the microcap segment of the market. Often these risks cause microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume and can lead to large spreads and high volatility in stock price. There are 90.2 million shares in the float and the average daily volume is approximately 1.3 million shares.

Miscellaneous risk **-** The company's financial results and equity values are subject to other risks and uncertainties including competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

Pareteum Corporation

Consolidated Balance Sheets
(in thousands $)

	2016A	2017A	9/18A
Cash and cash equivalents	931	13,538	18,434
Restricted cash	564	200	430
Receivables	615	2,058	7,200
Prepaid expenses	1,085	900	943
Total current assets	3,195	16,696	27,007
Other assets	129	91	39
Note receivable	1,012	595	588
Net property and equipment	8,709	4,714	3,945
Long term investments	-	3,230	3,230
Total assets	**13,045**	**25,326**	**34,809**
Accounts payable and customer deposits	2,317	1,979	2,796
Obligations under capital leases	11	-	-
Net billings in excess of revenues	952	243	123
Accrued expenses and other payables	6,013	5,250	3,891
Convertible promissory note	-	66	90
Loans payable	4,000	-	-
Total current liabilities	13,293	7,538	6,900
Derivative liabilites	4,266	1,598	-
Other long term liabilites	193	151	95
Convertible promissory note	821	618	-
Senior loan	3,716	-	-
Net billings in excess of revenues	121	-	-
Total liabilities	**22,410**	**9,905**	**6,995**
Total stockholders' equity*	**(9,365)**	**15,421**	**27,814**
Total liabilities & stockholders' equity	**13,045**	**25,326**	**34,809**

Source: Company filings and Taglich Brothers' estimates

Income Statements for the Fiscal Years Ended
(in thousands $)

	2016A	2017A	2018E	2019E
Revenue	12,856	13,548	31,324	113,000
Cost of revenue (excluding D&A)	3,659	3,684	10,054	45,000
Gross profit	9,197	9,864	21,270	68,000
Product development	3,544	1,480	3,347	9,600
Sales, general and administrative	13,049	11,672	20,323	34,000
Depreciation and amortization	4,247	4,533	3,868	4,000
Impairment, sale of assets, restructuring	7,260	966	2,074	-
Operating income (loss)	(18,903)	(8,787)	(8,342)	20,400
Interest income	112	172	186	200
Interest expense	(7,270)	(5,063)	(700)	(1,000)
Other income (expense)	(4,643)	103	2,040	-
Income (loss) before taxes	(30,704)	(13,575)	(6,816)	19,600
Income tax (benefit)	38	107	38	2,548
Net income (loss)	(30,742)	(13,682)	(6,854)	17,052
EPS	(4.56)	(0.84)	(0.10)	0.15
Shares Outstanding	6,739	16,338	69,451	113,125
EBITDA	(19,187)	(3,979)	(2,248)	24,600
Margin Analysis				
Gross margin	71.5%	72.8%	67.9%	60.2%
Product development	27.6%	10.9%	10.7%	8.5%
SG&A	101.5%	86.2%	64.9%	30.1%
Operating margin	(147.0)%	(64.9)%	(26.6)%	18.1%
Year / Year Growth				
Total Revenues		5.4%	131.2%	260.7%
Net Income		NMF	NMF	NMF
EPS		NMF	NMF	NMF

Source: Company filings and Taglich Brothers' estimates

Quarterly Income Statements 2017A - 2019E
(in thousands $)

	3/17A	6/17A	9/17A	12/17A	2017A	3/18A	6/18A	9/18A	12/18E	2018E	3/19E	6/19E	9/19E	12/19E	2019E
Revenue	2,795	3,239	3,499	4,015	13,548	4,113	6,003	8,008	13,200	31,324	20,000	26,000	31,000	36,000	113,000
Cost of revenue (excluding D&A)	842	946	791	1,105	3,684	1,195	1,780	2,129	4,950	10,054	7,800	10,400	12,400	14,400	45,000
Gross profit	1,953	2,293	2,708	2,910	9,864	2,918	4,223	5,879	8,250	21,270	12,200	15,600	18,600	21,600	68,000
Product development	285	273	497	425	1,480	727	754	766	1,100	3,347	2,100	2,300	2,500	2,700	9,600
Sales, general and administrative	2,685	1,861	1,992	5,134	11,672	2,986	2,867	8,970	5,500	20,323	8,500	8,500	8,500	8,500	34,000
Depreciation and amortization	844	873	1,433	1,383	4,533	965	994	999	910	3,868	1,000	1,000	1,000	1,000	4,000
Impairment, sale of assets, restructuring	129	459	253	125	966	74	5	1,995	-	2,074	-	-	-	-	-
Operating income (loss)	(1,990)	(1,173)	(1,467)	(4,157)	(8,787)	(1,834)	(397)	(6,851)	740	(8,342)	600	3,800	6,600	9,400	20,400
Interest income	39	55	42	36	172	43	43	50	50	186	50	50	50	50	200
Interest expense	(1,566)	(699)	(627)	(2,171)	(5,063)	(93)	(130)	(227)	(250)	(700)	(250)	(250)	(250)	(250)	(1,000)
Other income (expense)	2,198	423	(107)	(2,411)	103	(146)	2,159	27	-	2,040	-	-	-	-	-
Income (loss) before taxes	(1,319)	(1,394)	(2,159)	(8,703)	(13,575)	(2,030)	1,675	(7,001)	540	(6,816)	400	3,600	6,400	9,200	19,600
Income tax (benefit)	1	(68)	148	26	107	-	19	19	-	38	52	468	832	1,196	2,548
Net income (loss)	(1,320)	(1,326)	(2,307)	(8,729)	(13,682)	(2,030)	1,656	(7,020)	540	(6,854)	348	3,132	5,568	8,004	17,052
EPS	(0.14)	(0.10)	(0.16)	(0.31)	(0.84)	(0.04)	0.03	(0.12)	0.01	(0.10)	0.00	0.03	0.05	0.07	0.15
Shares Outstanding	9,322	12,911	14,304	28,613	16,338	50,062	64,741	59,315	103,685	69,451	109,000	114,500	114,500	114,500	113,125
EBITDA	1,091	178	(99)	(5,149)	(3,979)	(972)	2,799	(5,775)	1,700	(2,248)	1,650	4,850	7,650	10,450	24,600
<u>Margin Analysis</u>															
Gross margin	69.9%	70.8%	77.4%	72.5%	72.8%	70.9%	70.3%	73.4%	62.5%	67.9%	61.0%	60.0%	60.0%	60.0%	60.2%
Product development	10.2%	8.4%	14.2%	10.6%	10.9%	17.7%	12.6%	9.6%	8.3%	10.7%	10.5%	8.8%	8.1%	7.5%	8.5%
SG&A	96.1%	57.5%	56.9%	127.9%	86.2%	72.6%	47.8%	112.0%	41.7%	64.9%	42.5%	32.7%	27.4%	23.6%	30.1%
Operating margin	(71.2)%	(36.2)%	-41.9%	(103.5)%	(64.9)%	(44.6)%	(6.6)%	-85.6%	5.6%	(26.6)%	3.0%	14.6%	21.3%	26.1%	18.1%
<u>Year / Year Growth</u>															
Total Revenues					5.4%	47.2%	85.3%	128.9%	228.8%	131.2%	386.3%	333.1%	287.1%	172.7%	260.7%
Net Income					NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF
EPS					NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF	NMF

Source: Company filings and Taglich Brothers' estimates

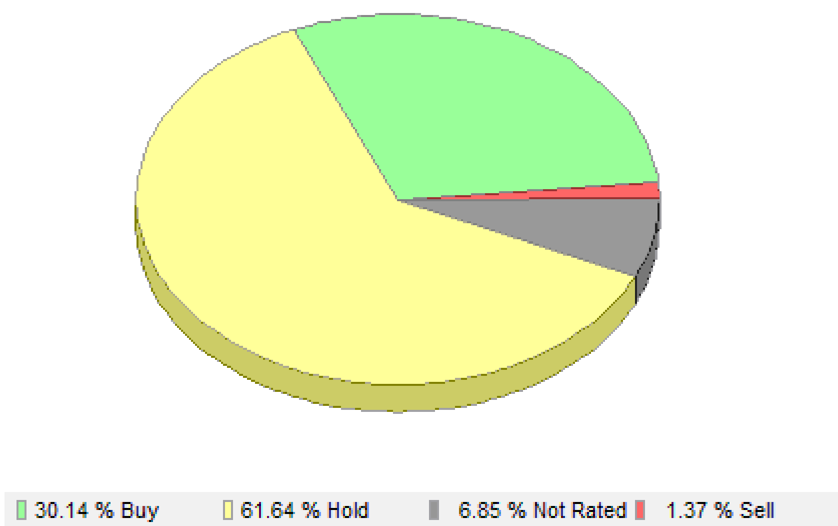
Statement of Cash Flows for the Periods Ended
(in thousands $)

	2016A	2017A	9m18A
Net income (loss)	(31,445)	(12,463)	(7,498)
Depreciation & amortization	4,247	4,533	2,958
Provision for doubtful accounts	(89)	3	-
Stock based compensation	3,897	4,289	7,410
Change in fair value of warrant liability	3,316	(795)	(1,284)
Amortization of deferred financing costs	1,267	341	21
Interest expense related to debt discount and conversion	6,042	3,409	175
Expense settled by issuance of shares	-	784	250
Other (income) expense	221	-	-
Amortization of debt discount and deferred financing costs	542	-	-
Impairment of assets	851	-	-
Impairment of goodwill	3,229	-	-
Loss on sale of assets	1,542	-	-
Cash earnings (loss)	(6,380)	101	2,032
Changes in assets and liabilities			
Receivables	622	(1,446)	(5,078)
Prepaid expenses, deposits and other	1,637	640	(28)
Payables and customer deposits	81	(349)	799
Net billings in excess of revenues	(1,169)	(830)	(128)
Accrued expenses and other	1,551	(732)	(1,421)
(Increase) decrease in working capital	2,722	(2,717)	(5,856)
Net cash provided by (used in) operations	**(3,658)**	**(2,616)**	**(3,824)**
Purchase of property, equipment, and software development	(1,413)	(722)	(2,189)
Advance purchase payment on assets held for sale	450	-	-
Proceeds from sale of assets	2,000	-	-
Net cash provided by (used in) investing	**1,037**	**(722)**	**(2,189)**
Financing receivable	355	-	-
Exercise of warrants and options	-	5,050	5,683
Equity and debt issuance costs	(1,339)	(227)	-
Principal payment on Eurodollar loan	(967)	-	(61)
Increase in short-term loans	-	-	-
Proceeds from convertible promissory note	2,273	-	-
Payment on convertible promissory note	-	-	-
Unsecured promissory note	350	-	-
Financing related fees	-	-	(633)
Gross proceeds from public offering	-	21,202	6,100
Reclassify accrued interest to principal	-	(84)	-
Principal repayment to senior lender	-	(10,082)	-
Gross proceeds from preferred stock	2,490	-	-
Net cash provided by (used in) financing	**3,162**	**15,859**	**11,089**
Effect of currency exchange rates	21	(279)	51
Net change in cash	**562**	**12,242**	**5,127**
Cash - beginning of period	**933**	**1,495**	**13,737**
Cash - end of period	**1,495**	**13,737**	**18,864**

Source: Company filings and Taglich Brothers' estimates

Price Chart

Taglich Brothers' Current Ratings Distribution



Investment Banking Services for Companies Covered in the Past 12 Months

Rating	#	%
Buy	**2**	**8**
Hold		
Sell		
Not Rated	**2**	**50**

Important Disclosures

As of the date of this report, we, our affiliates, any officer, director or stockholder, or any member of their families do not have a position in the stock of the company mentioned in this report. Taglich Brothers, Inc. does not currently have an Investment Banking relationship with the company mentioned in this report and was not a manager or co-manager of any offering for the company within the last three years.

All research issued by Taglich Brothers, Inc. is based on public information. The company paid a monetary fee of $4,500 (USD) in April 2018 for the creation and dissemination of research reports for the first three months. After the first three months from initial publication, the company will pay a monthly monetary fee of $1,500 (USD) to Taglich Brothers, Inc., for a minimum of six months for the creation and dissemination of research reports.

General Disclosures

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Analyst Certification

I, John Nobile, the research analyst of this report, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities and issuers; and that no part of my compensation was, is, or will be, directly, or indirectly, related to the specific recommendations or views contained in this report.

Public companies mentioned in this report:

Meaning of Ratings

Buy – The growth prospects, degree of investment risk, and valuation make the stock attractive relative to the general market or comparable stocks.

Speculative Buy – Long term prospects of the company are promising but investment risk is significantly higher than it is in our BUY-rated stocks. Risk-reward considerations justify purchase mainly by high risk-tolerant accounts. In the short run, the stock may be subject to high volatility and could continue to trade at a discount to its market.

Neutral – Based on our outlook the stock is adequately valued. If investment risks are within acceptable parameters, this equity could remain a holding if already owned.

Sell – Based on our outlook the stock is significantly overvalued. A weak company or sector outlook and a high degree of investment risk make it likely that the stock will underperform relative to the general market.

Dropping Coverage – Research coverage discontinued due to the acquisition of the company, termination of research services, non-payment for such services, diminished investor interest, or departure of the analyst.

Some notable Risks within the Microcap Market

Stocks in the Microcap segment of the market have many risks that are not as prevalent in Large-cap, Blue Chips or even Small-cap stocks. Often it is these risks that cause Microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume which can lead to large spreads and high volatility in stock price. In addition, Microcaps tend to have significant company specific risks that contribute to lower valuations. Investors need to be aware of the higher probability of financial default and higher degree of financial distress inherent in the microcap segment of the market.

From time to time our analysts may choose to withhold or suspend a rating on a company. We continue to publish informational reports on such companies; however, they have no ratings or price targets. In general, we will not rate any company that has too much business or financial uncertainty for our analysts to form an investment conclusion, or that is currently in the process of being acquired.