



November 2011

Elephant Talk Communications (OTCBB: ETAK) **On the path to becoming one of the great microcap winners of the decade**

ETAK and its 100%-owned ValidSoft subsidiary are aligned with pivotal trends of the emerging transaction-based mobile cloud with market-ready solutions. Together, they are capable of scaling revenues to a billion dollars and more within four years.

Rumble in the Telecom Jungle

When I go down my checklist of requirements for microcaps, Elephant Talk rates an "A" for each important item. But for all of the impressiveness of its technical capabilities, one characteristic that I find especially appealing is the sheer determination of its management to take on the very complex challenges of making it all work.

My initial recommendation for ETAK was in October 2009 at \$1.39. A few months ago, the shares traded as high as \$4. Despite the very speculative nature of the stock in late 2009, I wanted our subscribers to start building positions early because I had confidence in management's ability to execute on its ambitious growth strategy. If fully successful, the returns will be like a big venture capital winner - 10, 20, 30 times our investment.

When I first met with Elephant Talk's management and researched the company, management was in the process of completing its acquisition of ValidSoft. A critical part of the story is that Elephant Talk provides ValidSoft access to the telecom networks it could not otherwise get on its own. It took many months to make it official, but there was little doubt that it would be done and that it would transform the company.

In the meantime, Elephant Talk was establishing itself as a provider of a software services platform for the telecom industry. Today, Elephant Talk is at the center of a powerful wave in the telecom industry that is transforming the way businesses and organizations like supermarkets, banks, and government agencies connect with their customers. A lot of new businesses will be using the cloud by becoming mobile virtual network operators (MVNOs) to have a two-way discussion with their customers and communities.

Most major telecom companies are ill-equipped to operate on this level and prefer to outsource these operations. As a mobile virtual network enabler (MVNE), Elephant Talk serves up a full mobile operation out of a box. There is no need to build out spectrum and antennas because they are simply rented from mobile telecom operators such as Elephant Talk customers T-Mobile Netherlands and Vizzavi Spain, part of the Vodafone Group.

This is a huge global opportunity for Elephant Talk which extends from Europe, Asia and the Middle East to South America. Already, MVNOs have 85 million subscribers, according to the research firm Informa Telecoms & Media, with rapid growth continuing. The firm predicts that total revenues for MVNOs will climb to \$80 billion per year by 2012.

Now, as huge as this business will be for Elephant Talk, it is ValidSoft that is going after an even bigger market opportunity.

ValidSoft's Revolutionary Solution

The key to understanding ValidSoft is this: It has the only real-time solution for the global credit and debit card fraud problem. At the time of a transaction, whether it's in a store or at an ATM, ValidSoft's solution enables banks and credit card companies to make a decision about the transaction's legitimacy in less than a second. Amazingly, ValidSoft is proving that the decision is correct nearly every single time.

ValidSoft's point-of-sale solution (Valid-POS) works equally well for international transactions as it does for domestic U.S. transactions. In either case, the results are delivered to the credit-card company or bank in less than a second -- 400 milliseconds to be precise.

Working behind the scenes, within the systems of financial institutions, Valid-POS takes advantage of mobile communications to detect whether a cardholder is in the same country or state in which a transaction occurs. If it is shown that the cardholder is not in proximity then there's a very high probability the transaction is fraudulent.

Importantly, ValidSoft never reveals the location of the cardholder even though it knows. The privacy aspect is critical for success and ValidSoft met the toughest requirements when it was awarded the prestigious European Privacy Seal -- the only security software company in the world to ever achieve this.

In exhaustive pilot testing with Visa Europe and major global banks, Valid-POS has demonstrated 100% accuracy -- compared to the standard currently applied to those transactions that are declined at point-of-sale when nearly 90% turn out to be legitimate, know as false-positives.

By being 100% accurate, versus the industry's current 10% rate of accuracy, ValidSoft is going to cause a tidal change in how credit card companies and banks process card fraud.

Of course, any denied transaction can't just be declined without additional steps. What typically happens is that the embarrassed cardholder contacts his or her bank. At other times the bank picks up on a problem and wants to contact the customer -- either way there is a time delay.

For any transaction that Valid-POS considers potentially fraudulent, the cardholder is notified instantly on his or her mobile phone. If the customer is in close proximity (i.e., same state or country) to the location of the transaction, then he or she has an option to press the number "1" to confirm. A voice or message responds by thanking the person and apologizing for any inconvenience.

If, however, the customer is in, say, the UK and he or she is alerted that the card was used in New York, then he or she can press "#" on their mobile phone and be routed directly to the fraud center, which will deal with the potential fraud situation in real-time -- while it's happening!

In either situation, the bank looks intelligent and on the ball, and the customer is provided the best-possible service with the problem quickly addressed and/or resolved.

In the U.S. alone, credit and debit card fraud costs the financial industry \$100 billion a year -- a number expected to triple during the next three-to-five years.

There are 350 billion credit and debit card transactions annually worldwide, and ValidSoft presents a win-win solution for the industry and customers through an affordable, proven technology that passes the most stringent privacy tests.

The current testing with Visa Europe and multiple global banks is progressing very well and I expect ValidSoft's Valid-POS will be running live by Q4 this year in at least one institution, if not more. The stakes are enormous since ValidSoft will net in the neighborhood of 5 to 10 cents per transaction. And once ValidSoft establishes itself with one major financial player, it will force others to jump on the bandwagon to remain competitive.

Finally, ValidSoft's technology is perfectly suited for other financial applications, including NFC (or near-field communications) and mobile wallets, which represent an even grander scale of transactions. ValidSoft started down this path in 2003 and has built a robust intellectual property portfolio that will enable it to effectively control the market slated to become one of the biggest to emerge in the coming decade: Security for the mobile cloud.

Subscribe now to *MicroCap Investor*, and you will instantly gain access to all of Josh's stock picks and all of his insights for discovering the next 10-bagger winners.

[SUBSCRIBE NOW](#)

Biggest, Fastest-Growing Markets

The sizes of the markets ETAK and ValidSoft operate in are staggering. For example, just consider the *\$20.5 trillion global market* for in-store retail transactions that they are targeting.

This figure represents the total of all payment transactions that occur in stores around the world each year. As payments and other transactions such as banking move into the mobile cloud, Elephant Talk and ValidSoft will provide security and services solutions to the big players in this space as it emerges, including the banks and credit card companies, and telecom carriers. Of course, Apple and Google are vying for slices of this pie and are in a strong position to influence the market as it develops.

ValidSoft will generate revenues on a per transaction basis, so even at pennies for each transaction the company could scale to immense levels very rapidly.

In a recent presentation, ValidSoft CEO Pat Carroll points out that the growth of Near Field Communication (NFC) and "tap and go" payments using cell phones -- rather than credit cards -- would lead to a five-fold increase in electronic transaction volumes. It would also be advantageous for ValidSoft's multi-factor authentication approach to fraud prevention.

As NFC chips become increasingly embedded in smart phones and other devices and gain traction worldwide, the stakes get larger. A BusinessWeek article explains: "As this technology takes off the cell phone could become the central repository of not just bank account information but coupons, loyalty points, and membership cards, allowing companies such as Google to route deals to cell phones at just the right time and place."

As these trends unfold, a major portion of marketing is going to go through this personalized media channel. Retailers will be able to gather more point-of-sale data from their customers, while Google sees big dollars in helping retailers target customers with personalized, real-time deals and offers.

The pitch being made to consumers is that instead of juggling coupons, loyalty cards, credit cards and receipts, the entire payment process can be unified into a one-tap transaction. Most of us will be ready and willing to participate as long as privacy and security concerns are resolved.

Of course, the revolution cannot happen without cell phones being equipped for NFC. And nearly every phone manufacturer, including Nokia, Samsung, and Research In Motion, plans to pack its handsets with NFC chipsets, which in 2011 should cost \$2.13 on average, down from \$2.57 in 2009, according to ABI Research.

Despite these efforts, the game changer will be Apple, which last week reported out-of-this-world quarterly results on the strength of soaring demand for its iOS-based products, the iPhone and iPad.

Apple is believed to be vigorously pursuing NFC technologies and is expected to incorporate NFC chips in a version of the iPhone either this year or next. Meanwhile, since 2008 Apple has applied for 36 patents that involve NFC. They include a way to

turn NFC-equipped iPhones and iPads into cashier terminals, and allowing Apple devices within close proximity to quickly and easily share files with each other.

The other side of the equation consists of the world's largest credit card issuers -- the four biggest being MasterCard, Visa, American Express, and Discover. The four last week announced that they're joining ISIS, a partnership of American carriers formed last year aimed at bringing mobile payment capability to phones in early 2012.

With the leading phone manufacturers and the biggest credit card firms vested in seeing the widespread adoption of NFC, the probability is fast improving that mobile payments will reach nearly \$700 billion worldwide in 2015 as Juniper Research predicts.

ValidSoft's solutions were developed from the start for NFC-type payments. As NFC is implemented, the company will be ideally positioned to partner with leading players -- just as ValidSoft is doing now in regard to credit/bank card fraud prevention, detection, and authentication.

ValidSoft's relationship with parent Elephant Talk is even more valuable in an NFC universe because ETAK's innovative telecom software services and infrastructure were developed to support media and marketing channels like those emerging for the NFC environment. Elephant Talk's services have the capacity to process 400,000 transactions per second or 12.6 trillion transactions a year.

As I mentioned earlier, ValidSoft's security solutions are incredibly accurate. Current technologies used by card processors have up to a 98% false-positive rate while ValidSoft achieves virtually 100% accuracy in eliminating false positives, thereby enabling fraud discovery.

Everyone, Everything Connected

There will be explosive growth of mobile connected devices -- supporting an addressable revenue opportunity for mobile operators of nearly \$1.2 trillion by 2020, a sevenfold increase from expected revenues in 2011. It's safe to say that mobile will connect with almost everything in our lives.

To make it work will require collaboration across the entire ecosystem to demonstrate how mobile technology in everything from tablet PCs to new healthcare devices can enhance people's lives and businesses. Of course, security plays a central role in determining the pace of adoption since concerns about fraud and ID/information theft are so critical.

In a recent interview, ValidSoft Chairman and ETAK board member Phil Hickman said financial fraud for banks in the UK alone is more than \$3 billion. This total includes the costs of administrating fraud, but not the costs to reputation or customer loss.

Hickman has over 30 years experience and is regarded as an expert in payments processing. Prior to his association with ValidSoft he was CEO of Intelligent

Processing Solutions Limited, a role that naturally evolved from his previous role as head of strategy & planning for HSBC Commercial Bank.

In the US, the fraud problem is far bigger and the banks are even more vulnerable, since skimming of customers' credit card details could be used either to manufacture false credit cards or for online purchases.

"This is a lot easier in the US where credit card companies don't use the microchips common in European cards", writes ValidSoft CEO Pat Carroll. "But those chips don't prevent, for example, the use of stolen credit card details for online purchases", he says.

Carroll argues that the financials industry's primary focus should be on preventing fraudsters from using stolen data. He also explains how ValidSoft's solutions address this serious problem comprehensively:

"Technology can already show that an individual (in fact his/her mobile phone) is not in the US when his/her credit card is being used at a POS in New York. Technology can do so in total respect of privacy laws, through anonymous correlation, and in a way that is totally invisible to the customer before such withdrawals and purchases are authorized. Technology can also support additional strong transaction authentication and verification methods, namely through an automated call to that phone can immediately confirm that fact, and - if the card holder rejects the transaction - alert the issuing bank to block the card.

"And if the fraudsters have gone to the lengths of swapping the sim card or automatically forwarding calls to the customer's mobile number on to a number of their own, that can also be detected. The level of authentication can be tailored to the transaction type and size, and can even include voice biometrics for added security if the card issuer wants to use it.

"The key lies in real-time detection, prevention and immediate resolution enabled by the empowered customer. The security technology industry has a job to do in encouraging customers to question just how it is possible in 2011 for a skimming scam like the one uncovered in New York to be so profitable on such a scale. That really is a mind-boggling thought."

The New York incident Carroll refers to ended in the arrest of 111 people for a \$13 million card fraud scam that he characterizes as typical.

Have Visa, Will Travel

Recently, Google said it is adding Visa, American Express and Discover to its payment system, which aims to make cellphones the next credit cards. The company said it had licensed the right to add virtual 'cards' from the three payment networks to Google's Wallet. MasterCard Inc. is already part of the project.

With a card in the Wallet, owners can pay for merchandise by tapping their phones on wireless-capable payment terminals, instead of swiping a credit card. There are more than 135,000 such terminals in stores and other retail locations, but that's a small fraction of the total number of terminals.

Google's deal with Visa "paves the way for global Visa-issuing banks to add their credit, debit and prepaid accounts to Google Wallet," according to an analyst with Keefe, Bruyette & Woods. He added that the movement to phone-based payments is on "a steady course to achieve implementation" as long as more phone companies offer working products and more merchants accept the payments.

As if we need further proof of the financial industry's direction, American Express said it is looking at large international acquisitions that will help it benefit from booming demand for mobile payments and online commerce in emerging markets.

In developing countries such as India and China, a growing number of consumers are acquiring credit cards and smartphones. China will surpass the US as the world's largest credit-card market by 2020, MasterCard said last year.

As you can see, ValidSoft is in the sweet spot of a huge industry tidal wave. While ETAK's existence is not dependent on Visa or any other global bank, its future success will be largely determined by the commitment to commercializing ValidSoft's solution. If these organizations take the next steps as it appears they will, then the impact on ETAK and ValidSoft will be overwhelming!

Built for Amazing Growth

If there was a single message at ETAK's annual shareholder meeting in September 2011 it was this:

ETAK and its wholly-owned ValidSoft subsidiary have established proven world-class technical foundations and critical partnerships with multinational telecom and financial firms. The ramp is now in place for a sharp upward rise in high-margin revenues - both as providers of telecom software and services, and security and anti-fraud solutions.

The company's businesses are modeled on recurring revenues, which are a beautiful thing if you can do it. The reason ETAK and ValidSoft revenues will scale so fast and far is because major customers across several industries are:

Shifting investment from capital expenditures to the operational side, enabling them to free up resources;

Moving from fixed to variable costs, preferring "pay as you go" arrangements, and

Replacing overly complex and partial solutions with one-stop-shop solutions.

Elephant Talk and ValidSoft enable their customers to adapt to these changes and ETAK will profit immensely for providing the services. Let's look more closely at the basic numbers and the potential for amazing growth.

Cash Machine

Elephant Talk and ValidSoft are tackling some mighty big markets with their proprietary solutions. By managing the network embedded mobile cloud ETAK

targets 900 mobile operators with a rising tide of virtual operators. There are up to 8 billion handset SIM's and up to 50 billion machine-to-machine SIM's around the globe and growing.

As an enabler of mobile network operators, ETAK will on average charge \$1 per month per subscriber and nearly 100% of the revenue will fall to the bottom line. The company expects to have one million SIM cards in operation at the end of 2011, which translates to \$12 million for 2012.

In addition, I estimate ETAK will have a total of 2.5 million on board next year, 5 million in 2013, and 10 million in 2014. Using this model, from this business alone ETAK will be generating \$120 million on an annualized basis in about three years. And remember we're talking virtually pure earnings here!

By offering the most robust and comprehensive solution for securing the cloud and a range of financial transactions, ValidSoft targets the current 350 billion transactions per year, which is anticipated to soar once near-field communications is widely implemented.

Now, it gets really mind-blowing when we consider ValidSoft's revenue model, which is based on payments per transaction. The number of annualized transactions can quickly grow from hundreds of millions to tens of billions and even greater. At an estimated range of 7 cents to 22 cents (depending on volume) and with margins of at least 50%, ValidSoft will be the biggest growth engine for ETAK.

Using a conservative 10 cents, every billion transactions per year represents \$100 million in annual revenue for ValidSoft. If it covers only 10% of the transaction universe, this will generate more than \$3 billion annually. If ValidSoft's solutions become the industry standard, as I believe they will, then the ultimate revenue could be a multiple of this, especially if we factor in NFC transactions!

As you can see, ETAK and ValidSoft have an opportunity to become one of the fastest growing companies in history. While challenges and hurdles remain ahead, the company's newest strategic partner increases the probability for reaching such heights.

Pivotal New Partner

Elephant Talk briefly mentioned its new agreement with Adeptra in a press release and touched on the subject at its annual meeting. There will be more details in the near future, but what is clear is that Adeptra provides ValidSoft with a welcome entrée to a large market segment in its sights.

Adeptra provides communications for services, fraud processing, marketing, and collections for major credit card companies and other customers. These include the majority of world-leading consumer finance organizations -- half of North America's top 10 financial institutions, seven of the leading 10 UK card issuers, and four of the top five Australian card issuers.

Privately-held, Adeptra doesn't report financials and other information publicly, but it performs hundreds of millions of interactions for its customers and it is clearly a technology and market leader. As a group deeply committed to advanced technology

solutions, its partnership with ETAK is a strong endorsement for ValidSoft and a sign of what's to come.

Buy ETAK Ahead of Catalysts

As for its stock listing, Elephant Talk has completed the requisite steps to upgrade its listing to AMEX and it should be on board before year-end. This is my guesstimate since management cannot comment specifically on such things.

With only \$2.5 million in revenues from mobile and security solutions for the first half of 2011, it would be a mistake to dismiss the stock as 'pricey' and take a wait and watch stance. The time to get fully positioned is before any major catalysts happen. Once they do, the valuation model by The Street is going to be radically reformulated and investors will begin parading into the stock.

Meanwhile, ETAK's shares have slid back toward their long-term support and are ripe for aggressive buying. **I recommend accumulating a full position while the stock trades below \$2.50.**

Subscribe now to *MicroCap Investor*, and you will instantly gain access to all of Josh's stock picks and all of his insights for discovering the next 10-bagger winners.

[SUBSCRIBE NOW](#)

Subscribers to *Levine's MicroCap Investor* receive:

- *Weekly newsletter with insights, updates and specific advice*
- *Real time alerts if there is critical news*
- *Special reports and a primer on microcap investing strategies*
- *Login access to portfolio history and archive for each company*

DISCLOSURE

Josh Levine owns shares in Elephant Talk Communications (ETAK).

CUSTOMER SERVICE

You can reach us at admin@levinesmicrocapinvestor.com or you can call us at 800-665-0411.

MEMBER WEBSITE

www.levinesmicrocapinvestor.com

Copyright ©2011 Plexus Capital Management, Inc., all rights reserved.

No portion of the above message may be republished, retransmitted or forwarded without express written consent of Josh Levine. Violation of this copyright may result in service cancellation and/or collection of full or partial subscription charges from unauthorized users. Use and/or reliance on this service is strictly at the subscriber's own risk. Josh Levine and Levinesmicrocapinvestor.com will not be liable for the acts or omissions of any third party with regards to delay or non-delivery of the MicroCap Investor. Josh Levine and Levinesmicrocapinvestor.com shall not be liable for incidental, indirect, special or consequential damages or for lost profits, savings or revenues of any kind.