Zacks Small-Cap Research

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Integral Technologies, Inc. (ITKG-OTC)

ITKG: Believe First Quarter Validates Prospects for Multiple Revenue Streams

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	06/05/2014
Current Price (12/4/14)	$0.49
Six- Month Target Price	**$1.25**

OUTLOOK

Integral Technologies reported results for its first quarter fiscal 2015 recently that underscore, we believe, business, cost structure and financial improvements. Importantly we believe, the results provide proof of concept of Integral's potential to generate revenue from licensing, engineering support and sales of ElectriPlast.

SUMMARY DATA

52-Week High	**$0.79**
52-Week Low	**$0.24**
One-Year Return (%)	**48.5**
Beta	**1.04**
Average Daily Volume (sh)	**249,223**
Shares Outstanding (mil)	**101**
Market Capitalization ($mil)	**$50**
Short Interest Ratio (days)	**1.8**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**13**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2015 Estimate	**N/A**
P/E using 2016 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Elec-Misc Compn**
Zacks Rank in Industry	**14 of 34**

ZACKS ESTIMATES

Revenue
(in thousands of $)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2012	0.0 A	0.05 A	0.04 A	0.02 A	0.10 A
2013	0.07A	0.05 A	0.07 A	0.06 A	0.25 A
2014	6.41 A	6.31 A	6.31 A	10.14 A	29.17 A
2015	90.8 A	91.7 E	89.4 E	107.3 E	379.2 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2012	-$0.00 A	-$0.00 A	-$0.00 A	-$0.00 A	-$0.01 A
2013	-$0.00 A	-$0.01 A	-$0.00 A	-$0.01 A	-$0.00 A
2014	-$0.02 A	-$0.01 A	-$0.02 A	-$0.01 A	-$0.05 A
2015	-$0.01 A	-$0.01 E	-$0.01 E	-$0.01 E	-$0.04 E

Zacks Projected EPS Growth Rate - Next 5 Years %	**N/A**
Disclosures begins on page 8	**N/A**

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KEY POINTS

- Integral Technologies recently reported first quarter fiscal 2015 results. Revenue of $90,782 was up more than 8-fold sequentially from $10,139 recorded in 4Q FY 2014. Importantly, we believe, the results provide proof of concept of Integral's potential to generate revenue from licensing, engineering support and sales of ElectriPlast, as revenue in the quarter was driven by all three business lines.

- Engineering was the largest revenue driver in the quarter. Management believes that many companies will require Integral's engineering expertise on conductive plastic applications and specifically on ElectriPlast.

- The company's results also reflect management's cost containment efforts, as well as of balance sheet the improvements over the past several quarters. Reflecting the elimination of convertible debt, financial charges decreased by $59,433. The company was able to narrow its net loss to ($840,517) versus ($1,289,694) registered in the same period of fiscal 2014.

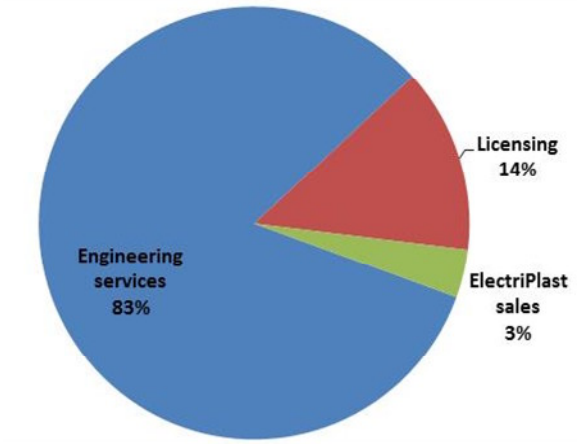
- Some business affiliations, such as with East Penn and Hanwha, have already produced revenue. Management is optimistic about the potential revenue opportunity with other partners, as well, including BASF, Delphi and Chang Rim. Management noted that Integral has been trialing ElectriPlast applications in the wire and cable niche with Delphi.

FIRST QUARTER FY 2015 HIGHLIGHTS

Integral Technologies (OTC: ITKG) recently reported first quarter fiscal 2015 results that underscore, we believe, business, cost structure and financial improvements. Revenue of $90,782 was ahead of our $85,168 forecast and up more than 8-fold sequentially from $10,139 recorded in the fourth quarter of fiscal 2014. Importantly we believe, the results provide proof of concept of Integral's potential to generate revenue from licensing, engineering support and sales of ElectriPlast. Revenue in the quarter was driven by all three business lines, with engineering services revenue of $75,000 accounting for 83% of the total. The engineering services revenue reflects Integral's recent agreement with East Penn Manufacturing. East Penn operates the largest single-site, lead-acid battery manufacturing facility in the world and, according to management, is a leader in custom wire and cable solutions. Under the terms of the contract, ElectriPlast will provide engineering and design services, materials and finished products to East Penn. The company received a $150,000 payment from East Penn and recorded 50% in the September quarter, with the balance expected to be recorded in the December quarter. We have raised our revenue projection for the December quarter.

In addition, the company recognized $12,500 of license revenue, as it amortizes the $500,000 payment it received from Hanwha over a 10-year period corresponding to the terms of Hanwha's license. Another $3,282, or 3% of total revenue, reflected sales of ElectriPlast. We anticipate that revenue streams are likely to ramp substantially over time, although we would also not be surprised to see revenue somewhat lumpy on an interim quarterly basis.

Integral 1Q FY15 Revenue Breakdown



Source: Company reports

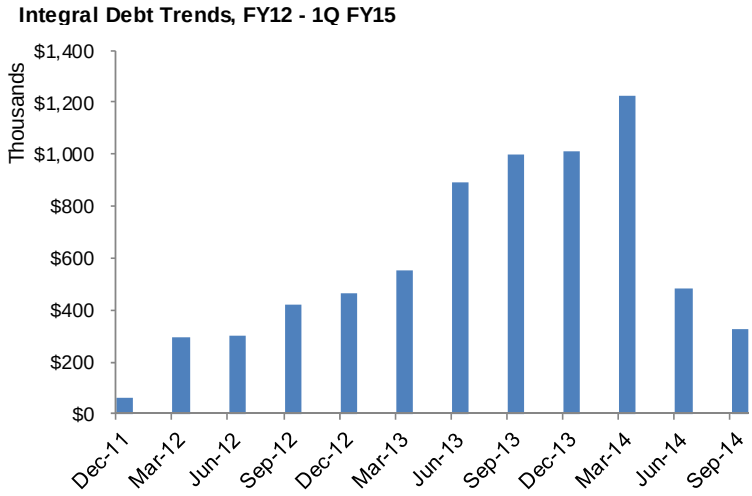
Engineering was the largest revenue driver in the quarter, as noted. Management believes that many companies will require Integral's engineering expertise on conductive plastic applications and specifically on ElectriPlast in order to use ElectriPlast. ElectriPlast is such a new product that others have not developed engineering expertise around it, management believes. In January 2014, the company opened a Tech Center in Detroit and has also put key engineering personnel in place. For example, in February 2014, Integral added Slobodan Pavlovic to the Detroit Tech Center engineering team. He has extensive industry experience, most recently from Lear Corporation. The company's CTO Mohamad Zeidan was formerly CTO of the Electrical Division for Lear Corporation. Integral's engineering team and the Tech Center can help customers such as East Penn move from the development stage on products incorporating ElectriPlast to design, prototyping and implementation of commercial applications, we believe.

Benefits of Cost Containment Efforts

The company's results also reflect management's cost containment efforts. S,G&A expenses of $909,233 were 28.9% or $253,717 lower compared to $1,162,950 registered in the first quarter of FY 2014. S,G&A included non-cash, stock based compensation expense and non-cash stock based payments that together were $151,415 compared to $601,996. In addition, Consulting expenses declined by $566,877 year-over-year, offset partially by a $229,730 increase in salaries and benefits. R&D was $7,847 or 21.8% lower compared to last year's first quarter. Reflecting the growing revenue and lower year-over-year costs, Integral's operating loss of ($837,800) was 29.2% narrower compared to ($1,183,733) recorded in 1Q FY14.

STRENTHENING THE BALANCE SHEET

The first quarter FY 2015 bottom line also benefited from the company's strengthening balance sheet over the past several quarters, with deleveraging measures and capital structure improvements**.** Integral has eliminated convertible notes. On May 1, 2014, Integral repaid a $96,681.70 outstanding convertible promissory note to Asher Enterprises and converted $55,120.00 into 342,035 ITKG shares. Integral also has eliminated convertible notes outstanding to JMJ Financial, as well as all preferred shares outstanding.



Source: Company reports

Reflecting the elimination of convertible debt noted above, first quarter FY 2015 financial charges decreased by $59,433. The company was able to narrow its net loss to ($840,517) versus ($1,289,694) registered in the same period of fiscal 2014.

The company had $181,196 in cash on its balance sheet as of September 2014. Management expects to raise funds as existing warrants are exercised. This implies no dilution, as the company's fully diluted share count already contemplates the exercise of those warrants. Moreover, management also believes that the warrants are generally in friendly hands and the shares also have a six month restriction following the exercise of the warrants. Outstanding warrants could yield $12.8 million to Integral, according to the company.

STRONG RELATIONSHIPS WITH KEY PARTNERS

Some affiliations, such as with East Penn and Hanwha, have already produced revenue; management is optimistic about the potential revenue opportunity with other partners, as well, including BASF, Delphi and Chang Rim. On its recent quarterly investor call, management noted that Integral has been trialing ElectriPlast applications in the wire and cable niche with Delphi.

In June 2013, the company entered into a co-development agreement with Delphi Automotive PLC. Delphi Automotive is a leading global supplier of electronics and technologies for automotive, commercial vehicle and other market segments. The two companies intend to jointly develop wire and cable insulation applications using ElectriPlast.

Delphi has a global footprint, with technical centers, manufacturing and customer support facilities in 32 countries. It also has large wire and cable customers. Integral hopes to leverage Delphi's distribution channels to drive commercial adoption of ElectriPlast in the sector.

The wire and cable industry is roughly a $115 billion industry. Integral's application is to replace the metal shielding around the cable. The company believes that ElectriPlast has competitive advantages versus the metal that is currently used, including that the manufacturing process is more efficient and that it is lighter weight. The company expects the bulk of cable and wire demand to eventually come from higher voltage cables in transportation and consumer electronics.

Hanwha has already opened a manufacturing line dedicated to ElectriPlast and continues to make progress in Asia, according to management, which believes that Hanwha could bring ElectriPlast products to market within the next 12-18 months.

With existing and potential partners, the company expects the Tech Center to address what it believes will be rising demand for Integral's technical expertise in conductive plastics as its customer base grows. The center also enables internal testing, engineering and product development, allowing Integral to conduct material testing itself rather than relying on outside consultants. The company also expects that the Detroit Tech Center will help it expand its strategic relationships with BASF, Delphi and Hanwha, as well.

RISKS

- The biggest risk, in our view, is that the commercialization strategy for ElectriPlast with existing partners fails to materialize in a meaningful way and Integral needs to seek new affiliations in order to implement its strategy.

- Market penetration and adoption for ElectriPlast could be slower than the company anticipates or could never materialize.

- The cost of retrofitting manufacturing plants in order to use ElectriPlast as a substitute material could also constrain its adoption.

- Integral is under-capitalized and will likely need to seek additional short-term funding until it reaches a certain revenue level. While the company intends to minimize the impact on its fully diluted share count largely through warrants, Integral could require more funding than management currently anticipates.

PROJECTED INCOME STATEMENT & BALANCE SHEET

Integral Technologies, Inc. Income Statement & Projections

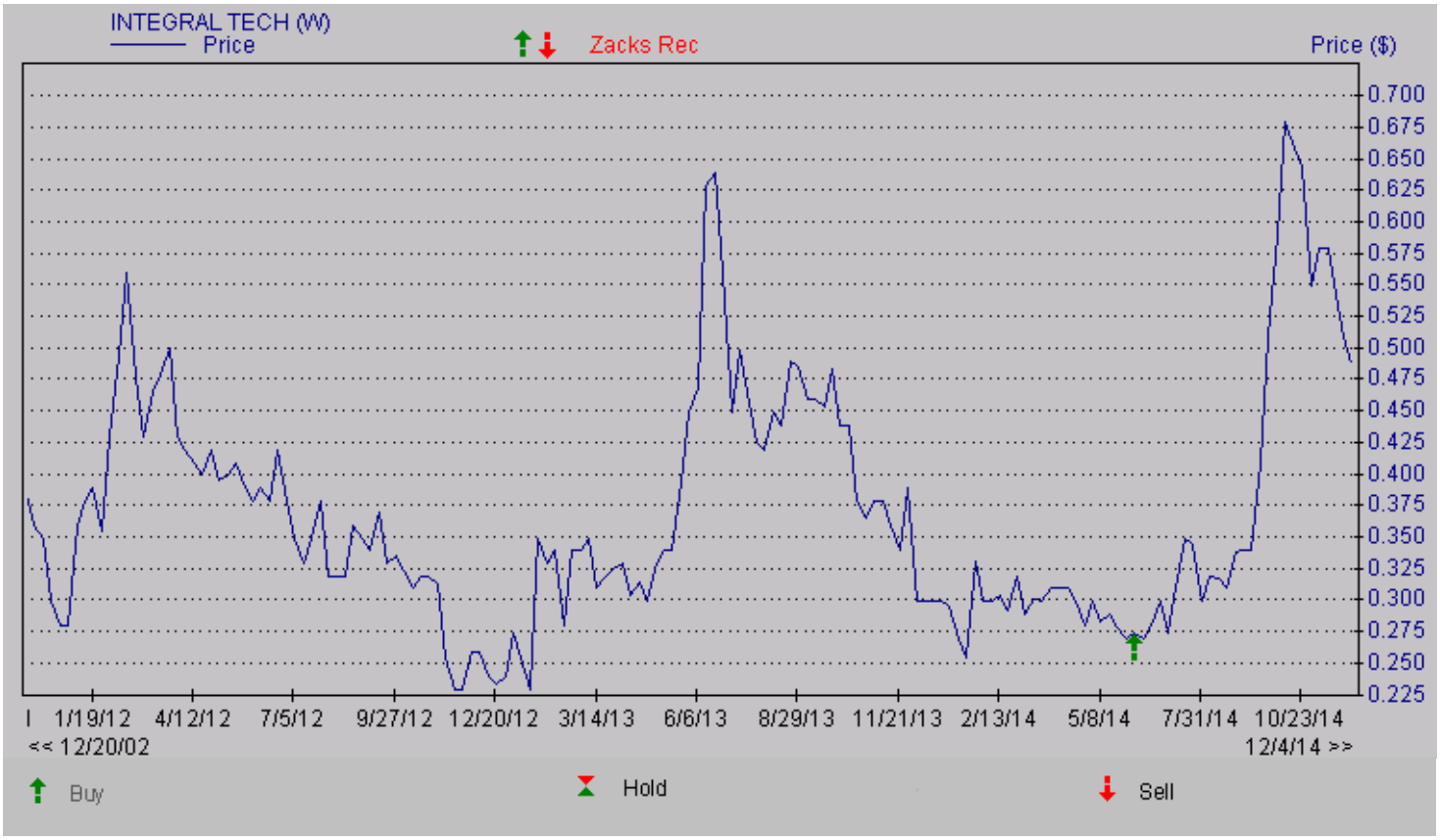
($)	Sep-13	Dec-13	Mar-14	Jun-14		Sep-14	Dec-14	Mar-15	Jun-15	
	1Q14	2Q14	3Q14	4Q14A	FY14A	1Q15A	2Q15E	3Q15E	4Q15E	FY15E
Licensing revenue	6,413	6,309	6,306	10,139	29,167	90,782	91,690	89,426	107,311	379,209
R&D	27,196	16,432	9,616	14,384	67,628	19,349	15,000	15,000	15,000	64,349
S,G&A	1,162,950	819,170	560,353	917,799	3,460,272	909,233	900,000	900,000	900,000	3,609,233
Non-recurring	-	-	675,000	-	675,000					-
Other	-	-	-	-	-	-	-	-	-	-
Total operating expense	1,190,146	835,602	1,244,969	932,183	4,202,900	928,582	915,000	915,000	915,000	3,673,582
Operating income	**(1,183,733)**	**(829,293)**	**(1,238,663)**	**(922,044)**	**(4,173,733)**	**(837,800)**	**(823,310)**	**(825,574)**	**(807,689)**	**(3,294,373)**
Other income net				(49,129)	(49,129)	62	(50,000)	(50,000)	(50,000)	(149,938)
Bank charges & interest	62,088	174,688	154,853	10,275	401,904	2,655	75,000	75,000	75,000	227,655
Fair value derivatives	103,842	(93,270)	15,205	(25,777)	-					-
Conv. debentures gain/ chg		(32,432)	-		-					-
Gain/ (loss) debt exting.	(75,429)	27,142	(150,367)		-					-
Financing fees	-	-	-	-	-	-	-	-	-	-
	90,501	76,128	19,691	(64,631)	352,775	2,717	25,000	25,000	25,000	77,717
Net Loss	(1,274,234)	(905,421)	(1,258,354)	(857,413)	(4,526,508)	(840,517)	(848,310)	(850,574)	(832,689)	(3,372,090)
Preferred stock dividends	(15,460)	(3,865)	(3,865)	7,730	(15,460)	-	-	-	-	-
Loss for common sharehol	(1,289,694)	(909,286)	(1,262,219)	(849,683)	(4,541,968)	(840,517)	(848,310)	(850,574)	(832,689)	(3,372,090)
Loss Per Share	($0.02)	($0.01)	($0.02)	($0.01)	($0.05)	($0.01)	($0.01)	($0.01)	($0.01)	($0.04)
Avg. shares out	77,057,027	77,738,310	81,015,996	83,475,729	85,935,461	99,824,249	99,824,249	99,824,249	99,824,249	99,824,249

Integral Technologies, Inc. Balance Sheet

($)	June 2012	Sept 2012	Dec 2012	March 2013	June 2013	Sept 2013	Dec 2013	March 2014	June 2014	Sept 2014
Cash	172,173	321,890	284,222	169,064	532,308	309,784	41,878	755,971	199,777	181,196
Prepaid expense	19,723	111,276	80,928	50,580	20,232	30,227		46,106	23,831	192,732
Account receivable	-	-	-	-	250,000	-	-	-	-	
Property & equipment	-	-	-	-	-	-	-	-	27,821	35,017
Total Assets	**$191,896**	**$433,166**	**$365,150**	**$219,644**	**$802,540**	**$340,011**	**$41,878**	**$802,077**	**$251,429**	**$408,945**
Accounts payable and accruals	2,032,309	2,353,369	2,410,715	1,890,307	2,270,727	1,803,061	1,650,692	943,930	973,220	739,613
Loan payable				31,708				52,323	60,000	
Notes payable	123,696	79,461	60,529	-	-	53,950	60,000	65,000		110,000
Deferred revenue	-		67,273		25,000	25,000	25,000	25,000	50,000	125,000
Loan payable		103,423				20,189				
Convertible debentures	93,356	129,576	48,773	116,207	174,827	108,895	137,030	217,846		
Derivative financial liabilities	84,718	105,610	56,426	107,616	414,102	517,109	300,117	271,957		
Redeemable preferred stock	-	-	120,000	150,000	180,000	210,000	240,000	170,000	-	-
Total current liabilities	**$2,334,079**	**$2,771,439**	**$2,763,716**	**$2,295,838**	**$3,064,656**	**$2,738,204**	**$2,412,839**	**$1,746,056**	**$1,083,220**	**$974,613**
Deferred revenue	-				225,000	218,750	212,500	206,250	229,500	408,333
Redeemable Preferred Stock	-		180,000	150,000	120,000	90,000	60,000	-		
Notes payable	-	-	-	-	-	-	215,000	450,000	420,833	219,000
Total Liabilities	**$2,334,079**	**$2,771,439**	**$2,943,716**	**$2,445,838**	**$3,409,656**	**$3,046,954**	**$2,900,339**	**$2,402,306**	**$1,733,553**	**$1,601,946**
Total Stockholders' Deficit	**($2,142,183)**	**($2,338,273)**	**($2,578,566)**	**($2,226,194)**	**($2,607,116)**	**($2,706,943)**	**($2,858,461)**	**($1,600,229)**	**($1,482,124)**	**($1,193,001)**
Total Liabilities and Stockholders'	**$191,896**	**$433,166**	**$365,150**	**$219,644**	**$802,540**	**$340,011**	**$41,878**	**$802,077**	**$251,429**	**$408,945**

Source: Company reports, Zacks

HISTORICAL ZACKS RECOMMENDATIONS



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Sell/Underperform: The analyst expects the company will underperform the broader U.S. Equity market over the next one to two quarters.

The current distribution is as follows: Buy/Outperform- 16.3%, Hold/Neutral- 77.2%, Sell/Underperform – 6.2%. Data is as of midnight on the business day immediately prior to this publication.