Zacks Small-Cap Research

July 27, 2015

Brian Marckx, CFA
bmarckx@zacks.com
Ph (312) 265-9474

scr.zacks.com

10 S. Riverside Plaza, Ste 1600, Chicago, IL 60606

Biomerica Inc (BMRA-OTCBB)

BMRA: Add'l Insight Into High-Potential IBS Product

OUTLOOK

Revenue growth had recently softened but is bouncing back. We think this recent strength will continue, despite a huge recent hiccup in Asia sales – this should now be ironed out. New distribution in Europe and product launches have facilitated growth there. Meanwhile, U.S. sales have been less regular but we think will return to growth by late 2015. Could see a big-winner with new GI test (still under dvlmpnt). We continue to see very little to no downside risk in the share price at this level. The stock is now trading at book value and balance sheet remains very solid. We see only upside as revenue is now returning to positive growth.

Current Recommendation	**Buy**
Prior Recommendation	N/A
Date of Last Change	01/23/2013
Current Price (07/27/15)	$0.75
Target Price	**$2.10**

SUMMARY DATA

One-Year Return (%)	**-16.67**
Beta	**0.54**
Average Daily Volume (sh)	**3,756**
Shares Outstanding (mil)	**8**
Market Capitalization ($mil)	**$6**
Short Interest Ratio (days)	**1.23**
Institutional Ownership (%)	**0**
Insider Ownership (%)	**25**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**0.5**
Earnings Per Share (%)	**42.0**
Dividend (%)	**N/A**
One-Year Return (%)	**-16.67**
Beta	**0.54**
P/E using TTM EPS	**N/A**
P/E using 2016 Estimate	**N/A**
P/E using 2017 Estimate	**12.5**
Zacks Rank	**N/A**

Risk Level	**High,**
Type of Stock	**Small-Value**
Industry	**Med-Drugs**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Aug)	Q2 (Nov)	Q3 (Feb)	Q4 (May)	Year (May)
2014	1.01 A	0.93 A	1.49 A	1.68 A	5.12 A
2015	1.03 A	1.13 A	1.30 A	1.47 E	4.94 E
2016					6.15 E
2017					7.70 E

Earnings per Share

	Q1 (Aug)	Q2 (Nov)	Q3 (Feb)	Q4 (May)	Year (May)
2014	-$0.02 A	-$0.03 A	$0.00 A	$0.02 A	-$0.03 A
2015	-$0.03 A	-$0.03 A	-$0.02 A	-$0.01 E	-$0.09 E
2016					-$0.01 E
2017					$0.06 E

Zacks Projected EPS Growth Rate - Next 5 Years % **NA**

© Copyright 2015, Zacks Investment Research. All Rights Reserved.

IBS Test Conference Call

Biomerica recently held a conference call regarding its under-development irritable bowel syndrome (IBS) diagnostic. As a reminder, in January the company filed the first set of patents related to the product and, more recently, brought on a scientific advisory board to help further guide their strategy related to the pipeline candidate. The board includes Dr. Doug Drossman, an expert in IBS who has authored several articles and publications on the disorder. Dr. Drossman is also the President of the Rome Foundation, a non-profit organization on the leading edge of GI disorder research and developer of the Rome III Questionnaire, which is a widely used clinical diagnostic for IBS. The advisory board, which also includes three other key opinion leaders in the GI and IBS field, will help guide BMRA through the FDA approval process.

BMRA has been largely tight-lipped about details of the IBS product as they lock down IP (patents are still pending). And while management still didn't provide specifics (on such things as biomarkers) on this recent conference call, they did confirm our prior suspicions that it is a diagnostic for food allergens (i.e. diet) which may be responsible for onset or aggravation of IBS. Additional details include;

- will identify certain trigger foods that may cause or exacerbate IBS symptoms
- will help physicians in guiding treatment protocol including putting the patient on a specific dietary regimen. This is different then other IBS tests which only focus on diagnosing presence of the condition. BMRA's test would be the first to both help diagnose IBS and to help guide treatment decisions
- test will be available for use in both the clinical lab and physician office settings
- would be reimbursed under existing CPT codes. As reimbursement is critical for maximizing early adoption, availability of payment under existing CPT codes is a significant benefit
- test is patent-pending at USPTO. BMRA has also filed for seven additional patents covering the technology

Zack Irani also did a nice job of framing the market opportunity for the test. Highlights of which included;

- Diagnostic cost of IBS in the U.S. is approximately $10.5B in annual direct costs and over $30B when including indirect costs
- IBS afflicts as much as 20% of the U.S. population, 25% of Japan, and 22%+ each of China and the U.K
- IBS is a top 10 reason for primary care doctor visits
- IBS is difficult to diagnose and difficult to treat
- Current diagnosis is more of ruling out other conditions than it is of a specific diagnosis for IBS
- A new blood-based test, recently highlighted on CBS Evening News in a segment titled *New tests offer hope for millions of patients with IBS*, has a false-negative rate of 56%. We think this highlights how elusive it has been to develop a reliable and effective IBS diagnostic. In addition, these new tests only aim to diagnose the disease but do not guide treatment decisions like BMRA's test is expected to do

As we noted in prior updates, we think having Dr. Drossman on board is a significant vote of confidence in the potential of BMRA's IBS product, which we continue to think could eventually be a big winner for the company. Once the initial patent is granted and published, we'll know more specifics about the test. We also expect management will be providing updates including more information as development of the product progresses. We will put out another update on BMRA when they file their 10-K, which should be near the end of August.

VALUATION / RECOMMENDATION

We use a comparable cohort of six companies of various market capitalizations in the medical diagnostics space with products/services that target the POC and/or clinical lab markets to value BMRA. Based on several metrics and excluding the low (and negative) and high values, BMRA is valued between $1.30 and $2.66 per share. Average is approximately $2.11/share.

The balance sheet remains solid. BMRA exited Q3 2015 with $1.2M in cash and equivalents and no debt. Book value at the end of fiscal Q3 2015 stood at $5.3 million or approximately $0.71/share. We continue to believe that book value should put a floor on valuation of the company.

We recommend buying the shares up to our $2.10/share target price and are maintaining our Buy rating.

Comparable Multiples

Ticker	P/E (ttm)	P/E (FY1)	P/E (FY4)	P/Book	EV / EBITDA (ttm)	P/S (ttm)	P/S (FY1)
TRIB	24.0	17.6	12.1	2.1	20.0	3.9	3.6
CEMI	N/A	N/A	10.0	2.1	N/A	1.5	1.5
VIVO	22.5	20.8	15.0	4.9	12.9	4.1	4.0
ERB	N/A	N/A	N/A	8.3	52.0	5.4	N/A
CONX	25.0	25.0	12.6	2.5	21.0	1.5	1.2
ABAX	74.0	51.0	32.9	6.9	33.6	7.1	6.7
Average	**36.4**	**28.6**	**16.5**	**4.5**	**21.9**	**3.9**	**3.6**

FY1, FY4 = forecast year 1, forecast year 4

Biomerica Stock Value Based On Comp:

	P/E (ttm)	P/E (FY1)	P/E (FY4)	P/Book	EV / EBITDA (ttm)	P/S (ttm)	P/S (FY1)	AVG
BMRA	~~$1.07~~	~~$2.54~~	$1.30	~~$3.37~~	~~$0.29~~	$2.66	$2.35	**$2.11**

FINANCIAL MODEL

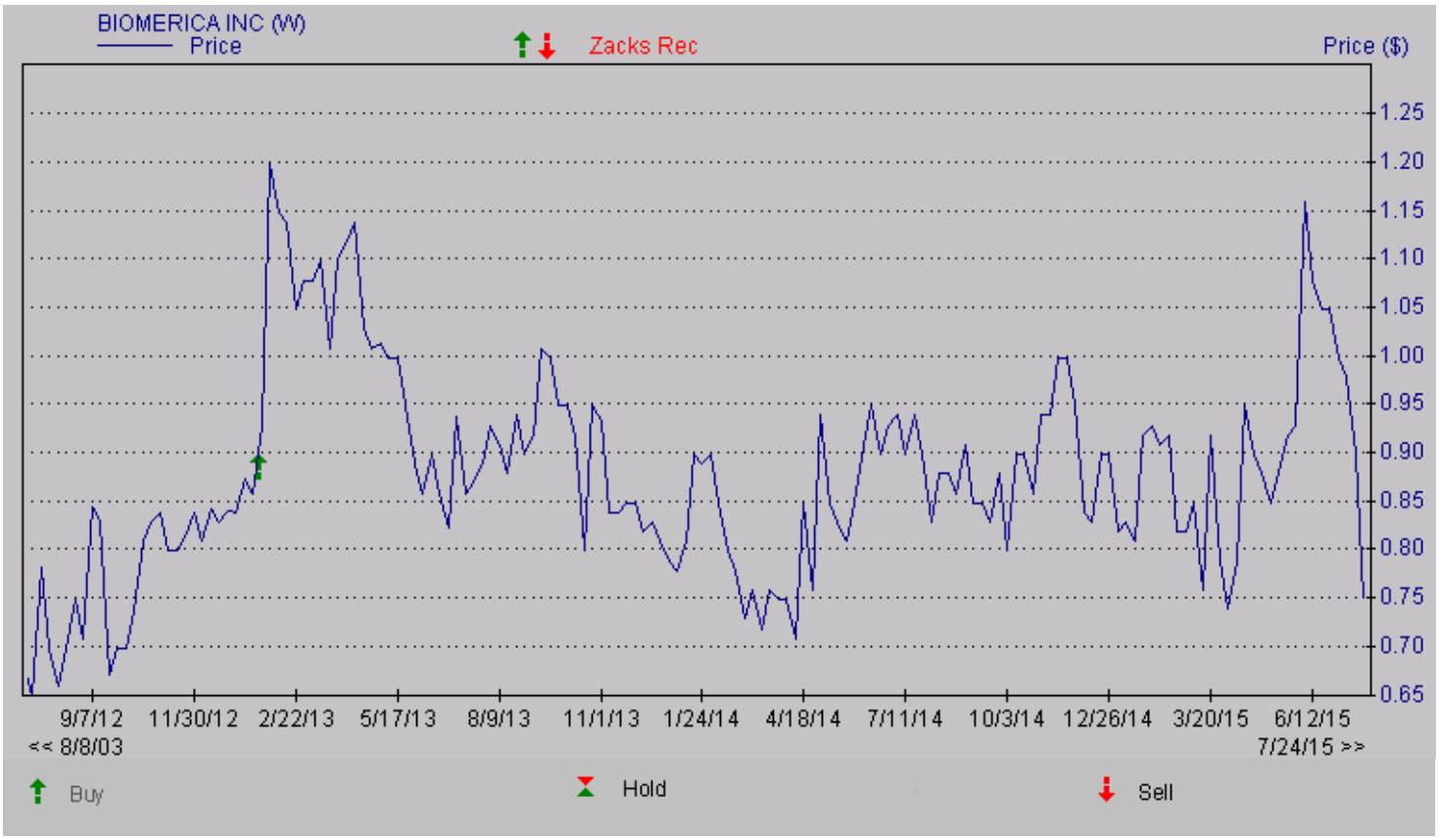
Biomerica Inc.

	2014 A	Q1A	Q2A	Q3A	Q4E	2015 E	2016 E	2017 E	2018 E
Total Revenues	$5,120.4	$1,034.5	$1,133.6	$1,299.4	$1,474.4	$4,941.8	$6,147.8	$7,103.3	$7,707.1
YOY Growth	*-20.9%*	*2.0%*	*21.3%*	*-13.0%*	*-12.2%*	*-3.5%*	*24.4%*	*15.5%*	*8.5%*
Cost of Goods Sold	$3,451.2	$724.5	$826.4	$840.6	$952.4	$3,343.9	$3,928.4	$4,347.2	$4,678.2
Gross Income	$1,669.2	$309.9	$307.2	$458.8	$521.9	$1,597.9	$2,219.3	$2,756.1	$3,028.9
Gross Margin	*32.6%*	*30.0%*	*27.1%*	*35.3%*	*35.4%*	*32.3%*	*36.1%*	*38.8%*	*39.3%*
SG&A	$1,526.0	$338.3	$375.0	$409.7	$415.8	$1,538.8	$1,666.0	$1,719.0	$1,780.3
% SG&A	*29.8%*	*32.7%*	*33.1%*	*31.5%*	*28.2%*	*31.1%*	*27.1%*	*24.2%*	*23.1%*
R&D	$589.9	$195.7	$182.1	$184.6	$191.0	$753.4	$608.0	$522.0	$507.0
% R&D	*11.5%*	*18.9%*	*16.1%*	*14.2%*	*13.0%*	*15.2%*	*9.9%*	*7.3%*	*6.6%*
Operating Income	($446.6)	($224.1)	($249.9)	($135.5)	($84.8)	($694.4)	($54.7)	$515.1	$741.5
Operating Margin	*-8.7%*	*-21.7%*	*-22.0%*	*-10.4%*	*-5.8%*	*-14.1%*	*-0.9%*	*7.3%*	*9.6%*
Total Other Income (Expense)	$20.1	$4.8	$11.8	$1.7	$5.0	$23.4	$9.1	$14.2	$18.0
Pre-Tax Income	($426.5)	($219.3)	($238.0)	($133.8)	($79.8)	($671.0)	($45.6)	$529.3	$759.5
Tax expense (benefit)	($210.7)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$113.9
Tax Rate	*49.4%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*15.0%*
Net Income	($215.8)	($219.3)	($238.0)	($133.8)	($79.8)	($671.0)	($45.6)	$529.3	$645.6
YOY Growth	*448.9%*	*21.2%*	*20.1%*	*-95.0%*	*115.2%*	*210.9%*	*-93.2%*	*-1260.7%*	*22.0%*
Net Margin	*-4.2%*	*-21.2%*	*-21.0%*	*-10.3%*	*-5.4%*	*-13.6%*	*-0.7%*	*7.5%*	*8.4%*
EPS	($0.03)	($0.03)	($0.03)	($0.02)	($0.01)	($0.09)	($0.01)	$0.06	$0.08
YOY Growth	*440.0%*	*18.0%*	*55.8%*	*-95.0%*	*112.2%*	*203.5%*	*-93.7%*	*-1255.0%*	*21.2%*
Diluted Shares O/S	7,371	7,548	7,552	7,555	7,556	7,553	8,120	8,160	8,210

Brian Marckx, CFA

© Copyright 2015, Zacks Investment Research. All Rights Reserved.

HISTORICAL ZACKS RECOMMENDATIONS



© Copyright 2015, Zacks Investment Research. All Rights Reserved.

DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, Brian Marckx, CFA, CFA, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered to be reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESMENT BANKING, REFERRALS, AND FEES FOR SERVICE

Zacks SCR does not provide nor has received compensation for investment banking services on the securities covered in this report. Zacks SCR does not expect to receive compensation for investment banking services on the Small-Cap Universe. Zacks SCR may seek to provide referrals for a fee to investment banks. Zacks & Co., a separate legal entity from ZIR, is, among others, one of these investment banks. Referrals may include securities and issuers noted in this report. Zacks & Co. may have paid referral fees to Zacks SCR related to some of the securities and issuers noted in this report. From time to time, Zacks SCR pays investment banks, including Zacks & Co., a referral fee for research coverage.

Zacks SCR has received compensation for non-investment banking services on the Small-Cap Universe, and expects to receive additional compensation for non-investment banking services on the Small-Cap Universe, paid by issuers of securities covered by Zacks SCR Analysts. Non-investment banking services include investor relations services and software, financial database analysis, advertising services, brokerage services, advisory services, equity research, investment management, non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per client basis and are subject to the number of services contracted. Fees typically range between ten thousand and fifty thousand USD per annum.

POLICY DISCLOSURES

Zacks SCR Analysts are restricted from holding or trading securities placed on the ZIR, SCR, or Zacks & Co. restricted list, which may include issuers in the Small-Cap Universe. ZIR and Zacks SCR do not make a market in any security nor do they act as dealers in securities. Each Zacks SCR Analyst has full discretion on the rating and price target based on his or her own due diligence. Analysts are paid in part based on the overall profitability of Zacks SCR. Such profitability is derived from a variety of sources and includes payments received from issuers of securities covered by Zacks SCR for services described above. No part of analyst compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports are based on data obtained from sources we believe to be reliable, but are not guaranteed as to be accurate nor do we purport to be complete. Because of individual objectives, this report should not be construed as advice designed to meet the particular investment needs of any investor. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.

ZACKS RATING & RECOMMENDATION

ZIR uses the following rating system for the 1162 companies whose securities it covers, including securities covered by Zacks SCR:
Buy/Outperform: The analyst expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters.
Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters.
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- 27.9%, Hold/Neutral- 51.0%, Sell/Underperform – 18.0%. Data is as of midnight on the business day immediately prior to this publication.