Zacks Small-Cap Research

June 10, 2015

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Integral Technologies, Inc. (ITKG-OTC)

ITKG: Battery Innovation Could Lead to New Revenue Streams

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	06/05/2014
Current Price (6/09/15)	$0.66
Six- Month Target Price	**$1.25**

OUTLOOK

Integral Technologies has invented a highly conductive plastic bipolar plate which it will develop into a lightweight, moldable and cost effective battery. Management believes this represents a significant opportunity, as the lead-acid battery market was estimated at $44.7 billion globally in 2014 and projected to reach $58.5 billion by 2020. The company intends to seek partners to help develop and commercialize the battery technology. Integral will create a separate business unit to allow potential partners to invest directly in the battery business.

SUMMARY DATA

52-Week High	**$0.85**
52-Week Low	**$0.25**
One-Year Return (%)	**153.8**
Beta	**1.04**
Average Daily Volume (sh)	**249,259**
Shares Outstanding (mil)	**112**
Market Capitalization ($mil)	**$74**
Short Interest Ratio (days)	**1.0**
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**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Elec-Misc Compn**

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	62.0 A	45.5 A	107.3 E	305.5 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 A	-$0.01 A	-$0.01 E	-$0.04 E

Zacks Projected EPS Growth Rate - Next 5 Years % **N/M**

Disclosures begins on page 9

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KEY POINTS

- Integral has invented a highly conductive plastic bipolar plate which it will develop into a lightweight, moldable, cost effective battery. Management believes this represents a significant improvement over existing technology and sizable opportunity. The lead-acid battery market was estimated at $44.7 billion globally in 2014 and is projected to reach $58.5 billion by 2020, according to Future Market Insights.

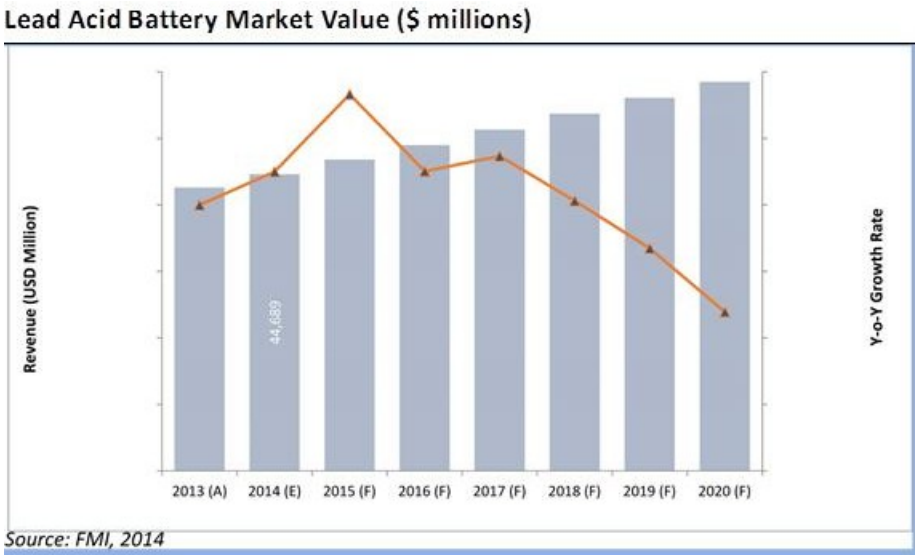
- According to management, the technology has applications in a variety of sectors including the automotive industry, which is one of the largest end user markets of lead-acid batteries.

- R&D and innovation of battery technology has not kept pace with strides in consumer electronics and electronic automobiles. The need for battery technology innovation has attracted significant investment in recent years. Integral does not intend to pursue the battery opportunity independently. The company intends to seek partners to help develop and commercialize the battery technology. Integral will create a separate business unit to allow potential partners to invest directly in the battery business.

- Separately, Integral recently reported third quarter fiscal 2015 results, with revenue of $45,450 up more than 7-fold compared to $6,250 recorded in the third quarter of fiscal 2014. Reflecting Integral's recent moves to strengthen its balance sheet, third quarter 2015 interest expense decreased by $72,409.

LAUNCHING NEW BIPOLAR PLATE TECHNOLOGY

Integral Technologies (OTC: ITKG) recently announced that it has invented a highly conductive plastic bipolar plate which it will develop into a lightweight, moldable, cost effective battery. We believe the company has four patents pending around this technology. Management believes this represents a significant improvement over existing technology and sizable opportunity. The lead-acid battery market was estimated at $44.7 billion globally in 2014. It is projected to reach $58.5 billion by 2020, according to Future Market Insights, which represents 4.6% CAGR.



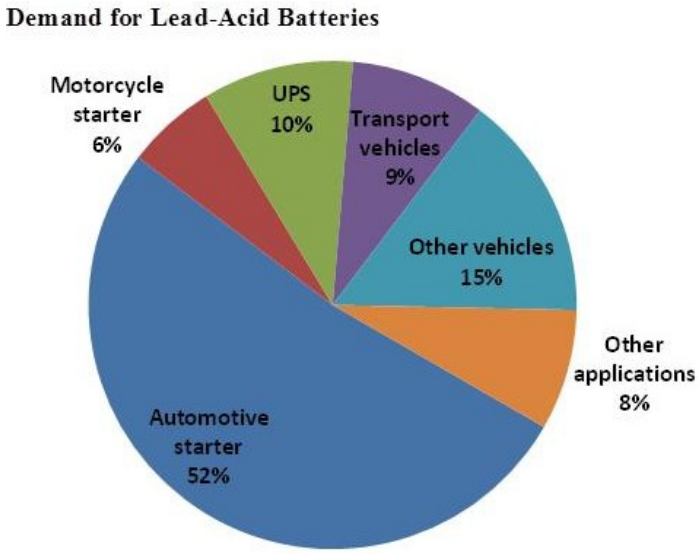
Competitive Advantages

Among the competitive advantages of Integral's technology, according to management, it is more efficient than current lead-acid battery technology, can produce the same level of energy using a smaller, lighter weight battery and can be molded into different shapes. The company believes its battery innovation underscores the light-weighting benefits of ElectriPlast. The ElectriPlast bipolar plate also streamlines the manufacturing process, reducing the production time, according to the company. In addition, management notes that it increases the flexibility in the forming and molding of the battery, which enables placement in a variety of different locations and applications. The technology is also environmentally friendly, according to Integral.

Slobodan Pavlovic, ElectriPlast's VP of Engineering, discussed the new bipolar plate technology on the company's recent quarterly investor call. He indicated that the battery would be 3x-4x more gravimetrically efficient than current lead-acid batteries, as well as more efficient than lithium-ion batteries.

The company also believes that its bipolar plate is highly cost effective, reflecting high volume processing capability and the elimination of the multiple components that are required to assemble plates made from other materials. Integral expects significant advantages from using plastic instead of metal, as lead corrodes and has a limited lifetime.

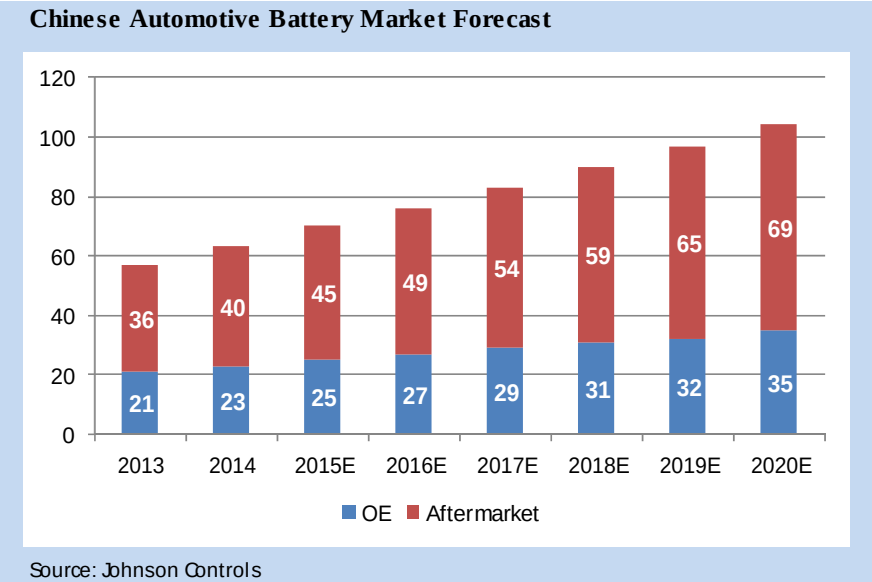
According to management, the technology has applications in a variety of sectors including the automotive industry, which is one of the largest end-user markets for lead-acid batteries. The transportation sector accounts for the lions' share of lead-acid battery demand, although this is expected to shift somewhat, particularly as use of lead-acid batteries to power grid storage is projected to grow dramatically from a small percentage currently. Integral believes that its battery technology has many other applications, in addition to the automotive sector.



Source: Industrial Technology Research Institute, 2011

Vehicle production is the primary driver of automotive demand for lead-acid batteries. China is the largest automobile market in the world, with 19 million new vehicles sold in 2012 and 18% per annum growth in 2006- 2012. According to McKinsey, the source of automotive industry profits has changed dramatically over the past few years. McKinsey notes that in 2012, the BRIC markets and RoW accounted for 55% of global automotive industry profits, up from only 30% in 2007. Sales in these markets grew 65%, outperforming growth in Europe, North America, Japan, and South Korea, with more than 50% of the

growth coming from China alone. McKinsey forecasts that by 2020, global profits for automotive OEMs could grow by nearly 50%, generated primarily from emerging markets, with China presumably a major contributor to that anticipated growth. Demand for automotive batteries is also forecast to grow significantly in China, according to Johnson Controls (JCI-not rated). Johnson Controls is a key manufacturer of lead-acid batteries, supplying about 33% of global lead-acid batteries to automotive manufacturers and aftermarket retailers. Integral's partnerships in Asia, including with Hanwha, and expanding presence in the region could position it well as it seeks to grow the battery business, in our view.



Over the years, consumer electronics have improved in a variety of ways, becoming thinner, lighter, more durable and more sophisticated. The rapid growth in portable smart devices, as well as of electric automobiles, has led to growing demand for battery power. However, despite strides on the consumer electronics and green automotive side, R&D and innovation of battery technology has not kept pace with those advances or with growing demand for power storage.

Structured as a Separate Business Unit: Targeting Direct Investment

As a result, there is considerable focus on the battery industry and the need for innovation has attracted significant investment in recent years. According to Dow Jones VentureSource, from 2003 to 2011 venture capitalists contributed $1.55 billion towards battery R&D. The sector is characterized by high R&D costs, competitive pressures from incumbent manufacturers adhering to existing technologies, the lengthy testing processes mandated by regulators and difficulties bringing new technologies to market. Given the challenges of innovating within the space, several battery startups have had a difficult time. For example, Silicon Valley based A123 Systems, which produces lithium-ion batteries, was hurt by the slower than expected introduction of electric vehicles, particularly Fisker-Karma, and issues with its Fisker-Karma battery. The company filed for Chapter 11 in 2012. Exide Technologies (XIDEQ-not rated), a leading manufacturer of lead-acid batteries for transportation and industrial applications, filed for Chapter 11 in 2013.

Integral does not intend to pursue the battery opportunity independently. Just as it has formulated partnerships for its core business, the company intends to seek partners to help develop and commercialize the battery technology. Towards this goal, Integral's strategy is to create a new battery business unit that will be separate from its main ElectriPlast business. Management believes this structure will allow potential partners to invest directly in the battery business. The company intends to leverage relationships of advisory board members to form partnerships for battery and power storage and

has noted that this process is already underway. In fact, management has indicated that it has already garnered interest from some high profile industry participants interested in its technology.

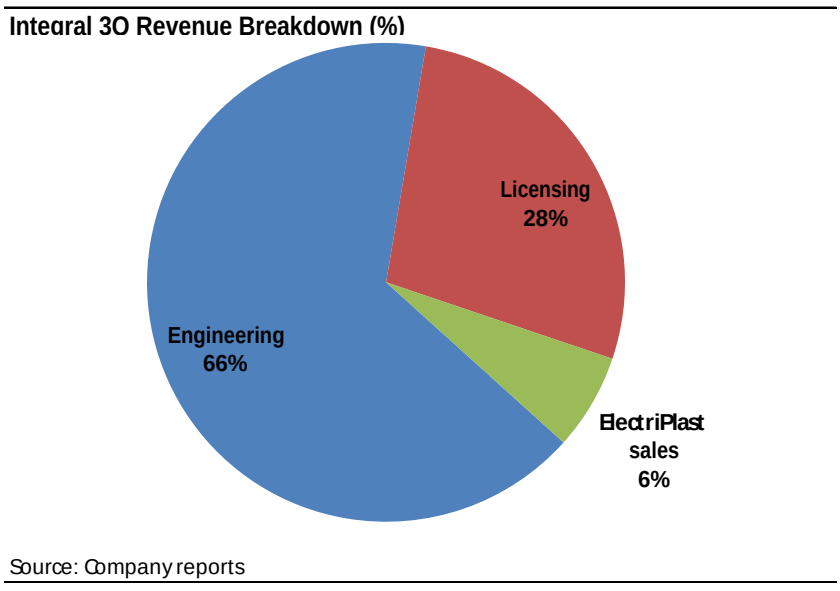
Integral intends to develop large market verticals including aerospace, consumer electronics, power grid storage and Department of Defense government contracting. While the company expects that battery partners will focus development efforts primarily on the new battery business, management believes there could be cross-over opportunities for partners to engage with multiple Integral verticals. This structure would also facilitate a potential spin-off or sale of the battery unit down the road, depending on the economics.

THIRD QUARTER FY 2015 HIGHLIGHTS

Separately, Integral recently reported third quarter fiscal 2015 results. Revenue of $45,450 was up more than 7-fold compared to $6,250 recorded in the third quarter of fiscal 2014. This was another quarter, we believe, that underscored 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. Engineering services revenue of $30,000 accounted for 66% of total revenue. The engineering services contribution reflects Integral's September 2014 agreement with East Penn Manufacturing, which 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 has provided engineering and design services, materials and finished products to East Penn. The company received a $150,000 payment from East Penn and has recognized that payment as revenue over the past three quarters.

Integral also 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. Hanwha has opened a manufacturing line dedicated to ElectriPlast and continues to make progress in Asia, according to management.

Another $2,950 or 6% of total revenue came from sales of ElectriPlast. This is still fairly minimal, in our view, although the company has recognized revenue from ElectriPlast sales over the last three quarters. We expect revenues from all three sources are likely to ramp substantially over time, despite some expected quarter-to-quarter lumpiness.



Source: Company reports

Engineering was the largest revenue driver in the quarter, accounting for 66% of total revenue. Management believes that many companies will require Integral's engineering expertise on conductive plastic applications and on ElectriPlast in order to use ElectriPlast. ElectriPlast is such a new product that others have not developed engineering expertise around it, management believes.

Reflecting Integral's recent moves to strengthen its balance sheet, third quarter 2015 interest expense decreased by $72,409, mirroring the reduction in convertible promissory notes. Integral's third quarter fiscal 2015 net loss attributable to common shareholders was ($1.156) million compared to ($1.262) million registered in last year's third quarter.

BALANCE SHEET

The company has reduced debt by some $825 thousand since March 2014, which contributed to lower interest expense in the fiscal 2015 third quarter, as noted. Moreover, Integral continues to pare debt. Subsequent to the close of the fiscal 2015 third quarter, Integral repaid an additional $200,000+, according to management, further strengthening its balance sheet.

Somewhat surprisingly, after retiring all of its convertible debt, the company issued new convertible notes in December 2014 and in January 2015. However, management has noted that it does not intend to issue convertible notes often and plans to repurchase the notes if dilutive conversion seems likely. Minimizing dilution to shareholders is an important goal for Integral.

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 outstanding warrants. In the first nine months of fiscal 2015, the company raised $2.9 million through private placements combined with some exercise of warrants and had $306,860 in cash on its balance sheet as of March 2015. The company believes its warrant holders are long-term investors.

RECENT NEWS

In April 2015, the company added James W. Wise, the Managing Partner of PACE Companies, LLP, to its Advisory Board. As someone who has represented clients to the Federal and state governments in policy areas such as energy, transportation, and defense contracting for 25 years, he is well positioned to help Integral build strategic alliances, we believe. According to his bio, he has been involved in White House briefing sessions on, among other issues, energy development and efficiency, which we believe could be extremely helpful to Integral as it seeks to exploit the light-weighting opportunity.

On April 28, 2015, Integral announced that CEO Doug Bathauer would speak at the *Chief Executive Magazine's* 2015 Smart Manufacturing Summit in April.

The company announced its conductive plastic bipolar plate battery technology on May 19, 2015.

RISKS

- Integral might not find a partner for its battery business, which could delay further development on the technology.
- The commercialization strategy for ElectriPlast with existing partners might not materialize in a meaningful way, spurring Integral to seek new affiliations and delaying revenue growth.
- Another company could gain traction with a competing technology. For this reason, management has aggressively launched a go-to market strategy to benefit from early mover advantage.
- 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. The company intends to minimize the dilutive impact largely through warrants, but could require more funding than management currently anticipates.

PROJECTED INCOME STATEMENT & BALANCE SHEET

Integral Technologies, Inc. Income Statement & Projections

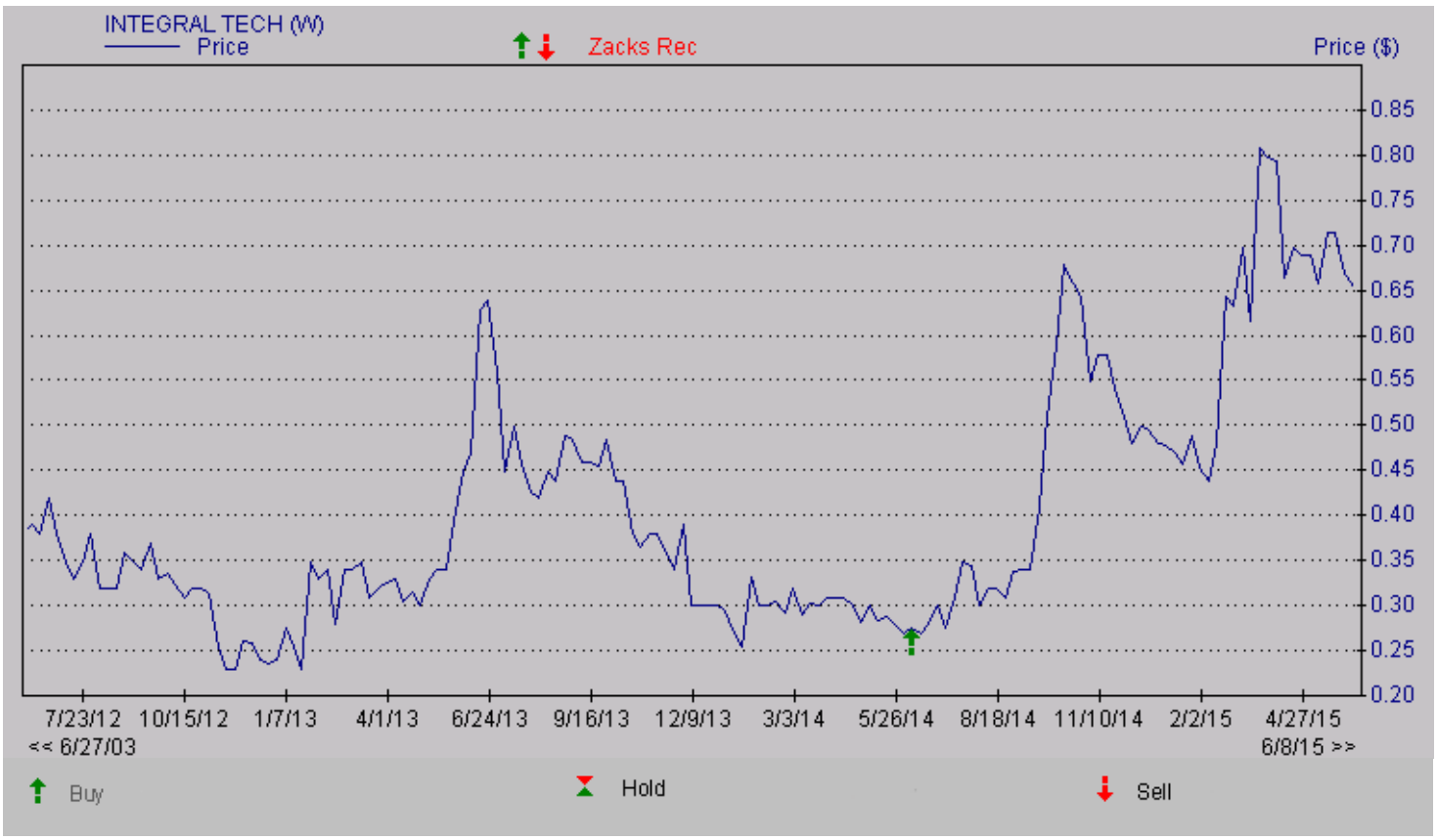
($)	**Sep-13**	**Dec-13**	**Mar-14**	**Jun-14**		**Sep-14**	**Dec-14**	**Mar-15**	**Jun-15**	
	1Q14	**2Q14**	**3Q14**	**4Q14A**	**FY14A**	**1Q15A**	**2Q15A**	**3Q15A**	**4Q15E**	**FY15E**
Revenue	6,413	6,309	6,306	10,139	29,167	90,782	62,000	45,450	107,311	305,543
R&D	27,196	16,432	9,616	14,384	67,628	19,349	41,217	19,715	15,000	95,281
S,G&A	1,162,950	819,170	560,353	917,799	3,460,272	909,233	1,096,696	1,105,749	900,000	4,011,678
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	1,137,913	1,125,464	915,000	4,106,959
Operating income	**(1,183,733)**	**(829,293)**	**(1,238,663)**	**(922,044)**	**(4,173,733)**	**(837,800)**	**(1,075,913)**	**(1,080,014)**	**(807,689)**	**(3,801,416)**
Other inc / exp net				(49,129)	(49,129)	62	913	6,490	(50,000)	(42,535)
Bank charges & interest	62,088	174,688	154,853	10,275	401,904	2,655	35,376	82,444	75,000	195,475
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	36,289	75,954	25,000	139,960
Net Loss	(1,274,234)	(905,421)	(1,258,354)	(857,413)	(4,526,508)	(840,517)	(1,112,202)	(1,004,060)	(832,689)	(3,789,468)
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)	(1,112,202)	(1,155,968)	(832,689)	(3,941,376)
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	104,154,424	105,375,238	105,375,238	105,375,238

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	Dec 2014	Mar 2015
Cash	172,173	321,890	284,222	169,064	532,308	309,784	41,878	755,971	199,777	181,196	80,552	306,860
Prepaid expense	19,723	111,276	80,928	50,580	20,232	30,227		46,106	23,831	192,732	79,212	75,305
Account receivable	-	-	-	-	250,000	-	-	-	-		4,500	
Property & equipment	-	-	-	-	-	-	-	-	27,821	35,017	50,572	66,820
Other	-	-	-	-	-	-	-	-	-	-	2,500	2,500
Total Assets	**$191,896**	**$433,166**	**$365,150**	**$219,644**	**$802,540**	**$340,011**	**$41,878**	**$802,077**	**$251,429**	**$408,945**	**$217,336**	**$451,485**
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	776,555	669,795
Loan payable				31,708				52,323	60,000			56,587
Notes payable	123,696	79,461	60,529	-	-	53,950	60,000	65,000		110,000	60,000	165,000
Deferred revenue	-		67,273		25,000	25,000	25,000	25,000	50,000	125,000	80,000	50,000
Loan payable		103,423				20,189						
Convertible debentures	93,356	129,576	48,773	116,207	174,827	108,895	137,030	217,846			44,779	55,254
Derivative financial liabilities	84,718	105,610	56,426	107,616	414,102	517,109	300,117	271,957			105,820	125,550
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**	**$1,067,154**	**$1,122,186**
Deferred revenue	-				225,000	218,750	212,500	206,250	229,500	408,333	395,833	383,333
Redeemable Preferred Stock	-		180,000	150,000	120,000	90,000	60,000	-				
Notes payable	-	-	-	-	-	-	215,000	450,000	420,833	219,000	204,000	-
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**	**$1,666,987**	**$1,505,519**
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)**	**($1,449,651)**	**($1,054,034)**
Total Liabilities and Stockholders'	**$191,896**	**$433,166**	**$365,150**	**$219,644**	**$802,540**	**$340,011**	**$41,878**	**$802,077**	**$251,429**	**$408,945**	**$217,336**	**$451,485**

Source: Company reports, Zacks

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