Zacks Small-Cap Research

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Lisa Thompson
312-265-9154
lthompson@zacks.com

scr.zacks.com

10 S. Riverside Plaza, Chicago, IL 60606

Finjan Holdings (FNJN-NASDAQ)

FNJN: Transforming from Pure IP Company: New Cybersecurity Consulting Business Adds New Revenue Stream; Non-Compete Ends

Current Recommendation	**Buy**
Prior Recommendation	Buy
Date of Last Change	9/15/2014
Current Price (06/16/15)	$1.30
Target Price	**$3.75**

OUTLOOK

Finjan Holdings, Inc. is an entity that was created in 2013 to enforce the patents of Finjan Inc., a former cybersecurity vendor from Israel founded in 1997. It is pursuing licensing arrangements and/or suing current vendors of cybersecurity hardware and software products it believes infringe upon its patents. Next week the Blue Coat trial will commence. It just added a new cybersecurity consulting business and released a web browser in addition to investing in cybersecurity startups in Israel, diversifying its business opportunities. With only a $15 million enterprise value, we believe the company has upside should licensing be successful.

SUMMARY DATA

52-Week High	**$5.30**
52-Week Low	**$1.23**
One-Year Return (%)	**-74.00**
Beta	**0.26**
Average Daily Volume (sh)	**61,570**
Shares Outstanding (mil)	**23**
Market Capitalization ($mil)	**$29**
Short Interest Ratio (days)	**0.08**
Institutional Ownership (%)	**27**
Insider Ownership (%)	**30**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/M**
Earnings Per Share (%)	**N/M**
Dividend (%)	**N/M**
P/E using TTM EPS	**N/M**
P/E using 2015 Estimate	**3.61**
P/E using 2016 Estimate	**NM**
Zacks Rank	**2**

Risk Level	**High**
Type of Stock	**Small-Blend**
Industry	**Internet-Software**
Zacks Rank in Industry	**13 of 69**

ZACKS ESTIMATES

Revenue
(in millions of $- Restated)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013	0.0 R	0.0 R	0.0 R	0.0 R	0.0 R
2014	0.0 R	0.0 R	5.0 R	0.0 A	5.0 A
2015	0.0 A	1.0 E	26.3 E	0.3 E	27.3 E
2016					13.0 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2013	NA	NA	NA	NA	-$0.26 A
2014	-$0.08 R	-$0.15 R	$0.03 R	-$0.18 A	-$0.38 A
2015	-$0.19 A	-$0.11 E	$0.82 E	-$0.12 E	$0.36 E
2016					-$0.01 E

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Transforming to Cybersecurity Startup: Finjan Establishes a New Consulting Business

Until this week, Finjan Holdings (FNJN)- has been a pure play in cyber security IP. Its sole source of revenues has been license agreements with other producers of cybersecurity products that use its behavior based threat detection technologies and infringe on it patents. However, it has already had considerable success with investing as a VC with Jerusalem Venture Partners Cybersecurity Fund VII and just received a cash pay out from its portion of an investment in CyActive, which was bought by PayPal for approximately $60 million. Finjan received a distribution from its JVP investment. This investment will yield a Gain on investment of approximately $826,000 in this June quarter and will appear on the income statement under other income.

To continue this diversification away from just licensing, this week Finjan announced the establishment of a new international consulting operation, "CybeRisk" by hiring two world-class executives based in Tel Aviv. It is in effect acting as a VC by starting up a new business. Heading up the group is Yoram Golandsky, who was General Manager of Cisco's Cyber Security Center of Excellence for the past year. Before that he was the founder and CEO of Security Art Ltd., a leader in providing worldwide cybersecurity and information risk management services for five years. He also was the Head of Information Security at RSA (the Security Division of EMC), and Chief Security Officer at PriceWaterhouseCoopers Israel. COO Eyal Harari, also from Cisco's Cyber Security Center of Excellence, joins him. He also worked for Security Art and consulting firm that performed red team exercises for clients.

The two started with Finjan on Monday June 15, 2015 and there are plans to add perhaps four or more people by year-end. We expect the company to begin adding revenues to the company in Q4 and operate on a cash flow neutral basis for the year.

The company also announced that its non-compete and confidentiality agreement with its former licensee and acquirer of its hardware business, M86 (who subsequently merged with Trustwave, and more recently into SingTel) has expired. It had restricted Finjan from making cybersecurity products. The company now plans to develop and release new products and is moving into direct to consumer applications. Development will be done entirely by Yeti, a San Francisco-based app developer. This company will create the products Finjan brings to them. The first release is mobile browser for IOS and Android (called "Finjan Mobile Secure Browser") that will scan a website for security and rate it safe, suspicious or avoid before a user actually lands on a page. This browser can be downloaded for free from the Apple App store and the Google Play Store.

Next Events

The next major event is a Markman hearing with Proofpoint, on June 24, 2015, and then a Markman hearing with Symantec on June 29, 2015 will follow this. After that is the **start of the trial with Blue Coat on July 20, 2015.** We expect the Blue Coat trial to take about two weeks and then the results of that trial to be issued another two weeks later. This trial should be an important indicator of future prospects for litigation.

2015 Model

We are updating our 2015 model to include the new consulting business by adding expenses and revenues in Q3 and Q4. Previously we had only modeled at licensing arrangement with Blue Coat into our 2015 estimate and no other settlements. Blue Coat is on schedule to start its trial on July 20, 2015,

maintaining its assertion of claims from each of the six patents against accused Blue Coat products that were named in its original complaint (5:13-cv-03999-BLF).

The consulting business is initially expected to target European clients and could be generating revenues by Q4. We expect these revenues will be half one-time projects and half long-term business that will be recognized ratably. By Q4 we believe the company could recognize $300,000 in revenues. The goal is to be cash flow breakeven adding in salaries and office space and start up expenses for this year.
We are using total revenues of $27 million for the year, which would yield EPS of $0.36 given our new estimate of the company's cost structure and revenue sources. A loss at the Blue Cost trial could of course reduce that revenue estimate to $1 million for the year from the other sources.

2016 Model

In 2016, the company will book another $2 million from Websense at 100% margins and could have a resolution with Proofpoint as a trial date is set on January 11, 2016. Since Proofpoint is much smaller, with $196 million forecasted in revenues for 2015, we are tentatively using $9 million in licensing. In addition we are expecting the consulting business plus the possibility of software products being sold could generate $2 million in revenues in 2016. Total revenues of $13 million could result in a loss per share of $0.01.

KEY POINTS

- Finjan holds a number of pioneering patents for cybersecurity hardware and software that is relevant to dozens of companies in this space.
- The company's non-compete with Trustwave has ended and they are pursuing new product launches.
- While its patents have already generated > $150M in its licensing and enforcement track record, the company has the potential to continue to reap large licensing revenues from the $20 billion market for cybersecurity software, services and appliance market.
- The technology licensing market in the U.S., once an afterthought, has grown from $33 billion in 1994 to $68 billion in 2002 and is likely over $100 billion today.
- The company's recent settlement with Websense shows its patents are still valued and able to be monetized.
- The company's has a market cap of $29 million and approximately $15 million in cash but could be worth considerably more if it is successful in its licensing pursuits. Estimating revenues of $23 million in 2015 and an industry multiple of 3.7 times sales, the company could be worth $115 million by next year if it succeeds in reaching successful licensing arrangements.

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OVERVIEW

Finjan Holdings is a patent licensing and enforcement firm based in NYC that owns the patents of its predecessor company Finjan Inc., a cybersecurity company that was founded in Israel in 1997. It invented several technologies that are used in current cybersecurity products today. Its three main patent areas:

- Behavior-based methods to detect and prevent threats from the Internet, including email and Web malware
- "Sandboxing" or stripping applications and running potentially malicious code in a safe environment
- Mobile code replacement where the malicious code is stripped and replaced by safe code

CYBERSECURITY MARKET

The market for cyber security products that may use technology covered by Finjan patents is expected to total $20 billion in sales in 2014, according to estimates by Gartner. These types of products include: endpoint and cloud, web gateway and next generation firewall software and hardware products as shown on the following chart.

Relevant Security Markets	2013	2014	2015	2016	2017
Endpoint & Cloud	$11.2 BN	$11.8 BN	$12.5 BN	$13.2 BN	$13.8 BN
Web Gateway	$4.1 BN	$4.4 BN	$4.7 BN	$5.0 BN	$5.3 BN
Next Gen. Firewall	$4.0 BN	$4.0 BN	$4.0 BN	$3.7 BN	$3.4 BN
Total Finjan Technology related Sales	$19.3 BN	$20.2 BN	$21.2 BN	$21.9 BN	$22.5 BN

Source: Gartner, IDC and Finjan estimates

Cybersecurity Consulting Business

According to Gartner, the market for information security consulting grew by 8.1% to $15.3 billion in 2014, from $14.2 billion in 2013. Combined, the top 10 providers grew by 12.7%. Three quarters of revenue comes from North America and Western Europe. Deloitte was ranked number one in this market. Other players, and competitors for Finjan in the cybersecurity consulting business include FireEye's Mandiant division, Hacknetics, a division of Ernst & Young, and root9B (RTNB) as well as IBM and Symantec.

THE PRESENT COMPANY ENFORCEMENT

Litigation Update

Company	Date and Location	Status	Patent numbers
FireEye **($426 m)**	US District Court for the Northern District of California on July 8, 2013	Stayed	**6,804,780**, 8,079,086, 7,975,305, 8,225,408, **7,058,822**, 7,647,633 and 6,154,844
Blue Coat **(est. >$500m)**	US District Court for the Northern District of California on August 28, 2013	**Trial for this action is scheduled for July 20, 2015.**	6,154,844, **6,804,780**, 6,965,968, **7,058,822**, 7,418,731, and 7,647,633
Proofpoint **($196 m)**	United States District Court for the Northern District of California on December 16, 2013	"Markman" scheduled for **June 24, 2015**. Trial date for March 7, 2016.	6,154,844, **7,058,822**, 7,613,918, 7,647,633, 7,975,305, 8,079,086, 8,141,154, and 8,225,408
Sophos **(est. $420 m)**	United States District Court for the Northern District of California on March 14, 2014	Markman concluded	6,154,844, **6,804,780**, 7,613,918, 7,613,926, 7,757,289, 8,141,154, 8,566,580, and 8,677,494
Symantec **($6.6 billion)**	United States District Court for the Northern District of California on June 1, 2014	"Markman" Hearing is scheduled for **June 29, 2015**, and a trial date has not been scheduled	6,154,844; 7,613,926; 7,756,996; 7,757,289; 7,930,299; 8,015,182; 8,141,154; and 8,677,494
Palo Alto Networks ($739 m)	United States District Court for the Northern District of California on November 4, 2014	"Markman" tentatively scheduled for **November 2, 2015**.	**6,804,780**; 6,965,968; **7,058,822**; 7,418,731; 7,613,918; 7,613,926; 7,647,633; 8,141,154; 8,225,408; and 8,677,494

VALUATION

Valuation of an IP company, even with a track record is very difficult and even more so with a company like Finjan that has only one court victory and one recent licensing arrangement. We can however look at other IP companies to see how the market values them to make some comparisons. There seems to be two different types of companies in this space, the older stable revenue generating companies like Rambus, and the upstarts that trade on events and potential. We can see from the table below, these range from values Inventergy Global with a $24 million enterprise value to Interdigital with an enterprise value of $1.7 billion and $398 million in sales expected this year. On average, the companies with revenues trade at an average of 3.7X 2015 estimated calendar revenues.

Using a valuation based on enterprise value to sales is easier for unprofitable companies. If Finjan were to generate $27 million in sales in 2015, we could see the market putting a 3.7 times sales multiple on it as shown in the industry average below. Using that and working back to enterprise value per share, we see that given those revenues, Finjan could be worth $3.75 per share by next year, assuming it still has the same amount of cash on the balance sheet as today and achieves those revenue levels in 2015 by licensing Blue Coat or other vendors.

IP Companies

Company	Ticker	Revenue 2015E	Revenue LTM	EV/ EBITDA	EBIDTA Margin	Enterprise Value / Sales 2015E	Enterprise Value / Sales LTM	Included in Average?	Enterprise Value
Interdigital	IDCC	$398	$468	6.5	57%	4.3x	3.7x	y	1,710
Inventergy Globa	INVT	NA	$1	-2.5	-166%	NM	27.5x	n	24
Neonode	NEON	$16	$6	-11.9	-200%	9.3x	23.9x	n	144
Parkervision	PRKR	$33	$0	-2.9	NM	1.3x	NM	y	45
Pendrell	PCO	$20	$43	-28.9	-19%	7.8x	3.7x	y	159
Rambus	RMBS	$307	$291	15.6	35%	5.2x	5.5x	y	1,600
RPX	RPXC	$293	$281	2.5	73.10%	1.8x	1.8x	y	515
Tessera	TSRA	$253	$270	8.1	72%	6.2x	5.8x	y	1,580
Unwired Planet	UPIP	$39	$40	6.2	-13%	0.5x	0.5x	y	21
VirnetX	VHC	$20	$1	-6.1	NM	10.3x	150.4x	n	206
Vringo	VRNG	NA	$1	-1.1	NM	NM	36.5x	n	49
Wi-Lan	WILN	$99	$93	3.6	67%	2.2x	2.4x	y	223
Average				**7.6**	**34%**	**3.7x**	**2.9x**		**$731**

	Revenue 2015E	Revenue LTM	EBITDA Margin	Enterprise Value / Sales 2015E	Enterprise Value / Sales LTM	Valuation Range Low	Valuation Range High
FinJan	**$27**	**$5**	**-243.00%**	**3.7x**	**2.9x**	**$15**	**$100**

Conclusion of Enterprise Value	**$100,484,808**
Market Value	**$115,489,808**
Shares Outstanding	24,315,000
Price per Share	**$4.75**

Another way to look at possible revenues from current activity is to compare the relevant revenues of the various companies involved. We are taking a general guess that 20% of Websense's revenues were affected by Finjan patents which resulted in a licensing fee of $8 million at this stage in the litigation. This

was settled before the Markman Hearing. Looking at the rest of the companies we can derive revenues over $200 million for similar licensing at the same stage as Websense.

Blue Coat is much further along in the process and had a Markman Hearing last August. There is a trial date set for July. Because of this we know that Finjan would be seeking higher licensing rates than Websense.

	Revenues	% Relevant		License
FireEye	$428	30%	$128	$13
Blue Coat	500	10%	$50	27
Websense	400	20%	$80	8
Proofpoint	186	50%	$93	9
Sophos	420	25%	$105	11
Symantec (2 seg)	4,200	30%	$1,260	126
Palo Alto Networks	710	42%	$300	30
TOTAL				**224**

Cybersecurity companies

The new consulting venture will have different peer comparables where valuations are much higher. For example, FireEye bought Madiant for $1 billion or approximately 7 times sales. Another comparable would be root9b, a company with $141 million enterprise value and a run rate of $38 million, or 3.7 times.

RISKS

- The company has a limited track record with which to set expectations.
- Finjan's patents have only prevailed in court once, in 2010, and only two patents in the portfolio, **7,058,822** and **6,804,780** have been upheld thus far.
- There is no way to predict the timing of lawsuit settlements or licensing agreements, or even the length of a lawsuit.
- As the current company burns cash and has little licensing revenue, it may not generate enough revenues to cover costs and continue operations in the future unless it generates greater income or receives further financing.
- The stock is high risk and is expected to have wide swings in stock price depending on unpredictable events.
- Government is expected to legislate new laws on patent enforcement that could affect the company's ability to monetize its patents as it currently expects.

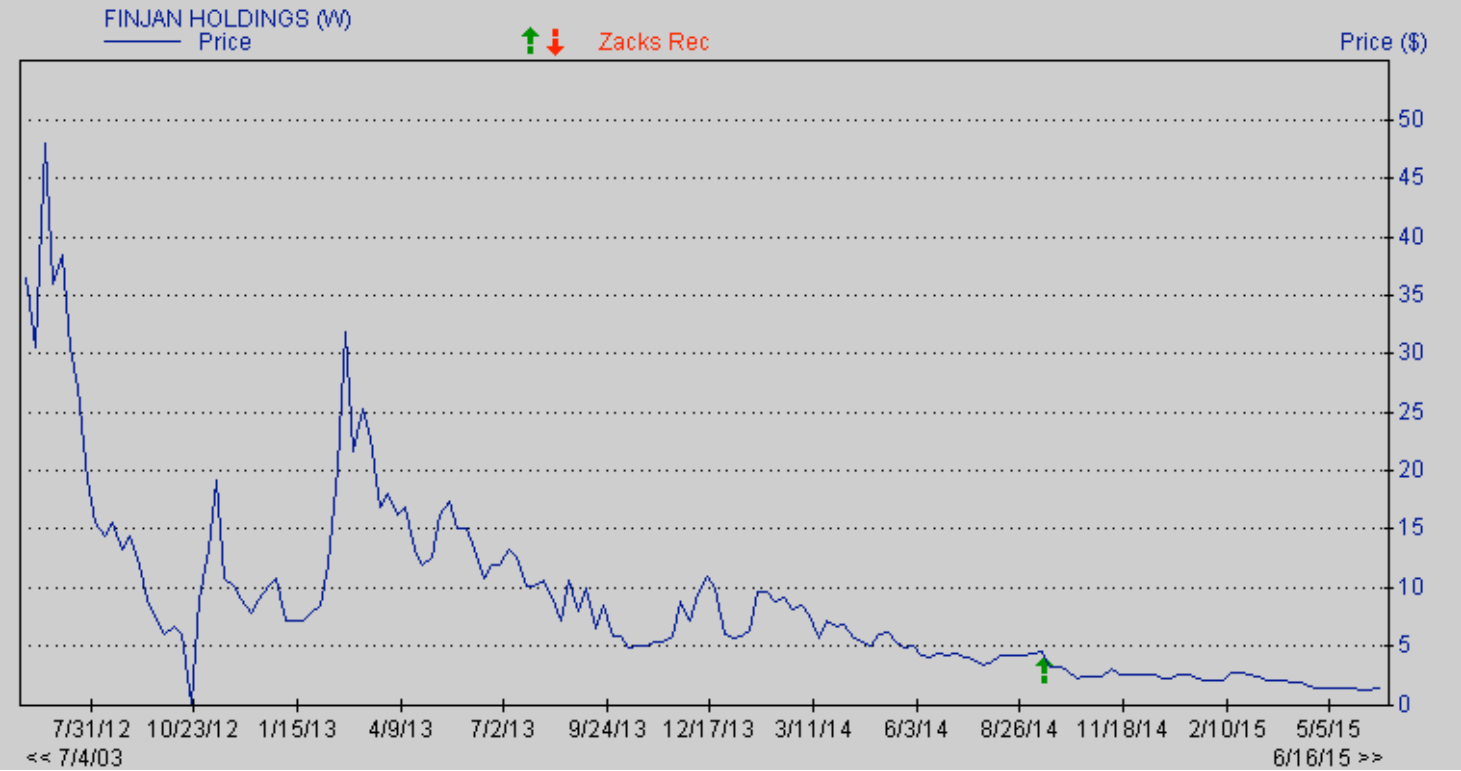
BALANCE SHEET

$ in Thousands	3/31/15	12/31/14	% Change
Current assets:			
Cash and cash equivalents	$15,005	$17,505	-14%
Accounts receivable, net	55	2,016	-97%
Prepaid expenses and other current assets	65	112	-42%
Total current assets	15,125	19,633	-23%
Property and equipment, net	136	66	106%
Investments	1000	1000	0%
Other long term assets	231	0	
Total Assets	16,492	20,699	-20%
Current Liabilities:			
Accounts payable	1,327	1,675	-21%
Accounts payable - related parties	18	100	-82%
Accrued expenses	842	800	5%
Accrued income taxes	8	0	
Total current liabilities	2,195	2,575	-15%
Total Liabilities	2,195	2,575	-15%
Stockholders' Equity			
Common stock	2	2	0%
Additional paid-in capital	23,501	23,126	2%
Retained earnings	(9,206)	(5,004)	84%
Total Stockholders' Equity	14,297	18,124	-21%
Total Liabilities & Stockholders' Equity	$16,492	$20,699	-20%

INCOME STATEMENT

	2014				2015							
In Thousands	**Q1R**	**Q2R**	**Q3R**	**Q4**	**Q1**	**Q2E**	**Q3E**	**Q4E**	**2013R**	**2014**	**2015E**	**2016E**
Websense	$0	$0	$4,998	$0	$0	$0	$0	$0	$0	$4,998	$0	$2,000
Other licenses					0	700	26,300	0	0	0	27,000	9,000
Consulting & Products					0	0	0	300	0	0	300	2000
Total Revenues	**0**	**0**	**4,998**	**0**	**0**	**1,000**	**26,300**	**300**	**0**	**4,998**	**27,300**	**13,000**
Cost of revenues	0	0	800	0	0	30	4,455	20	0	800	4,485	900
Gross profit	0	0	4,198	0	0	970	21,845	280	0	4,198	22,815	12,100
Gross Margin			84%			97%	83%	93%		84%	84%	93%
Operating Expenses:												
SG&A	1,792	3,331	3,535	5,157	4,205	4,200	3,000	3,000	6,225	13,813	14,405	12,000
R&D						100	100	100	0	0	300	500
Transaction costs	0	0	0	0	0	0	0	0	790	0	0	0
Total operating expenses	1,792	3,331	3,535	5,157	4,205	4,300	3,100	3,100	7,015	13,813	14,705	12,500
Operating Income	(1,792)	(3,331)	663	(5,157)	(4,205)	(3,330)	18,845	(2,820)	(7,015)	(9,615)	8,110	(400)
Other Income												
Gain on settlements	1,000	0	0	0	0	0	0	0	1,000	1,000	0	0
Other income	0	5	0	(5)	(1)	826	0	0	9	0	0	0
Interest income	68	6	8	8	9	7	6	5	153	90	27	100
Total other income		11	8	3	8	833	6	5	1,162	1,090	27	100
Loss before taxes	(724)	(3,320)	671	(5,154)	(4,196)	(2,490)	18,851	(2,815)	(5,853)	(8,525)	8,137	(300)
Income taxes	1	(2)	(2)	8	5	0	0	(5)	(260)	5	0	0
Net Income	(725)	(3,322)	673	(5,146)	(4,201)	(2,490)	18,851	(2,810)	(5,593)	(8,520)	8,137	(300)
Net Income Per Share:												
Basic EPS from Cont.	**($0.03)**	**($0.15)**	**$0.03**	**($0.23)**	**($0.19)**	**($0.11)**	**$0.82**	**($0.12)**	**($0.26)**	**($0.38)**	**$0.36**	**($0.01)**
Diluted EPS	($0.03)	($0.15)	$0.03	($0.21)	($0.19)	($0.11)	$0.76	($0.12)	($0.26)	($0.38)	$0.33	($0.01)
Basic Shares	22,368	22,379	22,422	22,445	22,409	22,682	22,955	23,228	21,602	22,404	22,818	22,500
Diluted Shares	22,368	22,379	23,036	24,250	24,315	24,487	24,760	25,033	23,227	24,209	24,648	24,948

STOCK PRICE CHART



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