Zacks Small-Cap Research

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XZERES Corporation (XPWR-OTCBB)

XPWR: Private placement secures capital needed to resume top-line growth.

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	02/23/2012
Current Price (03/02/12)	$0.55
Six- Month Target Price	**$1.00**

OUTLOOK

XZERES is positioned to benefit from the growth of the small wind energy industry. Though backlog continues to grow, the company experienced an interruption in the sequential quarterly revenue growth rate due to the inability to source components for small wind systems. However, the recently announced private placement has secured the capital required to purchase the components needed to fill current orders in the company's $3.5 million backlog. Management expects the company to achieve profitability in calendar 2012. We reiterate our Outperform rating; our revised price target is $1.00.

SUMMARY DATA

52-Week High	**$1.10**
52-Week Low	**$0.33**
One-Year Return (%)	**-75.1**
Beta	**-0.15**
Average Daily Volume (shrs.)	**10,889**
Shares Outstanding (million)	**23**
Market Capitalization ($ mil.)	**$12.6**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**N/A**
Insider Ownership (%)	**N/A**
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/M**
P/E using 2013 Estimate	**N/M**
P/E using 2014 Estimate	**N/M**
Zacks Rank	**3**

Risk Level	**Above Average**
Type of Stock	**Small - Growth**
Industry	**Other Alt. Energy**
Zacks Rank in Industry	**4 of 12**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (May)	Q2 (Aug)	Q3 (Nov)	Q4 (Feb)	Year (Feb)
2011	0.00 A	0.36 A	0.47 A	0.65 A	1.48 A
2012	1.02 A	1.37 A	0.93 A	0.93 E	4.24 E
2013	1.50 E	2.70 E	4.86 E	8.75 E	17.81 E
2014					22.26 E

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

	Q1 (May)	Q2 (Aug)	Q3 (Nov)	Q4 (Feb)	Year (Feb)
2011	-$0.07 A	-$0.10 A	-$0.10 A	-$0.13 A	-$0.41 A
2012	-$0.11 A	-$0.09 A	-$0.11 A	-$0.10 E	-$0.40 E
2013	-$0.07 E	-$0.05 E	-$0.01 E	$0.05 E	-$0.08 E
2014					$0.01 E

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

Quarterly EPS may not equal annual EPS due to rounding.

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KEY POINTS

- XZERES Corporation is an engineered systems company, with a focus on clean and renewable energy. Currently, XZERES primarily designs, develops, manufactures and markets premium small wind turbine systems and related equipment for the generation of electrical power to a wide range of customers. In April 2011, the company acquired Rochester Power Saver and now also offers power efficiency products.
- The company's small wind systems are competitive, and in most cases, superior in terms of performance to other wind systems. When power curves are used in conjunction with published pricing of competing wind turbines, management can demonstrate that the XZERES system has a superior return on investment based on the company's metric of modified internal rate of return.
- XZERES utilizes multiple sales channels: the traditional dealer network, direct-to-consumer and distributor channels. The company has three websites, each targeting a specific market.
- Through innovative marketing initiatives, such as the Buy Direct program, the availability of financing through lending partners and the Micro-Generation Utility model, XZERES is stimulating sales of it small wind systems.
- XZERES reported a disappointing third fiscal quarter with sequential revenue growth declining 32.2% due to the company's inability to source components for orders of small wind systems. The company's working capital needs have been bolstered by the recent private placement announced on February 27th.
- We reiterate our Outperform rating; however, our price target has been lowered to $1.00 due to the interruption in the company's sequential quarterly revenue growth rate profile.
- Consult the initiation report dated May 30, 2011 for additional background information.

RECENT NEWS

On February 27, 2012, XZERES completed a private placement, in which 3,517,500 restricted units were issued at $0.40 per unit providing gross proceeds of $1,407,000. Each unit consists of one share of common stock and one half of a warrant exercisable at $.80 per share for a period of three years. The proceeds will be utilized to purchase essential components needed to fill current orders.

Given the strong order flow and increase backlog, management reiterated calendar 2012 revenue guidance of at least $20 million. In addition, management expects the company to be profitable during calendar 2012. However, due to the private placement being closed approximately one month later than planned, results for the fiscal quarter ending February 29, 2012 are expected to be similar to those reported for the third fiscal quarter; therefore, it appears that the company will not attain management's goal of quadrupling revenues in fiscal 2012.

On January 17, 2012, XZERES reported results for the third fiscal quarter ending November 30, 2011. Quarterly revenues sequentially declined 32.2% to $927 thousand from $1.37 million, breaking the five consecutive quarter trend of 30%+ sequential revenue growth. The inability for the company to source components for orders of small wind systems due to insufficient working capital resulted in the disappointing top-line. However, on a year-over-year basis, revenues increased by 96.7% to $927 thousand versus $472 thousand in the comparable tear-ago quarter. The gross profit margin sequentially increased 357 basis points to 27.1%. Management expects the gross margin to rise as new products, services and business models are developed and deployed. The company has aggressively expanded sales and marketing efforts, targeting end-users, dealers and distributors. Sales expense increased 51.6% sequentially; however, marketing expense decreased 15.6% sequentially. In addition, G&A expenditures increased 13.6% sequentially.

XZERES reported a quarterly loss of $2.13 million or $0.11 per diluted share. During the third fiscal quarter, the company raised $1.25 million through two private placements (1,250,000 common shares at $0.80 per share and 625,000 common shares at $0.40 per share). During the first nine months of fiscal 2012, the company raised $4,928,461 through stock and warrant offerings.

Due to strong orders, especially in the UK, backlog increased to over $3.5 million, up from approximately $802,000 as of the end of the second fiscal quarter (November 30, 2011). Management expects at least $5 million in orders annually from the exclusive dealer arrangement with VG Energy, the UK's largest distributed wind energy dealer in the 15 kW-to-100 kW segment. Also, new dealers of small wind systems have been signed in France, Germany, Portugal and Australia. Follow-on orders of approximately $3 million for the island electrification program in Vietnam are expected in 2012. In addition, 23 dealers have been signed to distribute Power Efficiency in the US and internationally. Management expects the Power Efficiency Division to generate revenues of over $3 million in calendar 2012.

Management expects to generate revenues of at least $20 million during calendar 2012. Key assumptions include at least flat US wind turbine sales, VG Energy generating at least $5 million in orders and follow-on orders from the island electrification program in Vietnam.

On October 27, 2011, XZERES announced the signing of a dealer agreement with Weole Energy, the largest distributed wind energy dealer serving France. Having established distribution relationships in the UK, this agreement expands the company's presence into the distributed wind energy market of Continental Europe. Management plans to expand distribution throughout Continental Europe, including Germany and Italy, with similar dealer agreements in the near future. Ultimately, management intends to achieve a global sales and marketing footprint.

OVERVIEW

Based in Wilsonville, Oregon[1], XZERES Corporation (XPWR: OTCBB) designs, develops, manufactures and markets premium small wind turbine systems and related equipment for the generation of electrical power to a wide range of customers: residential, commercial, municipal, rural, agricultural, etc. In April 2011, the company acquired the assets of Rochester Power Saver, a manufacturer and distributor of power savers. The acquisition broadens the company's small wind systems product lines (the Wind Power Division) with the addition of power efficiency products (Power Management Division) that are designed to improve the power factor for both business and residential customers. Power saver products also act as surge suppression devices. The power management devices are offered both separately and in tandem with wind turbine systems.

Management's goal is to become a global, diversified engineered systems company, with a focus on clean and renewable energy, and primarily through acquisitions. Originally incorporated an oil & gas production company in 1984[2], the company began to focus on renewable energy in late 2008 and was renamed Cascade Wind Corp., Inc. After a developmental period, the company acquired the wind energy assets of Abundant Renewable Energy, LLC on March 25, 2010, and subsequently was renamed XZERES Wind Corp. After the acquisition of Rochester Power Saver, the company was renamed XZERES Corp.

The **Wind Power Division** focuses on the small wind market, which encompasses wind-powered turbines that are capable of producing up to 100 kilowatts[3] (kW). XZERES manufactures and assembles

[1] Though based in Oregon, XZERES Wind Corporation is incorporated in Nevada.
[2] XZERES Wind was originally incorporated in New Mexico as Intermountain Refining Company.
[3] A kilowatt is a unit of energy equal to 1,000 watt s. A watt is defined as one joule per second and defines the rate at which work is done according the formula: W = V x A (watts = volts x amperes).

wind turbine systems, towers and various wind power system components, including controllers, inverters and lightning protection equipment. The company currently offers two power ratings of small wind turbines: the **XZERES 110** (2.5 kW) and the **XZERES 442SR** (10 kW). Approximately 150 wind turbines have been deployed.

In August 2010, Frank Greco, former CEO of Southwest Windpower, was appointed Chief Executive Officer. Within a few months, XZERES rapidly developed with the implementation of a **Direct Buy** program, the initiation of a consumer **financing** option, the launch of **WindRx**™ site assessment tool both in the UK and US, and the creation of the **Micro-Generation Utility** business model, all between November 2010 and January 2011. The addition of Frank Greco to the team of co-founders of David Baker and Steve Shum synergistically accelerated the company's progress with the creation and implementation of non-typical industry sales and business models, including the expansion into multiple sales channels in the United States and opening a European subsidiary, XZERES Wind Europe Ltd., in January 2011.

The **Power Management Division** was formed with the acquisition of Rochester Power Saver in April 2011. The Division manufactures and markets power efficiency products, which are designed to improve the power factor for commercial and light-industrial customers, who should benefit from a 10% to 20% reduction in electricity costs. The products can also be used by residential customers as power conditioners (by smoothing voltage spikes) and as central surge suppressors. The power management devices are marketed both separately and in tandem with the company's wind turbine systems.

XZERES acquired Rochester Power Saver on April 25, 2011 for $450,000 worth of common stock and $50,000 in cash, along with a 5% royalty on gross profits over the next 24 months, up to a maximum of $150,000. The acquisition broadened the company's small wind systems product lines with the addition of power saver products. The Rochester Power Saver product line consists of several models with different capacity ratings with price points between $500 and $2,900. Payback periods range between 6 and 24 months.

The small wind industry is an emerging growth industry with industry sales expected to increase at least 20% per year. As market penetration increases, market participants with proven, established and certified products, like XZERES, should experience sales growth and achieve profitability. Due to the many initiatives recently implemented, we expect that sales will continue grow during calendar 2012.

VALUATION

The appropriate valuation methodology for XZERES is based on price-to-sales (P/S) due the character of the company's enterprise, namely a small-capitalization company with current negative profitability, but with a sales profile that should experience rapid growth through management's ramp up of multiple distribution channels for both the company's small wind systems and power efficiency products, along with potentially further acquisitions. Ultimately, the growing revenue stream should manifest itself into positive earnings. Based on historical norms for similar emerging growth companies, we expect a price-to-sales valuation range between 2.8 and 5.2; however, the sales base of XZERES is challenging to determine, since at first the company grew revenues at an exponential pace, and then revenues flattened for two quarters due to limited working capital. Therefore, we are now utilizing trailing four quarters: the latest reported quarter and the next quarter to be reported. Our $1.00 price target is based on a 5.2 price-to-sales ratio valuation, since XZERES has the potential and is expected to resume double-digit sequential sales growth.

The valuation process for small and mid-cap companies serving the alternative energy industry is based upon profiling the potential level of a specific company's profitability through gross margin analysis, and then applying that input to a price-to-sales valuation methodology. The gross margin indicates a company's structural cost advantage based on cost of goods sold. Analyzing a company's level of

profitability is often the most important aspect of equity valuation analysis. The overall gross margin of XZERES increased 357 basis points to 27.1% in the latest reported fiscal quarter.

Price-to-sales valuation also incorporates a company's ability to increase revenues and gain market share. Given management's stated business plan is to become a global, diversified engineered systems company, with a focus on clean and renewable energy and to increase the sales base and growth potential by acquisitions, XZERES is expected to expand its sales base significantly. Comparable companies have a historical price-to-sales valuation range between 2.8 and 5.2. Since the company has demonstrated its ability to generate double-digit sequential quarterly sales growth, the high-end of the range is being used to determine our target price of $1.50 (a 5.2 price-to-sales ratio).

PROJECTED INCOME STATEMENT & BALANCE SHEET

XZERES Corporation

Annual Earnings Analysis For the years ending February 28 (in $ US)	**FY 2008**	**FY 2009**	**FY 2010**	**FY 2011**	**FY 2012 E**	**FY 2013 E**	**FY 2014 E**
Revenue:	**0**	**0**	**0**	**1,489,061**	**4,237,569**	**17,808,000**	**22,260,000**
Cost of sales	0	0	0	1,099,456	3,191,959	10,759,920	12,688,200
Gross Profit	**0**	**0**	**0**	**389,605**	**1,045,610**	**7,048,080**	**9,571,800**
General & administrative	0	209,274	70,607	3,157,018	4,549,976	4,908,161	4,957,242
Marketing	0	0	0	172,158	371,439	365,363	369,017
Sales expense	0	0	0	629,580	1,826,946	1,926,721	1,945,988
Engineering/R&D expense	0	0	0	1,480,585	2,325,292	2,000,000	2,020,000
Total Expenses	**0**	**209,274**	**70,607**	**5,439,341**	**9,073,652**	**9,200,244**	**9,292,247**
Pre-tax profit from operations	**0**	**(209,274)**	**(70,607)**	**(5,049,736)**	**(8,028,042)**	**(2,152,164)**	**279,553**
Interest income (expense)	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Other Income	**0**	**0**	**0**	**3,332**	**(53,572)**	**3,700**	**5,000**
Income (loss) Continuing Operations	**0**	**(209,274)**	**(70,607)**	**(5,046,404)**	**(8,081,614)**	**(2,148,464)**	**284,553**
Income (loss) from Discontinued Operations	42,771	(237,495)	2,229	0	0	0	0
Other comprehensive income	6,019	(40,425)	0	0	0	0	0
Provision for income taxes	0	0	0	0	0	0	0
Net income for the year	**48,790**	**(487,194)**	**(68,378)**	**(5,046,404)**	**(8,081,614)**	**(2,148,464)**	**284,553**
Net income per common share (diluted)	**0.04**	**(0.19)**	**(0.01)**	**(0.41)**	**(0.40)**	**(0.08)**	**0.01**
Net income per common share (diluted) continuing operations	**0.00**	**(0.08)**	**(0.02)**	**(0.41)**	**(0.40)**	**(0.08)**	**0.01**
Weighted average common shares outstanding - diluted	1,155,609	2,529,933	4,652,643	12,447,305	19,964,376	27,520,325	33,024,390
Gross Margin	**N/M**	**N/M**	**N/M**	**26.2%**	**24.7%**	**39.6%**	**43.0%**

XZERES Corporation

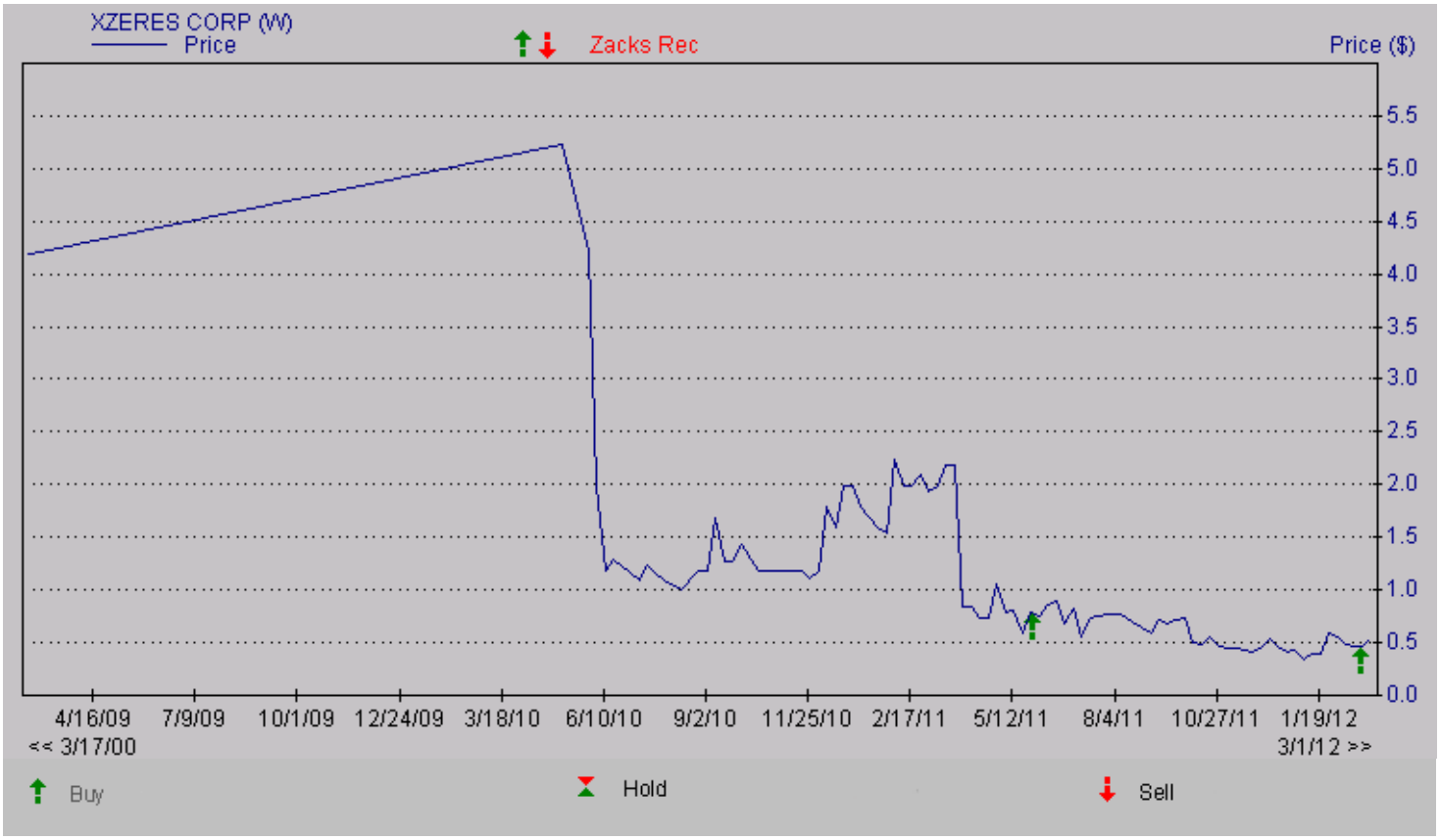
Quarterly Earnings Analysis	1Q 2012 (May 31)	2Q 2012 (Aug 31)	3Q 2012 (Nov 30)	4Q E 2012 (Feb 29)	**FY E 2012** (Feb 29)	1Q E 2013 (May 31)	2Q E 2013 (Aug 31)	3Q E 2013 (Nov 30)	4Q E 2013 (Feb 28)	**FY E 2013** (Feb 28)
Revenue:	**1,017,217**	**1,367,901**	**927,451**	**925,000**	**4,237,569**	**1,500,000**	**2,700,000**	**4,860,000**	**8,748,000**	**17,808,000**
Cost of sales	765,781	1,046,669	676,509	703,000	**3,191,959**	960,000	1,674,000	2,964,600	5,161,320	**10,759,920**
Gross Profit	**251,436**	**321,232**	**250,942**	**222,000**	**1,045,610**	**540,000**	**1,026,000**	**1,895,400**	**3,586,680**	**7,048,080**
General & administrative	1,177,879	1,025,478	1,164,575	1,182,044	**4,549,976**	1,199,774	1,217,771	1,236,037	1,254,578	**4,908,161**
Marketing	92,668	103,224	87,120	88,427	**371,439**	89,311	90,651	92,010	93,391	**365,363**
Sales expense	325,817	370,974	562,266	567,889	**1,826,946**	573,568	579,303	385,000	388,850	**1,926,721**
Engineering/R&D expense	639,583	571,051	554,556	560,102	**2,325,292**	500,000	500,000	500,000	500,000	**2,000,000**
Total Expenses	**2,235,947**	**2,070,727**	**2,368,517**	**2,398,461**	**9,073,652**	**2,362,653**	**2,387,725**	**2,213,048**	**2,236,819**	**9,200,244**
Pre-tax profit from operations	**(1,984,511)**	**(1,749,495)**	**(2,117,575)**	**(2,176,461)**	**(8,028,042)**	**(1,822,653)**	**(1,361,725)**	**(317,648)**	**1,349,861**	**(2,152,164)**
Interest income (expense)	0	0	0	0	**0**	0	0	0	0	**0**
Other Income	(14,187)	(13,445)	(12,940)	(13,000)	**(53,572)**	925	925	925	925	**3,700**
Income (loss) Continuing Operations	**(1,998,698)**	**(1,762,940)**	**(2,130,515)**	**(2,189,461)**	**(8,081,614)**	**(1,821,728)**	**(1,360,800)**	**(316,723)**	**1,350,786**	**(2,148,464)**
Income (loss) from Discontinued Operations	0	0	0	0	**0**	0	0	0	0	**0**
Provision for income taxes	0	0	0	0	**0**	0	0	0	0	**0**
Net income for the year	**(1,998,698)**	**(1,762,940)**	**(2,130,515)**	**(2,189,461)**	**(8,081,614)**	**(1,821,728)**	**(1,360,800)**	**(316,723)**	**1,350,786**	**(2,148,464)**
Net income per common share (diluted)	**(0.11)**	**(0.09)**	**(0.11)**	**(0.10)**	**(0.40)**	**(0.07)**	**(0.05)**	**(0.01)**	**0.05**	**(0.08)**
Weighted average common shares outstanding - diluted	18,031,530	19,302,825	19,502,825	23,020,325	**19,964,376**	26,020,325	27,020,325	28,020,325	29,020,325	**27,520,325**
Gross Margin	24.7%	23.5%	27.1%	24.0%	**24.7%**	36.0%	38.0%	39.0%	41.0%	**39.6%**

XZERES Corporation

Consolidated Balance Sheets (in $ US)

For the years ending February 28	**2008**	**2009**	**2010**	**2011**	**2012 E**	**2013 E**
ASSETS						
Cash and cash equivalents	0	1,978	195,990	364,068	1,300,000	500,000
Accounts receivable (net)	0	0	0	633,669	1,555,659	2,100,000
Inventories	0	0	0	502,548	800,000	1,100,000
Inventory deposit	0	0	0	40,066	0	0
Prepaid expense	0	0	0	110,281	175,000	142,386
Current Assets	**0**	**1,978**	**195,990**	**1,650,632**	**3,830,659**	**3,842,386**
Property, plant & equipment (net)	0	0	0	375,115	425,000	425,000
Intellectual property	0	0	0	1,320,226	1,603,082	1,800,000
Website development costs (net)	0	0	0	18,234	10,000	5,000
Deposits	0	0	0	18,198	18,198	18,198
Net assets of discontinued operations	2,847,226	0	0	0	0	0
Total Assets	**2,847,226**	**1,978**	**195,990**	**3,382,405**	**5,886,939**	**6,090,584**
LIABILITIES						
Accounts payable	0	0	0	600,451	2,580,028	850,000
Accrued expenses	0	161,093	337,578	107,277	348,140	248,140
Customer deposits	0	0	0	48,228	344,936	144,936
Warranty reserve	0	0	0	16,601	17,000	21,000
Notes payable to related party	0	5,140	0	97,500	0	0
Notes payable	0	0	90,740	100,000	36,000	12,000
Net liabilities of discontinued operations	35,674	0	0	0	0	0
Current Liabilities	**35,674**	**166,233**	**428,318**	**970,057**	**3,326,104**	**1,276,076**
Preferred stock	0	0	0	0	0	0
Common stock	0	4,652	4,683	15,383	24,824	32,380
Stock warrants	0	0	0	1,565,054	4,295,860	6,045,860
Additional paid in capital	1,455,314	40,367	40,641	6,207,203	11,697,057	14,341,639
Retained earnings (deficit)	1,315,813	(209,274)	(277,652)	(5,375,292)	(13,456,906)	(15,605,370)
Accumulated other comprehensive income	40,425	0	0	0	0	0
SHAREHOLDERS' EQUITY	**2,811,552**	**(164,255)**	**(232,328)**	**2,412,348**	**2,560,835**	**4,814,508**
Total Liabilities and Equity	**2,847,226**	**1,978**	**195,990**	**3,382,405**	**5,886,939**	**6,090,584**
Common shares outstanding	1,155,609	4,651,978	4,682,602	15,382,816	19,964,376	27,520,325

HISTORICAL ZACKS RECOMMENDATIONS



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