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: Zacks Company Report – Raising Q2 Estimates Based on Last Minute License Deal

Based on the average EV to Sales of comparable companies in the IP business we believe FNJN Stock could be worth $6.83 per share next year if it does indeed collect the Blue Coat judgment as expected.

UPDATE

Finjan is positioned to grow not only by pursuing IP licensing, but also by penetrating cybersecurity consulting services, and investing in new IP via R&D and in cybersecurity startups. Its new consulting business is having slow start. In May the company settled with Proofpoint for $10.9 million and just booked another $0.6 million license deal. In 2017 we expect it to collect over $40 million from Blue Coat if the ruling is upheld on appeal, and for the company to retire its new preferred stock.

Current Price (06/29/16)	$1.83
Valuation	**$6.83**

SUMMARY DATA

52-Week High	**$2.32**
52-Week Low	**$0.83**
One-Year Return (%)	**32.6**
Beta	**-0.98**
Average Daily Volume (sh)	**120,555**
Shares Outstanding (mil)	**22.7**
Market Capitalization ($mil)	**$42**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**28**
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 2016 Estimate	**N/M**
P/E using 2017 Estimate	**2.2**
Zacks Rank	**N/A**

Risk Level	**High**
Type of Stock	**Small-Growth**
Industry	**Internet-Software**

ZACKS ESTIMATES

Revenue
(in millions of $- Restated)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014	0.0 R	0.0 R	5.0 A	0.0 A	5.0 A
2015	0.0 A	0.7 A	0.0 A	4.0 A	4.7 A
2016	2.3 A	5.0 E	3.2 E	1.0 E	11.5 E
2017					53.9 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014	-$0.08 R	-$0.15 R	$0.03 R	-$0.18 A	-$0.38 A
2015	-$0.19 A	-$0.12 A	-$0.21 A	-$0.05 A	-$0.56 A
2016	-$0.05 A	$0.00 E	-$0.07 E	-$0.16 E	-$0.28 E
2017					$0.85 E

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WHAT'S NEW

Company Books $565,000 License Deal At Quarter End

On June 28, 2016, Finjan squeezed another license deal for $565,000 into the quarter resulting in our need to raise revenue and earnings estimates for Q2. This deal was with an unnamed European-based provider of cloud and on-premise cybersecurity solutions and it has already been paid. **Our revenue estimate now moves up to $5.0 million with breakeven net income and EPS.** The only variable in the revenue forecast is whatever CybeRisk brings in which we are modeling at $100,000.

Recap of Other Events in Q2:

Settlement With Proofpoint Yields $10.9 Million

Finjan reached at $10.9 million settlement with Proofpoint on May 20, 2016, before the trial that was scheduled to start June 16, 2016. It will be paid in three installments: $4.3 million to be paid within three days of signing, $3.3 million on or before January 4, 2017, and $3.3 million on or before January 3, 2018. Between already signed license deals and settlements and the equity raised from temporary preferred stock, the company is set for cash for the next two years.

Temporary Preferred Equity Issued

On May 12, 2016 Finjan inked a preferred stock deal sold to investors led by Halcyon Long Recovery Durations. In return for $10.2 million in cash, it has offered to repay a minimum of $15.2 million and a maximum of $28 million depending on timing. Its repayments occur in accordance with the wishes of the buyer or the seller. The company agreed to pay 20% of any licensing revenue that is booked and 50% of any court awards and settlements to retire this stock as the buyer requests. The schedule for what Finjan owes to redeem its preferred in this arrangement is as follows:

- From May 12, 2016 to August 10, 2016 (the 90 anniversary of the date of Issuance), 1.5 times or $15,300,000.
- From August 10, 2016 to the 360 day anniversary of the Date of Issuance (August 5, 2017), 1.65 times or $16,830,000.
- From August 5, 2017 to the August 1, 2018, 1.75 times or $17,850,000.
- Thereafter, 1.75 times plus 0.1 times for every 90 period following August 1, 2018.

  The maximum paid will be 2.8 times the purchase price or $28,560,000.

The company stated that there will be no effect on the income statement, but due to the uniqueness of this deal, the auditors are still working out the details. So rather than having this decrease in profitability of the company reflected in earnings, it will be reflected in enterprise value as this new debt is taken on and repaid. If the company needs to borrow the full $10.2 million for the next year, the company will have to pay back $16.83 million yielding annual interest rate of 65% on what is behaving somewhat like a zero coupon bond but is being called temporary equity.

Still Awaiting More Possible Settlements

As trial dates approach, and the Patent Office rules on petitions we believe there is also a chance that Sophos could be settled. This **trial is scheduled for September 6, 2016.**

Palo Alto Networks (PANW) may have its stay lifted since the Patent Office ruled on Finjan's patents. It may be more amenable to a licensing deal as this hurdle cleared. Of the 13 petitions for IPR, the PTAB has denied seven petitions in Finjan's favor, partially denied (and partially granted) three petitions, and granted three petitions for review.

'926 Patent: IPR2016-00145: denied
'968 Patent: IPR2016-00149: denied
'968 Patent: IPR2016-00150: denied
'154 Patent: IPR2016-00151: part denied/part granted
'494 Patent: IPR2016-00159: granted
'918 Patent: IPR2016-00164: denied
'780 Patent: IPR2016-00165: denied
'633 Patent: IPR2015-01974: part denied/part granted
'154 Patent: IPR2015-01979: part denied/part granted
'822 Patent: IPR2015-01999: denied
'731 Patent: IPR2015-02000: denied
'408 Patent: IPR2015-02001/IPR201600157 (consolidated): granted on certain claims

FireEye (FEYE) is still stayed pending rulings at PTAB.
Any or all of these may settle as the Proofpoint agreement may prove an impetus for the others.

RECAP: The Win Against Blue Coat

The big win for Finjan against Blue Coat on August 5, 2015 awarded the company $40 million plus an additional 10% in interest per year. However, litigation with Blue Coat has not ended. Most likely should Blue Coat not settle, it will appeal--a process that could take until the middle of 2017. We have tentative put revenue from this judgment in 2017. In addition there is the new suit against it that encompasses seven patents and addresses new products that have been introduced by Blue Coat since the lawsuit just won was filed in 2013. Specifically the company named certain of Blue Coat's ProxySG Appliances and Software, the ProxyAV Appliances and Software, and WebPulse Services (some of which Blue Coat recently launched) as products that are infringing. The patents Finjan believes are being infringed upon in this new suit are: 6,154,844; 6,965,968; 7,418,731; 8,079,086; 8,225,408; 8,566,580 and 8,677,494, the last four of which are being asserted against Blue Coat for the first time. The company is still working through the post-trial motions process for the first suit. There was a JMOL hearing and we are awaiting the final district court order on that verdict amount which could include pre and post-judgment interest and recovered fees and expenses in this case. This result could be in any day now.

THE PRESENT COMPANY ENFORCEMENT

Company	Date and Location	Status	Patent numbers
FireEye **($623 million)**	US District Court for the Northern District of California on July 8, 2013	Stayed pending review by PTAB.	**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 US District Court for the Northern District of California on July 16, 2015	**Won $40m judgment. All patents upheld. Only 7,058,822 did not infringe.** Post-trial motions April 28, 2016 Trial date October 30, 2017	6,154,844, **6,804,780**, 6,965,968, **7,058,822**, 7,418,731, and 7,647,633 6,154,844; 6,965,968; 7,418,731; 8,079,086; 8,225,408; 8,566,580; 8,677,494
Proofpoint **($265 million)**	United States District Court for the Northern District of California on December 16, 2013	Settled May 23, 2016 for $10.9 million.	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 **($447 million)**	United States District Court for the Northern District of California on March 14, 2014	Pretrial conference August 8, 2015. Trial set Sept. 6, 2016.	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 **($6.5 billion)**	United States District Court for the Northern District of California on June 1, 2014	Stay lifted. Proposed schedule submitted. Estimated date Q1 2018.	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 ($1.1 billion)	United States District Court for the Northern District of California on November 4, 2014	Review completed by PTAB. Waiting for stay to be lifted.	**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

Highlighted patent numbers have been successfully defended in court.

KEY POINTS

- Finjan holds a number of pioneering patents for cybersecurity hardware and software that is relevant to dozens of companies in this space.
- While it has already won a $40 million + judgment against Blue Coat; its biggest opportunity is its litigation with Symantec, a much larger company.
- The company is continuing to file new patents.
- While its patents have already generated > $130M in its licensing and enforcement track record, the company has the potential to continue to reap large licensing revenues from the $21 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 win against Blue Coat proves its patents are still valued and able to be successfully defended and therefore monetized.
- The company's has a market cap of $42 million and could be worth considerably more if it is successful in its licensing pursuits. Estimating revenues of $54 million in 2017 and an industry multiple of 2.6 times sales, the company could be worth as much as $139 million in enterprise value by 2017 if it succeeds in reaching new licensing arrangements.

OVERVIEW

Finjan Holdings is a patent licensing and enforcement firm based in East Palo Alto, California 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

VALUATION

Valuation of an IP company, even with a track record, is very difficult. It is even more so with a company like Finjan that has only two court victories, four recent licensing arrangements, and no recurring revenues. 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 (RMBS), and the upstarts that trade on events and potential. We can see from the table below, this ranges from Pendrell (PCO) with an negative $43 million enterprise value, to Interdigital (IDCC) with an enterprise value of $1.5 billion and $371 million in sales expected this year. On average, the companies with revenues trade at an average of 2.6X 2016 estimated calendar revenues.

Using a valuation based on enterprise value to sales is easier for unprofitable companies. If Finjan were to generate $54 million in sales in 2017, we could see the market putting a 2.6 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 $6.97 per share by 2017, assuming it achieves our estimated revenue levels in 2016 from licensing and consulting in addition to a settlement received from Blue Coat if the appeal is won.

Company	Ticker	Revenue 2016E	Revenue LTM	EV/ EBITDA	EBIDTA Margin	Enterprise Value / Sales 2016E	Enterprise Value / Sales LTM	Included in Average?	Enterprise Value
Acacia Research	ACTG	$101	$116	6.5x	40%	0.7x	0.6x	y	$73
Interdigital	IDCC	$371	$439	5.9x	58%	4.0x	3.4x	y	$1,480
Inventergy Global	INVT	$9	$5	-7.1x	-100%	2.0x	3.6x	y	$17
Marathon	MARA	$41	$17	-7.2x	-104%	1.5x	3.6x	y	$62
Neonode	NEON	$20	$12	-11.9x	-68%	3.4x	5.6x	y	$67
Network-1	NTIP	NA	$16	3.2x	45%	NA	2.7x	n	$43
Parkervision	PRKR	$10	$0	-2.5x	NM	3.7x	545.3x	n	$38
Pendrell	PCO	$36	$32	-4.0x	29%	-1.2x	-1.4x	n	-$43
Rambus	RMBS	$315	$296	11.7x	34%	3.8x	4.1x	y	$1,210
RPX	RPXC	$338	$288	1.8x	72%	1.0x	1.2x	y	$352
Tessera	TSRA	$253	$253	6.2x	73%	4.3x	4.3x	y	$1,100
VirnetX	VHC	$150	$2	-6.5x	NM	1.4x	131.2x	n	$209
FORM Holdings	FH	NA	$25	-1.7x	NM	NM	0.3x	n	$8
Wi-Lan	WILN	$100	$113	2.9x	72%	2.4x	2.1x	y	$238
Average				**1.0x**	**9%**	**2.6x**	**3.2x**		**$511**

	Revenue 2017E	Revenue LTM	EBITDA Margin	Enterprise Value / Sales 2017E	Enterprise Value / Sales LTM	Valuation Range Low	Valuation Range High
Finjan	**$54**	**$7**	**-154%**	**2.6x**	**3.2x**	**$22**	**$139**

Conclusion of Enterprise Value	**$139,468,239**
Market Value	**$155,468,239**
Shares Outstanding	22,778,925
Price per Share	**$6.83**

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 before the Markman Hearing. Proofpoint just yielded $10.9 million right at the pre-trial hearing. Sophos is past Markman and nearing trial so rates should be near Proofpoint rates. Blue Coat went through the full trial and was awarded $40 million. If this is appealed and the company wins on appeal, the sum will be higher as interest and royalties for additional products sold during the litigation process is added on as well as trial expenses. Looking at the rest of the companies we can derive revenues over $290 million adding actuals and for similar licensing at the same stage as Websense. Judgments, of course, may be all over the place.

	2015 Revenues	% Relevant	License	Judgment
Estimated				
FireEye	$623	30%	$18.7	
Proofpoint	265	50%	13.3	
Sophos	447	25%	11.2	
Symantec (2 segments)	4,200	30%	126.0	
Palo Alto Networks	1,100	27%	30.0	
Total potential			199.1	
Actual				
Blue Coat				40.0
Websense	DK	DK	8.0	
Avast Software	DK	DK	3.0	
Undisclosed	DK	DK	3.7	
Proofpoint	265		10.9	
European undisclosed			0.6	
Total actual	DK	DK	26.1	
TOTAL			$252.2	40.0
Plus Blue Coat			**292.2**	

Cybersecurity companies

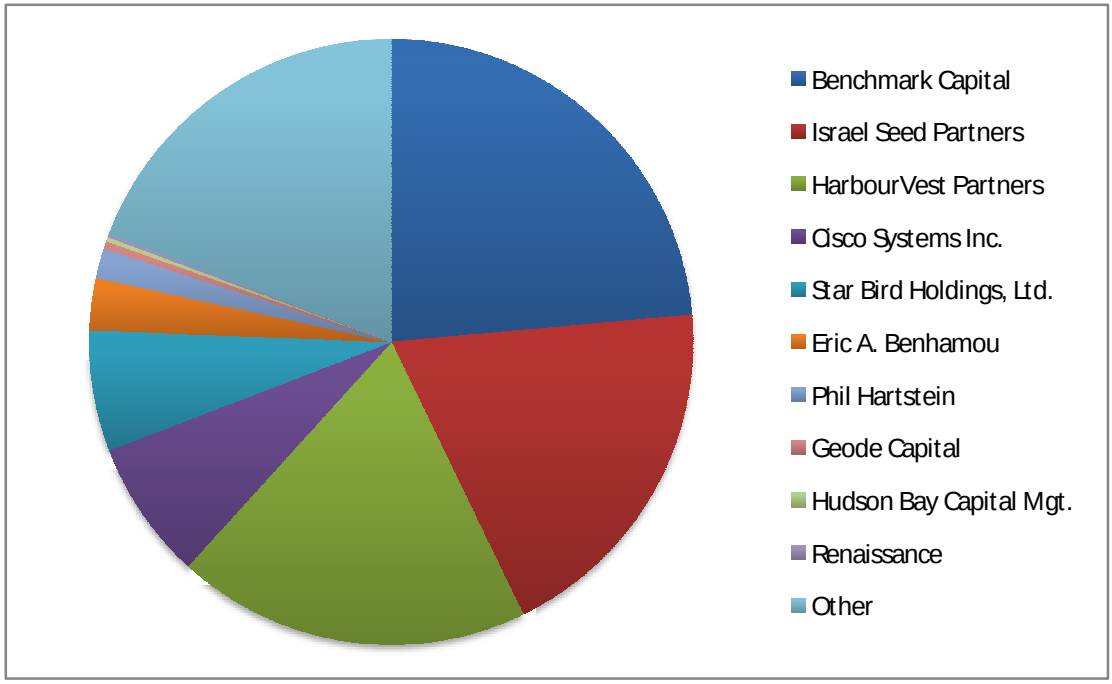
The new consulting venture, once it starts to generate meaningful revenues, will have different peer comparables where valuations are much higher. For example, FireEye bought Madiant for $1 billion or approximately 7 times sales. Another comparable would be root9b, a company with $141 million enterprise 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.
- There is no way to predict the timing of lawsuit settlements or licensing agreements, or even the length of a lawsuit.
- 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.

OWNERSHIP

As of June 30, 2016



INCOME STATEMENT

	2015				2016E							
In Thousands	**Q1**	**Q2**	**Q3**	**Q4**	**Q1**	**Q2E**	**Q3E**	**Q4E**	**2014**	**2015**	**2016E**	**2017E**
Websense	$0	$0	$0	$0	$2,000	$0	$0	$0	$4,998	$0	$2,000	$1,000
Other licenses	0	700	0	3,975	300	565	2,650	0	0	4,675	3,515	6,700
CybeRisk Security Solutions	0	0	0	12	20	100	550	1000	0	12	1,670	2,500
Blue Coat				0	0	0	0	0	0	0	0	40,400
Proofpoint						4,300	0	0	0	0	4,300	3,300
Total Revenues	**0**	**700**	**0**	**3,987**	**2,320**	**4,965**	**3,200**	**1,000**	**4,998**	**4,687**	**11,485**	**53,900**
Cost of revenues	0	60	0	754	0	907	39	70	800	814	1,015	12,680
Gross profit	0	640	0	3,233	2,320	4,058	3,162	930	4,198	3,873	10,470	41,220
Gross Margin		91%		81%	100%	82%	99%	93%	84%	83%	91%	76%
Operating Expenses:												
SG&A	4,205	4,413	4,490	4,254	3,433	4,000	4,600	4,600	13,813	17,362	16,633	20,000
R&D		146	206	39	51	50	50	50	0	391	201	200
Total operating expenses	4,205	4,559	4,696	4,293	3,484	4,050	4,650	4,650	13,813	17,753	16,834	20,200
Operating Income	(4,205)	(3,919)	1,596 (4,696)	(1,060)	(1,164)	8	(1,489)	(3,720)	(9,615)	(13,880)	(6,364)	21,020
Other Income												
Gain on settlements	0	0	0	0	0	0	0	0	1,000	0	0	0
Other income	(1)	1,271	0	1	0	0	0	0	0	1,271	0	0
Interest income	9	7	(4)	0	1	0	0	0	90	12	1	100
Total other income	8	1,278	(4)	1	1	0	0	0	1,090	1,283	1	100
Pretax profit	(4,196)	(2,634)	(4,700)	(1,060)	(1,163)	8	(1,489)	(3,720)	(8,525)	(12,597)	(6,363)	21,120
Income taxes	5	0	0	0	-	-	-	-	5	5	5	5
Tax rate					0%	0%	0%	0%	0%	0%	0%	0%
Net Income	(4,201)	(2,634)	(4,700)	(1,060)	(1,163)	8	(1,489)	(3,720)	(8,520)	(12,602)	(6,368)	21,115
Net Income Per Share:												
EPS	**($0.19)**	**($0.12)**	**($0.21)**	**($0.05)**	**($0.05)**	$0.00	**($0.07)**	**($0.16)**	**($0.38)**	**($0.56)**	**($0.28)**	$0.93
Diluted EPS	($0.19)	($0.12)	($0.19)	($0.05)	($0.05)	**$0.00**	($0.06)	($0.16)	($0.38)	($0.52)	($0.26)	**$0.85**
Avg Shares Outstanding	22,409	22,519	22,562	22,641	22,709	22,757	22,800	22,850	22,404	22,549	22,779	22,624
Diluted Shares	24,315	24,435	24,468	24,560	24,628	24,676	24,719	24,769	24,209	24,444	24,698	24,719
Stock-based Comp	355	100	187	124	142	142	142	142	1448	766	568	568
Non-GAAP Income	(3,846)	(2,534)	(4,513)	(936)	(1,021)	150	(1,347)	(3,578)	(7,072)	(11,836)	(5,800)	21,683
Non-GAAP EPS	**($0.17)**	**($0.11)**	**($0.20)**	**($0.04)**	**($0.04)**	**$0.01**	**($0.06)**	**($0.16)**	**($0.32)**	**($0.52)**	**($0.25)**	**$0.88**

BALANCE SHEET

$ in Thousands	March 31, 2016	Dec. 31, 2015	% Change
Current assets:			
Cash and cash equivalents	$5,062	$6,101	-17%
Accounts receivable, net	-	-	
Prepaid expenses and other current assets	284	322	-12%
Total current assets	5,346	6,423	-17%
Property and equipment, net	243	257	-5%
Investments	2,195	2195	0%
Other long term assets	325	325	0%
Total Assets	8,109	9,200	-12%
Current Liabilities:			
Accounts payable	2,181	2,220	-2%
Accounts payable - related parties	21	17	24%
Accrued expenses	446	450	-1%
Accrued income taxes	9	9	0%
Other current liabilities	0	32	-100%
Total current liabilities	2,657	2,728	-3%
Other non-current liabilities	131	130	1%
Total Liabilities	2,788	2,858	-2%
Stockholders' Equity			
Common stock	2	2	0%
Additional paid-in capital	24,088	23,946	1%
Retained earnings	(18,769)	(17,606)	7%
Total Stockholders' Equity	5,321	6,342	-16%
Total Liabilities & Stockholders' Equity	$8,109	$9,200	-12%
Cash per share	$0.22	$0.27	-17%

CASH FLOW

	Mar. 31, 2016	Dec. 31, 2015	Sept. 30, 2015	Jun. 30, 2015	March 31, 2015	2015 Year
Cash flows from operating activities:						
Net loss	$ (1,163)	$ (1,059)	$ (4,700)	$ (2,641)	$ (4,202)	$ (12,602)
Adjustments to reconcile net loss to net cash used in operating activities:						
Gain on Investment	0	0	0	(1,271)	0	(1,271)
Depreciation and amortization	14	15	9	19	7	50
Loss on disposal of assets	0	34	0	0	0	34
Stock-based compensation	142	124	187	100	355	766
Deferred tax liability	0	0	0	0	0	0
Changes in operating assets and liabilities:						
Accounts receivable	0	0	0	55	1,961	2,016
Inventories	0	0	0	0	0	0
Prepaid expenses and other current assets	38	(81)	(23)	(153)	47	(210)
Other long-term assets	0	(24)	(70)	0	(231)	(325)
Accrued expenses	(4)	13	(361)	(44)	42	(350)
Accounts payable	(39)	72	669	152	(348)	545
Accounts payable - related parties	4	9	0	(10)	(82)	(83)
Other assets	0	97	65	0	0	162
Other liabilities	(31)	0	0	0	0	0
Accrued income taxes	0	1	0	0	8	9
Total Adjustments	(32)	87	280	0	1,397	1,764
Net cash used in operating activities	(1,039)	260	476	(1,152)	(2,443)	1,343
Cash flows from investing activities:						
Purchases of property and equipment	0	(11)	(54)	(133)	(77)	(275)
Proceeds from investment	0	0	0	826	0	826
Purchase of additional investment	0	(250)	(500)	0	0	(750)
Net cash provided by (used in) investing activities	0	(261)	(554)	693	(77)	(199)
Proceeds from exercise of stock options						
Proceeds from exercise of stock options	0	97	29	0	20	54
Net cash provided by financing activities	0	97	29	0	20	54
Net decrease in cash and cash equivalents	(1,039)	96	(49)	(3,100)	(2,500)	1,198
Cash and cash equivalents - beginning	6,101	7,156	11,905	15,005	17,505	
Cash and cash equivalents - ending	15,005	6,101	7,156	11,905	15,005	6,101
Cash paid for income taxes	0	7	0	0	0	7
Non-cash investing and financing activities						
Additional investment held by investee	0	0	0	445	0	445
Purchase of property and equipment in exchange for finance agreement	0	0	0	0	0	0
Operating cash Flow	**(1,007)**	**(886)**	**(4,504)**	**(3,793)**	**(3,840)**	**(13,023)**
Free cash flow	(1,007)	(1,125)	(4,950)	(2,834)	(3,763)	(12,672)

HISTORICAL STOCK PRICE



DISCLOSURES

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