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Zacks Small-Cap Research

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Lisa Thompson
312-265-9517
lthompson@zacks.com

scr.zacks.com **10 S. Riverside Plaza, Chicago, IL 60606**

O2Micro International Ltd (OIIM-NASDAQ)

OIIM: A Strong Q1 Driven By Stay-At-Home Buying of TVs and Garden Tools

Using an industry average value to trailing 12-month sales of 6.6 times and OIIM's $63.7 m trailing 12-month revenue, we would calculate an enterprise value of $423 million, a market cap of $468 million and a price of **$17.28 per share**, if the company could reach breakeven and stay there.

OUTLOOK

O_2Micro International is a fabless semiconductor firm that designs, develops and markets high performance integrated circuits primarily for power management and battery management for TV backlighting, LED lighting, and portable tools and appliances. It has struggled to reach profitability and cash flow breakeven. The company trades at a **negative enterprise value of $4.1 million**, well below the value of its non-cash assets. It is enjoying a surge in TV and battery operated tools due to shutdowns around the world.

Current Price (05/08/20)	$1.52
Valuation	**$17.28**

SUMMARY DATA

52-Week High	**$1.77**
52-Week Low	**$1.00**
One-Year Return (%)	**9.4**
Beta	**0.7**
Average Daily Volume (sh)	**24,510**
Shares Outstanding (mil)	**26.7**
Market Capitalization ($mil)	**$40.6**
Short Interest Ratio (days)	**1.0**
Institutional Ownership (%)	**37**
Insider Ownership (%)	**8**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**2.9**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/M**
P/E using 2020 Estimate	**N/M**
P/E using 2021 Estimate	**N/M**

Risk Level	**Low**
Type of Stock	**Small-Value**
Industry	**Elec Comp-Semis**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2018	14.1 A	15.2 A	16.8 A	16.6 A	63 A
2019	12.8 A	14.3 A	16.0 A	17.9 A	61 A
2021	15.6 A	17.0 E	17.5 E	17.5 E	68 E
2020					73 E

Earnings Per Share
(non-GAAP EPS before non-recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2018	-$0.09 A	-$0.05 A	-$0.05 A	-$0.05 A	-$0.24 A
2019	-$0.13 A	-$0.08 A	-$0.02 A	$0.05 A	-$0.18 A
2020	-$0.00 A	-$0.01 E	$0.01 E	$0.04 E	-$0.00 E
2021					$0.04 E

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

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WHAT'S NEW

O2Micro's Strong Q1 Was Driven By Sales of TVs and Garden Tools Due to Stay at Home Policies

Following its strong Q4 (which benefitted from a one time license fee of $2.1 million,) Q1 came in above our estimate both in revenues and earnings mostly due to lower operating expenses. China which was hard hit by Covid19 earlier than in the US, was shut down in much of Q1. Consumers there bought TVs and garden tools to fill their time at home keeping orders to O2Micro flowing. O2Micro gets almost all its revenues from backlighting chips sold to Chinese manufacturers of televisions and portable devices powered by lithium batteries. Even laptops had a resurgence of demand as companies had their employees working from home. We know of one IT services companies that bought 70,000 laptops in one fell swoop last quarter. There has also been a surge in the sale of bicycles and ebikes as consumers have both leisure time and an aversion to mass transit. The BBC just reported that 61% of Britons are nervous of taking public transportation post-lockdown. In Q2 we expect these trends should continue throughout the world.

Revenues were $15.6 million compared with $12.8 million in Q1 a year ago, up 22%. Guidance for revenue for the second quarter of 2020 was for revenues between $16.5 and $17.5 million or a midpoint of $17 million, which would be growth of 19% year over year.

Coronavirus Impact

While the supply chain is mostly back to normal, there is disruption in logistics with limited air travel. While factories are operating, restaurants and stores are still not open. Orders in Q2 have continued strong and the company is mindful that some orders may have been pulled forward and is keeping an eye on demand.

Q1 Results

For Q1 the gross margin settled back to more normal levels without the impact of the $2.1 million 100% margin license fee booked in Q4. It was 51.9% compared to 50.5% a year ago and 56.7% in Q4 2019. The company said to expect Q2 2020 gross margin to be in the range of 51-53% as it phases out its low margin offerings to focus on high margin products.

Operating expenses were lower than expected as business was interrupted in Asia and spending was pushed out. Operating expenses were only $8.7 million down again from the $9.2 million spent in Q4 2019. The company had expected expenses to rise in Q1 2020.

R&D declined again in the quarter to $4.1 million, as the company reigned in expenses and SG&A decreased to $4.5 million from $4.8 million in Q3. For Q2, the midpoint of guidance is $9.5 million, up $820,000 sequentially. The company will be laying off staff, primarily those in difficult low margin efforts with limited return such as smartphones. The Chinese market for handsets decline 20% in Q1 2020 according to IDC with Apple and Huawei holding up better than the second and third tier players. In addition, the US government is scrutinizing sales of communications components to China making future prospects in that market even more risky.

The operating loss in Q1 was $571,000 versus a loss of $3.6 million last year. Adding back depreciation and amortization ($502,000) and stock-based compensation ($397,000,) and adding the rental income, the adjusted EBITDA looks to be a positive $445,000 versus a negative $2.4 million in Q1 2019.

Total other income was a negative $764,000 million versus a positive $74,000 last year. This year included a $1.1 million unrealized loss on the company holding in Excelliance MOS stock. In Q1 O2Micro sold 14,000 shares of Excelliance MOS stock for proceeds of $50,000 at an average price of $3.58. It

had a cost basis of $0.53. It still holds 780,000 shares, and expects to sell more in Q2 2020. EMC is up 54% since March 31, and there could be an unrealized gain in Q2.

The company reported a GAAP loss of $1.5 million versus last year's loss of $3.5 million last year. This yielded GAAP loss per share of $0.06 versus a loss per share of $0.15 a year ago.

Non-GAAP loss was $43,000, versus a loss of $3.5 million last year. N**on-GAAP EPS was virtually breakeven, versus a loss of $0.13 last year**. In Q1 2020, the company repurchased 83,479 ADS units at a cost of $100,000.

On March 31, 2020, the company had $44.7 million in cash and equivalents (or $1.67 per ADS), down $1.7 million sequentially. Net cash used by operating activities in the quarter was $1.3 million. Capital expenditures were $200,000 and depreciation and amortization was $502,000.

In Q2 the company is streamlining operations for profitability and to focus on higher margin products. The company plans to take a one-time charge for severance of between $1.1 and $1.2 million that will push the company's cash breakeven point down to between $14-16 million and the profit breakeven to $16-18 million. The full effect of these cost savings efforts will be felt in Q4 2020.

	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020
Consumer	40-45%	42-44%	49-51%	43-45%	46-48%	43-45%	44-46%	43-45%	44-46
Computer	10-15	15-17	8-10	6-8	6-8	6-8	6-8	5-7	5-7
Industrial	40-45	40-42	40-42	47-49	45-47	47-49	47-49	48-50	48-50
Communications	<5	0	0	0	0	0	0	0	0

Despite challenges in the supply chain due to both shutdowns and Chinese New Year, the company showed strong growth in the quarter. This is against a backdrop of a particularly weak Q1 in 2019 driven by lackluster TV sales in China, coming off an inventory correction from wafer shortages. O2Micro had particular strength in TV sales in China as well as HDR monitors and garden tools as people were forced to stay home. Other products that benefited were notebooks as companies sent their workers home with computers, ebikes as public transportation was shunned, and medical monitors. Notebooks are also benefiting from companies upgrading to Windows 10. While China is beginning to get back to normal, shutdowns are staggered throughout the rest of the world where these trends should continue in Q2 and possibly beyond. Over 90% of the company's sales come from TVs and battery-powered devices.



Source: Zacks Investment Research

Intelligent lighting, which includes both TVs and monitors, did very well in Q1. The company highlighted the new Sony MASTER series and noted that the 85-inch Z9G, 8k HDR has 64 chips in each one. It is made of a full-array LED with local dimming and brings more realistic peaks of brightness, more accurate shadow detail, and deeper inkier blacks than a standard LED TV. 4k/8k HDR monitors using O2Micro's chips also have improved brightness adjustment dependent on the screen content with improved adjustments for halos. O2Micro is sampling new multi-scale LED backlighting for LCD display monitors.

The battery business had excellent growth. In Q4 demand was for floor care, vacuum cleaners, the hair care application, uninterrupted power system, and battery storage systems and so long was in high demand. This quarter demand rotated into power tools and garden tool market as well as electrical bikes.

The company is now focusing on the Japanese high-end market in the charger product line. Customers use O2Micro's products for high-end camera chargers, automotive USB chargers, and floor care vacuum cleaner chargers.

VALUATION

Company Has Significant Upside If It Can End Cash Burn and Sustain a Profit

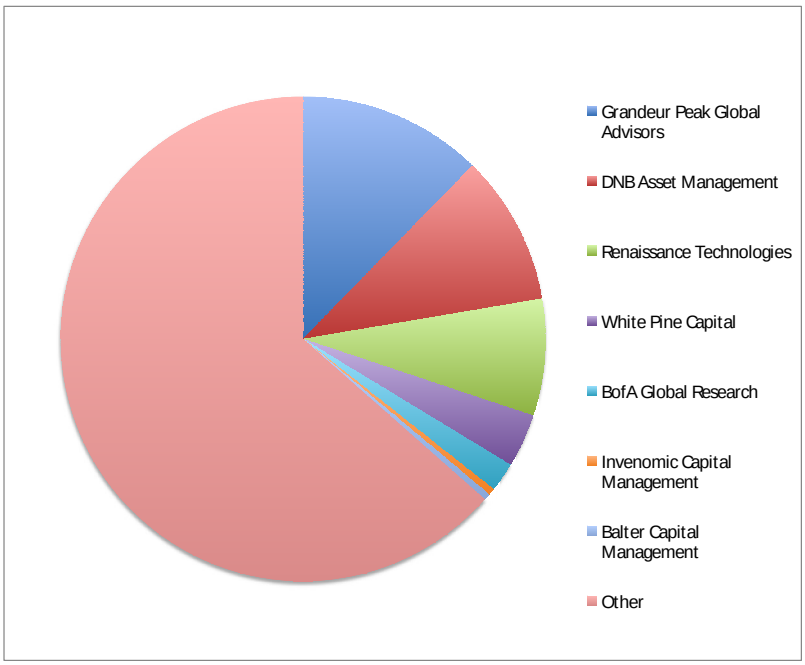
The company trades at a negative **enterprise value of $9.5 million**. At the end of Q1 2020, the company had $44.7 million (or $1.67 per ADS) in cash and equivalents, no debt, and valuable real estate in China and California. In California it owns a 37,180 square foot building where it has its USA operations, which was bought for $4.6 million in May 2004 and believe it is now easily worth more than $7 million. Plus it also owns other real estate in China and Taiwan. Also on the balance sheet are long-term investments in other companies, including 780,000 shares of stock in Excelliance MOS (worth $3.1 million.) The company has a very high liquidation, as well as acquisition, value. Activists have tried to encourage a transaction with an acquirer, but the company has no interest in a sale and due to restrictions, it is difficult to force one.

In May 2018, Microchip Technology bought Microsemi for $10.15 billion, which was a valuation of 5.5 times its trailing twelve-month revenues of $1.845 billion. Two other comparable companies we had been using, Intersil and Linear Technology, were acquired at very high valuations. Intersil was acquired by Renesas for $3.2 billion at a valuation of 5.9xs the company's trailing $542.1 million in revenue. Analog Devices acquired linear Technology for $14.8 billion. This was 9.9 times its trailing four quarters of revenue of $1.5 billion.

Were we to use the average enterprise value to trailing twelve-month sales of 6.6 times and apply it to OIIM's trailing 12-month $63.7 million revenues, we would calculate an enterprise value of $426 million. Adding to it $44.7 million in cash and equivalents gives us a market cap of $468 million or **$17.28 per share**. We believe that once the company shows sustainable revenue growth and cash breakeven, the market should afford it a valuation closer to this price.

	Competitors	EV	TTM Sales	EV/Sales
Monolithic Power Systems	**MPWR**	8,490	652	13.0
Cree Inc.	**CREE**	4,330	950	4.6
Microchip Technology	**MCHP**	30,250	5,270	5.7
Maxim	**MXIM**	13,400	2,200	6.1
Texas Instruments	**TXN**	103,220	14,120	7.3
Cirrus Logic	**CRUS**	4,010	1,280	3.1
	Average			6.6

OWNERSHIP



Source: Zacks Investment Research

RISKS

- O_2Micro has high exposure to the global demand for TVs, particularly those sold in China. It is depending on free dimming and high power LED lighting, 4K and 8K and other high end TVs and monitors, lithium ion battery powered tools and appliances, and IoT to give it revenue and margin growth.

- In 2019, two customers accounted for 26% of revenues and their loss could cause a meaningful decline in revenues. 86% of revenues were from China. Without the FEIT license fee, we believe that number would be 89%.

- The company is currently being affected by the proliferation of the coronavirus in China as their production and most of their customers are located in China and sell to the Chinese market. Right now is unknown how restrictions and health concerns will affect commerce in both the short and long term.

- The firm has had only one profitable GAAP quarter since 2011, it remains to be seen when positive results will be sustainable.

- Given its large number of patents, litigation risk is a possibility as the company enforces its patents.

INCOME STATEMENT

	March Q1 19	June Q2 19	Sept Q3 19	Dec Q4 19	March Q1 20	June Q2 20E	Sept Q3 20E	Dec Q4 20E	2018	2019	2020E	2021E
REVENUE												
Net Revenue	12.8	14.3	16.0	17.9	15.6	17.0	17.5	17.5	62.7	60.9	67.6	73.0
Yr-to-yr Gr.	-10%	-6%	-5%	8%	22%	19%	9%	-2%	4%	-3%	11%	8%
OPERATING EXPENSES												
Cost of goods sold	6.3	7.1	7.8	7.7	7.5	8.2	8.4	8.3	30.7	29.0	32.4	36.0
Gross Margin	6.4	7.1	8.2	10.1	8.1	8.8	9.1	9.2	32.0	32.0	35.2	37.0
% of Sales	50.5%	50.1%	51.4%	56.7%	51.9%	52.0%	52.0%	52.6%	51.0%	52.5%	52.1%	50.7%
R&D	5.1	4.8	4.7	4.4	4.1	4.6	4.4	4.1	19.8	19.1	17.3	19.5
SG&A	5.0	4.9	4.6	4.8	4.5	4.9	4.8	4.4	20.3	19.3	18.6	17.6
One-time expenses & Adj.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	(0.0)	0.0	0.0	0.0
Tot Operating Exp.	10.0	9.7	9.4	9.2	8.7	9.5	9.2	8.5	40.1	38.4	35.8	37.1
Operating Income	(3.6)	(2.6)	(1.1)	0.9	(0.6)	(0.6)	(0.1)	0.7	(8.1)	(6.4)	(0.6)	(0.1)
Interest income	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.4	0.5	0.7	0.7
Unrealized fair value on LT Investment	0.0	(0.2)	0.7	0.2	(1.1)	0.0	0.0	0.0	9.8	0.8	(1.1)	0.0
Foreign exchange loss	(0.1)	0.1	0.0	(0.1)	0.0	0.0	0.0	0.0	0.1	(0.2)	0.0	0.0
Gain on sale of real estate	0.0	0.0	0.0	0.5	0.0	0.0	0.0	0.0	0.0	0.5	0.0	0.0
Other (rent) - net	0.1	0.1	0.4	0.2	0.1	0.1	0.1	0.1	1.0	0.8	0.5	0.1
One-time charge	0.0	0.0	0.0	0.0	0.0	(1.2)	0.0	0.0	0.0	0.0	(1.2)	0.0
Total other Income	0.1	0.1	1.2	1.1	(0.8)	(0.8)	0.3	0.3	11.4	2.5	(1.0)	0.8
Pretax Income	(3.5)	(2.5)	0.1	2.0	(1.3)	(1.5)	0.2	1.0	3.3	(3.9)	(1.6)	0.7
Pretax margin	-27.6%	-17.4%	0.8%	11.3%	-8.6%	-8.7%	1.2%	5.7%	5.2%	-6.3%	-2.4%	1.0%
Taxes	0.3	0.3	0.3	0.3	0.2	0.3	0.3	0.3	1.1	1.2	1.0	1.1
Tax Rate	-8.5%	-11.6%	251.5%	12.4%	-15.4%	-17.5%	122.5%	27.9%	34.9%	-30.3%	-61.7%	152.3%
GAAP Net Income	(3.8)	(2.8)	(0.2)	1.8	(1.5)	(1.7)	(0.0)	0.7	2.1	(5.0)	(2.6)	(0.4)
Non-GAAP Net Income	(3.5)	(2.2)	(0.5)	1.4	(0.0)	(0.2)	0.3	1.1	(6.3)	(4.8)	(0.0)	1.1
GAAP EPS-Basic	($0.15)	($0.11)	($0.01)	$0.07	($0.06)	($0.07)	($0.00)	$0.03	$0.08	($0.19)	($0.10)	($0.01)
GAAP EPS-Fully dil.	($0.14)	($0.11)	($0.01)	$0.07	($0.06)	($0.07)	($0.00)	$0.03	$0.08	($0.19)	($0.10)	($0.01)
Non-GAAP	**($0.13)**	**($0.08)**	**($0.02)**	**$0.05**	**($0.00)**	**($0.01)**	**$0.01**	**$0.04**	**($0.24)**	**($0.18)**	**($0.00)**	**$0.04**
Share Out	26.3	26.4	26.3	26.3	26.7	26.7	26.7	26.7	26.0	26.3	26.7	26.5
Fully diluted shares	26.9	26.4	26.3	27.1	26.7	26.7	26.7	26.7	26.6	26.3	26.7	26.5
Yr-to-yr Gr.	2%	0%	0%	2%	-1%	1%	1%	-1%	3%	-1%	2%	-1%

BALANCE SHEET

	March 31, 2020	Dec 31, 2019	Qtr-to-Qtr % Change	March 31, 2019	Yr-to-Yr % Change
CURRENT ASSETS					
Cash and cash equivalents	$16,108	$10,696	50.6%	$31,058	-48.1%
Restricted cash	35	35	0.0%	34	2.9%
Short-term investments	28,595	35,693	-19.9%	4,189	582.6%
Accounts receivable, net	11,016	10,335	6.6%	8,592	28.2%
Inventories	9,876	8,796	12.3%	10,608	-6.9%
Prepaid expenses and other current assets	1,361	1,295	5.1%	2,347	-42.0%
Total current assets	**66,991**	**66,850**	0.2%	**56,828**	17.9%
LONG-TERM INVESTMENTS	3,020	4,172	-27.6%	8,567	-64.7%
PROPERTY AND EQUIPMENT, NET	15,222	15,551	-2.1%	15,283	-0.4%
OTHER ASSETS	2,662	2,426	9.7%	2,444	8.9%
Total other assets	20,904	22,149	-5.6%	26,294	-20.5%
TOTAL ASSETS	87,895	88,999	-1.2%	83,122	5.7%
CURRENT LIABILITIES					
Notes and accounts payable	6,596	4,867	35.5%	1,746	277.8%
Income tax payable	702	611	14.9%	444	58.1%
Lease liabilities	714	827	-13.7%	727	-1.8%
Accrued expenses and other current liabilities	3,540	4,839	-26.8%	3,188	11.0%
Total current liabilities	11,552	11,144	3.7%	6,105	89.2%
OTHER LONG-TERM LIABILITIES					
Accrued pension liabilities	207	214	-3.3%	315	-34.3%
Deferred tax liabilities	651	589	10.5%	735	-11.4%
Lease liabilities	1,829	1,932	-5.3%	344	431.7%
Other liabilities	65	65	0.0%	87	-25.3%
Total long-term liabilities	2,752	2,800	-1.7%	1,481	85.8%
Total liabilities	14,304	13,944	2.6%	7,586	88.6%
SHAREHOLDERS EQUITY					
Ordinary shares	33	33	0.0%	33	0.0%
Additional paid-in capital	142,853	143,484	-0.4%	142,424	0.3%
Accumulated deficits	(54,087)	(51,773)	4.5%	(50,440)	7.2%
Accumulated other comprehensive income	4,408	4,654	-5.3%	4,844	-9.0%
Treasury stock	(19,616)	(21,343)	-8.1%	(21,325)	-8.0%
Total shareholders equity	73,591	75,055	-2.0%	75,536	-2.6%
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	87,895	88,999	-1.2%	83,122	5.7%
Cash and equivalents	$44,703	$46,389	-3.6%	$35,247	26.8%
Change in cash and equivalents	(1,686)	11,142	-115.1%	(5,940)	-71.6%
Market value	40,614,400	45,248,650	-10.2%	40,512,870	0.3%
Enterprise value	(4,123,600)	(1,175,350)	250.8%	5,231,870	-178.8%
DSO	62	57	8.8%	62	0.0%
Inventory Days	112	108	3.7%	111	0.9%

ANNUAL CASH FLOW

	2019	2018	2017	2016	2015
OPERATING ACTIVITIES					
Net loss	$ (5,039)	$ 2,088	$ (6,145)	$ (2,986)	$ (21,095)
Adjustments to reconcile net loss to net cash used in operating activities:					
Depreciation and amortization	1,780	1,641	1,667	1,682	2,446
Stock-based compensation	1,462	1,421	1,589	1,606	1,912
Loss on asset write-off	0	0	0	0	0
Inventory write-downs	1,359	1,328	642	1,527	913
Net gain recognized on LT investments	(788)	(9,916)	0	0	0
Gain on sale of long-term investments	(500)	0	(20)	(948)	(8)
Impairment loss on long-term investments	0	0	0	0	4,953
Gain on disposal of property & eqt, net	2	(6)	(137)	(1,726)	(738)
Deferred income taxes	(133)	(155)	40	(1,231)	1,989
Other, net	0	0	0	0	0
Changes in operating assets and liabilities:					
Accounts receivable, net	1,053	(2,204)	(1,979)	(2,008)	1,592
Inventories	133	(2,286)	(697)	(1,140)	(1,933)
Prepaid expenses and other current assets	981	(1,031)	(139)	(6)	191
Deferred charges	(571)	(983)	(553)	(375)	(416)
Operating lease right of use assets	(1,477)	0	0	0	0
Notes and accounts payable	285	2,122	(1,869)	996	1,202
Income tax payable	198	72	161	(2,065)	1,595
Accrued expenses and other current liabilities	661	(105)	186	(1,064)	(1,039)
Operating lease liabilities	1,494	0	0	0	0
Accrued pension liabilities	(42)	(20)	13	(4)	(11)
Other liabilities	3	(1)	3	(56)	(168)
Net cash used in operating activities	861	(8,035)	(7,238)	(7,798)	(8,615)
Acquisition of:					
Short-term investments	(34,649)	(11,197)	(8,505)	(28,797)	(7,128)
Long-term investments	0	0	0	0	0
Property and equipment	(1,672)	(1,272)	(704)	(673)	(724)
Decrease (increase) in:					
Restricted assets	0	0	0	0	0
Restricted cash	0	0	0	0	132
Other assets	6	(12)	22	40	82
Proceeds from:					
Sale of short-term investments	4,953	22,540	12,635	18,331	16,755
Sale of long-term investments	7,061	2,582	0	5,982	167
Return of capital from LT investment	0	0	1,163	17	370
Sale of real estate	2,169				
Disposal of property and equipment	1	16	145	3,837	3,205
Net cash provided by investing activities	(22,131)	12,657	4,756	(1,263)	12,859
FINANCING ACTIVITIES					
Acquisition of treasury stock	(510)	(451)	(708)	(619)	(3,233)
Proceeds from:					
Exercise of stock options	7	10	29	2	31
Issuance of ordinary shares under the ESP Plan	109	86	84	73	180
Net cash used in financing activities	(394)	(355)	(595)	(544)	(3,022)
EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE	(53)	(374)	268	(261)	(1,092)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIV.	(21,717)	3,893	(2,809)	(9,866)	130
CASH & CASH EQUIV. AT BEGINNING OF YR	32,448	28,555	31,364	41,230	41,069
CASH & CASH EQUIVALENTS AT END OF YR	10,731	32,448	28,555	31,364	41,199
Cash paid for tax	$ 1,171	$ 1,218	$ 818	$ 4,349	$ 1,068
Cash Flow	(1,857)	(3,599)	(2,364)	(2,076)	(9,628)
Free cash flow	(3,529)	(4,871)	(3,068)	(2,749)	(10,352)

HISTORICAL STOCK PRICE



Source: Zacks Investment Research

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