Zacks Small-Cap Research

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Applied DNA Sciences (APDN-OTC)

APDN: Expect to see another strong quarter of revenue for fiscal 4Q13---Outperform

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	08/21/2013
Current Price (11/29/13)	$0.11
Twelve- Month Target Price	**$0.25**

OUTLOOK

We are optimistic about the Company's unique technology and two principle anti-counterfeiting and product authentication solutions: SigNature DNA and BioMaterial Genotyping, which can be used in numerous industries. With an ever booming anti-counterfeiting business worldwide, along with its unique technology and broad range of product offering, the Company is well positioned to grow in the coming years.

APDN reported record sales in fiscal 3Q13 and we expect to see another strong quarter of revenue growth for the fiscal fourth quarter of 2013.

SUMMARY DATA

52-Week High	**$0.29**
52-Week Low	**$0.09**
One-Year Return (%)	**-40.32**
Beta	**1.33**
Average Daily Volume (sh)	**997,150**
Shares Outstanding (mil)	**744**
Market Capitalization ($mil)	**$83**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**3**
Insider Ownership (%)	**23**
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 2011 Estimate	**N/A**
P/E using 2012 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**High,**
Type of Stock	**N/A**
Industry	**Protection-Sfty**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(In millions of $)

	Q1 (Dec)	Q2 (Mar)	Q3 (Jun)	Q4 (Sep)	Year (Sep)
2011	0.32 A	0.14 A	0.23 A	0.28 A	0.97 A
2012	0.52 A	0.52 A	0.53 A	0.29 A	1.85 A
2013	0.32 A	0.34 A	0.64 A	0.70 E	2.01 E
2014					5.50 E

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

	Q1 (Dec)	Q2 (Mar)	Q3 (Jun)	Q4 (Sep)	Year (Sep)
2011	-$0.00 A	-$0.01 A	-$0.01 A	-$0.01 A	-$0.03 A
2012	-$0.00 A	-$0.00 A	-$0.00 A	-$0.00 A	-$0.01 A
2013	-$0.00 A	-$0.00 A	-$0.00 A	-$0.00 E	-$0.01 E
2014					-$0.01 E

Zacks Projected EPS Growth Rate - Next 4 Years % **N/A**

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WHAT'S NEW

- Business continues to grow since end of fiscal third quarter;
- We expect to see another strong quarter of revenue growth for fiscal 4Q13;
- APDN reported record sales in fiscal third quarter of 2013;
- Balance sheet boosted by recent financing;
- Maintain Outperform rating for APDN shares;

Business Continues to Grow Since End of Fiscal Third Quarter

In the past few months, APDN has taken more steps concerning its SigNature DNA marking and authentication platform and bolstering its plant and staff. The Company continues to make great progress in business development. Personnel have been added, and plant capacity has been increased by over 50%. We believe APDN can stand ready to respond to all industry inquiries.

Following are the major business developments in the past few months.

On Nov 14, 2013, Applied DNA Sciences issued an update concerning the 2013 Electrical and Electronics Industry Outreach Forum, sponsored by the US Defense Logistics Agency (DLA) in Columbus, Ohio on October 24, 2013.

The conference included a briefing by DLA about SigNature® DNA Marking of Microcircuits. DLA is exploring SigNature DNA marking, along with other technologies as a possible solution to mitigate counterfeits in high risk items.

Currently there is a requirement for SigNature DNA marking of all Federal Supply Class (FSC) 5962 microcircuits supplied to DLA. DLA procures 93% of electrical and electronic parts procured in support of the DOD services. These commodities are of various sizes, shapes and substrates and represent a meaningful volume of parts procured by DLA. Applied DNA is poised to support DLA in its determination to safeguard any commodities necessary to ensure readiness for the warfighter.

On Oct 15, 2013, announced it has signed a ten-year option agreement with one of the top four U.S. defense contractors (Prime) to purchase SigNature DNA® marking technology. The international aerospace and defense company currently intends to apply APDN's unique SigNature DNA mark on FSC 5962 microcircuits in support of US Defense Logistics Agency acquisition requirement.

As a global leader, this defense contractor provides key defense systems to the Defense Logistics Agency, as well as a wide variety of advanced systems to military services and other government and private sector customers.

This company is a high-tech leader and supports military services such as: Navy, Army, Air Force, and the Missile Defense Agency, as well as non-military end users such as NASA and the Department of Homeland Security.

The signing brings the number of companies using SigNature DNA marking for DLA to 23, including two primes, one original equipment manufacturer (OEM), thirteen distributors, two authorized distributors, and the five OCMs.

On Nov 13, 2013, Applied DNA Sciences announced that **Brink's**, a leading global security solutions provider, has purchased a unique SigNature® DNA mark capable of deployment by Brink's in various worldwide operations.

The first Brink's SigNature DNA application will use the unique Brink's mark to protect cash and high-value items using a security tape for loss prevention purposes. Materials and support for the application will also come from The Label Printers, a leading custom label and packaging corporation globally.

SigNature DNA marks may be used in a variety of applications such as APDN's DNA Fog product, designed to repel and identify intruders into large areas such as warehouses, as well as evidentiary marking on individual items such as jewelry, protection of ATMs, and cash transport.

Based in Richmond, Virginia, Brink's is a global leader in security-related services for banks, financial institutions, retailers, government agencies, mints, jewelers, and a variety of other commercial and governmental customers. The SigNature DNA mark is relevant to many of these Brink's businesses, such as protection of high value items in transit, antitheft applications in banks and cash depots, and protection of cargo.

On Oct 8, 2013, Applied DNA announced that in collaboration with Nissha Printing Company, headquartered in Kyoto, Japan, the company is expanding SigNature® DNA-based inkjet solutions for new customers in areas that include, food, apparel, cosmetics, pharmaceutics, electronics, automotive and security driven businesses.

Marketed as CustomerQ, Nissha uses SigNature DNA-based ink with its inkjet printing systems to help secure the fresh fish supply chain for the Ōita Fisheries Co-operative. In essence, each fish is weighed and measured at the central distribution center, and assigned its own unique product label that certifies the origin, expiration and the shipment information. The Ōita fish label is automatically linked to a central database that enables the food supplier, retailer as well as the end consumer to verify the original product information at the point of sale.

Due to the successful launch of CustomerQ DNA ink, Nissha is expanding its reach to new customers in new markets to help keep products safe from interference, and to provide fast, thorough product tracking and traceability in the event of a product recall. CustomerQ DNA ink is more advanced than conventional inkjet inks.

Record Revenue Reported for Fiscal 3Q, Strong Revenue Growth Expected for Fiscal 4Q

On Aug 13, 2013, Applied DNA Sciences (APDN) announced its financial results for the third fiscal quarter ending June 30, 2013.

For the three months ended June 30, 2013, APDN generated $644,842 in revenues from operations, an increase of $116,268, or 22%, from revenue of $528,574 for the three months ended June 30, 2012. Revenues for the three months ended June 30, 2013 were principally from the sales of authentication services. The increase in sales for the three months ended June 30, 2013 compared to the three months ended June 30, 2012 was primarily caused by the increase in DNA-marking contracts with commercial electronics manufacturers and represents the company's highest quarterly revenues to date.

Selling, general and administrative (SG&A) expenses increased from $1,752,501 for the three months ended June 30, 2012 to $3,240,815 for the three months ended June 30, 2013. The increase of $1,488,314, or 84.9%, is primarily attributable to higher professional fees specifically for legal and consulting and increased salary due to the increased headcount. The increase is also due to expenses incurred for the relocation of the company’s corporate office during the three months ended June 30, 2013. Included in SG&A for the three months ended June 30, 2013 is approximately $956,000 of non-cash charges, including $886,000 for stock based compensation expense primarily related to the vesting and modification of employee stock options and $70,000 of bad debt expense.

Research and development expenses increased from $99,958 for the three months ended June 30, 2012 to $184,981 for the three months ended June 30, 2013. The increase of $85,023 or 85.1% is attributable

to additional research and development to extend the company's patent portfolio and to capitalize on emerging market requests.

Net loss for the three months ended June 30, 2013 increased to $2,135,612 from a net loss of $1,429,645 for the three months ended June 30, 2012 due to increased SG&A and R&D expenses.

We are impressed by the strong financial performance for the fiscal third quarter of 2013. APDN reported record revenue in the company's history. This quarter, APDN signed eight contracts related to Federal Supply Class (FSC) 5962, doubling the cumulative contracts that had been signed by the previous quarter. Management anticipates this trend will continue, judging from the increasing number of inquiries and companies in various stages of negotiation.

Since the company has completed the move into new facility, SG&A expenses will stabilize going forward. APDN is positioned to deliver against high demand while continuing necessary product development without additional major expenditures.

We expect APDN to report another strong quarter for fiscal fourth quarter ending September 30, 2013 based on recent business developments. We estimate total revenue for fiscal fourth quarter ending Sept 30, 2013 will grow to $0.70 million, an increase of 141%. Net loss will be $2.5 million or $0.00 per share.

Balance sheet boosted by recent financing

On Jul 22, 2013, APDN announced that it has entered into a Securities Purchase Agreement with an institutional accredited investor, Crede CG III, Ltd. to provide $7.5 million in financing.

Crede is an existing shareholder of the Company. At the initial closing, the Company received gross proceeds of $2,000,000 in exchange for restricted common stock priced at $0.187/share.

Pursuant to the Agreement, the investor is obligated to invest an additional $5,500,000 in the Company on the date a registration statement providing for the resale of the securities issued is declared effective by the Securities and Exchange Commission. This closing will be done at $1,000 per share of preferred stock with a conversion price the lesser of market value or $0.187/share. The investor is limited to 9.9% ownership at any given point in time. The investor is in a "passive" position and will not occupy a Board position. The preferred stock is subject to conversion into common stock at the Company's option following the effectiveness of the registration statement and automatically converts after one year.

Warrants issued as a part of this financing could contribute up to an additional $9.75 million in funds to the company if exercised for cash. The Warrants also have a cashless exercise feature. Warrants would be exercised at a strike price equal to $0.2431 per share which is a 30% premium to the original purchase price of $0.187/share.

This financing comes at an excellent time. It greatly boosted balance sheet of the Company. This financing will allow APDN to continue to scale its operations and broaden its product line to meet the demand of a growing number of contracts in electronics and other verticals, continue to hire top sales, operational, and scientific talent, leverage valuable assets acquired from RedWeb Technologies, and further expand the company's market share in Europe.

As of June 30, 2013, APDN had $1.8 million in cash. With the $7.5 million new financing, the company's cash balance should be able to last into fiscal 1Q15.

APDN is at a crucial stage in the development of Applied DNA Sciences. The strong balance sheet will enhance its capacity to respond to growth opportunities.

Valuation is Attractive Now

We maintain our Outperform rating for APDN shares and reiterate our 12-month price target of $0.25 per share.

Apparently, first half of the fiscal year 2013 financials were disappointing. Revenue for the first two fiscal quarters was down 39% and 34%, respectively. But as we pointed in our previous report we believe revenue will resume growth in the second half of this fiscal year due to the focused marketing efforts management has put in place.

This was exactly the case for fiscal third quarter ended June 30, 2013. APDN reported record sales of $0.64 million for the fiscal third quarter, an increase of 22% year over year. We believe this trend will continue in fiscal fourth quarter. We estimate revenue for fiscal 2013 will cross the mark of $2.0 million.

Business continues to grow in the last few months. Balances sheet has been boosted by recent financing. All this foundation will generate positive impact on the operations of the Company in our view.

We remain optimistic about APDN's prospect. APDN's fundamentals remain strong. The Company's technology is unique and has competitive advantages over its peers. The Company is well positioned to boost its top line and bottom line in the coming years. According to our long term financial model, the Company's revenue will grow at a compound annual growth rate (CAGR) of 88% in the four fiscal years from 2013 to 2017. The Company will break even in fiscal 2016, and become profitable in fiscal 2017 with net income of $8.5 million or EPS of $0.01 per share.

APDN is a high growth company. In terms of valuation, we think the Company should trade at a P/E of 45x. We apply a P/E of 45x to our estimated EPS of $0.01 in fiscal 2017, discounted at 20% for 3 years, we get our price target of $0.25 per share. This values the company at about $183 million in market cap, which is reasonable in our view. As long as the Company can execute its growth strategy correctly, we believe value should be generated for investors.

But Cash burn is still our chief concern at this time.

Since APDN will break even in fiscal 2016 and become profitable in fiscal 2017, the Company still needs to raise funds for its operation until positive cash flow can be generated in 2017.

We remind investors that any equity or convertible note financing will dilute the Company's current shareholder base and reduce its per share value. Actually, we have noticed that the Company's shares outstanding have increased dramatically from 135 million in fiscal 2007 to current 733 million at the end of June, 2013. And we expect this trend will continue in the next few years when the Company continues to issue new shares or new convertible notes to fund its operations.

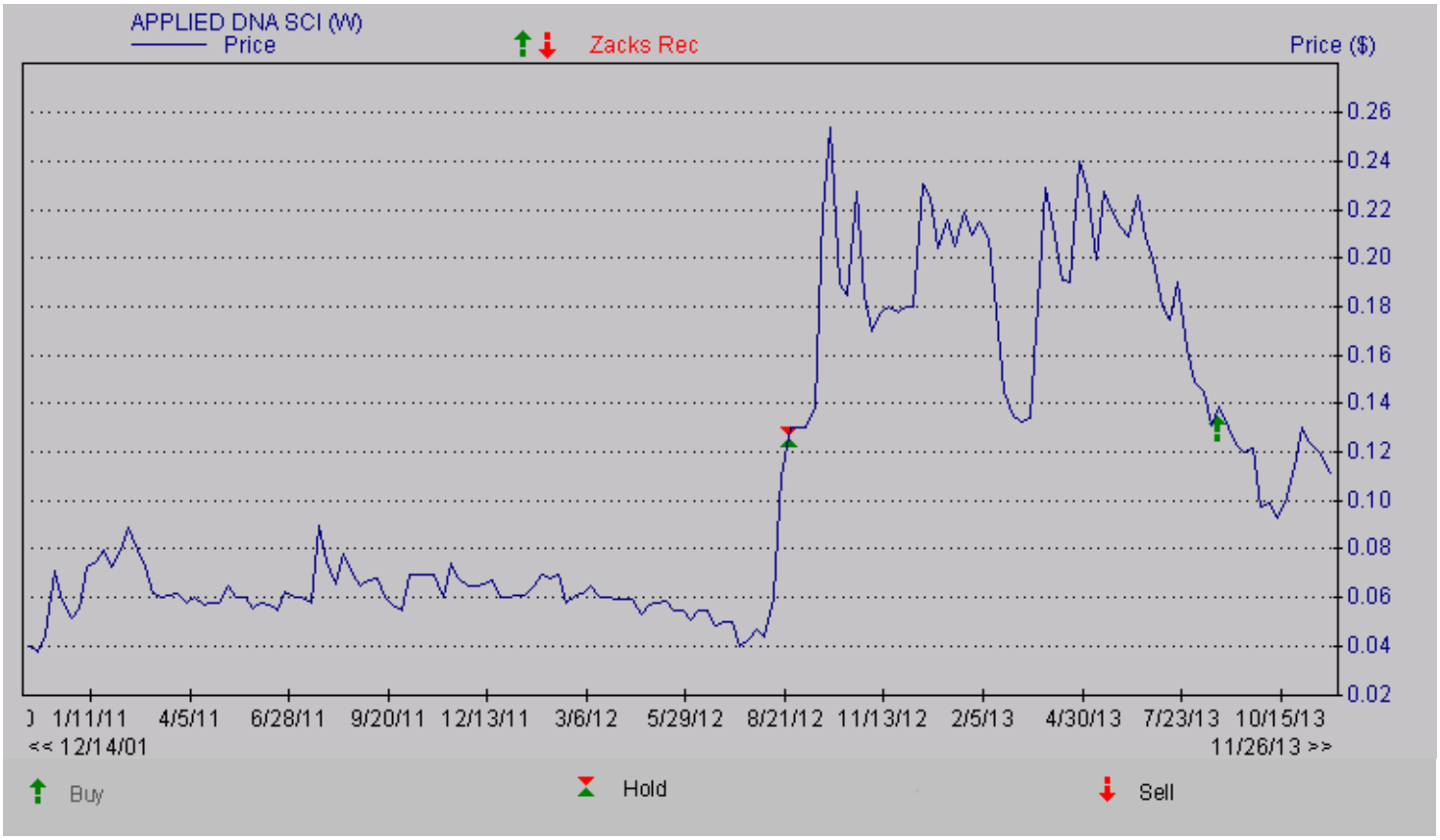
PROJECTED INCOME STATEMENT

	2012A (Sep)					2013E (SEP)					2014E (Sep)	2015E (Sep)	2016E (Sep)	2017E (Sep)
$ in million except per share data	Q1	Q2	Q3	Q4	FYA	Q1	Q2	Q3	Q4	FYE	FYE	FYE	FYE	FYE
Total Revenues	**$0.52**	**$0.52**	**$0.53**	**$0.29**	**$1.85**	**$0.32**	**$0.34**	**$0.64**	**$0.70**	**$2.01**	**$5.50**	**$12.50**	**$17.50**	**$25.00**
YOY Growth	*62.6%*	*269.1%*	*130.1%*	*3.6%*	*91.5%*	*-38.5%*	*-33.5%*	*22.0%*	*140.7%*	*8.2%*	*174.0%*	*127.3%*	*40.0%*	*42.9%*
CoGS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Gross Income	**0.52**	**0.52**	**0.53**	**0.29**	**1.85**	**0.32**	**0.34**	**0.64**	**0.70**	**2.01**	**5.50**	**12.50**	**17.50**	**25.00**
Gross Margin	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*
SG&A	$2.2	$1.8	$1.8	$1.9	$7.6	$2.5	$2.8	$3.2	$2.9	$11.4	$12.0	$12.5	$13.0	$14.0
% SG&A	*416.4%*	*352.0%*	*331.6%*	*648.6%*	*410.6%*	*793.6%*	*799.3%*	*502.6%*	*414.3%*	*568.8%*	*218.2%*	*100.0%*	*74.3%*	*56.0%*
R&D	$0.08	$0.10	$0.10	$0.16	$0.43	$0.15	$0.18	$0.18	$0.18	$0.69	$0.75	$0.90	$1.10	$1.25
% R&D	*15.2%*	*18.5%*	*18.9%*	*54.4%*	*23.3%*	*46.5%*	*51.2%*	*28.7%*	*25.7%*	*34.3%*	*13.6%*	*7.2%*	*6.3%*	*5.0%*
Other	$0.1	$0.1	$0.1	$0.0	$0.3	$0.0	$0.0	$0.1	$0.1	$0.2	$0.4	$0.3	$0.3	$0.3
% Other	*19.0%*	*19.0%*	*19.6%*	*4.6%*	*16.9%*	*6.6%*	*6.3%*	*9.7%*	*14.3%*	*10.2%*	*7.3%*	*2.4%*	*1.7%*	*1.2%*
Operating Income	**($1.8)**	**($1.5)**	**($1.4)**	**($1.8)**	**($6.5)**	**($2.4)**	**($2.6)**	**($2.8)**	**($2.5)**	**($10.3)**	**($7.7)**	**($1.2)**	**$3.1**	**$9.5**
Operating Margin	*-350.6%*	*-289.6%*	*-270.0%*	*-607.6%*	*-350.9%*	*-746.7%*	*-756.8%*	*-440.9%*	*-354.3%*	*-513.3%*	*-139.1%*	*-9.6%*	*17.7%*	*37.8%*
Other Net	($0.6)	($0.1)	($0.0)	$0.0	($0.6)	($6.3)	($0.5)	$0.7	$0.0	($6.1)	($1.0)	($1.0)	($1.0)	($1.0)
Pre-Tax Income	**($2.4)**	**($1.6)**	**($1.4)**	**($1.8)**	**($7.2)**	**($8.7)**	**($3.1)**	**($2.1)**	**($2.5)**	**($16.4)**	**($8.7)**	**($2.2)**	**$2.1**	**$8.5**
Income taxes(benefit)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Tax Rate	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*
Reported Net Income	**($2.4)**	**($1.6)**	**($1.4)**	**($1.8)**	**($7.2)**	**($8.7)**	**($3.1)**	**($2.1)**	**($2.5)**	**($16.4)**	**($8.7)**	**($2.2)**	**$2.1**	**$8.5**
YOY Growth	-	-	-	-	-	-	-	-	-	-	-	-	-	*302.38%*
Net Margin	*-466.2%*	*-301.1%*	*-270.5%*	*-601.8%*	*-385.5%*	*-2740.2%*	*-907.6%*	*-331.2%*	*-354.3%*	*-819.5%*	*-157.3%*	*-17.6%*	*12.0%*	*33.8%*
Shares Out	*490.3*	*583.6*	*594.9*	*635.5*	*576.1*	*649.9*	*680.4*	*721.1*	*733.0*	*696.1*	*800.0*	*870.0*	*940.0*	*1000.0*
Reported EPS	**($0.00)**	**($0.00)**	**($0.00)**	**($0.00)**	**($0.01)**	**($0.01)**	**($0.00)**	**($0.00)**	**($0.00)**	**($0.02)**	**($0.01)**	**($0.00)**	**$0.00**	**$0.01**
YOY Growth	-	-	-	-	-	-	-	-	-	-	-	-	-	*278.2%*
One time charge	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$6.33*	*$0.00*	*$0.00*	*$0.00*	*$6.33*	*$0.00*	*$0.00*	*$0.00*	*$0.00*
Non GAAP Net Income	**($2.4)**	**($1.6)**	**($1.4)**	**($1.8)**	**($7.2)**	**($2.4)**	**($3.1)**	**($2.1)**	**($2.5)**	**($10.1)**	**($8.7)**	**($2.2)**	**$2.1**	**$8.5**
Non GAAP EPS	**($0.00)**	**($0.00)**	**($0.00)**	**($0.00)**	**($0.01)**	**($0.00)**	**($0.00)**	**($0.00)**	**($0.00)**	**($0.01)**	**($0.01)**	**($0.00)**	**$0.00**	**$0.01**

Source: Company filing and Zacks Investment Research estimates

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