Zacks Equity Research

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XZERES Corporation (XPWR-OTCBB)

XPWR: Zacks Co. Report - OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	05/30/2011
Current Price (05/27/11)	$0.80
Six- Month Target Price	**$1.50**

OUTLOOK

XZERES is positioned to benefit from the growth of the small wind energy industry. Within three quarters, management has significantly improved the XZERES 442SR wind product, expanded into multiple sales channels in the United States and opened a European subsidiary. Sequential quarterly sales growth has exceeded 30% and is increasing. Initiatives are in place to expand into Asia and further stimulate sales in the United States. In addition, the company has acquired another growth platform: power efficiency products. We initiate coverage of XZERES with an Outperform rating and a price target of $1.50.

SUMMARY DATA

52-Week High	**$2.35**
52-Week Low	**$0.50**
One-Year Return (%)	**N/M**
Beta	**N/A**
Average Daily Volume (shrs.)	**15,427**
Shares Outstanding (million)	**18.7**
Market Capitalization ($ mil.)	**$15.0**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**N/A**
Insider Ownership (%)	**38.8**
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 2012 Estimate	**N/M**
P/E using 2013 Estimate	**N/M**
Zacks Rank	**N/A**

Risk Level	**Above Average**
Type of Stock	**Small - Growth**
Industry	**Other Alt. Energy**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (May)	Q2 (Aug)	Q3 (Nov)	Q4 (Feb)	Year (Feb)
2010	0.00 A	0.00 A	0.00 A	0.00 A	0.00 A
2011	0.00 A	0.36 A	0.47 A	0.65 A	1.48 A
2012	0.87 E	1.17 E	1.57 E	2.10 E	5.71 E
2013					15.14 E

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

	Q1 (May)	Q2 (Aug)	Q3 (Nov)	Q4 (Feb)	Year (Feb)
2010	-$0.00 A	-$0.00 A	-$0.00 A	-$0.01 A	-$0.01 A
2011	-$0.07 A	-$0.10 A	-$0.10 A	-$0.13 A	-$0.41 A
2012	-$0.07 E	-$0.06 E	-$0.06 E	-$0.05 E	-$0.23 E
2013					-$0.10 E

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

2011 quarterly EPS do 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. Recently, 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.
- We initiate coverage of XZERES with an Outperform rating and a price target of $1.50, which is based on a 5.2 price-to-sales valuation, the high-end of the expected range.

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 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.

[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).

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.

Sequential quarterly sales growth for the first three quarters of operations has been impressive. The company's initial selling efforts began during the 2011 fiscal year, near the end of first fiscal quarter ending May 31, 2010 and resulted in $361,484 in completed sales during the second quarter, which ended August 31, 2010. Strong 30.4% sequential quarterly sales growth followed in the third fiscal quarter ending November 30, 2010. Due to continued marketing efforts and the implementation of the Buy Direct program, among others, sequential quarterly sales increased 38.2% in the fourth fiscal quarter. The gross margin sequentially increased 292 basis points to 28.1% in the fourth fiscal quarter.

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 exponential sales growth and achieve profitability. Due to the many initiatives recently implemented and also planned for fiscal 2012, **we expect that the company's sequential sales growth rate will continue to be at least 34% during fiscal 2012**.

WIND POWER DIVISION - PRODUCTS

XZERES manufactures small wind turbine systems, towers and various wind power system components. The wind turbine systems are available in power ratings of 2.5 kW (**XZERES 110**) and 10 kW (**XZERES 442SR**). Both are also obtainable in marine versions for coastal applications. The wind turbines are manufactured with both internally engineered and standard third party components, which are integrated into proprietary systems. XZERES wind systems have been designed for performance, reliability and value with the minimal amount of moving parts in order to reduce maintenance costs.

XZERES wind turbines are tower mounted and usually generate electricity for use on-site, but can also be connected to the main electrical grid so that the excess generated power can be fed back into the grid for credit from the local utility provider. XZERES also provides a web-based assessment tool, **WindRx**™, which calculates the total cost of energy, including estimated installation costs, annual maintenance costs federal tax credit and state rebates.

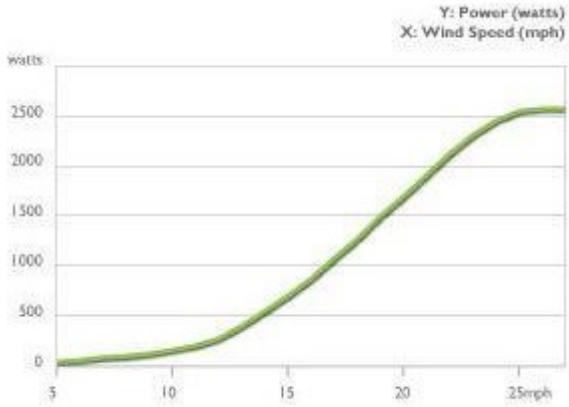
The **XZERES 110** is a 2.5 kW, three-bladed, horizontal-axis upwind small wind turbine with a swept area of 110 square feet. The large swept area relative to the capacity rating enables the generation of more energy at lower wind speeds. The unit is estimated to generate 419 kWh[4] per month at an average wind

[4] A kilowatt-hour is a measure of energy equal to the use of one kilowatt in one hour.

speed of 12 mph. The power curve of the XZERES 110 (below) shows the wind turbine's power output across a range of wind speeds. This measure of performance of a wind turbine system facilitates the comparison of different wind systems, and through extrapolation enables the projection of annual expected energy production of competing machines for comparative purposes.



XZERES 110



XZERES 110 Power Curve

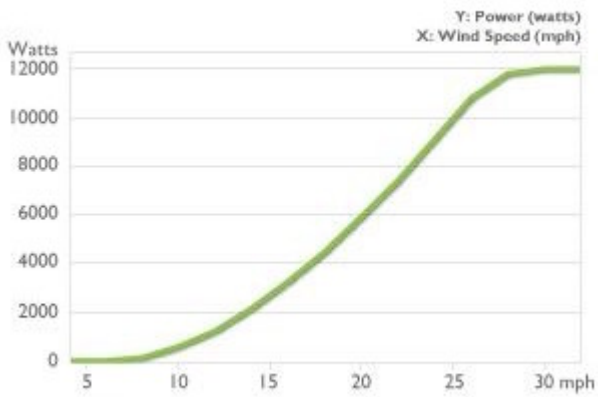
The **XZERES 442SR** is a 10 kW, three-bladed, horizontal-axis upwind small wind turbine with a swept area of 442 square feet. As with the XZERES 110, the large swept area relative to the capacity rating enables the generation of more energy at lower wind speeds, with the XZERES 442SR estimated to generate 1,524 kWh per month at an average wind speed of 12 mph.

The XZERES 442 has been independently tested by the National Renewable Energy Laboratory (NREL), a national laboratory of the U.S. Department of Energy, Office of Energy Efficiency and Renewable Energy, operated by the Alliance for Sustainable Energy, LLC. The NREL was established to reduce the barriers to expansion in the implementation of wind energy by providing independent testing results for small wind turbines.

The XZERES 442 (aka ARE 442) was tested in Colorado for 10 months between July 2008 and April 2009, inclusive. Five tests were performed: 1) acoustic noise emissions according to IEC Standard 61400-11, 2) duration testing to investigate structural according to IEC Standard 61400-2, 3) power performance to produce a graph for power versus wind speed according to IEC Standard 61400-12-1, 4) power quality for 3-phase grid-connected turbines, and 5) safety and function to verify that the turbine exhibits the designed behavior claimed by the manufacturer. The NREL has tested five commercially available small wind turbine systems (Small Wind Turbine Testing Results from the National Renewable Energy Laboratory, April 2010), of which two are 10-to-11 kW systems: the XZERES 442 and VT-10. Of the two, the XZERES 442 was the most efficient at all wind speeds, but especially at lower wind speeds, when significantly more energy was generated at low RPMs.



XZERES 442SR



XZERES 442SR Power Curve

Subsequent to the test, XZERES released its improved next generation 10-kilowatt system, the **XZERES 442SR**, whose monthly output is estimated to be 1,583 kWh at an average wind speed of 12 mph. The new model's turbine efficiency was enhanced with a new tail design and improved aerodynamic cowling for better cooling, which increases annual energy output up to 20%. In addition, a web-enabled and Wi-Fi accessible controller enables the wind system's performance and diagnostic information to be delivered wirelessly in real-time to a home computer or handheld device. Besides reporting wind speed and energy production via a graphic user interface, the monitoring system also notifies owners when maintenance is required. As a result, the XZERES 442SR is more durable and reliable than its predecessor, thereby reducing future service and maintenance costs. The XZERES 442SR began shipping in March 2011 and the XZERES 442 system was discontinued.

The XZERES 110 and XZERES 442SR are versatile wind turbine systems that can be used in a broad range of applications and functions. The wind systems can generate remote energy for residential homes, small commercial facilities, agricultural farms, communities, churches, schools and small businesses. Xzeres is also targeting specialty applications, such as island electrification, telecommunication sites, dairy farms, cattle ranches, wineries, municipal buildings, remote energy supply solutions, micro-grid-based rural electrification and critical uninterrupted power systems for critical essential services like water purification, refrigeration and communications.

XZERES is designing and developing improved and larger turbine systems so that company will be able to offer a broader product line of small wind systems. Management believes that the company can leverage existing designs for new systems in the 5 kW to 25 kW range as well as higher power systems up to 100 kW. The power ratings for the new turbines have not been disclosed by management for competitive reasons.

The marine systems (XZERES 110M and XZERES 442SR-M) are constructed with components designed to withstand high salinity and high humidity conditions present at marine, estuary and coastal environments. The surfaces are protected by marine-grade coatings, the fasteners are marine-grade and the electrical enclosures are sealed against moisture.

The company's small wind turbine systems are composed of both company and third-party products. XZERES markets and sells a system. The turbine sub-system (which converts wind energy into electricity) and the controller (which controls the turbine subsystem through monitoring hardware and software) are designed by XZERES and are contract manufactured. The inverters, lightning protection equipment, electronics enclosure boxes and towers are commercially available products, which are acquired from other companies and integrated into XZERES wind power systems. An inverter is based on the ground and converts the variable frequency voltage from wind generators into grid conforming AC

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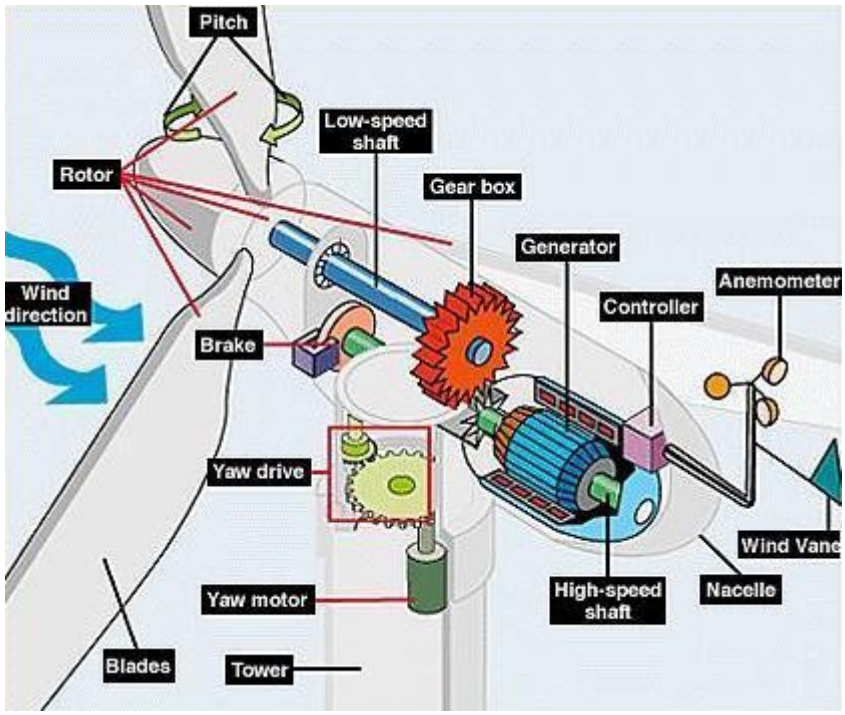
voltage. The inverter also provides the connection to the customer's electrical load, the electricity grid network or to a battery storage system.

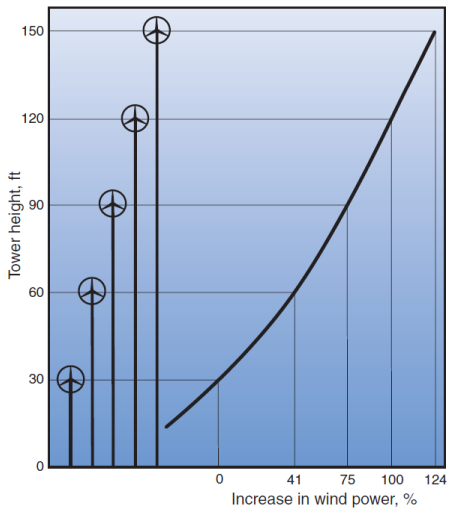


Components of a Wind Turbine Assembly

XZERES provides a wide range of tower designs and sizes to suit the particular requirements of each specific wind turbine site. Generally, the towers are between 45 feet to 140 feet tall, and depending on the specific site characteristics and customer preferences, monopole, self-supporting lattice and motorized tilt-up towers are offered. Frequently, monopole towers are the first choice, usually because of the small footprint and ease of installation. Self-supporting lattice towers are tapered, three-legged structures, which are the preferred choice when height is required, but guy wires are unacceptable. XZERES also provides 45 foot and 60 foot monopole towers with a mechanical tilt-up design, which permits the ability to raise and lower the tower when desired, for example in expectation of severe weather. The tilt-up towers are operated by either a small motor or a hand crank. Foundation engineering services are included with the installation of towers. All towers sold by XZERES come with a standard five-year warranty.



Tower Types



Wind Speeds Increase with Height (DOE)

XZERES can provide unique configurations and accessories for the towers, such as grounding kits, working platforms, stub tower extensions and lightning protection systems. Climbable towers come with safety climb systems and fall arrestors. A tower may also be customized to include a service crane that is permanently mounted on the tower, which can be used to lower the turbine to the ground and raise it back to the top of the tower. To protect the electrical components against voltage spikes and excessive transient voltages associated with lightening strikes, XZERES offers a lightning protection system that includes varistors[5] at the top and base of the tower, along with one at the service entrance, in addition to an arrestor at the AC panel to protect from voltage surges coming from the utility grid or the home wiring system. XZERES includes a five-year warranty against damage from lightning strikes on all electrical components with its lightning protection system.

SALES AND DISTRIBUTION MODELS

Initially utilizing the traditional dealer network sales model for wind power systems, XZERES expanded into consumer-direct channel in November 2010 with the introduction of its **Buy Direct** program, along with customer support tools, such as the web-based WindRx™ assessment software platform and the availability of financing. Also, XZERES created an innovative, non-typical business initiative, the Micro-Generation Utility model as a cost-effective energy solution that incentivizes customers and provides the company with a recurring revenue stream. In addition, XZERES uses national distributors of electrical equipment to supply its wind systems to dealers and consumers from warehouse locations.

Dealers have played an important part in the expansion of small wind power systems. Usually dealers have been the point men in the sales cycle, educating and advising the consumer, inspecting the proposed site to determine the optimal tower and its location, explaining the financial benefits of small wind systems and then closing the sales. During the installation phase, dealers help with the state and/or local permitting process, aid in necessary permits required by the utility company, contract for the preparation of the site and oversee the assembly and setting up of the system. After the installation, dealers train and support the consumer, along with providing on-going customer service, especially maintenance. In essence, dealers try to provide a turnkey experience for the consumer. XZERES wind systems are available from 50 dealers.

However, the traditional dealer sales model generates costs and reduces profitability for the manufacturer. Many dealers, especially small dealers with less than 5 employees, require immense support from XZERES in order to perform their responsibilities to the consumers. The company provides training programs and workshops for site assessment, system installation, operation and maintenance. The sales and marketing effort at XZERES mentors, supports and educates dealers. As a result, XZERES developed the expertise and infrastructure necessary to offer turnkey wind power systems directly to the end-user.

Therefore, in November 2010, XZERES introduced a **Buy Direct program** for its small wind power systems. This direct-to-consumer sales model, an adjunct to the dealer network, expands the company's customer reach and brand awareness, in addition to providing an important source of information and assistance for consumers in making purchasing decisions. XZERES provides customer support from site assessment analysis, through financing and permitting, and during the full installation process. Afterwards, XZERES offers technical services for ongoing maintenance. The company has experienced professionals that can support every stage of the project. In addition, XZERES operates installation and service contractor network, which can provide the proper the installation of wind systems and maintenance and repair services. Not only does the Buy Direct program enhance the company's

[5] Also known as Voltage Dependent Resistors, varistors shunt high voltage current away from sensitive electrical components.

profitability, but also XZERES can better control the sales cycle. Additionally, XZERES takes ownership of the customer relationship.

The first step in the sales cycle is a prospecting report that assesses a particular site for the potential installation of a small wind system and assists potential customers in making an informed purchasing decision. XZERES has trademarked a web-based assessment tool, **WindRx**™, which creates a comprehensive evaluation of a location's wind resources to determine monthly and annual energy production. Based on the customer-inputted location and average monthly power usage data, WindRx™ generates a detailed financial business review drawing on the site's average annual wind speed. The report summary itemizes every cost: system, installation, shipping and annual maintenance. Out-of-pocket costs for the system, installation, maintenance and finance fees are projected in a year-by-year table, incorporating expected government tax incentives (both federal and state) and probable energy savings[6] based on estimated electricity production. The anticipated net present value, internal rate of return and payback time are also presented. The web-based assessment platform gives interested end-users the ability to self-qualify themselves for an XZERES small wind power system. WindRx™ was launched for England, Scotland and Wales in November 2010 and for the United States in January 2011.

To further facilitate the sales process, XZERES offers the **option to finance the installation** of an XZERES small wind turbine system. Beginning in November 2010, the company made available the ability to obtain up to 100% financing. Specific programs target particular customers with customized financing solutions: XZERES American Agriculture Finance Program for agricultural farms, XZERES Building a Sustainable America Program for small businesses and residential locations and XZERES Finance Education & Municipal for public facilities and schools. Through various lending partners, customers can reduce or possibly eliminate up-front out-of-pocket costs when installing a distributed small wind energy system. The ability to receive financing facilitates the purchase decision and expands the potential market for XZERES.

XZERES supports its multiple sales channels with three categories of sales professionals: salaried sales representatives, brokers and independent contractors, the latter acting as company agents. Each group targets a specific channel and delivers support from a system's details that are needed to make an informed decision to professionally formatted presentations with financial and production reports. In addition, the XZERES sales team (12 employees as of May 2011) provides information and solutions to help dealers close specific sales opportunities. For example, XZERES provides step-by-step assistance for navigating local zoning and permitting ordinances. The sales professionals have experience from installations in nearly every state and can help guide customers through the permitting process.

In November 2010, XZERES launched its **Micro-Generation Utility model**, which appears to be the first Purchase Power Agreement (PPA) in the small wind industry. XZERES installs and operates between one and 50 wind turbines at the customer's site, depending upon site characteristics. XZERES then sells the wind-generated electric power to the customer at a rate below the local utility rates via a PPA. XZERES benefits from a high margin, recurring revenue stream while the customer benefits from low-cost wind energy without the upfront costs associated with system purchase. At the end of the contract term (20 years), the customer owns the wind power systems for the remaining useful life. Within a month, the company signed three separate contracts: two with dairy farms in Oregon and one with a construction consulting firm in California. A total of 14 XZERES 442 small wind power systems will be installed and provide a significant portion of each customer's energy needs. Through lending partners, XZERES provided a progressive financing option. The total combined dollar value of the three separate contracts was approximately $1.1 million.

In the traditional warehouse distribution model, XZERES continues to foster relationships with established distributors of electrical supplies and components. In March 2011, **two national distributors** began offering the company's products to their customers, broadening the distribution footprint of

[6] WindRx assumes annual maintenance costs of 0.5% of the total system cost, a 30% federal tax credit and a 25% state rebate, if applicable. The analysis also assumes energy usage is equal to energy output.

XZERES wind turbine systems. The distributors represent nearly 900 locations combined and over $20 billion in annual sales.

During fiscal 2012, XZERES will begin to pursue the U.S federal government market, including civil agencies and military contracts. Though the sales cycle tends to be longer, the ultimate purchase order are usually for multiple units. Given the longer lead time, management does not expect sales from the federal government market to be realized until the fourth fiscal quarter of 2012.

XZERES utilizes multiple sales channels: direct-to-consumer along with traditional dealer and distributor channels. Through the company's websites with online user tools, such as the WindRx™ site assessment platform, XZERES is benefiting from the consumer-direct channel, having introduced its Buy Direct program recently in November 2010. By augmenting the consumer-direct channel with the availability of financing through lending partners and the Micro-Generation Utility model, XZERES is stimulating sales through innovative marketing initiatives. In fiscal 2011, 18.3% of revenues were generated through the direct channel and 81.7% from indirect channels; however, the direct channel is expected to become prominent. With the Buy Direct program having been introduced in November 2010, the proportion of sales derived from the direct channel dramatically increased to 32.8% of revenues in the fourth fiscal quarter.

COMPETITION

XZERES competes with a number of established and start-up manufacturers, importers and distributors of small wind turbine systems in the 2.5 kW to 12 kW power range. The company primarily competes with Bergey WindPower, Southwest Windpower, Proven Energy, Ltd, Gaia-Wind, Endurance Wind Power, Ventera Energy and evancewind, among others.

Bergey WindPower offers the BWC Excel (10 kW), which is manufactured in Oklahoma. The Excel is offered in three versions: Excel-S for grid applications, Excel-R for battery charging and Excel-PD for pumping applications. Bergey also offers the XL.1 (1 kW), which is mass-produced in China. Bergey sells through a network of dealers/installers and directly to consumers.

Southwest Windpower produces small wind turbine systems under the Whisper, Skystream, AIR Breeze and AIR X brands, all rated at or below 3 kW. Its high-end Whisper 500 is rated 3 kW and is manufactured in the U.S. The Skystream 3.7 (2.4 kW) wind turbine began shipping in early 2009 and is the improved version of early prototype Skystream 1.8 kW, which was independently tested by the National Renewable Energy Laboratory (NREL) in 2004. Southwest Windpower sells through dealers and renewable energy distributors, such as Conergy and GroSolar. XZERES' CEO, Frank Greco, is the former CEO of Southwest Windpower.

Based in Scotland, **Proven Energy**, Ltd. installed its first wind turbine in 1982. The company offers three small wind products: Proven 7 (2.5 kW), Proven 11 (5.2 kW) and Proven 35-2 (12.1 kW - MCS certified[7]). Proven Energy is in the process of restructuring its distributor distribution model in North America to a dealer model. In addition, Proven Energy will open a North America headquarters facility in Chicago.

Headquartered in Glasgow, **Gaia-Wind** turbines utilize a Danish two-blade, oversized rotor design, which allows the Gaia-Wind 133 (11 kW) turbine to capture more wind energy at low-to-moderate wind speeds (10 – 12 mph). The company has a strong presence in the UK and appears to be targeting the California

[7] MCS (Microgeneration Certification Scheme) certification by the UK Government's Department for Energy and Climate Change qualifies wind turbines for feed-in tariffs in England, Scotland and Wales. The evaluation of wind systems during the MCS certification process requires the system to pass a power performance test, a safety and function evaluation, an acoustic performance test, a durability test, a manufacturing audit of factory process control and a technical file audit to ensure adherence to the requirements of IEC61400-2. MCS certification was designed to provide protection for consumers.

and New York State markets in the US. Gaia-Wind has an installed base of over 300 wind turbines and was independently tested and certified by the NREL in 2008.

Located in West Yorkshire**, Evoco Energy** produces the Evoco 10 kW wind turbine, which MCS certified and SWCC certified[8]. Evoco turbines are designed to operate at relatively low rotation speeds for low wind speed locations (7 – 10 mph). Evoco uses a reseller model, but will sell directly to key large scale corporate clients. Evoco Energy has an installed base of 50 wind turbines.

Endurance Wind Power offers the S-250 (5 kW), S-343 (5.2 kW), G3120 (35 kW) and E3120 (50 kW) wind turbines. Endurance Wind Power was formed in 2007 by **Windward Engineering** and offers its products through a network of regional dealers and a few distributors.

Based in Duluth, MN, **Ventera Energy** manufactures the Ventera VT10 (10 kW) wind turbine. Despite claiming the use of advanced, airfoil-shaped blades, the power curve of the XZERES 442SR is superior to the VT-10's at moderate wind speeds (10-25 mph). The Ventera VT10 was tested by the NREL in 2010.

The Evance R9000 (5.3 kW) is produced by **evancewind**, which is based in Leicestershire, UK. The Evance R9000 was MCS certified in July 2010, and over 500 have been installed, primarily in the UK. Evance wind turbines are sold through a network of resellers.

As XZERES broadens its product offerings by developing small wind turbines with power ratings at 50 kW and above, the company will begin to compete with Seaforth Energy's AOC 15/50 (50 kW), Entegrity Wind's EW50 (50 kW) and Northern Power's NorthWind 100 (100 kW). In 2009 (the latest statistics available[9]), the top five small wind manufacturers were (in order) Southwest Windpower, Northern Power Systems, Proven Energy, Wind Energy Solutions and Bergey WindPower.

Power curves, which plot the watts generated by a wind turbine system over a range of wind speeds, are publicly available for all the small wind turbines listed above. Using the published data, the power curves of XZERES wind systems can be plotted along side the power curves of competitors. At a given wind speed, XZERES 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 the XZERES system has a superior return on investment based on the company's metric of modified internal rate of return.

THE WIND POWER INDUSTRY

Winds are caused by the rotation of the earth and the uneven heating of the atmosphere by the sun (which leads differences in air temperatures and varying zones of air pressure). Irregularities of the earth's surface, including the earth's terrain, bodies of water and vegetation, modify wind flow patterns. Many contend that wind is a form of solar energy.

Wind power is the conversion of wind energy into mechanical power and/or electricity. The kinetic energy of wind can be captured by the blades of wind turbines and used to operate mechanical devices, such as water pumps, or to power generators, which convert the mechanical power into electricity. Usually wind generators are practical in areas of at least Class 2 wind[10], where the average wind speed in the range of

[8] The Small Wind Certification Council (SWCC) is an independent certification body that certifies small wind turbines. See the Small Wind Power Industry section below for further information.

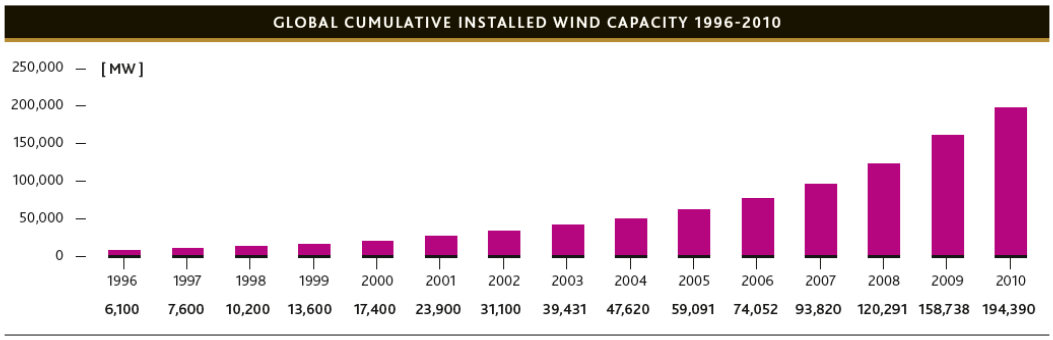
[9] AWEA Small Wind Turbine Global Market Study.

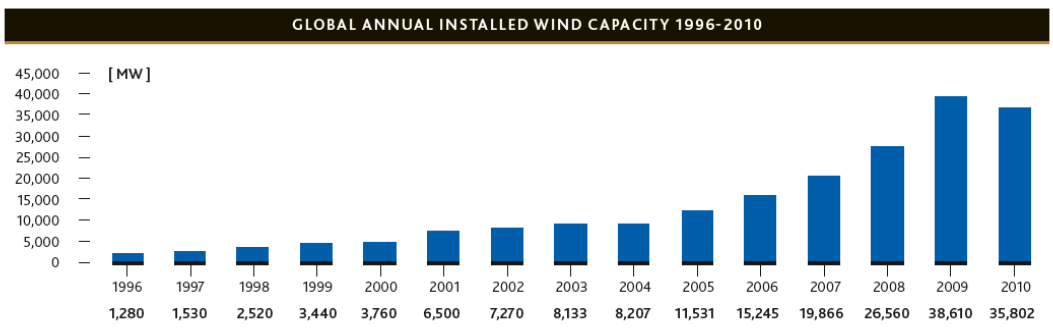
[10] Wind power is divided into 7 classes, with 1 being the lowest and 7 being the highest.

9.8 to 11.5 mph. A location with a near constant flow of non-turbulent wind would be ideal. Generally, the wind blows faster and steadier as the altitude increases since the drag caused by the earth's surface and obstacles, such as trees or buildings, is reduced. Wind energy is plentiful, renewable and clean. If used to replace fossil-fuel-derived electricity, wind power reduces toxic atmospheric and greenhouse gas emissions.

Wind power is a rapidly growing method of generating electricity, primarily due to governmental incentives and the rising cost of energy, both of which contribute to a reduced effective cost of electricity and a significantly reduced payback period for investments into wind turbines. The federal and state incentives take the form of significant tax breaks and/or cash incentives to purchasers of wind power systems. Many customers are attracted to renewable energy for environmental reasons, but the ultimate decision often depends on a cost/benefit study and investment return analysis. **Currently, governmental incentives are a key factor in lowering the effective cost of wind power systems.**

Global wind power capacity reached 194,390 megawatts (MW) by the end of 2010, up 22.5% from the previous year (see figure below) with the addition of 35,802 MW through new wind installations during the year according to the Global Wind Energy Council[11]. At the end of 2010, the United States was capable of producing 40,180 MW of electricity through wind systems, accounting for approximately 1.5% of domestic energy demand. However, during 2010, China's capacity rose 63.9% to 42,287 MW, overtaking the U.S. as the world leader in wind power capacity. Wind capacity in the European Union rose 12.2%. Germany[12] and Spain led Europe in new installations, now ranking third and fourth worldwide in total wind capacity with 27,214 MW and 20,676 MW, respectively. Wind power generates the equivalent of 9.0% of Germany's electricity consumption and 13% of Spain's electricity needs. **The World Wind Energy Association[13] expects that 600 GW of capacity may be installed worldwide by 2015, implying a compound annual growth rate (CAGR) of 25.3%.**





Courtesy of Global Wind Energy Council (GWEC)

[11] Global Wind Statistics 2010: Global Wind Energy Council GWEC), February 2, 2011.

[12] Germany provides an onshore feed-in tariff of 9.02 euro cents per kWh and 13 euro cents per kWh for offshore production.

[13] The World Wind Energy Association (WWEA) issued its World Wind Energy Report 2010 in 2011, confirming the rankings of capacity and capacity additions of the Global Wind Energy Council.

The National Renewable Energy Laboratory (NREL), a national laboratory of the U.S. Department of Energy (DOE) also conducts an annual survey of the domestic wind turbine market. The annual report, Wind Power Today, is generally is issued in May for the prior year. Therefore, the report for 2010 has not yet been issued.

Most of the wind industry's capacity wind Industry is based on large, utility-scale wind turbines, each of which has a rated power capacity 1.0 MW or more. The major companies in the large wind turbine industry are GE (GE: NYSE), Vestas (VWS: Copenhagen), Siemens (SI: NYSE) and Mitsubishi Heavy Industries (7011: TYO)[14]. Mid-size wind turbines have capacity ratings from 100 kW up to 1 MW.

THE SMALL WIND POWER INDUSTRY

The small wind turbine industry, in which XZERES competes, **is composed of manufacturers of wind turbines with power capacity ratings below 100 kW.** Small wind turbines are considered a "distributed" wind source of power by which homes, farms, businesses and public facilities generate electricity to offset a portion of or all on-site energy consumption. The small wind industry benefits from many of the same high-growth factors driving the large and mid-size turbine industries, including high energy costs, governmental incentive programs and technological advancements in turbine, blade and system design, along with changing attitudes toward alternative energy solutions.

The **American Wind Energy Association** (**AWEA**), an independent organization, conducts an **annual survey of the domestic small wind turbine market** and analyzes the sales of wind turbines rated below 100 kW. The report generally is issued in April or May for the prior year. The last report was issued on April 15, 2010 for the 2009 year. In 2009, despite a weak domestic economy with GDP declining 2.6%, 9,800 new small wind turbine systems were installed in the U.S. generating $82.4 million in sales. Installed capacity increased 15% or 20.3 MW, bringing cumulative installed small wind capacity to 100 MW. In 2008, small wind turbine sales increased 78% to $77 million with capacity increasing 30% or 17.3 MW. We expect **the small wind turbine industry to experience 20%+ sales growth over the next five years.**

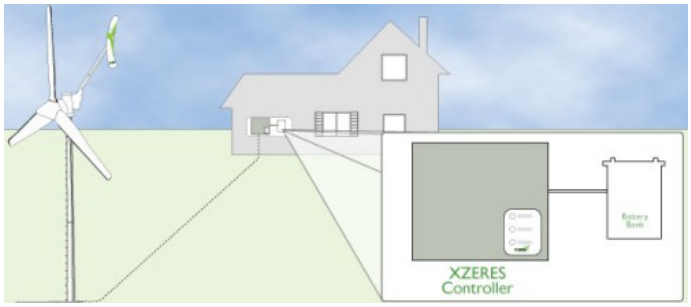
The **Small Wind Test Project** (**SWTP**) was launched in 2007 by The National Renewable Energy Laboratory and the U.S. Department of Energy in order to provide an independent assessment of small wind turbines. Initially, four commercially-available turbines were tested and certified to certain standards of power performance, power quality, acoustics, safety and function, namely the XZERES 442, Entegrity EW50, Gaia 11 kW and Ventera VT10. Currently, the Cascade SWIFT, Viryd 8000 and TALCO Proven are being evaluated.

The **Small Wind Certification Council** (**SWCC**), also an independent certification organization, evaluates and certifies small wind turbines which meet or exceed the requirements of the AWEA Small Wind Turbine Performance and Safety Standard. The SWCC will issue clear, self-explanatory labels for Rated Annual Energy Output, Rated Power and Rated Sound Level. Ultimately, the SWCC web site will include Power Curves, Annual Energy Performance Curves and measured sound pressure levels for all certified turbines. In February 2010, the SWCC began accepting certification applications and as of May 2011 received 25 applications, of which only three have received conditional temporary certification. **The SWCC certification is expected to become the North American standard for reporting small wind turbine performance.**

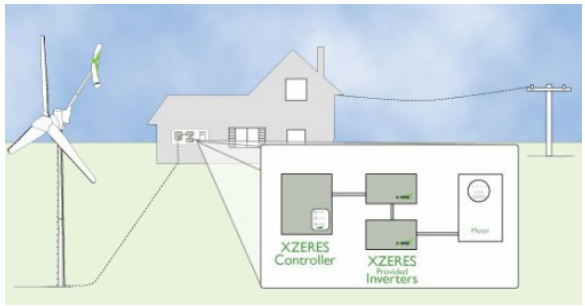
[14] Domestic market share by capacity in 2009 was GE 40%, Vestas 15%, Siemens 12%, Mitsubishi 8%, Suzlon 7%, Clipper 6%, Gamesa 6%, REpower 3%, Acciona 2% and Nordex 1%.

The small wind industry benefits from a variety of market drivers: governmental incentives (ITC and FiT), governmental programs (net-metering and RPS), the rising cost of energy and improved wind system performance through technological advancements. Ultimately, the decision to purchase and install a small wind system is financially-motivated, usually based on cash flow or the payback period. Due to better governmental incentives and creative structures, such as the Micro-Generation Utility model, the installation of a small wind turbine system is becoming more attractive alternative to utility-generated electrical power. Payback times have been reduced dramatically from over 15 years to as low as six years. Under the Micro-Generation Utility model, wind-generated energy can be less expensive than utility energy.

XZERES focuses on small wind energy systems where the generated electricity is generally used on-site (off-grid), but also provides on-grid systems which are connected to the main electrical grid so that any excess generated power can be fed back into the grid for credit from the local utility provider. In addition, the company's wind systems can be configured to link to a battery system, which stores the surplus electrical power generated by the wind turbine system. Then, the stored power is drawn upon by the customer when needed. Sometimes small wind turbines are part of hybrid systems, where wind systems are used in connection with diesel generators, batteries and/or solar photovoltaic systems. Typically hybrid systems are in remote locations where a connection to the utility grid is not available. The Energy Information Administration estimates there are 200,000 off-grid homes in the U.S.



Off-grid



On-grid

In the United States, many customers take advantage of **net-metering** rules to sell power back to the electrical grid of local utility companies. The Energy Policy Act of 2005 (Sec. 1251) requires all public electric utilities to make net metering available to their customers The surplus power produced from renewable energy systems (wind, solar power, home fuel cells, etc.) may be fed back into the network, with the system owners receiving credit for the electricity they generate. Smart electric meters record electric current in both directions, facilitating a method of effectively banking excess micro-generation for future credit. The compensation rate varies by state, usually being credited at the retail rate though other schemes exist. There are 47 states, including the District of Columbia, that have net metering plans.

Feed-in tariffs[15] (FiT) are above-market payments for electricity generated from renewable energy systems. Though common in Europe, only four states[16] in the U.S. have adopted feed-in tariffs, and not all four have fully implemented the legislation. In order to encourage the adoption of renewable energy production, the governments of states or cities provide this incentive to accelerate the construction of renewable energy systems, especially where the cost of environment-friendly power exceeds retail electric rates. Under a feed-in tariff, eligible renewable electricity generators receive a premium price for the electricity produced. The tariff rate may be different for each renewable energy technology (solar thermal, solar photovoltaics, landfill gas, wind, biomass, geothermal electric, municipal solid waste, anaerobic digestion, small hydroelectric, tidal energy, wave energy, ocean thermal, biodiesel, etc.),

[15] Feed-in tariffs are called production incentives in Washington State.

[16] California, Hawaii, Vermont and Washington.

depending on the cost of resource development so that investors can obtain a reasonable return on renewable energy investments.

In the United States, an uncapped 30% **investment tax credit** (ITC) is now available for new small wind equipment purchases and installations by the federal government. Through the Emergency Economic Stabilization Act of 2008, the 30% solar investment tax credit was expanded from applying only to commercial systems to encompassing home, farm and small business installations. The ITC was also extended through December 31, 2016. For small wind systems with a rated capacity of 100 kilowatts or less, the credit was limited by the project cost or the kilowatts of rated capacity, specifically $4,000 or $1,000 per kW of capacity (whichever was less). Though most incentives granted by the American Recovery and Reinvestment Act of 2009 (aka the Recovery Act) are geared toward utility-scale wind turbine installations[17], a few are germane to the small wind industry. Most importantly, the value of the credit for small wind systems is now uncapped due to the Recovery Act. The Database of State Incentives for Renewables & Efficiency (DSIRE) web site[18] is a comprehensive information resource on domestic renewable energy initiatives and incentives offered by federal, state and local governments and several utilities.

State governments also provide incentives to promote the use of alternative energy. States with RPS (**Renewable Portfolio Standard**) policies continue to have a significant impact on the development of wind power. An RPS requires utilities to generate or purchase a minimum percentage of energy from renewable energy sources. Over time, the percentage is only expected to increase. An RPS encourages the installation of all types of renewable energy systems, including small wind. Between 1999 and 2009, 61% of domestic wind power capacity was constructed in the 29 states with RPS policies. A federal RPS would have a major positive impact. In addition, many states have other specific incentives for the installation of wind systems.

For public sector small wind installations, the Energy Policy Act of 2005 authorized **interest-free debt** for eligible renewable projects. Specifically, the Act created the Clean Renewable Energy Bond (CREB) program whereby renewable energy projects can be funded by CREBs that are issued with a 0% interest rate. The borrower pays back only the principal of the bonds, while the bondholder receives federal tax credits in lieu of the traditional bond interest. A total of $1.2 billion Clean Renewable Energy Bonds were issued under the Act, followed by an additional $2.4 billion authorized by the Extension Act of 2008 ($800 million) and the Recovery Act of 2009 ($1.6 billion). Of the $2.4 billion awarded, over $450 million was allocated to wind power projects.

The Department of Agriculture (USDA) offers financial assistance in the form of **grants and loan guarantees for wind power projects located in rural areas**. The Farm Security and Rural Investment Act of 2002 established The Renewable Energy Systems and Energy Efficiency Improvements Program (Section 9006 of Title IX), which provided grants and loan guarantees to farmers, ranchers and rural small businesses for purchasing renewable energy systems and making energy efficiency improvements. The Food, Conservation, and Energy Act converted the Section 9006 program into the Rural Energy for America Program (REAP), which is almost identical to the Section 9006 program. Grants are limited to $500,000 or 25% of the project's cost (whichever is less) while loan guarantees may not exceed $25 million. Though only a portion was allocated to wind projects, the USDA awarded more than $60 million through the REAP program in 2009.

Local regulations govern the installation of small wind systems. The applicable local government regulates the permitting process, which involves a site evaluation to assure compliance to local

[17] The Recovery Act of 2009 extended the Production Tax Credit (PTC) for wind energy facilities placed in service by December 31, 2012, implemented the Section 1603 Treasury Grant Program (option to elect a 30% cash grant for projects where construction began before December 31, 2010); expanded the Title IV federal loan guarantee program for innovative clean energy technologies (Section 1703) and commercially proven technologies (Section 1705); and created 30% tax credit (Section 48C) new clean energy manufacturing facilities commission by February 2013.

[18] dsireusa.org

regulations. Tower height, aesthetic concerns and other restrictions are required to be complied with prior to the issuance of a permit. The American Wind Energy Association (AWEA) offers a Model Zoning Ordinance, but local officials may need to be educated regarding small wind turbines, and local ordinances may need to be updated to cover small wind installations.

INTERNATIONAL MARKETS CURRENTLY TARGETED BY XZERES

XZERES entered the European wind market in early 2011. In January, XZERES opened its European subsidiary, Wind Europe Ltd., in Dublin, Ireland, and in the same month, the company announced its first order (five units for delivery in the UK). The XZERES 442SR small wind power system is accredited to the Microgeneration Certification Scheme (MCS), which qualifies the system for the government sponsored feed-in tariffs (FiT) in England, Scotland and Wales. In addition, the XZERES 442SR achieved the CE Mark[19] (Conformite Europeene), a certification that allows it to be marketed and sold throughout the European Union. The company's foray into the UK market was bolstered in April by the launch of its United Kingdom website (www.xzeres.co.uk), which includes the company's assessment tool, XZERES WindRx™.

Residents of **England, Scotland and Wales** have access to one of the best feed-in-tariff schemes in the world. Emulating the successful Western European feed-in-tariff models, the UK Department of Energy and Climate Change offers financial incentives to stimulate residential investment in renewable energy sources, including small wind turbines. To be entitled to claim feed-in-tariffs, the qualifying product must be accredited to the MCS and installed by a MCS approved installer. Each small wind turbine (with a rated capacity between 1.5 kW and 15kW) is able to receive 28 pence per kilowatt hour (kWh) for all renewable electricity generated. In addition to receiving the FiT, the electricity used on-site lowers one's energy bill and the electricity fed back into the grid entitles the operator an additional 3 pence per kWh. After the system is registered, the tariff levels are guaranteed for the period of the tariff and index-linked. In addition, the income is tax free for individuals and for businesses the capital expenditure qualifies for writing down allowances. Management estimates that the XZERES 442SR wind energy system can receive £10,000 ($16,400) annually for 20 years based on annual wind speeds of 6.5 meters/second (m/s) and assuming half of the energy is used on-site and the other half is sold to the UK national grid.

The WindRx™ web-based software platform on the company's UK web site provides financial benefit analysis specifically tailored for the UK. The potential customer enters his address and monthly electricity usage; WindRx™ then estimates the potential energy production from an XZERES wind energy system at that location and calculates the value of the energy savings. The analysis incorporates the FiT payments that will be paid by the British government for 20 years.

XZERES has established the infrastructure to enter the small wind market in the United Kingdom. Having received MCS certification and launched the UK web site for direct sales opportunities, the company has also begun to develop other distribution channels by signing 10 dealer partners and will soon expand its sales force in its office in Glasgow, Scotland.

RenewableUK, formerly the British Wind Energy Association (BWEA), is the foremost renewable energy trade association in the UK and issues annual statistics of the small wind turbine market, generally in April[20]. In 2010, 2,853 new small wind turbine systems were deployed in the UK generating £29.27 million in sales. Installed capacity increased 65% or 14.23 MW, bringing cumulative installed small wind capacity to 42.97 MW. RenewableUK projects that the UK could have 1,300 MW of installed small wind system capacity by 2020, implying a compound annual growth rate (CAGR) of 40.6%.

[19] The CE Mark indicates that a product has met or exceeded the health, safety and environmental requirements of the European Union.

[20] Small Wind Systems UK Market Report April 2011.

Management is planning on extending its presence into the European Union (EU). All 37 countries in the EU have feed-in tariffs, with Germany, Spain, Italy, Portugal and France having accelerated the addition of new capacity in the last few years. On the other hand, in the 1970's, Denmark made the commitment to eventually produce half of the country's power by wind and currently generates almost 20% of its electricity with wind turbines (the highest percentage of any country). When entering the Europe Union market, the management of XZERES plans to use multiple distribution channels, including dealers, distributors and possibly even forming a joint venture.

Management has plans to expand globally in phases. With the groundwork having been laid for Europe, management plans to next expand into the international markets of **Asia**, specifically Vietnam, Japan, South Korea and the Philippines. The company is pursuing leads for island electrification projects and other off-grid applications, such as desalinization projects, in these countries. Also, management continues to research and plan the company's eventual entry into the Chinese and Indian markets. Management is keenly aware of China's micro-grid electrification project and wishes to benefit from its implementation, but also is mindful that China has mandated a local content requirement law as a mechanism to foster the domestic production of turbines and other components. Currently, the Chinese government requires that almost 70% of turbine components, including rotor blades, be sources from domestic Chinese manufacturers.

POWER MANAGEMENT DIVISION

In April 2011, XZERES acquired Rochester Power Saver and created the **Power Management Division** of the company. XZERES now manufactures and markets power efficiency products, which are designed to improve the power factor for commercial and light-industrial customers and reduce their electricity costs from 10% to 20%. The products can also be used by residential customers as power conditioners and as central surge suppressors. Within a month of the acquisition, XZERES launched a website (www.xzeresenergy.com) dedicated to direct sales of power efficiency products.

For commercial and light-industrial customers, the company offers five models: XR 250, XZCI 500, XZCI 600, XZCI800, XZCI 1000 and XZCI 1000+, each having a different size, application, capacity rating and price point ($299 - $499). Custom models for larger industrial applications can be provided. The products increase the power factor to unity, allowing the customer to be billed at a lower rate schedule since less reactive power will be drawn from the electrical utility. The detailed explanation of utility pricing of electricity to businesses based on reactive power consumption or penalty fees charged for low power factors (below 1) that require utilities to generate more than the minimum volt-amperes necessary to supply the real power watts is beyond the scope of this report. However, it should be noted that large industrial sites with many inductive motors often have banks of capacitors installed strictly for the purpose of correcting the power factor back toward unity in order to reduce electricity costs. XZERES is targeting small-to-medium-sized commercial businesses as well as public institutions, such as schools and libraries. The power efficiency products have a short payback period, generally between 6 and 24 months, depending upon the level of inductive motors on-site. Additional benefits include extending the life of inductive motors and providing whole electrical system surge protection

The XZERES power efficiency products act as **central surge suppressors**, protecting electronic devices from the damaging effects of power surges aka transient voltage. A surge is any increase above the standard power voltage for a given electrical line. Typically caused by lightning strikes, power outages, electromagnetic pulses (EMP) and transformer malfunctions, surges often damage electrical components, especially sensitive electronics, such computers, televisions, alarm systems etc., as well as inductive motors in refrigerators, freezers, air conditioners, etc. **For residential customers**, the company offers five models: XR 100, XR 250, XR 250 plug-in, XR 500 and XR 1000+.

For XZERES, power savers provide the company with high margin products with a significantly shorter sales cycle and lower price points than small wind systems. XZERES will leverage the company's sales and marketing expertise to expand the power efficiency product business, especially in the under-served commercial and light-industrial markets.

FINANCIAL HISTORY

XZERES Corporation was originally incorporated under the laws of the state of New Mexico in January 1984 as Intermountain Refining Company, an oil & natural gas production company with some ancillary leasing operations[21]. Intermountain was successful having over $2 million in net assets just prior to its merger into A.R.E Wind Corp. XZERES commenced operations on October 2, 2008 with David Baker and Steven Shum, who began to focus the company on the renewable energy industry through the wind energy market. In October 2008, the authorized common stock amount was increased from 10 million shares to 100 million shares, and par value was increased from no par to $0.001. Also, shares outstanding were reverse split at a ratio of 7.7 to 1 so that following the split, 150,079 shares of common stock were outstanding.

In March 2010, the wind energy assets of Abundant Renewable Energy were available for the completion of the acquisition, for which the company issued 3,192,150 shares. Over the prior 18 months, XZERES had accumulated attorney and professional fees related to the acquisition, along with obligations to the company's former CEO, William Hagler, and the Core Fund for prior financial assistance. A total of 4,587,150 shares were issued to satisfy these commitments, and $268,200 of additional equity capital was raised. Then in April and May 2010, XZERES completed two private offering of common stock and warrants[22], priced at $1.00 that provided $3,611,950 in net proceeds so that the company could begin operations in the small wind turbine business. The following quarter (the second fiscal quarter), the company generated $361,484 in revenues. Sequential revenue growth of 30.4% was reported in the next quarter ending November 30, 2010. The fourth fiscal quarter generated a 38.2% sequential sales increase due to the implementation of the company's direct-sales distribution model and the introduction of the Micro-Generation utility sales model.

The company has been very successful in obtaining capital through private equity fundraising. During fiscal 2011, XZERES raised $5,375,095 from private placements of common stock and warrants. The company has aggressively pursued product development by expanding the engineering staff since acquiring the A.R.E. wind energy assets in March 2010. Management spent $1.48 million for R&D expense in fiscal 2011 in order to improve existing wind systems and developing new higher power-rated turbines. In March 2011, XZERES raised an additional $4.6 million in net proceeds through a private placement of 4,891,815 shares and warrants[23] priced at $1.05. The cash will fund continued expansion into the renewable energy industry, including product development, the pursuit of international opportunities and enhanced sales efforts. At the end of fiscal 2011 year (February 28, 2011), XZERES had $364,068 in cash, no long-term debt and $2,412,348 in shareholders' equity; however, the subsequent proceeds of $4.6 million from issuance of shares in March 2011 have significantly enhanced the company's cash position and shareholders' equity. Also, 4.5 million warrants are outstanding with exercise strike prices of $1.25 and $1.50, which are potentially non-dilutive sources of additional capital currently.

[21] Intermountain leased asphalt paving products, office space and manufacturing & storage facilities in Fredonia, Arizona.

[22] The warrants issued in March 2010 are exercisable for three years at a strike price of $1.25 per share.

[23] The warrants issued in March 2011 are exercisable at a strike price of $1.50 per share and were distributed such that each purchaser of common shares received warrants to purchase additional common shares in an amount equal to 50% of the number of shares purchased.

RECENT NEWS

On May 27, 2011, XZERES reported results for the fourth fiscal quarter and fiscal year ending February 28, 2011. **Quarterly revenues sequentially increased 38.2%** to $652 thousand from $472 thousand, primarily due to the multitude of management initiatives, including the Direct Buy program, 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. Revenues for fiscal 2011, which consisted of only three quarters of operations, were $1.49 million with the company's initial selling efforts beginning very late in the first fiscal quarter. The gross profit margin sequentially increased 292 basis points to 28.1% in the fourth fiscal quarter. R&D/Engineering expenses totaled $1,480,585 for the year as the company improves current products and is developing wind turbines with higher power ratings. Operating costs were high due to the expenses associated with the beginning of business operations as a small wind turbine manufacturing and sales company. 16.9% of total operating expenses were non-cash expenses in the form of expensed employee options and shares issued to consultants during the year for various services. XZERES reported a quarterly loss of $1.80 million or $0.13 per diluted share and an annual loss of $5.10 million or $0.41 per diluted share.

Management is seeing a dramatic increase in sales for small wind power systems in the UK. In addition, there are significant opportunities in Asia, especially Vietnam, and in the federal government market. Management's internal goal (not guidance) is to generate over $5.9 million in revenues during fiscal 2012. In addition, management expects that ultimately, the majority of sales will be through the direct channel, leading to a higher gross margin, which will also be bolstered by higher margin new products, services and business models.

On May 16, 2011, in recognition of the acquisition of Rochester Power Saver and the broadening of the company's scope within the power industry, the company was renamed **XZERES Corp.**, and the ticker symbol was changed to **XPWR**.

On May 5, 2011**,** XZERES **launched a website** (www.xzeresenergy.com) **for direct sales of the power efficiency products**, which were attained through the Rochester Power Saver acquisition.

On April 25, 2011, XZERES announced **the acquisition of Rochester Power Saver**, a maker of a family of power efficiency products, 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 broadens the company's small wind systems product lines with the addition of power saver products that are designed to improve the power factor for both business and residential customers, thereby reducing their electricity costs by 10% to 20%. 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 Power Saver products also act as surge suppression devices. Management plans to offer these power management devices both separately and in tandem with wind turbine systems.

On April 7, 2011**,** XZERES **launched a United Kingdom website** (www.xzeres.co.uk), which includes the company's assessment tool, XZERES WindRx™, for England, Scotland and Wales. The web-based software platform provides financial benefit analysis for potential wind turbine site locations by estimating potential wind energy production and calculating the feed-in tariff offered by the British government, which is available for the MCS certified wind systems offered by XZERES.

On December 16, 2010, XZERES announced three customers signed contracts under the company's newly launched Micro-Generation Utility model. Two dairy farms in Oregon and a construction consulting firm in California will install a total of 14 XZERES 442 small wind power systems worth approximately $1.1 million.

On November 15, 2010, XZERES **introduced a Buy Direct program** for the company's wind power systems. In addition to the traditional dealer network, XZERES now provides turnkey wind power

systems directly to the end-user. XZERES provides customer support from site assessment throughout the financing, permitting and installation processes to ongoing technical services.

On November 3, 2010, XZERES **introduced a customer financing program** for its wind power systems. Through various lending partners, XZERES can offer a variety of financing programs for a range of customers, including agricultural, municipal, residential and commercial. Up to 100% financing is available, including installation. Coupled with Federal and State incentives, customer financing facilitates the purchase decision and provides the customer with the ability to attain a positive cash flow profile.

On August 19, 2010, XZERES **introduced marine versions** of XZERES 110 and XZERES 442 units, dubbed **XZERES 110M** and **XZERES 442M**. The two additional small wind power systems are designed for marine, estuary and coastal environments with high salinity and high humidity conditions.

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, a price-to-sales valuation range between 2.8 and 5.2 on 12 month forward sales is expected. Our $1.50 price target is based on a 5.2 price-to-sales ratio valuation. At $0.80, the comparable current P/S ratio of XZERES stock is 2.80, the low-end of our expected range.

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 was 28.1% in the latest reported fiscal quarter, and the gross margin has consistently improved every quarter since the company began its small wind operations three quarters ago. We expect the gross margin will increase to 36% by the end of fiscal 2012.

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. The sequential quarterly sales growth rate is impressive. Comparable companies have a historical price-to-sales valuation range between 2.8 and 5.2. Since the company has consistently reported increasing sequential quarterly sales growth in the 30% range, the high-end of the range is being used to determine our initial target price of $1.50 (a 5.2 price-to-sales ratio).

RISKS

- As with many emerging growth companies, the accounting firm's opinion in the last 10-K (for the period ending February 28, 2011) contains the standard language for a company that is incurring losses from operations and is in need of additional capital to grow its operations. However, the accounting firm (Silberstein Ungar, PLLC) opines that the financial statements "present fairly, in all material respects, the financial position of XZERES Corp." We believe, as management does, that the company can successfully raise capital and continue as a going concern.

- The demand and pricing of small wind systems are currently heavily dependent on federal and state incentives for renewable energy, especially investment tax credits and feed-in tariffs. The reduction or elimination of these government economic incentives would have a material adverse effect on the small wind industry, in general, and XZERES, specifically. The investment tax credit in the United States has been extended through December 31, 2016, and feed-in tariffs, both in Europe and the U.S., appear to be established or being implemented further, with no signs of abatement.
- XZERES does not recognize revenue until the system is delivered to the customer. A closed sale may not take delivery until the site has been prepared for installation. Any delays in site preparation, including the ability to obtain permits, could delay the revenues of a closed sale from being recognized until a subsequent quarters.

INSIDER TRADING AND OWNERSHIP

As of May 25, 2011, corporate insiders own[24] 38.8% of the outstanding common stock. David Baker (Chairman of the Board) owns 3,763,964 shares, and Steven Shum (CFO) holds 3,395,888 shares, which includes 2,691,382 held by the Core Fund, L.P., of which Steven Shum is the manager. S. Clayton Wood (EVP) owns 115,000 shares, and 145,000 shares are held by Frank Greco (CEO), who also has options to purchase up to 1.12 million shares of stock, of which 145,000 shares may be currently exercised. Insiders have only purchased shares. No insider sales have been reported, only purchases.

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**
Revenue:	**0**	**0**	**0**	**1,489,061**	**5,712,358**	**15,142,421**
Cost of sales	0	0	0	1,099,456	3,786,466	9,691,150
Gross Profit	**0**	**0**	**0**	**389,605**	**1,925,892**	**5,451,272**
General & administrative	0	209,274	70,607	3,157,018	3,268,450	4,539,514
Marketing	0	0	0	172,158	180,000	215,506
Sales expense	0	0	0	629,580	920,000	1,206,835
Engineering/R&D expense	0	0	0	1,480,585	1,750,000	1,900,000
Total Expenses	**0**	**209,274**	**70,607**	**5,439,341**	**6,118,450**	**7,861,855**
Pre-tax profit from operations	**0**	**(209,274)**	**(70,607)**	**(5,049,736)**	**(4,192,558)**	**(2,410,584)**
Interest income (expense)	**0**	**0**	**0**	**0**	**0**	**0**
Other Income	**0**	**0**	**0**	**3,332**	**3,500**	**3,700**
Income (loss) Continuing Operations	**0**	**(209,274)**	**(70,607)**	**(5,046,404)**	**(4,189,058)**	**(2,406,884)**
Income (loss) from Discontinued Operations	42,771	(237,495)	2,229	0	0	0
Other comprehensive income	6,019	(40,425)	0	0	0	0
Provision for income taxes	0	0	0	0	0	0
Net income for the year	**48,790**	**(487,194)**	**(68,378)**	**(5,046,404)**	**(4,189,058)**	**(2,406,884)**
Net income per common share (diluted)	**0.04**	**(0.19)**	**(0.01)**	**(0.41)**	**(0.23)**	**(0.10)**
Net income per common share (diluted) continuing operations	**0.00**	**(0.08)**	**(0.02)**	**(0.41)**	**(0.23)**	**(0.10)**
Weighted average common shares outstanding - diluted	1,155,609	2,529,933	4,652,643	12,447,305	18,497,128	23,500,000
Gross Margin	**N/M**	**N/M**	**N/M**	**26.2%**	**33.7%**	**36.0%**

[24] Includes beneficial ownership of shares.

XZERES Corporation

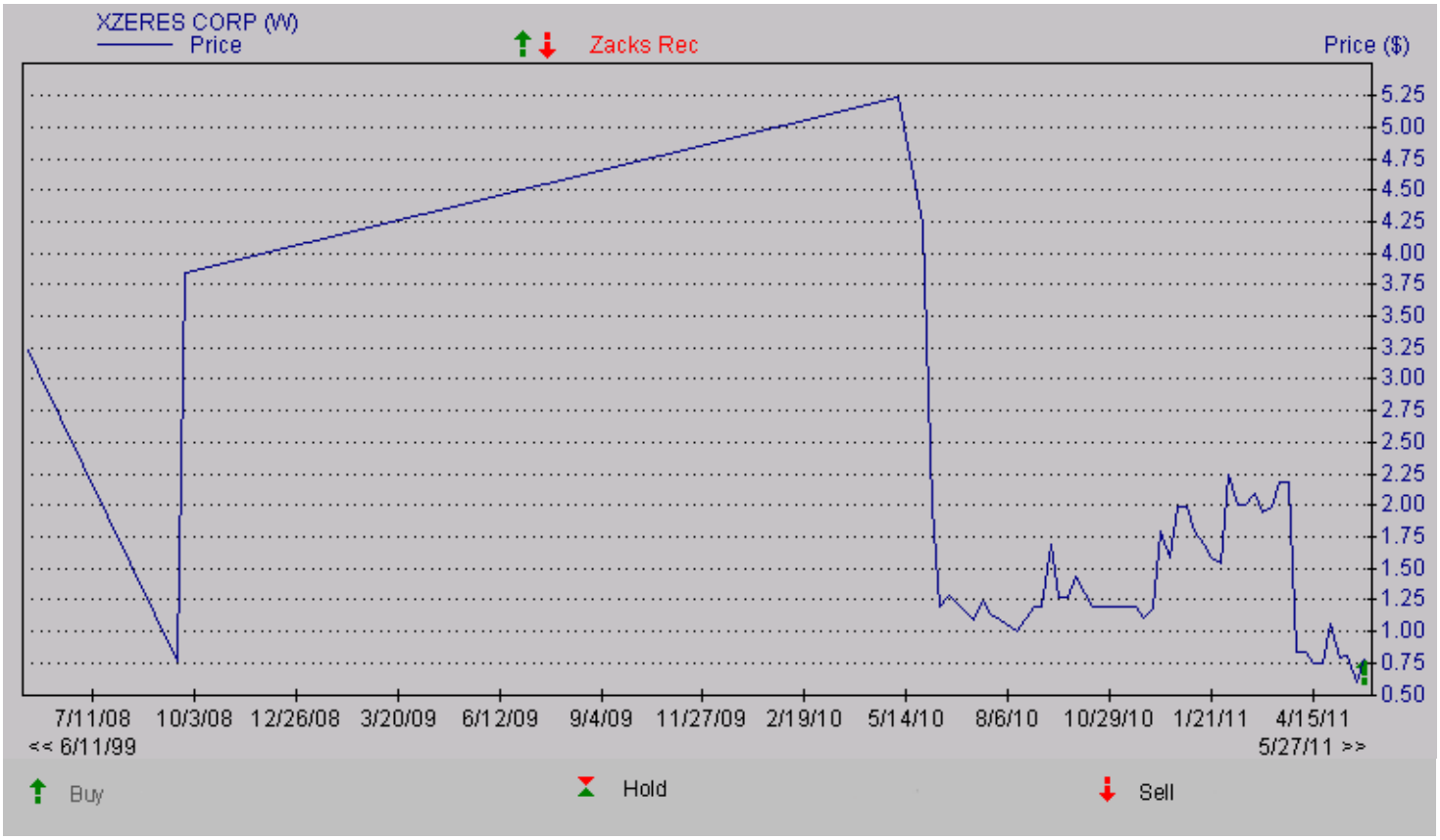
Quarterly Earnings Analysis	1Q 2011 (May 31)	2Q 2011 (Aug 31)	3Q 2011 (Nov 30)	4Q 2011 (Feb 28)	**FY 2011** (Feb 28)	1Q E 2012 (May 31)	2Q E 2012 (Aug 31)	3Q E 2012 (Nov 30)	4Q E 2012 (Feb 28)	**FY E 2012** (Feb 28)
Revenue:	**4,385**	**361,484**	**471,534**	**651,658**	**1,489,061**	**873,222**	**1,170,117**	**1,567,957**	**2,101,062**	**5,712,358**
Cost of sales	1,709	276,309	352,832	468,606	**1,099,456**	611,255	795,680	1,034,852	1,344,680	**3,786,466**
Gross Profit	**2,676**	**85,175**	**118,702**	**183,052**	**389,605**	**261,967**	**374,437**	**533,105**	**756,382**	**1,925,892**
General & administrative	508,423	782,296	696,471	1,169,828	**3,157,018**	720,000	781,200	847,602	919,648	**3,268,450**
Marketing	35,596	72,688	41,173	22,701	**172,158**	42,000	44,000	46,000	48,000	**180,000**
Sales expense	23,034	152,325	232,885	221,336	**629,580**	200,000	220,000	240,000	260,000	**920,000**
Engineering/R&D expense	77,953	403,906	420,693	578,033	**1,480,585**	420,000	437,500	437,500	455,000	**1,750,000**
Total Expenses	**645,006**	**1,411,215**	**1,391,222**	**1,991,898**	**5,439,341**	**1,382,000**	**1,482,700**	**1,571,102**	**1,682,648**	**6,118,450**
Pre-tax profit from operations	**(642,330)**	**(1,326,040)**	**(1,272,520)**	**(1,808,846)**	**(5,049,736)**	**(1,120,033)**	**(1,108,263)**	**(1,037,997)**	**(926,266)**	**(4,192,558)**
Interest income (expense)	0	0	0	(51,236)	**(51,236)**	0	0	0	0	**0**
Other Income	1,074	2,143	918	(803)	**3,332**	875	875	875	875	**3,500**
Income (loss) Continuing Operations	**(641,256)**	**(1,323,897)**	**(1,271,602)**	**(1,860,885)**	**(5,097,640)**	**(1,119,158)**	**(1,107,388)**	**(1,037,122)**	**(925,391)**	**(4,189,058)**
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	**(641,256)**	**(1,323,897)**	**(1,271,602)**	**(1,860,885)**	**(5,097,640)**	**(1,119,158)**	**(1,107,388)**	**(1,037,122)**	**(925,391)**	**(4,189,058)**
Net income per common share (diluted)	**(0.07)**	**(0.10)**	**(0.10)**	**(0.14)**	**(0.41)**	**(0.07)**	**(0.06)**	**(0.06)**	**(0.05)**	**(0.23)**
Weighted average common shares outstanding - diluted	9,486,919	13,280,255	13,280,255	13,741,790	**12,447,305**	17,187,698	18,633,605	18,833,605	19,333,605	**18,497,128**
Gross Margin	61.0%	23.6%	25.2%	28.1%	**26.2%**	30.0%	32.0%	34.0%	36.0%	**33.7%**

XZERES Corporation

Consolidated Balance Sheets (in $ US)

For the years ending February 28	**2008**	**2009**	**2010**	**2011**	**2012 E**
ASSETS					
Cash and cash equivalents	0	1,978	195,990	364,068	2,213,475
Accounts receivable (net)	0	0	0	633,669	2,407,942
Inventories	0	0	0	502,548	1,909,682
Inventory deposit	0	0	0	40,066	152,251
Prepaid expense	0	0	0	110,281	419,068
Current Assets	0	1,978	195,990	1,650,632	7,102,418
Property, plant & equipment (net)	0	0	0	375,115	400,000
Intellectual property	0	0	0	1,320,226	1,320,226
Website development costs (net)	0	0	0	18,234	24,000
Deposits	0	0	0	18,198	20,000
Net assets of discontinued operations	2,847,226	0	0	0	0
Total Assets	**2,847,226**	**1,978**	**195,990**	**3,382,405**	**8,866,644**
LIABILITIES					
Accounts payable	0	0	0	600,451	2,281,714
Accrued expenses	0	161,093	337,578	107,277	200,000
Customer deposits	0	0	0	48,228	150,000
Warranty reserve	0	0	0	16,601	63,084
Notes payable to related party	0	5,140	0	97,500	0
Notes payable	0	0	90,740	100,000	100,000
Net liabilities of discontinued operations	35,674	0	0	0	0
Current Liabilities	35,674	166,233	428,318	970,057	2,794,798
Preferred stock	0	0	0	0	0
Common stock	0	4,652	4,683	15,383	20,775
Stock warrants	0	0	0	1,565,054	4,000,000
Additional paid in capital	1,455,314	40,367	40,641	6,207,203	12,946,972
Retained earnings (deficit)	1,315,813	(209,274)	(277,652)	(5,375,292)	(10,895,900)
Accumulated other comprehensive income	40,425	0	0	0	0
SHAREHOLDERS' EQUITY	2,811,552	(164,255)	(232,328)	2,412,348	6,071,846
Total Liabilities and Equity	**2,847,226**	**1,978**	**195,990**	**3,382,405**	**8,866,644**
Common shares outstanding	1,155,609	4,651,978	4,682,602	15,382,816	20,000,000

HISTORICAL ZACKS RECOMMENDATIONS



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