Zacks Small-Cap Research

September 21, 2011

Brian Marckx, CFA
bmarckx@zacks.com
Ph (312) 265-9474

www.zacks.com

111 North Canal Street, Chicago, IL 60606

Verisante Technology Inc. (V.VRS)

V.VRS: Q2 2011, ISO Cert, Increasing Price Target.

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	02/04/2011
Current Price (09/21/11)	$0.77
Six- Month Target Price	**$2.60**

OUTLOOK

Based on preliminary trial data, high throughput and other advantages, Verisante's Aura could eventually become the new gold-standard for skin cancer diagnosis. We look for Aura to launch in Europe/Canada/Australia by early 2012 and in the U.S. in late 2013. The size and high incidence of skin cancer in these markets, combined with Verisante's razor / razor blade business model and low cost base means revenue and earnings could ramp very quickly. We have moved our price target from $2.25 to $2.60/share, reflecting recent feedback on proposed unit pricing for Aura. While the stock is up 97% since our February initiation, with the shares currently trading at $0.77, we continue to believe the stock is undervalued and are maintaining our Outperform rating.

SUMMARY DATA

52-Week High	**$1.26**
52-Week Low	**$0.14**
One-Year Return (%)	**N/A**
Beta	**N/A**
Average Daily Volume (sh)	**486,296**
Shares Outstanding (mil)	**57**
Market Capitalization ($mil)	**43.8**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**N/A**
Insider Ownership (%)	**N/A**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**N/A**
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	**N/A**
Type of Stock	**N/A**
Industry	**Med/Dental-Supp**

ZACKS ESTIMATES

Revenue
(in '000 of $)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2010	5 A	6 A	0 A	0 E	11 A
2011	0 A	0 A	0 E	0 E	0 E
2012					5,385 E
2013					21,185 E

Earnings per Share

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2010	-$0.01 A	-$0.01 A	-$0.01 A	-$0.01 A	-$0.04 A
2011	-$0.02 A	-$0.01 A	-$0.01 E	-$0.01 E	-$0.05 E
2012					-$0.05 E
2013					$0.07 E

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

© Copyright 2011, Zacks Investment Research. All Rights Reserved.

WHAT'S NEW

Q2 2011 Results

Verisante filed results for the second quarter ending June 30, 2011 on August 29th. Similar to Q1, results were largely in-line with our estimates. SG&A came in at CDN $753k versus our CDN $572k estimate, the difference almost entirely related to higher than modeled promotional expenses as a result of the company's rebranding (including a new website) and trade show attendance and presentations. Verisante's CEO, Thomas Braun, has been very active presenting at medical conferences and trade shows and meeting with prospective customers which could pay dividends once Aura launches. These have also provided valuable feedback from industry professionals - including that management's initial estimated pricing of Aura, at CDN $30k, may be very conservative.

Net income and EPS came in at CDN ($759k) and CDN ($0.01) versus our CDN ($517k) and CDN ($0.01) estimates.

Cash used in operations was CDN $498k in the quarter, similar to the CDN $469k in Q1 of this year. Investing activities used CDN $407k related to the acquisition of licenses and technology (intangibles) and CDN $16k in office equipment. Verisante exited the quarter with CDN $4.9MM in cash and liquid investments, which was bolstered by the CDN $4.5MM (net) proceeds from the April private placement of 12.5 million shares of common stock and warrants. Cash from financing activities in Q2 also included CDN $344k from the exercise of options and warrants. Verisante notes in the filing that they expect the cash balance at 6/30/2011 to be sufficient to fund operations for at least 12 months (i.e. - through 6/30/2012).

Business Update

- **Lung Cancer Trial Results Published:** Results of a small (26 patients) pilot study which used Verisante's Raman system technology, combined with white light and fluorescence bronchoscopy (technology which Verisante acquired in June) for the early detection of lung cancer were published in the July issue of the *Journal of Thoracic Oncology*. Results showed that when Verisante's Core lung cancer detection device (using Raman technology) is combined with the ClearVu and ClearVu Elite endoscopy system (which Verisante acquired) the number of false positives were reduced by over 75% compared to traditional endoscopic methods.

  While the results of the study are encouraging, as is Verisante's continued efforts to move their lung cancer detection program forward, we feel it is still too early to reasonably judge the potential for approvability of the device. In addition, management's current major focus is with getting Aura commercialized. As a result, we feel it is appropriate to continue to not incorporate a contribution from Core in our model until there is more information to comfortably judge the probability of regulatory approval and gauge launch timelines. If and when that happens, we will update our model accordingly – as we noted in the past, this could potentially add significant upside to our current revenue and earnings estimates (especially given the relatively large size of the lung cancer diagnostics market).

- **Aura Development / Commercialization Progress:** Verisante has made significant progress with development and commercialization of Aura over the last few months. This was highlighted by the July announcement that they had obtained ISO 13485:2003 certification for Aura, their flagship device for the detection of skin cancer. Gaining ISO certification was the most significant near-term milestone to gaining regulatory approval of Aura in Canada, Europe and Australia - the expected initial markets for Aura. With the ISO certification now in-hand, Verisante can begin to finalize the required deliverables to gain Health Canada approval - which could be filed with regulators in the coming weeks. The company expects Aura to be approved for sale in Canada before the end of 2011.

  Verisante has retained Emergo Group as their European representative to assist with the CE Marking process. Non-European based medical device manufacturers, such as Verisante, must appoint a European authorized representative in order for CE Marking to be valid. The CE Marking process is a little more involved than gaining Health Canada approval and requires Verisante to provide clinical data. Statistical analysis from the 1,000-lesion study is now completed which means Verisante could be in a position to complete its documentation for CE Marking in the near-term. The file will then be assessed and assuming no deficiencies, Aura can bear the CE Mark. If deficiencies are noted, Verisante will have the opportunity to remedy and the file then re-evaluated.

If all goes well Aura will be cleared for sale in Canada, Europe and Australia (once CE Marked, Australian regulatory approval should come in short-order) by year-end 2011 - hopefully we will hear more about the status of CE Mark within the next couple of months. While regulatory approval(s) may be in place by year-end, any sales will likely be insignificant until commercial production is under way - which will not be until 2012 (commensurate with our initial expectations).

Verisante expects to have 7 functional prototypes completed within the next couple of months and recently began their commercial manufacturing strategy. In an August 3, 2011 press release the company announced they engaged StarFish Medical, a small medical device engineering and consultancy firm, to guide their manufacturing plan.

- **Conferences / Trade Shows / Presentations:** Thomas Braun, Verisante's CEO, continues to attend and present at industry conferences and trade shows which, per our discussions with Mr. Braun, have been very productive - both from the standpoint of getting Aura in front of potentially early adopters as well as providing encouraging feedback. Mr. Braun recently attended the 2011 Annual Conference and Scientific Meeting of the Australasian College of Skin Cancer Medicine in Queensland, Australia. Of particular interest from conferences and trade shows that Verisante has attended was feedback from physicians, including dermatologists and medical device company executives that suggested Verisante's initial estimated pricing of Aura, at CDN $30k, may be very conservative - and that CDN $60k would not be an unrealistic price point for Aura. Our model, since initiating on Verisante in February of this year, has incorporated an assumption that Aura sells for CDN $30k - based on this recent feedback and our discussions with management, we feel that our CDN $30k price may be conservative.

  Mr. Braun will continue to circle the globe. He was scheduled to be a keynote speaker at the 4th Annual Congress and Expo of Molecular Diagnostics in Beijing next week but had to cancel due to a case of the flu. Verisante will have information booths at the 20th Congress of the European Academy of Dermatology and Venereology in Lisbon, Portugal in October and at Medica 2011 in November. Medica is the world's largest international medical trade show.

Our Updated Outlook / Financial Model

As noted, when we initiated coverage of Verisante in February our financial model incorporated the assumption that Aura would be priced at CDN $30k (which was the figure used in Verisante's investor presentation at the time). Based on the feedback that management has received relative to pricing, we feel CDN $30k may be conservative and have updated our model with the assumption that Aura sells for CDN $45k instead - which is still more conservative than the CDN $60k that was mentioned would not be an unrealistic price point for Aura. Depending on where demand / price shakes out when Aura launches, we will update our model again.

Our forecasted launch timelines remain unchanged as does our estimated unit sales (of both Aura and the endcaps) and gross margins. We look for Verisante to gain Health Canada regulatory approval and CE Marking by the current year-end and model Verisante to begin generating revenue through sales of Aura in Canada, Europe and Australia beginning in 2012 - which is also unchanged from our initial expectations. We are very encouraged by the progress Verisante has made to-date relative to commercialization of Aura and continue to be highly positive on the company.

Increasing the assumed price point for Aura had the effect of moving our revenue estimates for 2012, 2013 and 2014 (the latest year we model) from CDN $3.8MM, $15.6MM and $36MM to CDN $5.4MM, $21.2MM and $48.3MM currently. We have also made some adjustments to projected operating expenses and share count outstanding. The net result was EPS in 2012, 2013 and 2014 moving from CDN ($0.05), $0.05 and $0.18 to CDN ($0.05) - unchanged, $0.07 and $0.20 currently.

Valuation - Increasing Slightly

We continue to value Verisante using 25x our 2014 EPS estimate and discounting this back at 20% per year. With our 2014 EPS estimate moving from CDN $0.18 to $0.20 our valuation for Verisante has moved from approximately $2.25/share to $2.60/share (U.S.$ / CDN $ exchange rate remains at approximately 1/1). While the stock is up 97% since our February initiation, with the shares currently trading at $0.77, we continue to believe the stock is undervalued and are maintaining our Outperform rating on Verisante.

FINANCIAL STATEMENTS

INCOME STATEMENT (CDN $)

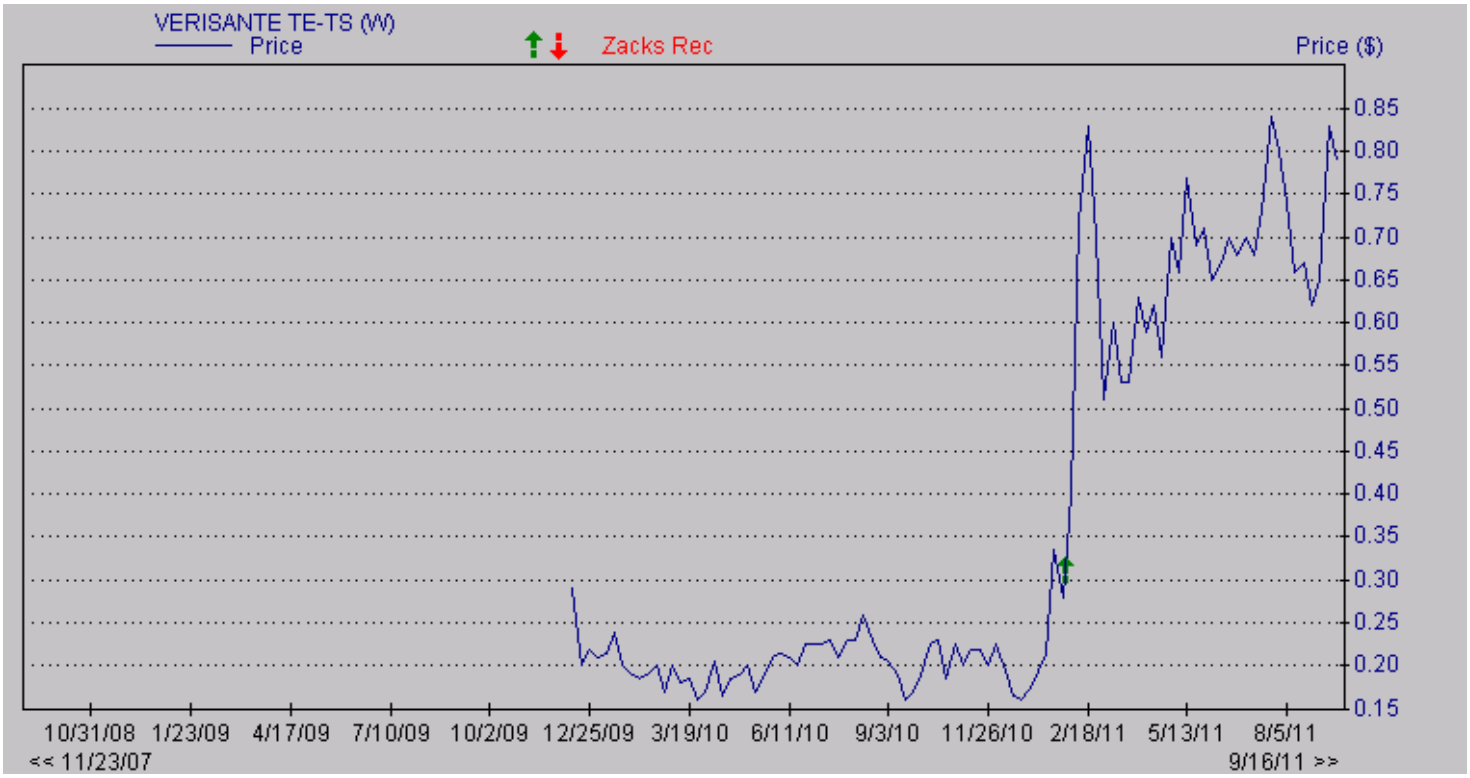
Verisante Technology

	2010 A	Q1A	Q2A	Q3E	Q4E	2011 E	2012 E	2013 E	2014 E
Device sales	$0	$0	$0	$0	$0	$0	$4,725	$16,853	$36,855
% total sales	-	-	-	-	-	-	*87.7%*	*79.6%*	*76.3%*
Cap sales	$0	$0	$0	$0	$0	$0	$660	$4,332	$11,448
% total sales	-	-	-	-	-	-	*12.3%*	*20.4%*	*23.7%*
Revenue	$11	$0	$0	$0	$0	$0	$5,385	$21,185	$48,303
YOY Growth	*-62.5%*	*-100.0%*	*-100.0%*	*#DIV/0!*	*#DIV/0!*	-	-	*293.4%*	*128.0%*
Device COGS	$0	$0	$0	$0	$0	$0	$2,363	$8,426	$18,428
Cap COGS	$0	$0	$0	$0	$0	$0	$33	$217	$572
Cost of sales	$8	$0	$0	$0	$0	$0	$2,396	$8,643	$19,000
Gross Income	$3	$0	$0	$0	$0	$0	$2,990	$12,542	$29,303
Gross Margin	*26.0%*	-	-	-	-	-	*55.5%*	*59.2%*	*60.7%*
SG&A	$1,435	$639	$753	$740	$757	$2,889	$3,222	$3,718	$4,012
% SG&A	-	-	-	-	-	-	*59.8%*	*17.6%*	*8.3%*
R&D	$215	$7	$0	$20	$40	$67	$2,720	$1,055	$1,010
% R&D	-	-	*4.9%*	*4.7%*	*5.1%*	-	*50.5%*	*5.0%*	*2.1%*
Interest expense (income), net	$0.4	$0.0	($13.5)	$0.0	$0.0	($13.5)	$0.0	$0.0	$0.0
Operating Income	($1,648)	($646)	($739)	($760)	($797)	($2,956)	($2,953)	$7,769	$24,281
Operating Margin	-	*#DIV/0!*	*#DIV/0!*	*#DIV/0!*	*#DIV/0!*	-	-	*36.7%*	*50.3%*
Government grants	$160	$0	$0	$75	$75	$150	$100	$50	$50
Royalty payments	$0	($57)	($20)	($25)	($25)	($127)	($323)	($1,271)	($2,898)
FX gain (loss)	$3	($2)	($0)	$0	$0	($2)	$0	$0	$0
Total Other Income	$163	($93)	($20)	$50	$50	($13)	($223)	($1,221)	($2,848)
Pre-Tax Income	($1,485)	($739)	($759)	($710)	($747)	($2,969)	($3,176)	$6,548	$21,433
Taxes (benefit)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$1,636.9	$5,786.9
Tax Rate	*0.0%*	*0.0%*	*40.0%*	*40.0%*	*40.0%*	*0.0%*	*0.0%*	*25.0%*	*27.0%*
Net Income	($1,485)	($739)	($759)	($710)	($747)	($2,969)	($3,176)	$4,911	$15,646
Net Margin	-	*#DIV/0!*	*#DIV/0!*	*#DIV/0!*	*#DIV/0!*	-	-	*23.2%*	*32.4%*
EPS	($0.04)	($0.02)	($0.01)	($0.01)	($0.01)	($0.05)	($0.05)	$0.07	$0.20
YOY Growth	*30.4%*	*78.8%*	-	-	-	*26.7%*	*-15.0%*	*-244.3%*	*198.7%*
Diluted Shares O/S	35,159	43,109	56,897	60,000	62,500	55,627	70,000	75,000	80,000

Source: Zacks Investment Research *Brian Marckx, CFA*

© Copyright 2011, Zacks Investment Research. All Rights Reserved.

HISTORICAL ZACKS RECOMMENDATIONS



DISCLOSURES

Zacks SCR certifies that all of the views expressed in our reports or blogs accurately reflect the personal views of the analyst or analysts contributing to the report or blog about the subject company or companies and its or their securities. We also certify that no part of an analysts' compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in any report or blog.

The following disclosures relate to relationships between Zacks Investment Research ("ZIR") and Zacks Small-Cap Research ("Zacks SCR") and the companies covered by the Zacks SCR analysts in the Small-Cap Universe.

ZIR or Zacks SCR Analysts do not hold shares in the companies in which they cover. Each analyst has full discretion on the rating and price target based on their own due diligence. Analysts are paid in part based on the profitability of Zacks SCR, which includes payments received for non-investment banking revenues and services.

ZIR and Zacks SCR do not make a market in any stock. Zacks SCR has never received compensation for investment banking services on the small-cap universe. Zacks SCR does not expect received compensation for investment banking services on the small-cap universe. Zacks SCR has received compensation for non-investment banking services on the small-cap universe. Zacks SCR expects to receive additional compensation for non-investment banking services on the small-cap universe. Non-investment banking services include investor relations services and software, financial database analysis, advertising services, brokerage services, advisory services, investment research, and investment management.

Additional information is available upon request. Zacks SCR reports are based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Because of individual objectives, the report should not be construed as advice designed to meet the particular investment needs of any investor. Any opinions expressed by Zacks SCR Analysts are subject to change. Reports are not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. Zacks SCR uses the following rating system for the securities it covers. Buy/Outperform: The analyst expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters. Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters. Sell/Underperform: The analyst expects the company will underperform the broader U.S. Equity market over the next one to two quarters.

The current distribution of Zacks Ratings is as follows on the 1012 companies covered: Buy/Outperform- 16.9%, Hold/Neutral- 77.2%, Sell/Underperform – 5.4%. Data is as of midnight on the business day immediately prior to this publication.

© Copyright 2011, Zacks Investment Research. All Rights Reserved.