

Align Technology (ALGN)

\$308.75 (As of 07/27/20)

Price Target (6-12 Months): **\$318.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 06/21/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:F

Value: C

Growth: F

Momentum: F

Summary

Align Technology exited the second quarter of 2020 with better-than-expected revenues and wider-than-expected loss. APAC saw recovery efforts and exceeded company's expectations. It reflected improving trends as practices reopened and got the Invisalign business back on track and implemented COVID-19 recovery measures in China. exocad revenues were strong. Invisalign's potential and strong solvency position buoy optimism. Align has outperformed its industry over the past six months. Yet, the company saw significantly lower-than-expected sales of clear aligners and iTero scanners due to the pandemic. Dismal international performance in most geographies and foreign exchange impacts are other headwinds. Overdependence on Invisalign and tough competitive landscape are also deterring. Align did not provide third-quarter guidance, raising concerns.

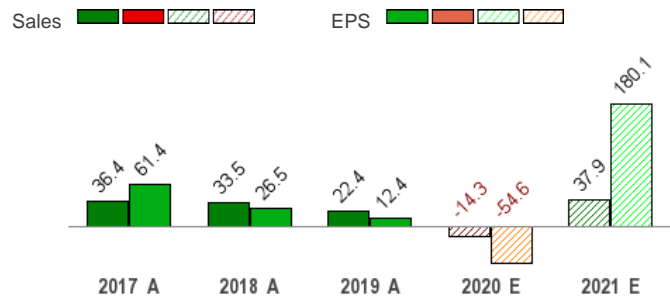
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$326.36 - \$127.88
20 Day Average Volume (sh)	871,997
Market Cap	\$24.3 B
YTD Price Change	10.7%
Beta	2.01
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Medical - Dental Supplies
Zacks Industry Rank	Bottom 36% (162 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-3,400.0%
Last Sales Surprise	2.0%
EPS F1 Est- 4 week change	-22.0%
Expected Report Date	10/28/2020
Earnings ESP	0.0%
P/E TTM	96.8
P/E F1	123.0
PEG F1	5.3
P/S TTM	11.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	668 E	645 E	720 E	813 E	2,847 E
2020	551 A	352 A	502 E	659 E	2,064 E
2019	549 A	601 A	607 A	650 A	2,407 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.56 E	\$1.52 E	\$1.78 E	\$2.13 E	\$7.03 E
2020	\$0.73 A	-\$0.35 A	\$0.42 E	\$1.46 E	\$2.51 E
2019	\$0.89 A	\$1.83 A	\$1.28 A	\$1.53 A	\$5.53 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/27/2020. The reports text is as of 07/28/2020.

Overview

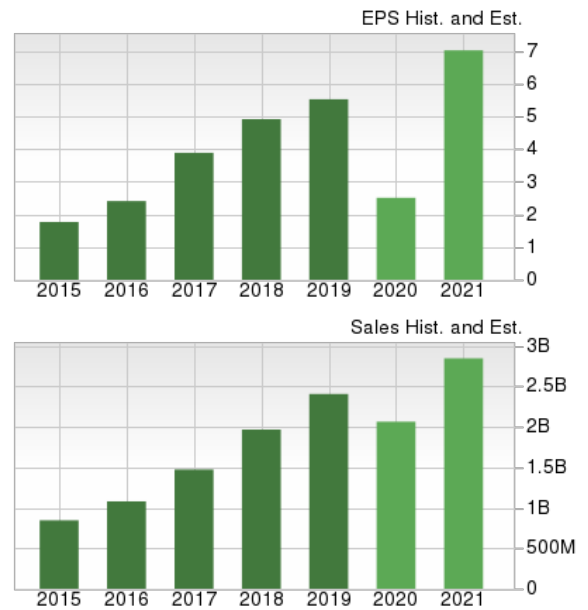
Align Technology, based in California, manufactures and markets a system of clear aligner therapy, intra-oral scanners and CAD/CAM (computer-aided design and computer-aided manufacturing) digital services used in dentistry, orthodontics, and dental records storage. The clear aligner system corrects malocclusion using nearly invisible and removable appliances that gently move the tooth to a desired final position.

Align presently has 2 operating segments, **Clear Aligner** (84.2% of total revenues in 2019), known as the Invisalign system and the **CAD/CAM Services** (15.8% of total revenues in 2019) which is known as the iTero intra-oral scanners and OrthoCAD services (which we earlier referred to as Scanner and CAD/CAM Services). In fiscal 2019, the Clear Aligner segment registered revenue growth of 19.8% from 2018, while the latter registered revenue growth of 38.5% from 2018.

Product portfolio:

Invisalign System – An exclusive method to treat malocclusion based on a series of doctor-prescribed, custom manufactured, clear plastic removable orthodontic aligners. The Invisalign system offers a range of treatment options, specialized services, and proprietary software for treatment visualization and comprises several phases.

The Clear Aligner products are Invisalign Full, Teen and Assist (Full Products), Express/Lite (Express Products), Vivera retainers, along with training and ancillary products for treating malocclusion.



Reasons To Buy:

▲ **Share Price Performance:** Align Technology has been outperforming its industry over the past six months. The stock has surged 18% compared with the industry's 3.5% rise. Align Technology exited the second quarter of 2020 with better-than-expected revenues. In APAC, Japan, Taiwan and South Korea saw successful recovery efforts and performed better than the company's expectations. APAC's growth was led by China, Taiwan, Hong Kong and South Korea's position in the recovery curve. APAC reflected improving trends as practices reopened and got the Invisalign business back on track along with COVID-19 recovery measures implemented by Align Technology in China. Revenues from the exocad Global Holdings GmbH (a global CAD/CAM software leader) partially offset promotional discounts and lower service revenues. The potential of the company's Invisalign portfolio and strong solvency position buoy optimism.

Align Technology's recent product development, balanced growth observed across all channels and the company's consistent focus in international markets to drive growth and bolster our confidence in the stock.

▲ **Invisalign Holds Potential:** Align Technology's Invisalign clear aligner has been receiving positive feedback and holds huge long-term market potential. The global clear aligners market size was valued at \$2.31 billion in 2019 and is projected to reach \$5.58 billion by 2027, at a CAGR of 18.7% (a Fortune Business Insight report).

The recent performance of this business, although dull, exhibited the pandemic-led market crisis and accordingly is not expected to last long. We are in fact impressed that even amid such a situation, the company trained a significantly higher number of doctors through virtual courses, summits and forums. The company trained approximately 3,500 new doctors in the reported quarter, which includes 2,350 international doctors. Further, Invisalign's teen market recorded growth from APAC across comprehensive products. Toward the quarter-end, Align Technology witnessed recovery in its orthodontic channel with an uptick in Invisalign comprehensive treatments in the teens and pre-teen segment across most regions, with pronounced positive growth in APAC in the teen segment. Further, utilization improved in June, with teen shipments witnessing faster recovery in North America in late May and through June.

Invisalign First for Invisalign treatment in young patients continued its momentum.

Despite the softness within the GP channels, overall, the company saw slower deceleration in teen shipment growth than adults, driven by Germany and France. Further, the expansion markets saw lesser decline and accounted for a negligible decline in EMEA.

▲ **Invisalign Portfolio Expansion:** Align Technology's Invisalign portfolio offers orthodontic treatment to straighten teeth without metal braces.

In May, amid the coronavirus hullabaloo, Align Technology has launched two virtual solutions that help doctors connect with existing Invisalign patients to ensure continuity of care. These are Invisalign Virtual Appointment and Invisalign Virtual Care, both enable doctors to manage a range of practice services remotely. In February, the company launched the ClinCheck "In-Face" Visualization tool for the Invisalign Go system.

Further, Align Technology launched the Invisalign Go Plus system in the U.K., Nordic and Benelux in July. The company's GP segment recorded growth in non-comprehensive cases with Invisalign Go and the launch of Moderate in China (launched in March). This continues to demonstrate customer preferences in treating young patients with Invisalign.

Other notable offerings from Align Technology include the Invisalign Moderate package, which was earlier launched in North America and SmileView. The company is witnessing continued acceleration of the Invisalign First clear aligners for treatment of younger patients. The overall mandibular advancement is also progressing well.

▲ **iTero in Focus:** Align Technology has been focusing on expanding work flow options of its leading iTero scanners. Cumulatively, 20.5 million orthodontic scans and 4.7 million restorative scans have been performed with iTero scanners by 2019-end. According to the company, use of the iTero scanners for Invisalign case submissions continues to grow and remains a positive catalyst for Invisalign utilization.

Despite dismal performance in the second quarter due to the pandemic-led practice closures, iTero has been receiving positive feedback and momentum from customers. The robust performance of Element 5D Imaging Systems in North America and APAC along with iTero Element 1 scanner model sales in China and notable sales of the Flex scanner model in EMEA instills confidence.

The company completed acquisition of exocad Global Holdings GmbH, a privately-held key player in the dental computer-aided design/computer-aided manufacturing (CAD/CAM) software market, on Apr 1. The inclusion of this business slightly offset the fall in revenues in the Systems and Services segment. The revenue generated by exocad also partially offset the year-over-year decline in revenues due to the drop in volumes across most regions, promotional discounts and decrease in service revenues.

▲ **International Focus to Drive Growth:** Align Technology has undertaken several strategies to improve adoption of Invisalign Technology that includes product/technology development, extending clinical effectiveness, extension of the Invisalign Technology brand and driving international growth.

For the international business, the quarter recorded Invisalign case volume uptick in APAC despite significant fall in revenues in EMEA due to the pandemic. On a year-over-year basis, International shipments too witnessed slight growth in APAC despite fall in EMEA. Invisalign's teen market recorded growth from APAC across comprehensive products. Overall, increased adoption of the company's moderate product among the orthodontic portfolio was witnessed despite decline in both non comprehensive and comprehensive shipments.

APAC's Japan, Taiwan and South Korea saw successful recovery efforts and performed better than the company's expectations. APAC's growth was led by China, Taiwan, Hong Kong and South Korea's position in the recovery curve. APAC reflected improving trends as practices reopened and got the Invisalign business back on track along with COVID-19 recovery measures implemented by Align Technology in China.

▲ **Strong Solvency Position:** Align Technology exited the second quarter of 2020 with cash and cash equivalents, and short-term marketable

securities of \$404.4 million, compared with \$790.1 million at the end of the first quarter of 2020. Meanwhile, the company has no debt in the reported quarter, which is a significant improvement from the total debt of \$54 million at the end of the first quarter of 2020. This is good news in terms of solvency position of the company, at least during the year of economic downturn, implying that the company is holding sufficient cash.

Cumulative net cash provided by operating activities was \$69.7 million at the end of the second quarter, compared with \$294.6 million in the year-ago period. When the company is grossly suffering from coronavirus-led procedural deferrals, this is particularly good news for the investors.

Reasons To Sell:

- ▼ **Coronavirus-Deferred Elective Procedures Hit Sales Hard:** In the second quarter, Align Technology witnessed lower-than-expected sales of Invisalign clear aligners and iTero scanners due to the COVID-19 pandemic. In the quarter, revenues at the Clear Aligner segment fell 39.9% year over year due to volume decline across most regions. Within the segment, Invisalign case shipments were down 38.3% year over year. Invisalign volumes were down 52.2% and 27.1% year over year in the Americas and International regions, respectively. Invisalign volume for teenage patients was down 31.9% year over year.

Revenues from CAD/CAM Services declined 48.1% in the quarter due to COVID-19-led sales decline in most regions, promotional discounts and lower service revenues.

More concerning fact is that, the uncertainties regarding the duration and impact of the coronavirus pandemic on the company's overall business have compelled Align Technology to refrain from providing any guidance for the third quarter of 2020.

- ▼ **Invisalign Store Closure Hampers Growth:** Since April 2018 Align Technology was engaged in an arbitration proceeding with the SDC Entities stemming from the claim that the company's Invisalign retail stores violate non-compete provisions applicable to the members of SDC Financial LLC, including Align. In March 2019, Align Tehcnology finally announced that the outcome of the proceedings did not come in favor of the company.

- ▼ **Competitive Landscape:** Align Technology faces significant competition from traditional orthodontic appliance (or wires and brackets) players such as 3M's Unitek, Danaher Corporation's Sybron Dental Specialties and Dentsply International. The company also competes with products similar to InvisAlign Technology, such as the products from Ormco Orthodontics, a division of Sybron Dental Specialties. Align Technology has witnessed a continuous decline in ASP primarily resulting from advantage rebate, promotional activity and product mix.

- ▼ **Economic Uncertainty:** The general slowdown in the United States and certain international economies is having a negative impact on consumer spending and affecting Align Technology's business fundamentals. Align Technology attributed the waning earnings to the macro economic crisis that affected the overall dental market and led to continued soft dental sales for Align Technology. Dental procedures are primarily elective in nature and are deferred when unemployment levels rise.

Continued weakness in the global economy results in a challenging environment for dental technology sales; dentists may postpone investments in capital equipment, such as intra-oral scanners. Although we expect a gradual pickup in patient traffic, any hiccup in the recovery process will aggravate the situation. Further, the recent coronavirus outbreak has been causing a very unstable economic condition for the company.

- ▼ **Currency Headwinds:** The significant challenges arising from unfavorable foreign currency translation have been affecting Align Technology's financials over the past few quarters. Per management, significant currency fluctuations could have a material impact on revenues, cost of sales and operational results.

- ▼ **Overdependence on Invisalign Technology System:** A vast majority of Align Technology's total net revenues largely depends on the sale of its InvisAlign Technology System, primarily InvisAlign Technology Full and Invisalign Technology Teen, and the same trend is expected to continue at least in the near future. Thereby, continued and widespread market acceptance of Invisalign Technology by orthodontists, GPs and consumers is critical to Align Technology's future success.

Management fears that if orthodontists and GPs somehow experience a reduction in consumer demand for orthodontic services, or consumers become reluctant to adopt Invisalign Technology as rapidly as management expects that might hurt the company's business heavily. Also, if consumers start to prefer a competitive product over InvisAlign Technology or if the average selling price of Align Technology product declines, the company's operating results will suffer a severe setback.

We remain concerned about the current economic uncertainty which continues to cast a negative impact on Align's dental procedures. The competitive landscape also remains an overhang.

Last Earnings Report

Align Technology Earnings Fall Shy of Estimates in Q2

Align Technology second-quarter 2020 loss per share was 35 cents, reflecting a sharp decline from year-ago earnings per share of \$1.49. The quarter's loss was wider than the Zacks Consensus Estimate of a loss of a penny. The significantly lower-than-expected revenues of Invisalign Clear Aligners and iTero scanners during the second quarter due to the COVID-19 pandemic resulted in the bottom-line miss.

Revenues declined 41.3% year over year to \$352.3 million in the quarter but beat the Zacks Consensus Estimate by 1.9%.

Quarter Ending **06/2020**

Report Date	Jul 22, 2020
Sales Surprise	1.97%
EPS Surprise	-3,400.00%
Quarterly EPS	-0.35
Annual EPS (TTM)	3.19

Segments in Detail

In the second quarter, revenues at the **Clear Aligner** segment fell 39.9% year over year to \$298.3 million due to volume decline across most regions. Within the segment, Invisalign case shipments amounted to 221.9 thousand, down 38.3% year over year.

The segment was driven by APAC, which was partially offset by North America and EMEA and Latin America. The segment also affected by foreign exchange fluctuations of approximately \$6 million.

During the quarter, Invisalign volumes were down 52.2% and down 27.1% year over year in the Americas and International regions, respectively.

Invisalign volume for teenage patients was 70.6 thousand cases, down 31.9% year over year. The teen market recorded growth from APAC across comprehensive products. However, on an overall basis, both non comprehensive and comprehensive shipments declined but with increased adoption of the company's moderate product among the orthodontic portfolio.

Revenues from **CAD/CAM Services** declined 48.1% to \$54 million in the quarter due to COVID-19-led sales decline in most regions, except APAC. Revenues from the exocad Global Holdings GmbH (a global CAD/CAM software leader) partially offset promotional discounts and lower service revenue.

Margins

Gross margin in the quarter under review contracted 829 basis points (bps) year over year to 63.7% despite a 24% decline in cost of net revenues.

During the quarter, Align Technology witnessed a 4.1% year-over-year decrease in selling, general and administrative expenses to \$256.9 million and a 3.9% rise in research and development expenses to \$40.4 million.

Operating loss in the quarter under review was \$73 million compared with operating profit of \$125.5 million year over year.

Financial Details

At the end of the second quarter, Align Technology had cash, cash equivalents and short-term marketable securities of \$404.4 million compared with \$790.1 million at the end of the first quarter of 2020.

Cumulative net cash provided by operating activities was \$69.7 million at the end of the second quarter compared with \$294.6 million in the year-ago period.

The company currently has approximately \$100 million left under its May 2018 repurchase program.

Guidance

The uncertainties regarding the duration and impact of the coronavirus pandemic on the company's overall business have compelled Align Technology to refrain from providing any guidance for the third quarter of 2020.

Recent News

Align Technology Launches ADAPT Service for Doctors: Jul 22, 2020

Align Technology launched the Align Digital and Practice Transformation (ADAPT) service across the globe for doctors who use its Invisalign and iTero products.

Align Technology Inks Partnership Deal: Jun 18, 2020

Align Technology announced entering into a partnership with MedTech Innovator, which is a nonprofit startup accelerator in the medical technology industry.

Align Technology Launches Latest Version of its Treatment Planning Software: May 14, 2020

Align Technology launched the latest version of its ClinCheck treatment planning software, ClinCheck Pro 6.0. The release includes the new ClinCheck "In-Face" Visualization tool, which creates a personalized view of how the patients' new smile could look.

Align Technology Announces Availability of Virtual Solutions: May 7, 2020

Align Technology announced the availability of two virtual solutions viz. Invisalign Virtual Appointment and Invisalign Virtual Care that help doctors connect with existing Invisalign patients to ensure continuity of care.

Valuation

Align Technology shares are up 10.7% and up 57.5% in the year to date period and the trailing 12-month period, respectively. Stocks in the Zacks sub-industry are up 8.7% while the Zacks Medical sector is up 1.1% in the year to date period. Over the past year, the Zacks sub-industry is down 1.8% and sector is up 6.7%.

The S&P 500 index is up 0.8% in the year to date period and up 7.7% in the past year.

The stock is currently trading at 57.7X Forward 12-months earnings, which compares to 20.2X for the Zacks sub-industry, 23X for the Zacks sector and 22.6X for the S&P 500 index.

Over the past five years, the stock has traded as high as 87.4X and as low as 21.7X, with a 5-year median of 39.9X.

Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$318 price target reflects 60.5X forward 12-months earnings.

The table below shows summary valuation data for ALGN.

Valuation Multiples - ALGN					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	57.66	20.24	23.00	22.63
	5-Year High	87.44	20.24	23.17	22.63
	5-Year Low	21.72	13.63	15.89	15.25
	5-Year Median	39.86	16.47	18.98	17.52
P/S F12M	Current	9.60	0.38	2.84	3.57
	5-Year High	13.81	0.38	3.74	3.57
	5-Year Low	3.71	0.23	2.22	2.53
	5-Year Median	7.33	0.28	2.90	3.02
P/B TTM	Current	8.55	4.86	4.41	4.43
	5-Year High	26.31	4.86	5.07	4.56
	5-Year Low	4.20	2.54	2.94	2.83
	5-Year Median	11.49	3.45	4.30	3.71

As of 07/27/2020

Industry Analysis Zacks Industry Rank: Bottom 36% (162 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Danaher Corporation (DHR)	Outperform	1
Laboratory Corporation of America Holdings (LH)	Outperform	2
Patterson Companies, Inc. (PDCO)	Outperform	1
CONMED Corporation (CNMD)	Neutral	3
Henry Schein, Inc. (HSIC)	Neutral	3
3M Company (MMM)	Neutral	3
Merit Medical Systems, Inc. (MMSI)	Neutral	3
DENTSPLY SIRONA Inc. (XRAY)	Neutral	3

Industry Comparison Industry: Medical - Dental Supplies				Industry Peers		
	ALGN	X Industry	S&P 500	HSIC	PDCO	XRAY
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Outperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	1	3
VGM Score	F	-	-	A	A	D
Market Cap	24.32 B	2.43 B	22.74 B	9.57 B	2.43 B	9.52 B
# of Analysts	6	5	14	9	8	9
Dividend Yield	0.00%	0.00%	1.8%	0.00%	4.11%	0.92%
Value Score	C	-	-	B	A	C
Cash/Price	0.02	0.06	0.07	0.06	0.03	0.02
EV/EBITDA	37.35	13.87	13.03	10.90	13.75	15.44
PEG Ratio	5.16	3.60	3.03	4.94	1.96	3.90
Price/Book (P/B)	8.55	4.45	3.17	2.65	2.90	2.03
Price/Cash Flow (P/CF)	51.14	15.31	12.05	13.88	2.66	11.04
P/E (F1)	120.72	32.59	21.90	31.27	18.61	30.96
Price/Sales (P/S)	11.26	2.41	2.38	0.95	0.44	2.41
Earnings Yield	0.81%	1.97%	4.30%	3.19%	5.37%	3.22%
Debt/Equity	0.02	0.31	0.76	0.29	0.76	0.33
Cash Flow (\$/share)	6.04	1.35	7.01	4.83	9.54	3.94
Growth Score	F	-	-	B	B	F
Hist. EPS Growth (3-5 yrs)	52.39%	10.40%	10.85%	6.46%	-13.56%	-4.35%
Proj. EPS Growth (F1/F0)	-54.58%	-7.09%	-7.56%	-38.94%	-12.17%	-42.72%
Curr. Cash Flow Growth	4.59%	3.87%	5.47%	-9.03%	327.70%	-53.28%
Hist. Cash Flow Growth (3-5 yrs)	23.79%	12.37%	8.55%	2.76%	27.55%	12.09%
Current Ratio	1.22	1.51	1.31	1.64	1.44	2.02
Debt/Capital	1.75%	27.05%	44.41%	26.51%	43.26%	24.59%
Net Margin	78.75%	0.86%	10.45%	7.11%	-10.72%	2.12%
Return on Equity	81.50%	12.84%	15.13%	15.19%	11.20%	10.70%
Sales/Assets	0.67	1.07	0.54	1.39	1.69	0.47
Proj. Sales Growth (F1/F0)	-14.23%	0.00%	-2.00%	-15.28%	-2.68%	-20.50%
Momentum Score	F	-	-	B	C	C
Daily Price Chg	3.56%	0.62%	0.48%	0.00%	1.18%	0.49%
1 Week Price Chg	-7.50%	-0.18%	0.37%	0.09%	-2.87%	-3.42%
4 Week Price Chg	15.86%	5.06%	5.61%	15.45%	12.60%	-1.05%
12 Week Price Chg	46.93%	16.25%	13.36%	27.70%	55.91%	9.72%
52 Week Price Chg	57.49%	10.32%	-3.30%	-1.69%	28.47%	-22.92%
20 Day Average Volume	871,997	456,923	1,917,592	1,276,086	1,054,328	1,292,072
(F1) EPS Est 1 week change	-23.48%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-22.03%	0.00%	0.21%	1.10%	0.51%	1.85%
(F1) EPS Est 12 week change	-73.26%	-11.84%	-2.00%	-22.80%	3.71%	-26.72%
(Q1) EPS Est Mthly Chg	-14.12%	0.00%	0.00%	1.35%	2.86%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	F
Momentum Score	F
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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