

## Coty, Inc. (COTY)

**\$3.54** (As of 08/27/20)

Price Target (6-12 Months): **\$4.25**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 03/11/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:D

Value: C

Growth: F

Momentum: A

### Summary

Shares of Coty have underperformed the industry on a year-to-date basis. The company has been witnessing softness in its Consumer Beauty segment. Also, coronavirus-led concerns put pressure on its fourth-quarter fiscal 2020 results. During the quarter, the top and the bottom line slumped year over year and fell significantly short of the respective Zacks Consensus Estimate. Results were marred by broad-based channel shutdowns caused by coronavirus-induced restrictions. Nevertheless, the company's e-commerce business continued to be impressive in EMEA and Americas business. Apart from this, Coty is committed toward its turnaround plans. This is evident from its strategic partnership with KKR. The company is on track to generate about one-third savings from its fixed cost-reduction program of \$600 million by the end of fiscal 2021.

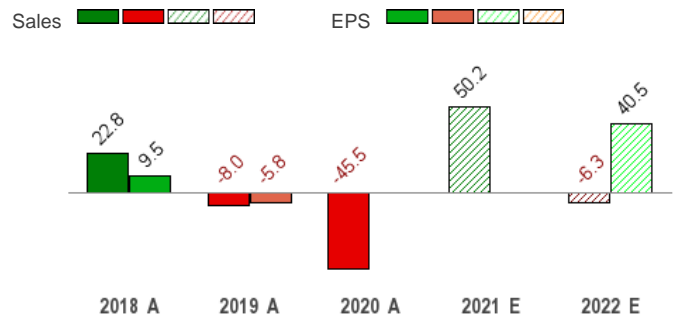
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$13.42 - \$3.02
20 Day Average Volume (sh)	8,344,950
Market Cap	\$2.7 B
YTD Price Change	-68.5%
Beta	0.97
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<a href="#">Cosmetics</a>
Zacks Industry Rank	Bottom 32% (171 out of 252)

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-475.0%
Last Sales Surprise	-59.8%
EPS F1 Est- 4 week change	4.0%
Expected Report Date	11/04/2020
Earnings ESP	-110.0%

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	1,938 E	2,396 E	1,670 E	1,451 E	6,640 E
2021	1,815 E	2,331 E	1,578 E	1,557 E	7,088 E
2020	1,943 A	2,345 A	1,528 A	560 A	4,718 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$0.13 E	\$0.20 E	\$0.09 E	\$0.09 E	\$0.52 E
2021	\$0.05 E	\$0.24 E	\$0.02 E	\$0.12 E	\$0.37 E
2020	\$0.07 A	\$0.27 A	-\$0.08 A	-\$0.46 A	-\$0.48 A

\*Quarterly figures may not add up to annual.

P/E TTM	NA
P/E F1	9.6
PEG F1	1.4
P/S TTM	0.4

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/27/2020. The reports text is as of 08/28/2020.

## Overview

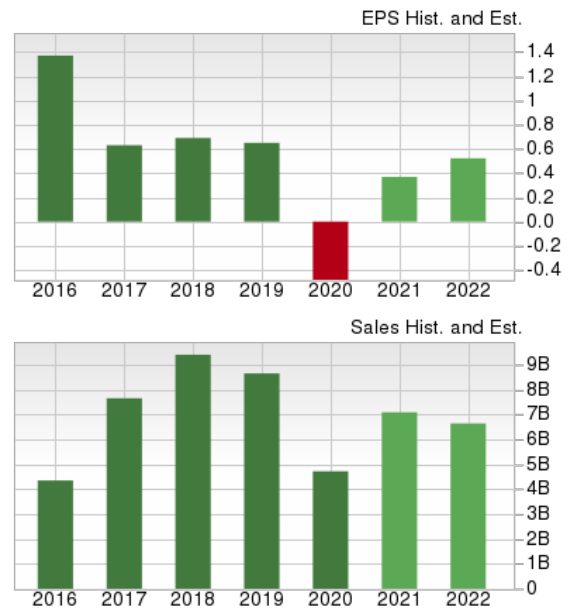
New York-based **Coty Inc.**, along with its subsidiaries, manufactures, markets, and distributes beauty products worldwide. The company sells its products through retailers, including hypermarkets, supermarkets, independent and chain drug stores and pharmacies, upscale perfumeries, upscale and mid-tier department stores, nail salons, specialty retailers, duty-free shops and traditional food, and drug and mass retailers. It also markets products under the Astor, Coty, Joop!, Jovan, Manhattan, and N.Y.C. New York Color brands.

On Jun 1, 2020 Coty entered into a definitive deal with KKR for the Professional and Retail Hair business of the former, which includes Wella, OPI, Clairol and ghd brands (collectively known as Wella). Per the deal, KKR will have a 60% stake in the separately managed business, whereas Coty will hold the remaining 40%.

The company recognizes its business into three divisions:

- **Luxury division** (39.2% of fiscal 2020 sales) is focused on prestige fragrances, premium skin care and premium cosmetics. Some of the brands under this segment include Burberry, Hugo Boss, Escada, Gucci, Chloe, Bottega Veneta, Marc Jacobs, MiuMiu, Tiffany, Davidoff, Alexander McQueen, Balenciaga, Lacoste and Calvin Klein among others.
- **Consumer Beauty division** (60.8% of fiscal 2020 sales) is focused on color cosmetics, retail hair coloring and styling products, mass fragrance, mass skin care and body care. The segment includes brands such as Nautica, Jovan, Enrique, Cover Girl, Clairol, Max Factor, Mexx, Risque, Stetson, Sally Hansen, Adidas, Beckham and Beyonce among others.
- **Corporate division**

Additionally, in connection with the company's acquisition of the P&G Beauty Business, Coty reorganized its geographical structure into three regions: North America (Canada and the United States), Europe and ALMEA (Asia, Latin America, the Middle East, Africa and Australia).



## Reasons To Buy:

▲ **Transformation Plans on Track:** Coty is on course to turn around its operations. Coty's latest move in this regard is its strategic alliance with KKR, including an immediate investment of \$750 million by KKR. On Jun 1, Coty entered into a definitive deal with KKR for the Professional and Retail Hair business of the former, which includes Wella, OPI, Clairol and ghd brands (collectively known as Wella) valuing the business for an enterprise value of \$4.3 billion. Per the deal, KKR will have a 60% stake in the separately managed business, whereas Coty will hold the remaining 40%. The deal is expected to be closed by the end of 2020. This is likely to boost the company's balance sheet.

Coty is on track with transformation efforts. The company's latest move in this regard includes its strategic alliance with KKR.

The company is on track with building and streamlining operations, upgrading systems, optimizing manufacturing and logistics, and simplifying overall operations. Simultaneously, it is focused on investing in brands and transforming digital capabilities to drive sustainable growth. Prudent promotional tactics are an important part of the company's efforts to build brands. Coty has eliminated many of the supply-chain hurdles that limited its performance in the past. Further, the company is on track with efforts to revive the Consumer Beauty business. In this context, it divested its 60% stake in Younique in September 2019. Also, the company had earlier unveiled plans to explore alternatives for its Brazilian operations. The review process also includes intentions of a divestiture. Apart from these, Coty is on track to balance and strengthen its portfolio by staying tuned to the evolving consumer demand. Toward this end, it is making efforts to expand its exposure toward skincare, Northern Asia and e-commerce, while seeking scope for more brand-building investments.

▲ **Cost-Saving Efforts:** Management is committed to optimizing the overall cost structure. Incidentally, with its fourth-quarter fiscal 2020 results, management announced that it expects to generate about one-third savings from its fixed cost-reduction program of \$600 million by the end of fiscal 2021. Notably, the company has lowered its third-party costs, people on people expenses as well as non-working advertising and consumer promotion spends. Also, Coty is on track with reducing its capital expenditures. In fact, management anticipates returning to profit in the first quarter of fiscal 2021, in terms of adjusted operating income from continuing operations.

▲ **Strategic Acquisitions Aid Top Line:** Coty has made several strategic acquisitions to enhance its brand portfolio. On Jun 29, the company announced partnership with one of the most influential celebrity—Kim Kardashian West. Per the deal, Coty will buy a 20% ownership stake in Kim Kardashian's beauty business for \$200 million. The partnership is aimed at introducing new beauty categories and expanding into new product lines for the beauty business. The agreement is expected to be closed in third-quarter fiscal 2021. Further, Coty acquired a 51% stake in King Kylie this January and entered into a deal to produce, promote, distribute and sell certain products of King Kylie. Apart from this, the company's buyout of the iconic Burberry brand, in the second quarter of fiscal 2018, has been yielding favorably. This acquisition has been supporting growth in the Luxury segment. Additionally, the company's buyout of Procter & Gamble Company's global fine fragrances, salon professional, cosmetics and retail hair color businesses, along with select hair styling brands (the P&G Beauty Business) in 2016 bodes well.

▲ **E-Commerce Strength:** While Coty saw soft sales in the fiscal fourth quarter due to coronavirus-led concerns, the company's e-commerce business was quite impressive. In fact the company is witnessing strong momentum as well as market share gains for its ecommerce business. In Americas segment the company saw solid e-commerce sell-out for both mass and prestige brands. Even in the EMEA segment Coty witnessed double to triple digit e-commerce sell-out growth in its prestige and mass businesses. Persistence of such trends is likely to aid the company's performance.

▲ **Debt Analysis:** Coty's net debt of \$7,848 million as of Jun 30, 2020, declined \$299.4 million on a sequential basis. Notably, this net debt reduction reflects \$750 million of proceeds from the floating of convertible preferred equity to KKR. The company's cash and cash equivalents as of Jun 30 amounted to \$308.3 million, while its short-term debt (including current portion of long-term debt) stood at \$188.3. During the fiscal fourth quarter, it repaid \$1,300 million of its revolving credit facility worth \$2,750 million.

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## Reasons To Sell:

- ▼ **COVID-19 Hurts Q4 Results:** Shares of Coty have slumped 68.2% year to date compared with the industry's decline of 25.6%. The company posted dismal fourth-quarter fiscal 2020 results, with both top and bottom lines deteriorating year over year and falling significantly short of the respective Zacks Consensus Estimate. In fact, the company reported adjusted loss in the quarter. Results were battered by the impacts of the coronavirus pandemic.

Coty's Consumer Beauty segment has been sluggish. Also, the company is reeling under coronavirus-led concerns.

Notably, Coty generated revenues from continuing operations of \$560.4 million which slumped 62.8%. Like for Like or LFL revenues tanked 59.7%. LFL revenues were down in all regions, with mass business seeing a 39% decline and the prestige business being down more than 70%. Results were marred by broad-based channel shutdowns in the fourth quarter. Further, adjusted loss from continuing operations came in at 46 cents per share, which compared unfavorably from earnings of 3 cents recorded in the year-ago period.

- ▼ **Soft Consumer Beauty Unit:** Coty's Consumer Beauty segment has been posting drab sales since the last few quarters. The segment continued to be under pressure in the fiscal fourth quarter of 2020, wherein revenues declined 55% year over year while LFL sales fell 48%. Revenues in the segment were hurt by absence of Younique's sales, which were included in the prior-year quarter. Also, reduced traffic in drugstores and mass retailers globally hampered results. Consumers' shifting preference for more important personal care products put pressure on the color cosmetic category. We believe that, persistence of this trend is likely to remain a concern for the company.
- ▼ **Currency Headwinds:** Coty is exposed to unfavorable foreign currency translations owing to the company's exposure to international markets. The weakening of foreign currencies against the U.S. dollar may compel the company to either raise prices or lower profit margins in locations outside the country. During the fourth quarter of fiscal 2020, currency translations negatively impacted revenues to the tune of 2%. Therefore, volatility in exchange rates pose formidable risks for the periods ahead.
- ▼ **Stiff Competition:** Coty faces competition from various products and product lines, in both domestic and international markets. The beauty and beauty-related products industry is highly competitive with the number of competitors and degree of competition varying widely from country to country. Worldwide, Coty competes against products sold to consumers by other direct-selling and direct-sales companies and through the Internet, and against products sold through the mass market and prestige retail channels.
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## Last Earnings Report

### Coty Posts Wider-Than-Expected Q4 Loss & Drab Sales

Coty came out with dismal fourth-quarter fiscal 2020 results, wherein both top and bottom lines slumped year over year and fell significantly short of the respective Zacks Consensus Estimate. In fact, the company reported adjusted loss in the quarter. Results were battered by the impacts of the COVID-19 pandemic.

Nonetheless, management noted that it has been witnessing considerable business improvements over the last two months and expects such trends to continue. Coty anticipates returning to profit in the first quarter of fiscal 2021, in terms of adjusted operating income from continuing operations. The company remains on track to balance and strengthen its portfolio by staying tuned to the evolving consumer demand. Toward this end, it is making efforts to expand its exposure toward skincare, Northern Asia and e-commerce, alongside keeping scope for more brand-building investments.

Coty is also taking robust steps to enhance financial leverage and on track to generate about one-third savings from its fixed cost-reduction program of \$600 million by the end of fiscal 2021.

Quarter Ending **06/2020**

Report Date	<b>Aug 27, 2020</b>
Sales Surprise	<b>-59.80%</b>
EPS Surprise	<b>-475.00%</b>
Quarterly EPS	<b>-0.46</b>
Annual EPS (TTM)	<b>-0.20</b>

### Quarter in Detail

Results from continuing operations reflect the total company results, excluding revenues and costs that are directly associated with the Wella business, which will be offloaded soon. Ongoing Coty results reflect the performance from continuing operations, together with some cost recovery anticipated under the Wella transitional service agreement (or Wella TSA).

Adjusted loss from continuing operations came in at 46 cents per share, which was significantly wider than the Zacks Consensus Estimate of a loss of 8 cents. Moreover, the bottom line deteriorated from earnings of 3 cents recorded in the year-ago period.

Coty generated revenues from continuing operations of \$560.4 million, which fell considerably short of the Zacks Consensus Estimate of \$1,394 million. Moreover, the top line slumped 62.8% year over year. Currency translations negatively impacted revenues to the tune of 2%. Like for Like or LFL revenues tanked 59.7%. LFL revenues were down in all regions, with mass business seeing a 39% decline and the prestige business being down more than 70%. Results were marred by broad-based channel shutdowns in the fourth quarter.

Adjusted gross margin from continuing operations nosedived from 60.8% to 40.6%, thanks to reduced volumes induced by the coronavirus outbreak. Also, higher excess and obsolescence expenses due to the soft demand, along with underutilization costs resulting from manufacturing plant closures, were deterrents.

Adjusted operating loss from continuing operations came in at \$335.3 million against adjusted operating income of \$126.2 million reported in the year-ago quarter. Adjusted operating loss for Ongoing Coty came in at \$322 million against income of \$139 million in the year-ago period.

### Channel-Wise Details (From Continuing Operations)

Luxury: Net revenues in the segment fell 71% to \$219.4 million, while LFL revenues declined 73%. Segment sales saw considerable pressure from several channel closures, such as departmental stores, specialty retailers, travel retail and perfumeries, for a significant part of the quarter. Though retailers have reopened stores, sales are still under pressure. Nevertheless, e-commerce accounted for about 30% of Luxury segment revenues in the quarter, given consumers' growing shift toward this mode of shopping amid the pandemic. Further, segment revenues were aided by Kylie Beauty sales inclusion.

Consumer Beauty: Consumer Beauty revenues declined 55% year over year to \$340.7 million while LFL sales fell 48%. Revenues were hurt by absence of Younique's revenues, which were included in the prior-year quarter. Also, reduced traffic in drugstores and mass retailers globally hampered results. Also, consumers' shifting preference for more important personal care products put pressure on the color cosmetic category. On the brighter side, e-commerce sell-out saw solid growth across brick & click as well as e-retailers, especially at Amazon. Markedly, e-commerce formed for about 10% of Consumer Beauty segment revenues in the quarter.

Corporate: Net revenues in the segment amounted to \$0.3 million compared with \$0.2 million in the year-ago period.

### Segment Results

Net revenues in Americas plunged 52.2% (down 51.5% on an LFL basis) year on year to \$264.8 million. Sales in EMEA dropped 68.2% (down 67.2% at LFL) year over year to \$211 million. Sales in the Asia Pacific region declined 59% (down 57.5% at LFL) year on year to \$84.6 million.

### Other Financial Updates

Coty ended fiscal 2020 with cash and cash equivalents of \$308.3 million. Notably, during the fourth quarter, the company repaid \$1,300 million of its revolving credit facility worth \$2,750 million. In fiscal 2020, Coty used net cash in operating activities of \$50.9 million. Free cash outflow during the same time frame was \$318.3 million. Markedly, Coty's net debt of \$7,848 million as of Jun 30, 2020, declined \$299.4 million on a sequential basis.

## Recent News

### Coty to Buy Stake in Kim Kardashian's Beauty Business – Jun 29, 2020

Coty announced partnership with one of the most influential celebrity with nearly 300 million followers on social media platforms—Kim Kardashian West. Per the deal, Coty will buy a 20% ownership stake in Kim Kardashian's beauty business for \$200 million. The partnership is aimed at introducing new beauty categories and expanding into new product lines for the beauty business. The agreement is expected to be closed in third-quarter fiscal 2021.

Per the agreement, Coty will focus on developing new products for the beauty business in skincare, personal care, hair care as well as nail categories. Meanwhile, Kim Kardashian and her team will assume creative responsibilities like product as well as communications initiatives. The products will be sold via renowned luxury beauty retailers as well as various online channels.

## Valuation

Coty shares are down 68.2% in the year-to-date period and 60.8% for the trailing 12-month period. Stocks in the Zacks sub-industry are down 25.6% and the Zacks Consumer Staples sector is down 4.1% in the year-to-date period. Over the past year, the Zacks sub-industry and sector are down 22.7% and 1.3%, respectively.

The S&P 500 index is up 9.5% in the year-to-date period and 21.7% in the past year.

The stock is currently trading at 9.28X forward 12-month earnings, which compares to 40.76X for the Zacks sub-industry, 20.3X for the Zacks sector and 23.36X for the S&P 500 index.

Over the past five years, the stock has traded as high as 29.77X and as low as 5.34X, with a 5-year median of 19.15X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$4.25 price target reflects 11.14X forward 12-month earnings.

The table below shows summary valuation data for COTY

Valuation Multiples - COTY					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	9.28	40.76	20.3	23.36
	5-Year High	29.77	40.76	22.37	23.36
	5-Year Low	5.34	19.65	16.63	15.25
	5-Year Median	19.15	24.86	19.58	17.58
P/S F12M	Current	0.4	4.77	9.62	3.81
	5-Year High	2.48	4.77	11.15	3.81
	5-Year Low	0.35	1.53	8.1	2.53
	5-Year Median	1.13	2.86	9.89	3.05
EV/EBITDA F12M	Current	10.1	26.8	34.88	13.55
	5-Year High	18.02	33.2	37.28	14.19
	5-Year Low	6.2	8.68	25.88	9.15
	5-Year Median	11.32	18.03	33.7	11.04

As of 08/27/2020

## Industry Analysis Zacks Industry Rank: Bottom 32% (171 out of 252)



## Top Peers

Company (Ticker)	Rec	Rank
Helen of Troy Limited (HELE)	Outperform	2
Nu Skin Enterprises, Inc. (NUS)	Outperform	1
The Estee Lauder Companies Inc. (EL)	Neutral	4
e.l.f. Beauty Inc. (ELF)	Neutral	3
Inter Parfums, Inc. (IPAR)	Neutral	3
L'Oreal SA (LRLCY)	Neutral	3
Revlon, Inc. (REV)	Underperform	5
Shiseido Co. (SSDOY)	Underperform	4

Industry Comparison Industry: Cosmetics				Industry Peers		
	COTY	X Industry	S&P 500	EL	HELE	SSDOY
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Outperform	Underperform
Zacks Rank (Short Term)	3	-	-	4	2	4
VGM Score	D	-	-	D	C	C
Market Cap	2.70 B	1.92 B	23.67 B	77.91 B	5.34 B	22.49 B
# of Analysts	7	3	14	12	3	2
Dividend Yield	0.00%	0.00%	1.64%	0.00%	0.00%	0.38%
Value Score	C	-	-	D	D	C
Cash/Price	0.45	0.06	0.07	0.07	0.02	0.04
EV/EBITDA	-3.36	14.43	13.33	25.96	25.81	14.92
PEG Ratio	1.43	3.06	3.05	3.56	3.32	NA
Price/Book (P/B)	1.07	2.80	3.18	19.66	4.37	4.85
Price/Cash Flow (P/CF)	7.67	20.57	12.81	33.55	20.95	18.36
P/E (F1)	9.68	40.32	21.68	45.30	21.68	76.10
Price/Sales (P/S)	0.42	2.47	2.50	5.45	3.05	2.47
Earnings Yield	10.45%	2.44%	4.43%	2.21%	4.61%	1.31%
Debt/Equity	3.14	0.43	0.74	1.24	0.30	0.32
Cash Flow (\$/share)	0.46	1.36	6.94	6.45	10.07	3.07
Growth Score	F	-	-	B	B	C
Hist. EPS Growth (3-5 yrs)	-15.60%	5.98%	10.41%	14.73%	8.72%	11.72%
Proj. EPS Growth (F1/F0)	176.79%	-4.92%	-4.94%	15.96%	4.66%	-56.98%
Curr. Cash Flow Growth	-71.21%	4.55%	5.22%	-8.37%	13.99%	22.67%
Hist. Cash Flow Growth (3-5 yrs)	17.39%	8.16%	8.50%	7.97%	4.22%	57.54%
Current Ratio	1.81	1.67	1.35	1.72	2.07	1.33
Debt/Capital	71.17%	34.92%	43.86%	55.36%	22.95%	24.30%
Net Margin	-15.89%	2.38%	10.25%	4.79%	9.81%	-0.03%
Return on Equity	-4.14%	7.54%	14.66%	34.57%	20.17%	3.13%
Sales/Assets	0.37	0.84	0.50	0.82	0.94	0.85
Proj. Sales Growth (F1/F0)	11.16%	-0.10%	-1.43%	6.14%	7.44%	-20.34%
Momentum Score	A	-	-	F	F	D
Daily Price Chg	-8.05%	-0.17%	0.43%	-0.12%	0.00%	-0.12%
1 Week Price Chg	-9.55%	-0.36%	-1.45%	-2.40%	-1.76%	2.62%
4 Week Price Chg	-7.33%	0.00%	3.75%	12.11%	11.31%	-0.45%
12 Week Price Chg	-26.86%	0.00%	3.95%	7.60%	16.32%	-12.15%
52 Week Price Chg	-62.14%	-6.25%	2.75%	6.29%	39.56%	-32.34%
20 Day Average Volume	8,344,950	54,072	1,887,168	1,406,630	121,922	129,689
(F1) EPS Est 1 week change	4.03%	0.00%	0.00%	-5.35%	0.00%	0.00%
(F1) EPS Est 4 week change	4.03%	0.00%	0.79%	-7.44%	0.00%	0.00%
(F1) EPS Est 12 week change	7.95%	0.00%	3.43%	-7.34%	25.08%	-45.39%
(Q1) EPS Est Mthly Chg	42.86%	0.00%	0.00%	-21.87%	0.00%	0.00%



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## 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.

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### 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	A
VGM Score	D

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.

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