

## Fossil Group (FOSL)

**\$7.94** (As of 01/07/20)

Price Target (6-12 Months): **\$8.50**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 01/06/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

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

**3-Hold**

Zacks Style Scores:

VGM:D

Value: B

Growth: F

Momentum: D

### Summary

Shares of Fossil have declined and underperformed the industry in the past three months. The company has been battling dismal sales trend, which persisted in the third quarter of 2019. The quarter continued to witness sluggishness in watches, leather and jewelry businesses. Results were dismal in the Americas and in Europe due to headwinds in the wholesale channel. Moreover, adverse impacts from currency fluctuations and business exits have been deterrents. These adversities are likely to persist in fourth-quarter 2019. Nevertheless, expansion in the connected watches category has been an upside. Also, the company is focused on product launches to bolster this unit. Fossil has been making investments to improve its digital operations. Additionally, it is on track with the New World Fossil initiative to boost efficiency.

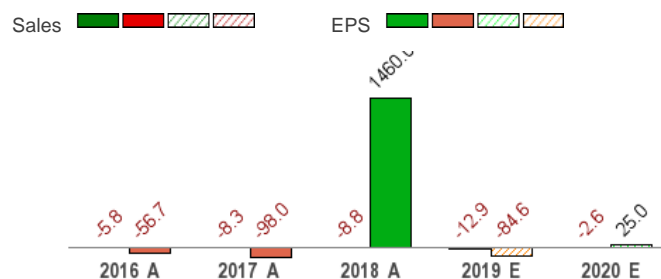
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$19.35 - \$6.83
20 Day Average Volume (sh)	1,035,728
Market Cap	\$401.1 M
YTD Price Change	0.8%
Beta	0.28
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<a href="#">Retail - Apparel and Shoes</a>
Zacks Industry Rank	Top 12% (30 out of 254)

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



Last EPS Surprise	-137.5%
Last Sales Surprise	-5.2%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/12/2020
Earnings ESP	0.0%
P/E TTM	19.9
P/E F1	52.9
PEG F1	NA
P/S TTM	0.2

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	450 E	488 E	521 E	697 E	2,156 E
2019	465 A	501 A	540 A	708 E	2,214 E
2018	569 A	577 A	609 A	787 A	2,542 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.20 E	-\$0.27 E	-\$0.73 E	\$0.94 E	\$0.15 E
2019	-\$0.42 A	-\$0.04 A	-\$0.15 A	\$0.73 E	\$0.12 E
2018	-\$0.99 A	\$0.17 A	\$0.19 A	\$1.01 A	\$0.78 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 01/07/2020. The reports text is as of 01/08/2020.

## Overview

Headquartered in Richardson, TX, **Fossil Group, Inc.** is a designer and manufacturer of clothing and accessories. The company's principal offerings include an extensive line of men's and women's fashion watches and jewelry (sold under proprietary and licensed brands), handbags, small leather goods, belts, sunglasses, neckwear, underwear, lounge wear, jewelry, gloves, hats, hosiery and socks.

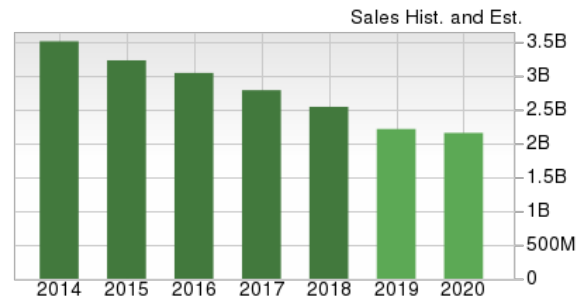
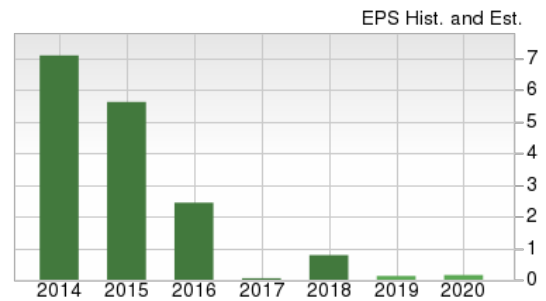
Their brands include Fossil, Relic, Abacus, Michele Watch & Now Coach NY, Skagen and Zodiac Watches. Fossil also makes watches for brands such as Adidas, Emporio Armani, Karl Lagerfeld, Michael Kors, Marc by Marc Jacobs, DKNY, Diesel and Armani Exchange.

Fossil also has multi-year licensing agreements for the production, sale and distribution of watches by several brands. These include Armani Exchange, Chaps, BMW, Diesel, DKNY, Michael Kors, Tory Burch, Marc Jacobs, Kate Spade New York, Puma and Emporio Armani.

Fossil's products are sold to department stores, specialty retail stores, and specialty watch and jewelry stores in the U.S. and in over 150 countries worldwide through 23 company-owned foreign sales subsidiaries and a network of approximately 70 independent distributors.

The company's operations are divided into three segments – **Americas** (46.2% of 2018 sales), **Europe** (33.7% of 2018 sales), **Asia** (19.9% of 2018 sales). Each unit includes the respective region's wholesale, retail and e-commerce activities. Product-wise, the company categorizes its sales numbers under watches, leathers, jewelry and other businesses.

Fossil operated 456 stores as of Jun 29, 2019, including 226 full-priced accessory stores and 223 outlet stores. Out of all Fossil stores, 202 are located in the Americas, while 165 and 89 are located in Europe and Asia, respectively.



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## Reasons To Buy:

- ▲ **Expansion in Wearables:** The introduction of wearable technology in watches has offered ample opportunity to Fossil to extend its reach of brands and offer customers new functionality with accessories, including activity trackers, hybrid watches and smart watches. Notably, the company is getting the advantage of Android's popularity and Google's technology in its watches. Fossil launched the latest generation Gen 5 watch during the third quarter.

The company's expansion plans in the wearables space, robust e-commerce performance and focus on New World Fossil Plan bode well.

Notably, connected watch sales constituted 16% of Fossil's total watch sales in the third quarter of 2019. Management had earlier projected that the wearable business is expected to grow \$32 billion by 2020. In fact, management expects connected watches to grow 20% annually over the next three to five years. The company's partnerships with Qualcomm and Google, and addition of new brands to its smartwatch line-up are likely to enrich Fossil's wearables portfolio. Further, the company joined hands with Citizen Watch Company to boost growth in its hybrid smartwatch category. Well, the wearables market provides Fossil the opportunity to combine fashion and technology and come up with exciting products to cater to consumers evolving needs of tech-enabled advanced connected gears. The company's wearables segment is adorned by renowned brands such as Diesel, Emporio Armani, Fossil, Michael Kors and Misfit.

- ▲ **Focus on Widening E-commerce Capabilities:** Fossil remains keen on expanding its digital platform and meet consumers growing demand for online purchasing. To this end, the company has been making several investments to improve digital marketing and drive online sales, both for the company's website as well as other online wholesale partners. In fact, such dedicated endeavors in the e-commerce space provided some cushion to Fossil's performance during the third quarter of 2019. In the said quarter, the company witnessed double digit growth in the e-commerce channel.

Notably, the e-commerce platform has also served as an important sales channel for wearables. Further, management is optimistic regarding the company's expansion plans in the smartwatch and other digital offerings category and expects such moves to further bolster online sales. Additionally, the company is on track with bolstering the buy online, pickup in store and ship from store capabilities.

- ▲ **New World Fossil Plan Bodes Well:** Fossil is on track with its New World Fossil ("NWF") Plan that was initiated in 2016. The program aims to transform the company, fuel efficiencies, improve margins, better manage revenues and enhance the overall operating structure of the business to drive profitability. Fossil Group intends to achieve these targets while simultaneously enriching customers' experience amid a difficult retail landscape.

As part of the NWF 1.0 transformation plan, Fossil is prioritizing consumer market and channel opportunities, revenue optimization, delivering gross margin and productivity savings. Notably, the NWF plan helped the company reduce expenses and aid gross margin in the second quarter of 2019. NWF 1.0 is expected to conclude in 2019, by the end of which the company expects to achieve run-rate savings of \$200 million. Also, it is on track with the New World Fossil 2.0 - Transform to Grow initiative that will help enhance efficiencies across the company. This along with solid free cash flow will provide the company with an opportunity to reinvest in innovation and digital initiatives. Markedly, Fossil earlier stated that it targets witnessing double-digit operating margin over the long term.

- ▲ **Diversified Fossil Brand & Licensing Agreements:** Fossil offers innovative and unique products to keep pace with emerging lifestyle and fashion trends. The brand name Fossil originated as a watch brand and later encompassed other accessory categories, including handbags, belts, small leather goods, jewelry, soft accessories, sunglasses and clothing. The company has diversified into new accessory product categories within the existing brands to further leverage its branded portfolio, given the significant consumer interest in the category. In this regard, the company introduced jewelry collections under the brands Diesel, DKNY, Emporio Armani, Fossil and Michael Kors brands after first establishing a market for the brands in watches. Also, the Skagen brand acquisition in August 2012 solidified Fossil's watch assortment. In fact, the aforementioned expansions in the wearable category further underscore Fossil's focus on diversification. Moreover in 2017, Fossil added several fitness applications to its digital products which have also been receiving positive response from consumers.

Additionally, to further expand the company's size and offerings, Fossil has signed various licensing agreements with several brands. The company has extended the licensing deals with two of its brands — Tory Burch and DKNY. Earlier, it had announced Puma and BMW as its new licensed watch brands. The company is on track with its plans to start distributing Puma and BMW watches in 2019. Further, with the renewal of Fossil's global licensing agreement with Michael Kors and Emporio Armani through 2024, the companies are able to expand the extensive line of watches and jewelry and explore other opportunities in the accessories category. The company also signed the global licensing agreement with Kate Spade & Company through 2025 and extended its global watch licensing agreement with Diesel through 2025. Further, it partnered with Ralph Lauren Corporation in 2015 to develop watches under the Chaps label, which will further enhance its watch portfolio.

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## Reasons To Sell:

▼ **Dismal Sales Trend to Linger:** Fossil has been battling soft sales, which have been declining year over year for a while. Continued softness in the company's traditional watch category has been the prime deterrent. In the third quarter of 2019, worldwide net sales fell 11% year over year, due to adverse currency impacts, store closures, business exits, low inventory liquidation and reduced sales in low-margin off-price channel. On a constant-currency (cc) basis, worldwide net sales fell 10% year over year. Sluggish trends across the company's segments affected the quarterly outcome. Region-wise, results were dismal in the Americas and in Europe due to headwinds in the wholesale channel.

Fossil has been witnessing soft sales in traditional watches for a long time now due to increased competition and rising demand for connected watches.

For 2019, Fossil expects net sales to decline in the range of 11-13% compared with the earlier expectation of 8-12% decline. This includes negative impacts of 2.5% stemming from business exits. For fourth-quarter 2019, the company expects net sales to be down 5-10%, including the negative impacts of approximately 1.8% from business exits. Such headwinds have put pressure on the stock that has plunged 25.5% in the past three months against the industry's growth of 12.2%.

▼ **Softness in Traditional Watches & Leathers and Jewelry Business:** Consumers' changing preferences and a tough retail landscape has been a hurdle for Fossil's business for a while now. Incidentally, Fossil has been witnessing soft sales in traditional watches for a long time now due to increased competition and rising demand for connected watches. Further, sales of leathers and jewelry have persistently been weak since past few quarters on account of soft demand.

Well, these trends continued in third-quarter 2019, wherein jewelry and leather business sales fell 18.8% and 33.3%, respectively. Also, the company's watch sales dropped 8.6% due to sluggishness in the traditional watch category. Moreover, performance of mid-priced fashion watches continued to remain dismal. Though Fossil Group has been expanding its smartwatches and wearable portfolio, we believe it may take time for these efforts to completely offset the softness in the aforementioned categories.

▼ **Currency Headwinds:** Fossil's significant international presence keeps the company exposed to risks like adverse currency movements. In fact, currency woes adversely impacted Fossil's net sales during the third quarter. Moreover, the bottom line in the reported quarter was negatively impacted by 4 cents due to adverse currency fluctuations. Currency headwinds are likely to hit net sales by 1.6% in the fourth quarters and by 2% in 2019.

▼ **Government Regulations:** Fossil faces the risk of import restrictions such as antidumping or countervailing duties, tariffs or other restrictions, as most of its products are manufactured overseas. This has a negative impact on prices in the U.S. and other countries where the company's products are primarily sold.

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## Last Earnings Report

### Fossil Posts Q3 Loss, Y/Y Revenue Decline

Fossil Group released third-quarter 2019 results, wherein adjusted loss of 15 cents per share declined considerably from adjusted earnings of 19 cents in the prior-year quarter. Also, the bottom line compared unfavorably with the Zacks Consensus Estimate of earnings of 40 cents. The metric was affected by unfavorable taxes and reduced operating profits. Further, the bottom line was negatively impacted by 4 cents due to adverse currency fluctuations.

Worldwide net sales of \$539.5 million declined 11% from the prior-year quarter's figure due to adverse currency impacts, store closures, business exits, low inventory liquidation and reduced sales in low-margin off-price channel. On a constant-currency (cc) basis, worldwide net sales fell 10% year over year. The top line also missed the Zacks Consensus Estimate of \$565 million. Further, net sales were hurt by headwinds in the wholesale channel across the Americas and Europe. This more than offset sales growth witnessed in Asia.

Global retail comps declined 2% due to softness in Americas e-commerce and declines in full-price stores, which more than offset positive comps in Americas outlet stores as well as e-commerce in Asia and Europe. Based on product categories, weak comps in leather and jewelry more than offset positive comps in watches.

Fossil's gross margin contracted 200 basis points (bps) to 51.6%, courtesy of higher inventory valuation adjustments, foreign-currency headwinds and factory cost absorption related to lower sales volumes.

The company posted an operating loss of \$9.2 million against operating income of \$22.7 million in the year-ago quarter. The decline was caused by reduced sales and gross margin as well as adverse currency impacts.

### Performance of Business Categories

Category wise, sales in the watches segment declined 8.6% year over year to \$445 million in the quarter. Sales in the leather and jewelry businesses fell 18.8% year on year to \$54 million and 33.3% to \$28 million, respectively. Sales in the other businesses came in at \$12 million, down 14.3% on a year-over-year basis.

### Region-Wise Performance

Sales dropped 18% in the Americas to \$220 million, while it declined around 16% in Europe to \$174 million.

Net sales from Asia increased 9% to \$143 million driven by strong watch category and e-commerce channel performance in Mainland China, India and Korea.

### Other Updates

At the end of the quarter, the company had cash and cash equivalents of \$147.5 million, long-term debt of \$242.1 million and shareholders' equity of \$509.9 million.

The company operated 454 stores as of Sep 28, 2019, including 226 full-priced accessory, 6 full-priced multi-brand and 222 outlet stores. Out of all Fossil stores, 202 are located in the Americas, 162 are in Europe and 90 are in Asia.

### 2019 Guidance

For 2019, Fossil expects net sales to decline in the range of 11-13% compared with the earlier expectation of 8-12% decline. This includes negative impacts of 2.5% and 2% stemming from business exits and currency movements, respectively. The company now expects gross margin in the range of 51-52% compared with the previous expectation of 52-53%. Operating margin is now anticipated to be 1-1.7% compared with the prior view of 2.5-3.5%. Interest expenses are projected to be nearly \$30 million.

### Q4 Forecasts

For fourth-quarter 2019, the company expects net sales to decline 5-10%, considering the negative impacts of approximately 1.8% from business exits and around 1.6% due to unfavorable currency movements. Gross margin is predicted to be 49-51%. Interest expenses are expected to be nearly \$7 million.

### Growth Plans

The company is committed to transform its business to keep pace with consumers' changing preferences. In this context, it plans to launch new products under the traditional and connected watch categories. The company also intends to increase investments in e-commerce. Management expects favorable yields from the New World Fossil 2.0 Transform to Grow initiative.

Quarter Ending **09/2019**

Report Date	Nov 06, 2019
Sales Surprise	-5.22%
EPS Surprise	-137.50%
Quarterly EPS	-0.15
Annual EPS (TTM)	0.40

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## Valuation

Fossil shares are down 51.2% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 25.2%, whereas stocks in the Zacks Retail – Wholesale sector are up 19% the past year.

The S&P 500 index is up 24.6% in the past year.

The stock is currently trading at 0.19X forward 12-month sales, which compares to 0.61X for the Zacks sub-industry, 1.07X for the Zacks sector and 3.48X for the S&P 500 index.

Over the past five years, the stock has traded as high as 1.38X and as low as 0.1X, with a 5-year median of 0.39X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$8.5 price target reflects 0.2X forward 12-month sales.

The table below shows summary valuation data for FOSL

Valuation Multiples - FOSL					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	0.19	0.61	1.07	3.48
	5-Year High	1.38	1.31	1.1	3.48
	5-Year Low	0.1	0.55	0.8	2.54
	5-Year Median	0.39	0.82	0.9	3
P/B TTM	Current	0.79	3.21	5.17	4.43
	5-Year High	5.4	6.49	5.82	4.45
	5-Year Low	0.42	2.66	3.58	2.85
	5-Year Median	1.41	4.72	4.79	3.6
EV/EBITDA TTM	Current	6.53	8.74	15.28	11.99
	5-Year High	14.91	9.29	15.3	12.86
	5-Year Low	3.68	4.76	10.27	8.48
	5-Year Median	6.4	6.92	12.32	10.67

As of 01/07/2020

## Industry Analysis Zacks Industry Rank: Top 12% (30 out of 254)



## Top Peers

Genesco Inc. (GCO)	Outperform
Signet Jewelers Limited (SIG)	Outperform
Chicos FAS, Inc. (CHS)	Neutral
Capri Holdings Limited (CPRI)	Neutral
Guess?, Inc. (GES)	Neutral
Tiffany & Co. (TIF)	Neutral
Tapestry, Inc. (TPR)	Neutral
Movado Group Inc. (MOV)	Underperform

Industry Comparison Industry: Retail - Apparel And Shoes				Industry Peers		
	FOSL Neutral	X Industry	S&P 500	CHS Neutral	GCO Outperform	TIF Neutral
<b>VGM Score</b>	<b>D</b>	-	-	<b>C</b>	<b>A</b>	<b>F</b>
Market Cap	401.10 M	881.94 M	23.82 B	468.55 M	698.70 M	16.03 B
# of Analysts	1	3	13	5	2	10
Dividend Yield	0.00%	0.00%	1.8%	8.86%	0.00%	1.74%
<b>Value Score</b>	<b>B</b>	-	-	<b>B</b>	<b>A</b>	<b>D</b>
Cash/Price	0.37	0.12	0.04	0.28	0.08	0.03
EV/EBITDA	5.85	8.43	13.92	7.16	8.27	17.28
PEG Ratio	NA	1.58	2.00	NA	2.24	2.61
Price/Book (P/B)	0.79	1.85	3.32	0.86	1.22	5.10
Price/Cash Flow (P/CF)	3.58	6.72	13.58	3.82	6.52	20.59
P/E (F1)	52.73	13.70	18.86	NA	11.18	28.73
Price/Sales (P/S)	0.17	0.51	2.63	0.23	0.32	3.65
Earnings Yield	1.89%	6.78%	5.30%	-3.54%	8.94%	3.48%
Debt/Equity	1.04	1.07	0.72	1.15	1.27	0.59
Cash Flow (\$/share)	2.22	1.60	6.94	1.04	7.29	6.49
<b>Growth Score</b>	<b>F</b>	-	-	<b>D</b>	<b>A</b>	<b>D</b>
Hist. EPS Growth (3-5 yrs)	-56.82%	-0.46%	10.56%	-28.91%	-8.06%	4.46%
Proj. EPS Growth (F1/F0)	25.00%	4.51%	7.49%	-145.16%	29.57%	0.69%
Curr. Cash Flow Growth	25.00%	9.92%	14.83%	-29.00%	-54.21%	10.63%
Hist. Cash Flow Growth (3-5 yrs)	-24.59%	0.23%	9.00%	-16.86%	-4.79%	3.95%
Current Ratio	2.06	1.44	1.23	1.09	1.34	4.10
Debt/Capital	51.00%	53.51%	42.92%	53.51%	55.85%	37.06%
Net Margin	0.10%	2.74%	11.08%	-1.23%	-1.74%	12.41%
Return on Equity	3.84%	10.96%	17.16%	-1.37%	10.98%	16.98%
Sales/Assets	1.43	1.33	0.55	1.37	1.34	0.73
Proj. Sales Growth (F1/F0)	-2.60%	1.01%	4.15%	-5.01%	-18.01%	-0.04%
<b>Momentum Score</b>	<b>D</b>	-	-	<b>C</b>	<b>D</b>	<b>C</b>
Daily Price Chg	1.66%	0.23%	-0.22%	0.51%	-0.15%	-0.01%
1 Week Price Chg	0.78%	0.00%	-0.30%	-0.26%	-1.51%	-0.01%
4 Week Price Chg	5.73%	0.44%	2.11%	-4.82%	-8.79%	0.13%
12 Week Price Chg	-27.62%	8.57%	5.70%	12.86%	21.59%	46.78%
52 Week Price Chg	-57.52%	-8.75%	22.84%	-36.90%	-5.11%	53.65%
20 Day Average Volume	1,035,728	275,832	1,570,747	1,935,960	294,817	1,524,645
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.00%	0.00%	-1.52%
(F1) EPS Est 12 week change	-91.07%	0.00%	-0.53%	5.41%	6.12%	-3.17%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	5.47%	-1.26%



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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	<b>B</b>
Growth Score	<b>F</b>
Momentum Score	<b>D</b>
VGM Score	<b>D</b>

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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