

Papa Johns(PZZA)

\$66.53 (As of 01/24/20)

Price Target (6-12 Months): **\$70.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 12/06/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: D

Growth: B

Momentum: D

Summary

Shares of Papa John's have outperformed the industry in the past year. The impressive performance can be primarily attributed to continued international expansion plans, strategic partnerships, strong digital platform and various sales initiatives. Notably, Papa John's is committed to develop and maintain a strong franchise system. However, Papa John's expects 2019 adjusted earnings per share within \$1.00-\$1.20, indicating a decline from \$1.34 in 2018. Earnings for the current year are likely to be affected by lower operating profit, higher costs pertaining to technology and softer revenues in its International segment due to currency headwinds. Moreover, estimates for the current year and 2020 have witnessed downward revisions over the past 60 days, reflecting analyst concern regarding the company's earnings growth potential.

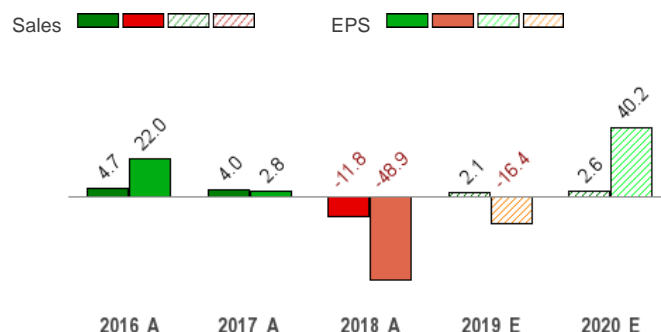
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$67.11 - \$38.29
20 Day Average Volume (sh)	564,500
Market Cap	\$2.1 B
YTD Price Change	5.4%
Beta	0.41
Dividend / Div Yld	\$0.90 / 1.4%
Industry	Retail - Restaurants
Zacks Industry Rank	Top 33% (84 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-8.7%
Last Sales Surprise	4.1%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/25/2020
Earnings ESP	0.0%
P/E TTM	70.0
P/E F1	42.4
PEG F1	3.4
P/S TTM	1.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	413 E	414 E	413 E	422 E	1,648 E
2019	398 A	400 A	404 A	405 E	1,606 E
2018	427 A	408 A	364 A	374 A	1,573 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.41 E	\$0.45 E	\$0.33 E	\$0.42 E	\$1.57 E
2019	\$0.31 A	\$0.28 A	\$0.21 A	\$0.31 E	\$1.12 E
2018	\$0.50 A	\$0.49 A	\$0.20 A	\$0.15 A	\$1.34 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 01/24/2020. The reports text is as of 01/27/2020.

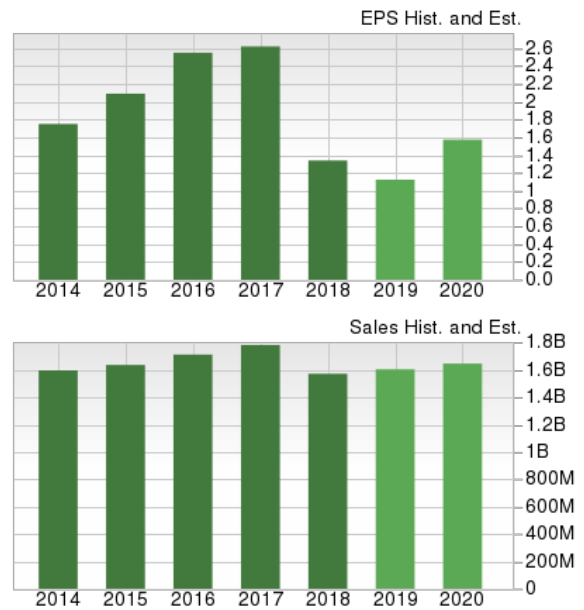
Overview

Headquartered in Louisville, KY, Papa John's began its operations in 1984. This Delaware Corporation, operates and franchises pizza delivery and carryout restaurants in the United States and other specific international markets. The company's dine-in and delivery restaurants operate under the brand name Papa John's.

As of Dec 30, 2018, there were 5,303 Papa John's restaurants operating in all 50 states, and 46 international countries and territories. Out of these restaurants, 645 were company-owned while the remaining 4,658 were franchised restaurants.

Papa John's reportable segments include domestic company-owned restaurants, domestic commissaries, North America franchising and international operations. North America encompasses operations in the United States and Canada. Domestic incorporates the adjoining areas of the United States. International franchisees are defined as all franchise operations outside of the United States and Canada.

Papa John's has been reeling under negative publicity for quite a long time, owing to the denouncement of its ex-CEO, John H. Schnatter, on grounds of a racial slur. Ever since Papa John's have been trying to make significant changes in its board and is trying to revive consumer sentiment.



Reasons To Buy:

▲ **Assistance Program & Changes in Board Aims to Revive Sales Slump:** Papa John's has been reeling under negative publicity for quite a long time, owing to the denouncement of its ex-CEO on grounds of a racial slur. In order to revive its brand image and reinvigorate growth, the company has been taking numerous initiatives, which started to resuscitate the falling consumer sentiment.

Papa John's is making significant changes in its board. The company recently extended its board to appoint Jeffrey C. Smith, CEO of Starboard, and Anthony M. Sanfilippo, former Chairman and CEO of Pinnacle Entertainment, as new directors. Additionally, Papa John's president and CEO, Rob Lynch was appointed to the board. In fact, with the proceeds from this partnership, Papa John's is confident to strengthen its balance sheet and make investments and retain its brand image. The company also announced a partnership with Shaquille O'Neal, the NBA Hall of Famer, Entrepreneur and restaurateur. All in all, Papa John's added six new directors in 2019.

During second quarter, O'Neal invested in nine of Papa John's restaurants in Atlanta. These nine restaurants will undergo remodeling and feature O'Neal's personalized designs. The design in the front of the building will have the signature of the legendary NBA champion and television sports analyst. The company, which launched its better day campaign featuring Shaquille O'Neal in September, has a great potential to attract customers and influence its brand image.

Meanwhile, in addition to board enhancement, Papa John's announced an assistance program for its U.S. and Canada franchisees. The program is expected to offer advice on the sales and operating challenges that Papa John's franchisees are facing, with full support from the Company's Franchise Advisory Council ("FAC") and Papa John's Franchise Association ("PJFA"). Under the assistance program, the company plans to reduce royalties, food-service pricing and online fees throughout the current year. The company is also arranging funds for its franchisees to implement marketing and reimagining initiatives. On Jun 19, 2019, Papa John's announced the increment of intended investments in marketing and brand building. The company will also provide the previously planned financial assistance to its domestic franchisees, whose franchise agreement will end in 2020.

▲ **Strong Brand Building in Focus:** Papa John's is a leading take-out and pizza delivery restaurant chain in the world. As part of its clean label commitment, Papa John's was the first pizza delivery chain to announce the removal of preservatives such as BHA and BHT, flavor enhancer, MSG, cellulose, partially hydrogenated oils and high-fructose corn syrup. All these efforts reinforce the company's commitment to provide quality food and deliver better ingredients to its customers, and thereby living up to its strong brand commitment.

▲ **International Expansion & Focus on Franchising:** Many of Papa John's restaurants are located in international markets like Europe, the Middle East, Latin America and China and continue to perform strongly. The China region continues to experience growth, driven by the company's optimized restaurant model, brand design enhancements and increased integration with third-party aggregators that is broadening its accessibility channels. Papa John's has inked developmental agreements in many regions including Mexico, Egypt, Russia, Spain, Chile, the Netherlands, Colombia and Boston. It also debuted in France and Israel in the past year and in Morocco in 2017. Meanwhile, the company plans to open five units in the Bahamas by 2021. During the third quarter, it opened 15 restaurants in North America and exited 38, with the global restaurant count being 5,343. Additionally, it opened its first restaurant in Portugal. The company is presently operating in 49 countries and territories on a worldwide basis.

Notably, Papa John's is committed to develop and maintain a strong franchise system. The company is continually striving to eliminate barriers to expansion in existing international markets and identify new market opportunities. Notably, during the last reported quarter, it re-franchised 21 company-owned restaurants — including 19 in Georgia — for \$5.6 million. Over the next several years, the company plans to increase its international units, a large portion of which will be franchised. We believe re-franchising a large chunk of its system reduces a company's capital requirements and facilitates earnings per share growth and ROE expansion. Alongside, free cash flow continues to grow, allowing reinvestment for increasing brand recognition and shareholder return.

▲ **Capitalizing on Technology to Boost Sales:** Papa John's is investing heavily in technology-driven initiatives like digital ordering to boost sales. The company's online and digital marketing activities have increased significantly over the past several years in response to increasing use of online and mobile web technology. In fact, Papa John's continues to reinforce its commitment toward providing a better customer experience with enhancements to its digital ordering process. The company further expanded its digital ordering capabilities with the launch of Facebook Instant Ordering and became the first national pizza chain to do so. It is also the foremost national restaurant chain to launch a custom ordering app for Apple TV, commence a nationwide digital rewards program and surpass 60% of the total U.S. sales via digital channels. Currently, the company has 100 corporate and franchise restaurants that enable customers to visually track delivery on a map. Notably, Papa John's announced that it has entered into a national partnership with UberEATS, and its existing fastest-growing door-to-door delivery service providers DoorDash and Postmates.

Meanwhile, Papa John's continues to invest in direct customer delivery. Delivery currently covers 1,000 U.S. restaurants and has nearly doubled from the last quarter.

▲ **Comps Growth Back on Track:** Although the company posted mixed third-quarter 2019 results, the biggest takeaway from the quarter was positive comparable sales growth, which was recorded by Papa John's for the first time in two years. Global restaurant sales were up 2.3%, comparing favorably with the year-ago quarter's fall of 6.6%. Also, domestic company-owned restaurant comps were up 2.2% in the reported quarter against a 13.2% decline in the year-ago quarter.

The company's continued international expansion plans, strategic partnerships, strong digital platform and various sales initiatives bode well

Reasons To Sell:

- ▼ **Currency Headwinds:** Papa John's has a considerable international presence, which exposes it to risks of fluctuations in currency exchange rates. As the U.S. dollar continues to show strength against various other currencies, the negative currency impact is likely to continue to hurt revenues.
- ▼ **Affordable Care Act to Hurt Profits:** The Affordable Care Act, commonly known as Obamacare, is expected to have an adverse impact on restaurant operators. The Affordable Care Act required employers to extend health benefits. The law entails restaurants with 100 or more full-time equivalent employees to offer health care coverage to substantially all full-time employees and their dependents. Meanwhile, from 2016, these rules apply for employers with 50 to 99 full-time-equivalent employees. Moreover, the collapse of the Republican-led bill, which was intended to replace Obamacare, means that the Affordable Care Act is here to stay. This means that the restaurant operators will have to continue shouldering increased labor costs, which in turn will hurt margins.
- ▼ **Cutthroat Competition:** The restaurant space is highly competitive as numerous restaurant operators are ongoing advanced and prudent strategies to increase their sales. In fact, going by the current retail scenario, adapting to shifting demand has become a major precedence for retailers. Companies with continual digital innovation, focus on product customization, and launch and delivery of seamless consumer experience can only thrive in the competitive space. This puts a lot of pressure on Papa John's to continuously change its strategies in correspondence to the fickle consumer demand.
- ▼ **Soft International Performance a Concern:** The company has been generating soft revenues over the last several quarters in the International segment. During the first, second and third quarters of 2019, its revenues declined 14.8%, 12.3% and 3.8%, respectively. Papa John's, which has a significant international presence, is exposed to unfavourable fluctuations in currency. Also, the International segment's revenues are hurt by the same.
- ▼ **Valuation Looks Stretched:** Papa John's valuation looks a bit stretched compared with the industry average. Looking at the company's forward 12-month price-to-earnings (P/E) ratio, which is one of the most commonly used valuation ratios and is best suited for evaluating restaurants, investors might not want to pay any further premium. It currently has a forward 12-month P/E ratio of 41.6. Hence, the stock is relatively overvalued right now compared with its peers, as the industry's average P/E is 23.25.

High costs along with a challenging sales environment remain potent headwinds

Last Earnings Report

Papa John's Q3 Earnings Miss

Papa John's International, reported mixed third-quarter 2019 results, wherein earnings missed the Zacks Consensus Estimate but revenues surpassed the same. However, the biggest takeaway from the quarter was positive comparable sales growth, which was reported by the company for the first time in two years.

Its adjusted earnings of 21 cents per share lagged the Zacks Consensus Estimate of 23 cents by 8.7%. However, the bottom line increased 10.5% from the year-ago figure.

Revenues totaled \$403.7 million, which outpaced the Zacks Consensus Estimate of \$388 million.

The top line also increased 5% on a year-over-year basis. This upside can be attributed to positive comparable sales achieved by the company in North America for the first time in two years.

During the third quarter, it opened 15 restaurants in North America and exited 38, with the global restaurant count being 5,343. Additionally, it opened its first restaurant in Portugal. Notably, the company is presently operating in 49 countries and territories worldwide. It re-franchised 21 company-owned restaurants, which include 19 in Georgia, for \$5.6 million.

Global Restaurant Sales & Comps

In the third quarter, global restaurant sales moved up 2.3% against the year-ago quarter's fall of 6.6%. Excluding foreign currency impact, global restaurant sales rose 3.3% versus the year-ago quarter's decline of 5.9%.

Domestic company-owned restaurant comps were up 2.2% in the reported quarter versus a 13.2% decline in the year-ago quarter.

At North America franchised restaurants, comps rose 0.6% against a decline of 8.6% in third-quarter 2018. Also, comps at system-wide North America restaurants moved up 1% against 9.8% decline recorded in the year-ago quarter.

Comps at system-wide international restaurants were up 1.6% against a decline of 3.3% in the prior-year quarter.

Operating Highlights

Total operating income was \$4.9 million in the third quarter against operating loss of \$14.2 million in the year-ago period. Total costs and expenses amounted to \$400.5 million, up 0.3% from third-quarter 2018.

Balance Sheet

As of Sep 29, 2019, cash and cash equivalents totaled \$28.4 million compared with \$33.3 million on Dec 30, 2018. Long-term debt was \$346.1 million at the end of third-quarter 2019 compared with \$601.1 million at 2018-end.

Inventories at the end of the reported quarter declined to \$25.2 million from \$27.2 million on Dec 30, 2018. Free cash flow at the end of third-quarter 2019 summed \$15.8 million compared with \$74.4 million at 2018-end.

The company paid out cash dividends of \$10.5 million in third-quarter 2019 and declared fourth-quarter cash dividend of approximately \$10.6 million.

2019 Guidance

Papa John's expects adjusted earnings per share (EPS) within \$1-\$1.20, indicating a decline from \$1.34 in 2018. North America comps are now expected to decline 1.5-3.5% compared with the prior guidance of 1-4% decrease. International comps are anticipated to be flat to up 2% compared with 3% expected earlier. Capital expenditure for 2019 is still expected in the range of \$45-\$50 million. Additionally, net global unit growth is anticipated in the band of 85-115 units compared with earlier expectation of 100-150 units due to temporary slowdown of openings in Russia and Spain.

Quarter Ending **09/2019**

Report Date	Nov 06, 2019
Sales Surprise	4.13%
EPS Surprise	-8.70%
Quarterly EPS	0.21
Annual EPS (TTM)	0.95

Recent News

Papa John's on Expansion Spree, Opens Restaurant in Portugal- Sep 23, 2019

In a bid to drive sales, Papa John's continues to expand its global footprint. Recently, the company opened a restaurant in Portugal. This new restaurant is situated in Lisbon, in the Amoreiras zone.

Notably, the latest restaurant was opened under Papa John's master franchise, Drake Food Service International, in the Iberian Peninsula, Chile, Panamá, and Costa Rica. The latest move underscores Papa John's two basic strategies of continual international expansion and increased focus on franchising.

Papa John's Fortifies Franchise Relations to Revive Sales — Jun 19, 2019

Papa John's announced a program under which it is increasing intended investments in marketing and brand building. The company will also provide the previously planned financial assistance to its domestic franchisees, whose franchise agreement will end in 2020. Beginning the third quarter of 2019, it will invest an additional \$80 million for the long-term support of its brand and franchisees.

The program is supported by the company's elected Franchise Advisory Council (FAC). Through the program, Papa John's further plans to strengthen the partnership with its franchisees and provide them with investment resources as was promised in the agreement. The company will assist domestic franchisees in forms of lower royalties, royalty-based service incentives and targeted relief. It is also arranging funds for its franchises to implement marketing and reimagining initiatives.

Valuation

Papa John's shares are up by 56% over the trailing 12-month period. Over the past year, the Zacks sub-industry and sector are up 18.9% and 16.6%, respectively.

The S&P 500 index is up 23.9% in the past year.

The stock is currently trading at 41.6x forward 12-month Price to Earnings value, which compares with 25.11x for the Zacks sub-industry, 25.09x for the Zacks sector and 18.94x for the S&P 500 index.

Over the past five years, the stock has traded as high as 56.18x and as low as 18.04x, with a 5-year median of 28.3x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$70 price target reflects 43.75x forward 12-month Price to Earnings value.

Valuation Multiples - PZZA					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	41.6	25.11	25.09	18.94
	5-Year High	56.18	26.41	26.23	19.33
	5-Year Low	18.04	20.45	19.07	15.17
	5-Year Median	28.3	23.25	22.95	17.44
P/S F 12M	Current	1.29	3.62	1.07	3.52
	5-Year High	1.86	3.85	1.11	3.52
	5-Year Low	0.76	2.91	0.8	2.54
	5-Year Median	1.26	3.25	0.91	3
P/CF	Current	87.66	17.44	14.39	23.11
	5-Year High	87.66	20.39	15.17	23.11
	5-Year Low	9.54	8.5	10.73	11.78
	5-Year Median	18.32	16.5	12.85	16.26

As of 01/24/2020

Industry Analysis Zacks Industry Rank: Top 33% (84 out of 255)



Top Peers

BJs Restaurants, Inc. (BJRI)	Neutral
Dunkin Brands Group, Inc. (DNKN)	Neutral
Jack In The Box Inc. (JACK)	Neutral
Dave & Busters Entertainment, Inc. (PLAY)	Neutral
Red Robin Gourmet Burgers, Inc. (RRGB)	Neutral
RESTAURANT GRP (RSTGF)	Neutral
The Wendys Company (WEN)	Neutral
Carrols Restaurant Group, Inc. (TAST)	Underperform

Industry Comparison Industry: Retail - Restaurants				Industry Peers		
	PZZA Neutral	X Industry	S&P 500	DNKN Neutral	RRGB Neutral	WEN Neutral
VGM Score	C	-	-	D	D	C
Market Cap	2.13 B	434.02 M	24.13 B	6.49 B	450.18 M	5.08 B
# of Analysts	5	5.5	13	12	5	10
Dividend Yield	1.35%	0.00%	1.78%	1.91%	0.00%	2.17%
Value Score	D	-	-	D	B	D
Cash/Price	0.01	0.03	0.04	0.09	0.04	0.09
EV/EBITDA	33.15	14.86	14.02	19.81	12.99	10.04
PEG Ratio	3.37	2.16	2.03	2.18	5.16	3.06
Price/Book (P/B)	NA	3.02	3.30	NA	1.23	7.82
Price/Cash Flow (P/CF)	23.40	11.84	13.52	21.84	3.83	19.21
P/E (F1)	42.07	22.16	18.92	23.75	49.84	34.52
Price/Sales (P/S)	1.35	0.93	2.65	4.79	0.34	3.03
Earnings Yield	2.36%	4.45%	5.28%	4.21%	2.01%	2.90%
Debt/Equity	-1.46	0.94	0.72	-5.47	1.82	5.62
Cash Flow (\$/share)	2.84	1.53	6.94	3.59	9.09	1.15
Growth Score	B	-	-	C	D	B
Hist. EPS Growth (3-5 yrs)	-10.52%	7.71%	10.60%	13.28%	-15.50%	15.49%
Proj. EPS Growth (F1/F0)	40.04%	8.26%	7.59%	5.46%	-4.12%	8.11%
Curr. Cash Flow Growth	-35.21%	7.73%	13.90%	7.69%	-5.58%	16.17%
Hist. Cash Flow Growth (3-5 yrs)	-2.72%	6.24%	9.00%	6.16%	4.85%	-3.14%
Current Ratio	0.88	0.63	1.22	1.62	0.38	2.00
Debt/Capital	NA%	61.12%	42.99%	NA	64.57%	84.90%
Net Margin	-0.43%	3.14%	11.35%	17.54%	-0.82%	7.69%
Return on Equity	-12.34%	8.47%	17.10%	-38.96%	4.89%	24.72%
Sales/Assets	2.28	1.17	0.55	0.37	1.14	0.34
Proj. Sales Growth (F1/F0)	2.63%	3.14%	4.03%	3.27%	-2.58%	7.03%
Momentum Score	D	-	-	F	D	C
Daily Price Chg	-0.58%	-0.45%	-1.01%	-0.80%	-0.03%	-0.50%
1 Week Price Chg	0.35%	1.65%	2.29%	1.66%	5.88%	0.35%
4 Week Price Chg	2.29%	1.75%	1.02%	5.63%	15.08%	-0.23%
12 Week Price Chg	13.63%	1.92%	6.85%	-0.33%	14.07%	4.30%
52 Week Price Chg	45.58%	0.32%	20.39%	10.07%	6.00%	27.17%
20 Day Average Volume	564,500	196,336	1,536,379	529,243	247,922	1,992,792
(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%	0.05%	-5.42%	-0.14%
(F1) EPS Est 12 week change	-2.69%	0.15%	-0.23%	1.04%	-31.23%	-0.42%
(Q1) EPS Est Mthly Chg	-0.81%	0.00%	0.00%	-0.35%	2.42%	4.29%

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	D
Growth Score	B
Momentum Score	D
VGM Score	C

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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