

Shopify Inc. (SHOP)

\$767.00 (As of 05/15/20)

Price Target (6-12 Months): **\$805.00**

Long Term: 6-12 Months | **Zacks Recommendation:** **Neutral**
 (Since: 03/30/20)
 Prior Recommendation: Underperform

Short Term: 1-3 Months | **Zacks Rank:** (1-5) **2-Buy**
 Zacks Style Scores: **VGM:F**
 Value: D | Growth: F | Momentum: F

Summary

Shopify delivered stellar first-quarter results. The top line benefited from growth in the number of merchants and increased buying of essentials due to COVID-19 induced lockdowns. Moreover, robust performance of Shopify Shipping, Shopify Payments and Shopify Capital are key catalysts. The company continues to launch merchant-friendly applications to cater to the demands of a dynamic retail environment, thereby bolstering merchant base. Initiatives aimed at international expansion also remain noteworthy. Notably, shares have outperformed the industry in the past year. However, increasing investments on product development and platform are likely to limit margin expansion in the near term. Moreover, the company suspended its guidance for 2020 due to COVID-19 induced uncertainties prevailing in the market.

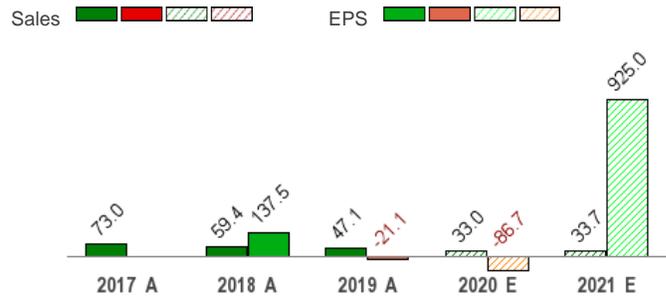
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$774.79 - \$262.17
20 Day Average Volume (sh)	4,603,979
Market Cap	\$89.9 B
YTD Price Change	92.9%
Beta	1.51
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Services
Zacks Industry Rank	Top 11% (28 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	205.6%
Last Sales Surprise	5.9%
EPS F1 Est- 4 week change	0.4%
Expected Report Date	NA
Earnings ESP	33.2%
P/E TTM	861.8
P/E F1	19,175.0
PEG F1	525.3
P/S TTM	52.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	604 E	634 E	675 E	875 E	2,806 E
2020	470 A	475 E	506 E	657 E	2,099 E
2019	320 A	362 A	391 A	505 A	1,578 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	-\$0.01 E	\$0.06 E	\$0.13 E	\$0.43 E	\$0.41 E
2020	\$0.19 A	-\$0.06 E	\$0.02 E	\$0.26 E	\$0.04 E
2019	\$0.09 A	\$0.14 A	\$0.13 A	\$0.43 A	\$0.30 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 05/15/2020. The reports text is as of 05/18/2020.

Overview

Ottawa, Canada-based Shopify Inc. (SHOP) provides a multi-tenant, cloud-based, multi-channel commerce platform for small and medium-sized businesses (SMBs). The company completed Initial Public Offering (IPO) in May 2015.

Merchants use the company's software to run business across various sales channels, including web and mobile storefronts, physical retail locations, social media storefronts, and marketplaces.

Shopify's platform enables merchants to manage products and inventory, process orders and payments, ship orders, build customer relationships and leverage analytics along with reporting from one integrated back office.

Moreover, Shopify hosts a huge database of merchant and customer interactions. Merchants leverage this transactional dataset to get meaningful insight into the sales channel growth prospects and consumer behavioral aspects. This improves their ability to target prospective customers more easily, which drives sales growth.

Apart from the company's own payment solution, payment wallets like Apple Pay, Google Pay is also available to the merchants, which they offer to customers for completing transaction done on the Shopify platform.

In 2019, revenues came in at \$1.578 billion. The company generates revenues from two sources: Subscriptions Solutions (40.7% of 2019 revenues) and Merchant Solutions (59.3%).

Subscription revenue is recognized on a ratable basis over the contractual term. The terms range from monthly, annual or multi-year subscription terms. The company earns revenue based on the services it delivers either directly to merchants or indirectly through resellers.

Shopify generates the majority of merchant solutions revenue from fees that it charges merchants on their customer orders processed through Shopify Payments.

The company also derives merchant solutions revenue relating to Shopify Shipping, Shopify Capital, other transaction services and referral fees, as well as from the sale of Point-of-Sale (POS) hardware.



Reasons To Buy:

- ▲ According to market research firm eMarketer, global retail eCommerce sales (excluding travel, restaurant and event ticket sales) are expected to increase to \$893.4 trillion by 2022, which will make up 14.8% of total retail spending. We believe that the massive growth in eCommerce spending bodes well for Shopify. The company's cloud-based platform is well-positioned to address the growing needs of merchants at a time when social media, mobile devices and data analytics are transforming the eCommerce market place.
- ▲ Shopify's biggest USP lies in the fact that it is a brand oriented platform as compared with an online marketplace. Here, the brand hogs the limelight, which helps the merchant win customer much faster through focused interaction. The platform helps in improving customer's brand loyalty, which drives merchant revenues. Further, we note that Shopify hosts a huge database of merchant and customer interactions. Merchants leverage this transactional dataset to get meaningful insight into the sales channel growth prospects and consumer behavioral aspects. This improves their ability to target prospective customers more easily, which drives sales growth. Management noted that merchants on average became more successful on Shopify, as number of merchants with GMV exceeding \$1 million grew 44% in 2019. In first-quarter 2020, GMV of \$17.4 billion surged 46% on a year-over-year basis. The company's plan to invest on leveraging this transactional data will further enhance merchant's ability to attract customers going ahead. We believe that the company's merchant focus strategy will aid it to dominate the SMB eCommerce market in the long run.
- ▲ Moreover, the company continues to add functionality to its platform, which is responsible for driving merchant base. The launch of Shopify Payments, Shipping and Capital have made it easier for merchants to process payments, ship products and secure financing for their working capital needs, respectively. Notably, the percentage of merchants using Shopify Payments grew every quarter throughout 2019. The company has introduced Shopify Payments across 15 countries to date. Moreover, merchant adoption of Shopify Shipping continues to expand in both the U.S. and Canada. Management anticipates this trend to continue as the company expands shipping partners and add new features. Further, Shopify is well poised to benefit from robust adoption of Fraud Protect and Shopify Email solutions. Shopify is also working on extending language capabilities beyond English. In fact, Shopify reported merchant base of 29% from outside of core geography (with significant non-English-speaking population) in 2019, comparing favorably with 24% in 2018. Further, the company recently rolled out Shopify Fulfillment Network in the United States, for the first time, to facilitate commerce. On Oct 17, 2019, Shopify concluded the acquisition of 6 River Systems. The deal is anticipated to boost growth of the company's fulfillment network. We believe that its merchant focus business model will help it to achieve its growth target in the long haul.
- ▲ Notably, net new merchants on Shopify are expected to improve as newly added sales channels like Google Pay, Facebook Messenger, Instagram, Pinterest, eBay and Amazon continues to attract new merchants. Shopify noted that the addition of Houzz, Wanelo, eBates and others has driven the number of channels over which a merchant can sell to more than a dozen. The company also noted that merchants are buying more apps through app store, which is positive. Shopify app store currently offers around 4,100 apps. Moreover, availability of Apple Pay and addition of Canada Post are some other notable developments that will boost merchant base. We also believe that the company's strong partner referral system will boost merchant base that will eventually drive top-line growth in 2020. More than 26,400 partners referred merchants to Shopify in the past 12 months.
- ▲ Shopify has a rich partner ecosystem, which is a growth driver. The company noted that the Monthly Recurring Revenue (MRR) per merchant surged 35% year over year to \$55.4 million as of Mar 31, 2020, primarily on strong growth in Shopify Plus subscription base. The company's plan to offer variable pricing structure under Shopify Plus is also prudent move, in our view.
- ▲ Mobile focus provides significant leverage to Shopify. The company launched its iPhone-based Shopify Mobile application way back in 2010. Also, the company released Shopify Ping for Apple's iOS devices, which is compatible with Facebook and Instagram ads and is enabled for Apple Business Chat. Mobile traffic to merchants' stores continued to grow, reaching 80% of traffic and garnered 68% of orders for the quarter ended Dec 31, 2019, up from 78% and 66%, respectively, reported in the year-ago quarter. We note that Shopify is benefiting from retail's rapid transition to mobile and social sales channels. We believe that this rapid growth presents significant opportunities for Shopify in the long term. In fact, Shopify platform garnered GMV of approximately \$2.9 billion in the Black Friday-Cyber Monday period in 2019. Notably, year-ago GMV figure in the same period stood at \$1.8 billion. Management noted that around two thirds of online orders from the U.S.-based Shopify merchants were registered via mobile devices.
- ▲ Shopify has a strong balance sheet with ample liquidity position and no debt obligations. As of Mar 31, 2020, Shopify had cash, cash equivalents and marketable securities balance of \$2.360 billion compared with \$2.455 billion on Dec 31, 2019. Increasing liquidity trend reflects that the company is making investments in the right direction. Since it carries no long-term debt, the cash is available for pursuing strategic acquisitions and investment in other growth initiatives.

Shopify's focus on developing merchant base, international expansion, addition of new functionalities, rich partner ecosystem and mobile focus are key catalysts.

Reasons To Sell:

- ▼ Shopify is relatively a new player in the eCommerce marketplace. Although it is not a direct competitor to behemoths like Alibaba and Amazon, many of its customers are. This presents significant risk for its growth prospects.
- ▼ Moreover, the company focuses on the SMB segment which is more susceptible to macro-economic headwinds and makes the business challenging.
- ▼ Furthermore, lack of big-shot international customers is a headwind for Shopify. The company doesn't have significant presence in the Asia-Pacific market, which is fastest growing retail eCommerce market according to eMarketer. This is a major deterrent in our view.
- ▼ We believe that increasing investments on product development, Shopify Plus and cloud infrastructure will make it difficult for the company to sustain profitability. Moreover, it expects to further increase research & development (R&D) expense. Markedly, management intends to invest \$1 billion over the subsequent five years to develop the new fulfillment network, which is likely to impact margin expansion. We also note that Shopify has been incurring losses in the last three years and has an accumulated deficit of \$335.7 million as of Mar 31, 2020. Despite the improving top line, mounting losses might dent investors' optimism.
- ▼ The company is trading at premium in terms of Price/Book (P/B). Shopify currently has a trailing 12-month P/B ratio of 29.57X, which compares unfavorably with what the industry witnessed over the last year. Hence, valuation looks slightly stretched from P/B perspective.

Shopify's focus on SMB segment, lack of international exposure, increasing operation expenses and stretched valuation are primary negatives.

Last Earnings Report

Shopify Q1 Earnings Surpass Estimates

Shopify reported first-quarter 2020 adjusted earnings of 19 cents per share, which surged 216.7% on a year-over-year basis.

Total revenues increased 47% from the year-ago quarter's figure to \$470 million.

The top line benefited from growth in the number of merchants as more of them joined the Shopify platform due to COVID-19 induced lockdowns. Moreover, growth was driven by increased buying of essentials in the first quarter due to the pandemic.

Quarter Ending **03/2020**

Report Date	May 06, 2020
Sales Surprise	5.94%
EPS Surprise	205.56%
Quarterly EPS	0.19
Annual EPS (TTM)	0.89

Quarter in Detail

Subscription Solutions revenues (39.9% of total revenues) surged 34% to \$187.6 million driven by persistent growth in Monthly Recurring Revenue (MRR) due to the addition of new merchants. Moreover, strong app growth and Shopify Plus variable platform fee revenue growth were positives.

As of Mar 31, MRR was \$55.4 million, up 35% from the year-ago quarter's tally. Shopify Plus accounted for \$15.3 million, representing 29% of MRR compared with 26% in the quarter ended Mar 31, 2019.

Merchant Solutions revenues (60.1%) advanced 57% to \$282.4 million, primarily on growth in Gross Merchandise Volume (GMV) that improved 46% from the year-ago quarter's figure to \$17.4 billion.

Shopify Capital advanced \$162.4 million cash to merchants in the reported quarter, surging 85% compared with \$87.8 million in the year-ago quarter. Since the launch of Shopify Capital, cumulative merchant cash advances have increased to \$1.05 billion, out of which \$192 million was outstanding as of Mar 31.

Shopify Shipping witnessed robust adoption in the fourth quarter. The offering is being leveraged by 46% of total eligible merchants across the United States and Canada.

Gross Payments Volume (GPV) came in at \$7.3 billion, accounting for 42% of GMV processed in the first quarter and up from \$4.9 billion (41%) in the prior-year quarter.

Notable Developments

More new merchants signed in to Shopify Fulfillment Network in the first quarter of 2020 compared with previous quarters since its launch in June 2019. Moreover, Shopify opened a R&D Centre in Ottawa, Canada to test new robotics and fulfillment technologies as well as fulfill Canada-based orders in the first quarter.

Further, the company's strong partner referral system is expected to boost merchant base that will drive the top line in 2020. More than 26,400 partners referred merchants to Shopify in the past 12 months.

The company also joined the Libra Association, which is currently collaborating to build a simple, inclusive and global cryptocurrency, proposed by social media giant — Facebook.

Operating Details

Non-GAAP gross profit (adjusted for amortization of acquired intangibles) surged 44% year over year to \$263.8 million. This can be attributed to robust performance of Shopify Plus merchants as well as efficiencies in hosting costs and better payment margins.

Non-GAAP gross margin contracted 100 basis points (bps) from the year-ago quarter's level to 56%.

Non-GAAP operating expenses surged 48.6% year over year to \$271.1 million.

Non-GAAP operating expenses, as a percentage of revenues, expanded 100 bps year over year to 58%.

Shopify reported adjusted operating loss of \$7.3 million against operating profit of \$300K in the year ago quarter. The deterioration was caused by higher operating expenses pertaining to the acquisition of 6 River Systems, more brand spend and an increase in the allowance for potential losses related to Shopify Payments and Capital to account for the impact of COVID-19.

Balance Sheet & Cash Flow

As of Mar 31, 2020, Shopify ended the reported quarter with cash, cash equivalents and marketable securities balance of \$2.360 billion compared with \$2.455 billion as of Dec 31, 2019.

Net cash used in operations was \$85 million in the reported quarter compared with cash flow of \$70.6 million in the prior quarter.

Refrains From Providing Guidance

Shopify reaffirmed the suspension of its guidance for 2020. On Apr 1, the company had suspended its guidance for the year due to COVID-19 induced uncertainties prevailing in the market. Citing the same, the company refrained from providing second-quarter guidance as well.

Recent News

On May 12, Shopify announced the launch of contactless payment hardware for Canadian retailers using Shopify POS. This includes the Shopify Tap & Chip Card Reader, Shopify Tap & Chip Case and Shopify Retail Kit.

On May 4, Shopify rolled out new point of sale (POS) system to help integrate online and in-person sales in a bid to aid merchants in staying abreast of evolving commerce practices, in the wake of tough retail environment.

On Apr 28, Shopify launched Shop — a shopping assistant app — to aid merchants boost customer experience and sales on the platform.

On Apr 17, Shopify stock gained 12.2%, following the company's chief technology officer's Jean-Michel Lemieux tweet on Apr 16, stating that Shopify platform is "now handling Black Friday level traffic every day" and predicting more growth backed by more online sales triggered by the coronavirus outbreak. Notably shares were up 5.9% on Apr 16.

On Apr 1, Shopify provided an update on impact of COVID-19 on its business. Despite the economic crisis triggered by COVID-19, the company anticipates reporting revenues and adjusted operating financials for the first quarter within or ahead of the guided range provided on Feb12, 2020, driven by momentum witnessed in January and February. For first-quarter 2020, Shopify had guided revenues in the range of \$440-\$446 million. In the first quarter, the company anticipates adjusted operating loss to be in the range of \$30 to \$34 million. However, the company has withdrawn guidance for full year 2020, owing to uncertainty.

On Mar 30, Shopify introduced Shopify Capital in the U.K., with an aim to aid eligible merchants with cash advances amid the coronavirus-induced crisis.

On Feb 21, Shopify announced that it is joining Facebook's ambitious crypto-currency venture, Libra. The company is becoming a member of the Libra Association, in a bid to co-develop a payment network which makes money transfer easy to support both merchants and consumers, and facilitate commerce.

Valuation

Shopify shares are up 93% in the year-to-date period and 177.3% over the trailing 12-month period. Stocks in the Zacks sub-industry are up 3.7% while the Zacks Computer & Technology sector is down 0.9% in the year-to-date period. Over the past year, the Zacks sub-industry is down 1.5%, while the sector is up 11.3%.

The S&P 500 index is down 10.9% in the year-to-date period and up 0.2% in the past year.

The stock is currently trading at 37.96X forward 12-month sales, which compares to 6.26X for the Zacks sub-industry, 3.54X for the Zacks sector and 3.24X for the S&P 500 index.

Over the past three years, the stock has traded as high as 37.96X and as low as 9.04X, with a 3-year median of 13.33X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$805 price target reflects 39.85X forward 12-month sales.

The table below shows summary valuation data for SHOP

Valuation Multiples - SHOP					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	37.96	6.26	3.54	3.24
	3-Year High	37.96	11.51	3.59	3.44
	3-Year Low	9.04	5.01	2.62	2.76
	3-Year Median	13.33	7.02	3.21	3.16
P/B TTM	Current	29.57	4.97	4.97	3.91
	3-Year High	29.57	7.12	5.38	4.56
	3-Year Low	6.85	3.85	3.58	3.03
	3-Year Median	10.89	5.34	4.58	3.92
EV/Sales TTM	Current	50.68	5.98	4	2.79
	3-Year High	50.68	10.74	4.43	3.46
	3-Year Low	11.46	4.3	3.05	2.24
	3-Year Median	17.8	6.31	3.79	3

As of 05/15/2020

Industry Analysis Zacks Industry Rank: Top 11% (28 out of 254)



Top Peers

Company (Ticker)	Rec	Rank
ANGI Homeservices Inc. (ANGI)	Neutral	3
Autohome Inc. (ATHM)	Neutral	3
eBay Inc. (EBAY)	Neutral	2
Etsy, Inc. (ETSY)	Neutral	2
Groupon, Inc. (GRPN)	Neutral	3
Square, Inc. (SQ)	Neutral	3
Wix.com Ltd. (WIX)	Neutral	3
Zillow Group, Inc. (ZG)	Neutral	2

Industry Comparison Industry: Internet - Services				Industry Peers		
	SHOP	X Industry	S&P 500	EBAY	GRPN	WIX
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	2	3	3
VGM Score	F	-	-	A	A	C
Market Cap	89.91 B	586.91 M	18.98 B	29.51 B	616.16 M	10.06 B
# of Analysts	26	3	14	11	3	8
Dividend Yield	0.00%	0.00%	2.21%	1.52%	0.00%	0.00%
Value Score	D	-	-	B	A	F
Cash/Price	0.03	0.13	0.06	0.15	1.14	0.09
EV/EBITDA	-1,457.42	1.64	11.60	11.52	0.76	-227.86
PEG Ratio	518.80	2.21	2.58	1.09	NA	5.53
Price/Book (P/B)	29.57	2.22	2.59	13.95	1.55	48.43
Price/Cash Flow (P/CF)	NA	14.64	10.28	12.61	4.57	NA
P/E (F1)	19,361.16	29.01	19.01	13.57	NA	193.32
Price/Sales (P/S)	52.04	1.88	1.92	2.80	0.28	12.53
Earnings Yield	0.01%	1.16%	5.06%	7.36%	-15.60%	0.52%
Debt/Equity	0.04	0.10	0.75	3.87	0.54	1.73
Cash Flow (\$/share)	-0.60	0.10	7.01	3.34	0.24	-0.25
Growth Score	F	-	-	B	B	A
Hist. EPS Growth (3-5 yrs)	NA%	21.93%	10.82%	0.82%	NA	NA
Proj. EPS Growth (F1/F0)	-86.80%	9.09%	-10.48%	9.67%	-228.21%	-10.79%
Curr. Cash Flow Growth	85.89%	10.73%	5.68%	8.64%	-29.11%	-2,949.32%
Hist. Cash Flow Growth (3-5 yrs)	NA%	19.91%	8.52%	-6.76%	11.55%	11.92%
Current Ratio	9.45	1.70	1.27	1.34	1.08	1.72
Debt/Capital	4.15%	11.41%	44.25%	79.46%	35.23%	63.40%
Net Margin	-7.65%	-7.05%	10.54%	44.44%	-1.01%	-11.81%
Return on Equity	-2.56%	-3.82%	16.29%	63.44%	3.39%	-29.97%
Sales/Assets	0.55	0.62	0.54	0.55	1.50	0.77
Proj. Sales Growth (F1/F0)	33.16%	0.69%	-2.55%	-10.17%	-46.37%	23.79%
Momentum Score	F	-	-	B	C	C
Daily Price Chg	1.68%	0.00%	0.20%	0.18%	1.88%	6.43%
1 Week Price Chg	15.54%	5.07%	3.23%	7.39%	-3.33%	28.80%
4 Week Price Chg	45.70%	1.69%	0.88%	13.14%	26.16%	64.18%
12 Week Price Chg	43.21%	-9.24%	-23.26%	11.73%	-36.18%	42.42%
52 Week Price Chg	175.89%	-21.00%	-12.56%	12.99%	-69.00%	49.62%
20 Day Average Volume	4,603,979	120,065	2,553,422	13,027,094	12,006,196	989,625
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.41%	0.00%	-5.57%	4.39%	0.00%	-1.95%
(F1) EPS Est 12 week change	-12.33%	-12.37%	-16.22%	3.30%	-140.00%	-18.42%
(Q1) EPS Est Mthly Chg	1.73%	0.00%	-11.63%	10.06%	0.00%	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	D
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.

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