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## Profire Energy, Inc. (NASDAQ: PFIE)

August 8, 2022

### Buy: Revenue Better than Expected. Margins Pressured.

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Q2 revenue was better than expected, but margins were lower due to continued inflationary pressures and supply chain disruptions. We expect these issues to mitigate over time. We believe the company has significant leverage to higher prices in oil and natural gas and can grow revenue and EBITDA to much higher levels, driving substantial stock price appreciation.

Revenue of \$9.6 million was better than our \$9.3 million estimate, but cost increases pressured gross margins and operating expenses. EBITDA for the quarter was \$650 thousand, about half of our \$1.2 million estimate and lower than Q1's \$1.1 million. We expect cost pressures to continue through the rest of the year. We have increased our revenue estimates for this year and next, while lowering our EBITDA estimates.

Oil prices have declined recently from the Q2 WTI average of close to \$110 per barrel but remain at healthy levels relative to prices required by operators to drill and far above year-ago levels. Natural gas prices are significantly higher than year ago levels. The EIA's reference case estimates tight oil production in the U.S. will increase almost 25% from 2021 to 2025, and that is assuming wellhead prices of about \$65 per barrel. Also, EIA expects natural gas production from shale gas and tight oil plays to increase 14% from 2021 to 2025. This is based on Henry Hub spot prices declining to \$3.00 per million BTU from \$4.11 in 2021 and far below current prices of \$7.80. Also, the drilled but uncompleted inventory of wells has dropped over 50% since June of 2020 and is at the lowest level since 2014.

The Biden administration's animus towards oil and gas production and consumption has increased costs to consumers. Whether this is a sustainable policy supported by voters we will discover in November. Also, natural gas accounts for 38% of electricity generation in the U.S., and it will remain above 35% for then next decade even if the massive subsidies to solar and wind remain (a question mark if there is a change in control of Congress and/or the White House, and if budget deficits put these subsidies under closer scrutiny). The move to electric vehicles is still nascent and even optimistic consumer adoption projections will result in increased electricity demand and the necessity of robust natural gas production.

We remain bullish on Profire Energy given the company's dominant market share in burner management systems, its expansion into larger, more complex downstream markets, the continued strength in oil prices and the resulting growth in the North American rig count and well completions.

**Valuation:** Our price target of \$2.00 is based on an EV/Sales multiple of about 2x the 2022 revenue estimate of \$39.4 million. Our EV/sales target multiple is a discount to the 2.4x EV/sales multiple in 2018 when WTI averaged over \$65 per barrel. We believe the discount is warranted to reflect the risks of reaching our revenue estimate.

**Risks:** Risks to achieving our price target include changes in oil and gas prices, global economic growth and its impact on demand for oil and gas, regulation that could impact the ability to drill for oil and gas, and regulation that could impede the development of pipelines in the U.S.

Current Price	\$1.23		
Price Target	\$2.00		
<b>Estimates</b>	<b>F2021A</b>	<b>F2022E</b>	<b>F2023E</b>
<b>Revenues (\$000s)</b>	\$ 26,356	\$ 39,366 E	\$ 45,821
1Q March	\$ 5,092	\$ 9,503 A	\$ 11,391
2Q June	\$ 6,034	\$ 9,633 A	\$ 11,106
3Q September	\$ 6,943	\$ 9,633 E	\$ 11,106
4Q December	\$ 8,286	\$ 10,596 E	\$ 12,217
	<b>F2021A</b>	<b>F2022E</b>	<b>F2023E</b>
<b>EBITDA (\$000s)</b>	\$ (192)	\$ 3,821 E	\$ 7,734
1Q March	\$ (386)	\$ 1,109 A	\$ 1,748
2Q June	\$ 3	\$ 647 A	\$ 1,741
3Q September	\$ 113	\$ 840 E	\$ 1,822
4Q December	\$ 78	\$ 1,226 E	\$ 2,423
EV/Sales	1.6 x	1.1 x	0.9 x
EV/EBITDA	NM	10.8 x	5.3 x
<b>Stock Data</b>			
52-Week Range	\$0.88	-	\$1.59
Shares Outstanding (mil.)	47.0		
Market Capitalization (mil.)	\$58		
Enterprise Value (mil.)	\$41		
Debt to Capital	0%		
Cash (mil.)	\$17		
Cash/Share	\$0.35		
Average Three Months Trading Volume (K)	89		
Insider Ownership	23.0%		
Institutional Ownership	42.7%		
Short interest (mil.)	0.0%		
Dividend / Yield	\$0.00/0.0%		



## Q2 Results

Revenue of \$9.6 million was 4% better than our estimate but gross margin fell short. For the quarter gross margin was 45.7%, down from 47.9% in Q1. Service margins have been much lower than prior periods and product margins have also been below typical levels. We have assumed margins remain under trend for the rest of this year.

Operating expenses were also higher than we forecast. Part of the delta is accrual of compensation expenses, but the inflationary environment is the major driver of cost growth, and we have adjusted our estimates to reflect continue cost increases for the remainder of the year.

Actual v Estimates				
Q2 22	Actual	Est.	Delta	% Delta
Total Revenues	\$ 9,633	\$ 9,266	\$ 368	4%
Total COGS	5,230	4,619	611	13%
Gross Profit-Total	4,403	4,647	(244)	-5%
G&A	3,787	3,342	444	
R&D	362	323	39	
Depreciation	160	167	(7)	
Opex	4,308	3,833	476	12%
Operating income	\$ 95	\$ 814	\$ (719)	-88%
Interest and Other	217	99	119	
Pretax income	312	913	(601)	-66%
Taxes	27	237	(210)	
Net Income	\$ 285	\$ 675	\$ (391)	-58%
Basic Shares	47,092	47,200		
Diluted Shares	48,699	47,600		
Basic EPS	\$ 0.01	\$ 0.01	\$ (0.01)	-58%
Diluted EPS	\$ 0.01	\$ 0.01	\$ (0.01)	-59%
Operating Income	95	814	(719)	-88%
D&A	278	281		
Stock Comp	274	139		
EBITDA	\$ 647	\$ 1,234	\$ (587)	-48%
EBITDA Margin	6.7%	13.3%		

Source: Profire Energy and Dawson James Securities estimates

For this year and next we have increased our revenue estimates, but EPS and EBITDA projections are lower to reflect the lower gross margin assumption and higher operating expense forecast.

	2022E		2023E	
	Old	New	Old	New
Revenue (\$M)	\$ 38.2	\$ 39.4	\$ 44.1	\$ 45.8
EPS	\$ 0.06	\$ 0.04	\$ 0.11	\$ 0.10
EBITDA (\$M)	\$ 5.4	\$ 3.8	\$ 8.3	\$ 7.7

Source: Dawson James Securities estimates

**Outlook**

In the smaller and mid-size oilfield applications, demand for burner management systems are driven by the number of well completions, and to a lesser extent, by replacement demand and retrofit of existing wells. According to EIA data, in the U.S., the number of well completions in 2018 was almost 15,000, which fell to under 14,000 in 2019 and to 7,400 in 2020. However, well completions in 2021 increased 32% to 9,793.

We project revenue for Profire in 2022 of \$39.4 million, up from \$26.4 million in 2021. For 2023, we forecast revenue of \$45.8 million, based on stable oil and gas prices and continued improvement in drilling and completion activity. We believe Profire is in a better position than many of its competitors, with a strong balance sheet and positive cash flow. However, it remains at the mercy of oil prices, and its attempts to reduce its dependence on the upstream BMS market have met with limited success.

**Profire Energy, Inc. Comparable Group**

		Price	TEV (\$M)	FTM Sales (\$M)	EV/Sales	FTM EBITDA (\$M)	EV/EBITDA
CHX	ChampionX Corporation	\$ 20.72	\$ 4,814.2	\$ 3,776.2	1.27	\$ 670.7	7.2
CLB	Core Laboratories NV	16.35	990.1	530.7	1.87	75.8	13.1
BOOM	DMC Global Inc.	21.75	801.0	661.5	1.21	89.7	8.9
HTG-GB	Hunting PLC	£ 2.14	£ 286.1	£ 585.9	0.49	£ 55.0	5.2
LBRT	Liberty Energy, Inc. Class A	13.07	2,783.3	4,414.9	0.63	883.8	3.1
OIS	Oil States International, Inc.	4.72	480.6	786.9	0.61	86.0	5.6
	Median				1.01		7.2
PFIE	Profire Energy, Inc.	\$ 1.23	\$ 41.3	\$ 43.2	0.96	\$ 6.2	6.7

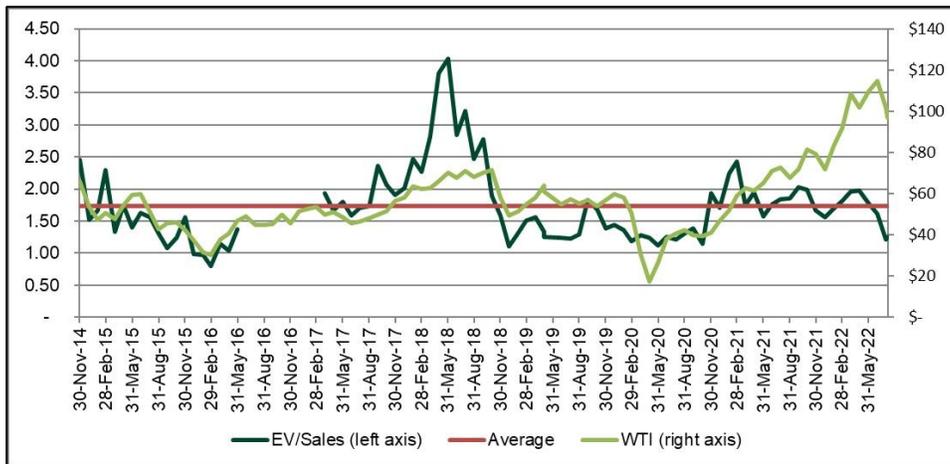
Source: FactSet and Dawson James Securities estimates.

If oil and natural gas prices remain firm, we expect the rig count, drilled wells, and completed wells will continue to increase and the outlook for Profire to improve. WTI is currently far above the average price in 2018 of \$65.23 and the average price in 2019 of \$56.99. The Baker Hughes U.S. rig count, however, at 764, remains about 25% below the average rig counts in 2018 and 2019. Energy Information Administration (EIA) data indicate the number of wells drilled fell 57% in 2020 and the number of completed wells fell 45%, compared to the 2018-2019 period. There was a 32% increase in completions in 2021 vs. 2020 but there is substantial room for improvement. The number of completed wells in Q1 2022 is 30% below its peak level in 2018.



Source: Baker Hughes, EIA

Profire's shares have moved up with the increase in oil prices, but the company's current EV/Sales is lower than levels achieved at much lower oil prices and we think there is further room for improvement.



Source: Dawson James Securities, EIA, Factset

**Valuation:**

Our price target of \$2.00 is based on an EV/Sales multiple of about 2x our 2022 revenue estimate of \$39.4 million. Our EV/sales target multiple is a discount to the 2.4x EV/sales multiple in 2018 when WTI averaged over \$65 per barrel. We believe the discount is warranted to reflect the risks of reaching our revenue estimate.

**Risk Analysis:**

Risks to achieving our price target include changes in oil and gas prices, global economic growth and its impact on demand for oil and gas, regulation that could impact the ability to drill for oil and gas, and regulation that could impede the development of pipelines in the U.S.

**Exhibit 1. Income Statement**

\$ in 000's except per share data	FY 19	FY 20	FY 21	Mar-22 Q1 22 A	Jun-22 Q2 22 A	Sep-22 Q3 22 E	Dec-22 Q4 22 E	FY 22E	FY 23E
Sales of Goods	36,208	19,396	23,691	8,878	8,861	8,861	9,747	36,347	42,147
Sales of Services	2,773	2,063	2,665	625	772	772	850	3,019	3,674
<b>Total Revenues</b>	<b>\$ 38,981</b>	<b>\$ 21,459</b>	<b>\$ 26,356</b>	<b>\$ 9,503</b>	<b>\$ 9,633</b>	<b>\$ 9,633</b>	<b>\$ 10,596</b>	<b>\$ 39,366</b>	<b>\$ 45,821</b>
Cost of Goods	17,588	10,378	12,826	4,383	4,530	4,430	4,873	18,216	20,274
Cost of Services	1,865	1,554	2,129	564	700	695	765	2,724	2,892
<b>Total COGS</b>	<b>19,453</b>	<b>11,932</b>	<b>14,955</b>	<b>4,946</b>	<b>5,230</b>	<b>5,126</b>	<b>5,638</b>	<b>20,940</b>	<b>23,166</b>
Gross Profit-Goods	18,620	9,017	10,865	4,496	4,331	4,430	4,873	18,130	21,873
Gross Profit-Services	908	509	536	61	73	77	85	296	783
<b>Gross Profit-Total</b>	<b>19,528</b>	<b>9,526</b>	<b>11,401</b>	<b>4,557</b>	<b>4,403</b>	<b>4,508</b>	<b>4,958</b>	<b>18,426</b>	<b>22,656</b>
G&A	13,454	10,641	11,533	3,392	3,787	3,687	3,737	14,602	14,846
R&D	1,933	1,299	1,120	308	362	377	392	1,440	1,659
Depreciation	977	666	762	167	160	160	160	646	638
Opex	16,364	12,606	13,416	3,868	4,308	4,223	4,288	16,688	17,143
<b>Operating income</b>	<b>3,164</b>	<b>(3,080)</b>	<b>(2,015)</b>	<b>689</b>	<b>95</b>	<b>284</b>	<b>670</b>	<b>1,738</b>	<b>5,512</b>
Interest and Other	403	421	334	99	217	217	217	750	869
Pretax income	3,567,561	(2,659)	(1,681)	788	312	501	887	2,488	6,381
Taxes	1,546	(484)	(629)	160	27	130	231	549	1,659
<b>Net Income</b>	<b>\$ 2,021</b>	<b>\$ (2,176)</b>	<b>\$ (1,052)</b>	<b>\$ 627</b>	<b>\$ 285</b>	<b>\$ 371</b>	<b>\$ 657</b>	<b>\$ 1,940</b>	<b>\$ 4,722</b>
Basic Shares	47,491	47,778	48,071	47,481	47,092	47,033	47,083	47,958	47,312
Diluted Shares	48,134	47,778	48,071	48,536	48,699	47,433	47,483	48,387	47,959
Basic EPS	\$ 0.04	\$ (0.05)	\$ (0.02)	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.04	\$ 0.10
Diluted EPS	\$ 0.04	\$ (0.05)	\$ (0.02)	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.04	\$ 0.10
Operating Income	3,164	(3,080)	(2,015)	689	95	284	670	1,738	5,512
D&A	1,467	1,177	1,256	281	278	281	281	1,121	1,124
Stock Comp	391	443	567	139	274	274	274	962	1,098
<b>EBITDA</b>	<b>\$ 5,022</b>	<b>\$ (1,460)</b>	<b>\$ (192)</b>	<b>\$ 1,109</b>	<b>\$ 647</b>	<b>\$ 840</b>	<b>\$ 1,226</b>	<b>\$ 3,821</b>	<b>\$ 7,734</b>
<b>WTI \$/barrel</b>	<b>\$ 56.98</b>	<b>\$ 39.12</b>	<b>\$ 68.09</b>	<b>\$ 95.18</b>	<b>\$ 108.72</b>	<b>\$ 101.38</b>			
	FY 19	FY 20	FY 21	Q1 22 A	Q2 22 A	Q3 22 E	Q4 22 E	FY 22E	FY 23E
Sales of Goods	92.9%	90.4%	89.9%	93.4%	92.0%	92.0%	92.0%	92.3%	92.0%
Sales of Services	7.1%	9.6%	10.1%	6.6%	8.0%	8.0%	8.0%	7.7%	8.0%
<b>Total Revenues</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>
Cost of goods	48.6%	53.5%	54.1%	49.4%	51.1%	50.0%	50.0%	50.1%	48.1%
Cost of services	67.3%	75.3%	79.9%	90.2%	90.6%	90.0%	90.0%	90.2%	78.7%
<b>Total COGS</b>	<b>49.9%</b>	<b>55.6%</b>	<b>56.7%</b>	<b>52.1%</b>	<b>54.3%</b>	<b>53.2%</b>	<b>53.2%</b>	<b>53.2%</b>	<b>50.6%</b>
Gross Profit-Goods	51.4%	46.5%	45.9%	50.6%	48.9%	50.0%	50.0%	49.9%	51.9%
Gross Profit-Services	32.7%	24.7%	20.1%	9.8%	9.4%	10.0%	10.0%	9.8%	21.3%
<b>Gross Profit-Total</b>	<b>50.1%</b>	<b>44.4%</b>	<b>43.3%</b>	<b>47.9%</b>	<b>45.7%</b>	<b>46.8%</b>	<b>46.8%</b>	<b>46.8%</b>	<b>49.4%</b>
G&A	34.5%	49.6%	43.8%	35.7%	39.3%	38.3%	35.3%	37.1%	32.4%
Payroll Expense	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Depreciation	2.5%	3.1%	2.9%	1.8%	1.7%	1.7%	1.5%	1.6%	1.4%
Opex	42.0%	58.7%	50.9%	40.7%	44.7%	43.8%	40.5%	42.4%	37.4%
<b>Operating income</b>	<b>8.1%</b>	<b>-14.4%</b>	<b>-7.6%</b>	<b>7.3%</b>	<b>1.0%</b>	<b>3.0%</b>	<b>6.3%</b>	<b>4.4%</b>	<b>12.0%</b>
Interest and Other	1.0%	2.0%	1.3%	1.0%	2.3%	2.3%	2.0%	1.9%	1.9%
Pretax income	9.2%	-12.4%	-6.4%	8.3%	3.2%	5.2%	8.4%	6.3%	13.9%
Tax Rate	43.3%	18.2%	37.4%	20.4%	8.7%	26.0%	26.0%	22.1%	26.0%
<b>Net Income</b>	<b>5.2%</b>	<b>-10.1%</b>	<b>-4.0%</b>	<b>6.6%</b>	<b>3.0%</b>	<b>3.9%</b>	<b>6.2%</b>	<b>4.9%</b>	<b>10.3%</b>
<b>EBITDA</b>	<b>12.9%</b>	<b>-6.8%</b>	<b>-0.7%</b>	<b>11.7%</b>	<b>6.7%</b>	<b>8.7%</b>	<b>11.6%</b>	<b>9.7%</b>	<b>16.9%</b>

Source: Profire Energy, Inc. and Dawson James Securities estimates

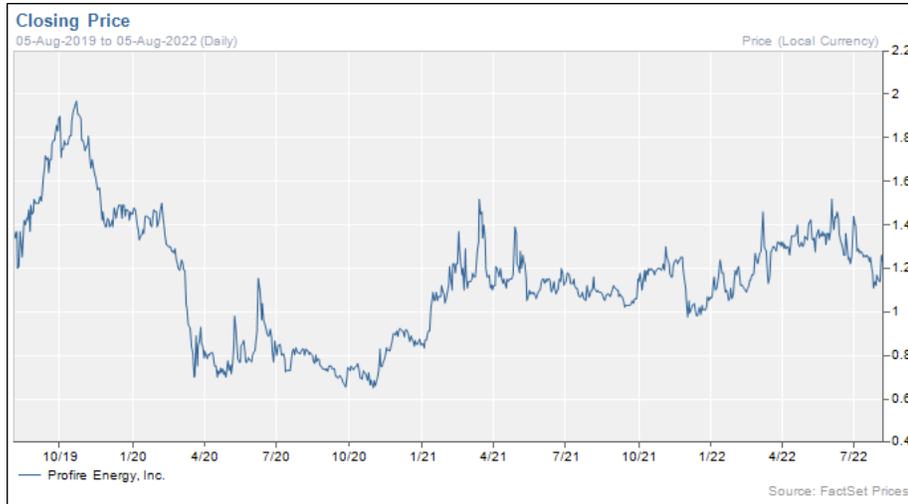
**Exhibit 2. Balance Sheet and Cash Flow Statement**

\$ in 000's	FY 19	FY 20	FY 21	FY 22E	FY 23E
Cash	7,359	9,148	8,188	10,392	14,939
ST Investments	3,822	2,389	1,014	463	463
A/R	5,598	3,720	6,263	7,064	8,145
Inventories	9,572	8,415	7,185	8,828	9,626
Prepaid Expenses & Other	1,750	2,165	1,586	1,301	1,499
<b>Current Assets</b>	<b>\$ 28,100</b>	<b>\$ 25,836</b>	<b>\$ 24,236</b>	<b>\$ 28,048</b>	<b>\$ 34,673</b>
LT Investments	7,400	6,064	8,260	8,619	8,619
Financing right of use asset	108	50	65	146	146
PP&E	12,071	12,022	11,186	10,487	10,362
Deferred Tax Asset	0	0	163	161	161
Intangible Assets	1,990	1,772	1,549	1,438	1,438
Goodwill	2,579	2,579	2,579	2,579	2,579
<b>Total Assets</b>	<b>\$ 52,248</b>	<b>\$ 48,323</b>	<b>\$ 48,038</b>	<b>\$ 51,479</b>	<b>\$ 57,979</b>
A/P	2,634	1,179	1,823	3,241	3,736
Accrued liabilities	2,089	1,197	1,872	2,555	2,740
Financing lease	59	39	30	53	53
Income tax payable	403	0	0	0	0
<b>Current Liabilities</b>	<b>\$ 5,185</b>	<b>\$ 2,415</b>	<b>\$ 3,725</b>	<b>\$ 5,849</b>	<b>\$ 6,530</b>
Deferred Tax Liability	439	523	136	136	136
Financing Lease Liability	52	13	36	95	95
Equity	46,572	45,372	44,141	45,400	51,219
<b>Total Equity &amp; Liab.</b>	<b>\$ 52,248</b>	<b>\$ 48,323</b>	<b>\$ 48,038</b>	<b>\$ 51,479</b>	<b>\$ 57,979</b>
	FY 19	FY 20	FY 21	FY 22E	FY 23E
Net	2,021	(2,176)	(1,052)	1,940	4,722
D&A	1,467	1,177	1,256	1,121	1,124
Stock issued for services	391	443	567	962	1,098
Other	201	(123)	(176)	(282)	0
Working Capital	3,633	943	54	105	(1,397)
<b>Operating Cash Flow</b>	<b>\$ 7,713</b>	<b>\$ 264</b>	<b>\$ 649</b>	<b>\$ 3,845</b>	<b>\$ 5,547</b>
Other	1,611	3,314	(649)	181	0
Acquisition	(4,384)	0	0	0	0
CapEx	(4,665)	(1,547)	(169)	(473)	(1,000)
<b>Investing Activities</b>	<b>\$ (7,437)</b>	<b>\$ 1,767</b>	<b>\$ (818)</b>	<b>\$ (292)</b>	<b>\$ (1,000)</b>
Equity	(2,977)	(153)	(795)	(1,297)	0
Lease Liability	(74)	(58)	(41)	(20)	0
<b>Financing Activities</b>	<b>\$ (3,050)</b>	<b>\$ (210)</b>	<b>\$ (836)</b>	<b>\$ (1,317)</b>	<b>\$ -</b>
FX	31	(31)	45	(32)	0
<b>Change in Cash</b>	<b>\$ (2,743)</b>	<b>\$ 1,789</b>	<b>\$ (960)</b>	<b>\$ 2,204</b>	<b>\$ 4,547</b>

Source: Profire Energy, Inc. and Dawson James Securities estimates

**Important Disclosures:**

**Price Chart:**



**Price target and ratings changes over the past three years:**

- Initiated – Buy – May 12, 2021 – Price Target \$1.65
- Update – Buy – June 21, 2021 – Price Target \$1.65
- Update – Buy – August 6, 2021 – Price Target \$1.65
- Update – Buy – September 28, 2021 – Price Target \$1.65
- Update – Buy – October 18, 2021 – Price Target \$1.65
- Update – Buy – November 5, 2021 – Price Target \$1.65
- Update – Buy – February 18, 2022 – Price Target \$1.65
- Update – Buy – February 18, 2022 – Price Target \$1.65
- Price Target Change – Buy – March 9, 2022 – Price Target changed from \$1.65 to \$2.00
- Update – Buy – May 4, 2022 – Price Target \$2.00
- Update – Buy – July 5, 2022 – Price Target \$2.00
- Update – Buy – August 4, 2022 – Price Target \$2.00
- Update – Buy – August 8, 2022 – Price Target \$2.00

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**Information about valuation methods and risks can be found in the "Valuation" and "Risk Analysis" sections of this report.**

The securities of the company discussed in this report may be unsuitable for investors depending on their specific investment objectives and financial position. This report is offered for informational purposes only and does not constitute an offer or solicitation to buy or sell any securities discussed herein in any jurisdiction where such would be prohibited. Additional information is available upon request.

**Ratings Definitions:**

- 1) **Buy:** the analyst believes the price of the stock will appreciate and produce a total return of at least 20% over the next 12-18 months;
- 2) **Neutral:** the analyst believes the price of the stock is fairly valued for the next 12-18 months;
- 3) **Sell:** the analyst believes the price of the stock will decline by at least 20% over the next 12-18 months and should be sold.

The following chart reflects the range of current research report ratings for all companies, followed by the analysts of the Firm. The chart also reflects the research report ratings relating to those companies for which the Firm has performed investment banking services.

Current as of 1-Aug-22

	Company Coverage		Investment Banking	
<b>Ratings Distribution</b>	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	30	68%	4	13%
Market Perform (Neutral)	13	30%	0	0%
Market Underperform (Sell)	1	2%	0	0%
Total	44	100%	4	9%

**Analyst Certification:**

The analyst(s) whose name appears on this research report certifies that 1) all of the views expressed in this report accurately reflect his (their) personal views about any and all of the subject securities or issuers discussed; and 2) no part of the research analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst in this research report; and 3) all Dawson James employees, including the analyst(s) responsible for preparing this research report, may be eligible to receive non-product or service-specific monetary bonus compensation that is based upon various factors, including total revenues of Dawson James and its affiliates as well as a portion of the proceeds from a broad pool of investment vehicles consisting of components of the compensation generated by investment banking activities, including but not limited to shares of stock and/or warrants, which may or may not include the securities referenced in this report.