

## TRAVELZOO (NasdaqGS: TZOO)

Founded in 1998, Travelzoo is a global Internet media company with more than 30 million members worldwide. Travelzoo publishes offers and experiences from more than 5,000 travel, entertainment and local-event companies, and aggregates deals on its technology platforms to enhance members' experiences.

### COMPANY HIGHLIGHTS

- \* TZOO: Bridging Global Travel Suppliers and Customers
- \* Travelzoo has built a robust network of global travel and entertainment suppliers and a strong technology platform that aggregates travel deals for customers. Despite an uneven recovery in demand coming out of the COVID-19 pandemic, the company seems well positioned to capitalize on favorable long-term industry trends.
- \* The company has discontinued unprofitable operations in the Asia Pacific region, increased sales of longer-duration travel vouchers to enhance cash flow, and implemented cost reductions across the business.
- \* Travelzoo revenues rose 18% in 2021 and 6% in the first nine months of 2022. Although revenues remain below pre-pandemic levels, we look for significant revenue growth and increased operating leverage, as we expect expenses to grow more slowly than revenue. We believe that this has been underappreciated by investors.
- \* We like the long-term growth potential of initiatives such as Jack's Flight Club, in which Travelzoo acquired a majority stake in January 2020, and Travelzoo Meta, which is in the early stages of a rollout. We also expect a shift towards premium subscription-based membership models that should provide a more stable revenue and margin profile over time.

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### KEY STATISTICS

#### Key Stock Statistics

Recent price (11/8/22)	\$5.41
Fair Value Estimate	\$13.00
52 week high/low	\$11.01- \$4.22
Shares outstanding (M)	12.6
Market cap (M)	\$68.0
Dividend	Nil
Yield	Nil

#### Sector Overview

Sector	Consumer Discretionary
Sector % of S&P 500	10.9%

#### Financials (\$M, as of 9/30/22)

Cash & Mkt Securities	20.5
Debt	10.1
Working Capital (\$M)	-17.4
Current Ratio	0.7
Total Debt/Equity (%)	191.5%
Payout ratio	NM
Revenue (M) TTM	65.7
Net Income (M) TTM	0.9
Net Margin	1.4%

#### Risk

Beta	1.42
Inst. ownership	25%

#### Valuation

P/E forward EPS	11.3
Price/Sales (TTM)	1.0
Price/Book (TTM)	NA

#### Top Holders

Forager Capital Management LLC  
 Invenomic Capital Management LP  
 Acadian Asset Management LLC

#### Management

CEO	Mr. Holger Bartel
Chairman	Mr. Ralph Bartel
CFO	Mr. Wayne Lee
Company website	www.travelzoo.com

### PRICE CHART



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- \* As of September 30, 2022, Travelzoo had \$20.5 million in cash, cash equivalents, and restricted cash, down from recent quarters as the company has made payments to merchants following the redemption of previously sold vouchers. We expect Travelzoo to reach the end of this cash outflow cycle by early 2023, and look for stronger demand to result in positive operating cash flow.
- \* Year-to-date, TZOO shares have declined more than 45%, compared to a 20% decline for the S&P 500. We attribute this underperformance to an uneven recovery from the pandemic, which has led to volatile travel demand and less favorable deal sourcing opportunities. However, management now expects an increase in promotional deals from travel industry suppliers.
- \* We believe that the company's improving outlook, past record of profitability, and cost-containment efforts point to undervaluation in TZOO shares.
- \* Based on our forward P/E analysis, we arrive at a fair value for TZOO of \$13 per share, well above current levels above \$5.

## INVESTMENT THESIS

For more than 20 years, Travelzoo has worked in partnership with top travel suppliers to aggregate insider travel, entertainment, and lifestyle deals to a member base that has grown to, and been sustained at, more than 30 million. Travelzoo has more than 20 offices worldwide, which allows it to develop relationships with local suppliers and content contributors, and provide enhanced deals and experiences to its members.

The company's core strategy has been to build a travel and lifestyle brand with a large user base in the travel, entertainment and local-event markets. Travelzoo's supplier partner base consists of more than 5,000 companies, including airlines, hotel chains, cruise line operators, and tourism organizations around the world. Travelzoo generates most of its revenue by selling advertising rather than by taking a percentage of the transaction value. This enables Travelzoo to lower costs and helps its suppliers to maintain higher returns on invested capital. Prominent publications and products are published in 11 countries and include Local Deals and Getaways, which allow members to purchase vouchers for deals from local businesses such as spas, hotels, and restaurants, and from which Travelzoo receives a percentage of the transaction value.

For Local Deals and Getaways, the company earns a fee for acting as an agent for voucher sales with third-party merchants. Such transactions historically accounted for approximately one-third of revenue, but became more attractive in 2020, as a source of upfront cash to support operating cash flow. The vouchers are

recorded as merchant accounts payable, and paid to the merchant only when redeemed. Given that these vouchers tend to be redeemed over extended periods, the near-term economics were favorable, in our view, to provide operating cash flow during the pandemic. Merchant payables on Travelzoo's balance sheet were \$38.2 million as of September 30, 2022, down from \$68.7 million on December 31, 2021.

Travelzoo's technology delivery platforms include a website, an app, and an e-mail alert service. According to management, Travelzoo's website is visited by up to 11 million unique visitors each month, and supplements its audience reach with website networks that syndicate deal content. In addition, the company has more than 4 million social media followers on sites that include Facebook and Twitter, and its mobile applications have been downloaded more than 7 million times. To keep pace with the migration of consumers to digital and mobile platforms, Travelzoo has made its content available on both mobile devices and hotel booking platforms.

Historically, the company has been a counter-cyclical business, as travel-related customer traffic and deals have been highest when occupancy rates of travel suppliers are decreasing -- resulting in more aggressive discounting. In addition, periods of high inflation tend to dampen traveler enthusiasm, thus increasing demand for compelling travel-related deals. However, in the current inflationary cycle, pent-up demand coming out of the pandemic and staffing pressures in the travel and entertainment industries have resulted in a less favorable climate for deals offered by vendors. This was particularly evident in the third quarter of 2022. We expect these challenges to be transient in nature, and see Travelzoo's affluent customer base positioning the company for stronger results in the coming quarters.

During the pandemic, Travelzoo realigned its cost structure, which we expect will support sustainable growth and profitability over the long term. We expect advertising revenues to return to pre-pandemic levels and look for further operating margin expansion. Earlier in 2022, North America operating margin rose to 25%, its highest level since 2015.

As of September 30, 2022, Travelzoo had 30.5 million members worldwide. North America accounted for 16.4 million and Europe for 9.1 million. Jack's Flight Club had 1.9 million members. Travelzoo has discontinued Asia Pacific operations, but retains its member base in the region, which provides royalties under a license agreement. Despite recent attrition in the membership base, we expect many former members to return as the pandemic recedes

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## PEER COMPARISON

Company	Ticker	Recent Price (\$)	52-Week High (\$)	52-Week Low (\$)	Mkt. Cap (\$MIL)	1-yr Price Change (%)	1-yr Rev Growth (%)	1 YR EPS Growth (%)	P/E Ratio	Beta	Yield (%)
TRAVELZOO	NASDAQ: TZOO	5.41	11.01	4.22	68	-49	18	NA	60.1	1.42	NA
EXPEDIA GROUP	NASDAQ: EXPE	89.70	217.72	85.02	14002	-52	65	NA	NA	1.51	NA
TRIP ADVISOR	NASDAQ: TRIP	19.68	37.21	16.87	2767	-37	49	NA	NA	1.27	NA
BOOKING HOLDINGS	NASDAQ: BKNG	1859.19	2715.66	1616.85	72058	-30	61	1856	66.0	1.26	NA

and travel restrictions ease. We see the potential for Travelzoo to expand its user base with modest marketing spending over time.

In March 2021, Travelzoo added 2 million new North American members upon the exit of a European competitor from the U.S. market, and the company added nearly a million Europe-based members in March 2022 in a transition with the acquisition of a business unit of Secret Escapes in Spain. We expect such consolidation to continue across the industry and see expansion of its user base enabling the company to raise advertising rates as conditions continue to revert to pre-pandemic levels.

Travelzoo has two regional operating segments: North America, which consists of Canada and the United States; and Europe, which includes France, Germany, Spain, and the United Kingdom. In 2020, Travelzoo exited its Asia Pacific business, which contributed only 6% of revenues in 2019. The unit was unprofitable, and offset approximately two-thirds of North America/Europe profitability in 2019. In our view, the decision to exit Asia Pacific was prudent given the disruption from the COVID-19 pandemic, declining revenue-per-member and per-employee operating metrics, the longstanding drag on earnings, and the region's modest contribution revenues in 2019.

We have a positive view of Travelzoo's retention of its Asia Pacific member base and licensing of this data under a royalty-based model. In June 2020, the company sold its Japan-based subsidiary, and entered into a licensing agreement, under which it retained ownership of the existing regional member base. Similarly, in August 2020, Travelzoo sold its Singapore subsidiary and entered into a royalty bearing licensing agreement for use of Travelzoo's members in Australia, New Zealand, and Singapore. Initial royalty revenues began being recognized in the fourth quarter of 2020. Although we expect such royalties to remain modest contributors to Travelzoo's operations, we are encouraged that these collaborations have served as referral sources to advertising and revenue generating activities in its core markets.

In 2019, North America and Europe achieved 18% and 12% operating margins, respectively. As recently as 2018, Europe generated 14% in operating margin. We expect future results to benefit from the 2020 acquisition of Jack's Flight Club, a subscription service that has traditionally generated strong operating margins and whose member base is primarily in the UK. Jack's offers a free subscription, as well as a premium service for which members pay \$40-\$60 annually. The unit generated \$3.5 million in revenues for Travelzoo in 2020 and \$3.3 million in 2021.

Over the past two years, North America has accounted for approximately two-thirds of revenue from continuing operations (66% thus far in 2022 and in 2021, and 65% in 2020); Europe (29% in 2022 and 2021, and 28% in 2020) and Jack's Flight Club (5% year-to-date and in 2021, and 7% in 2020) have provided the balance. In 2022, North America has remained ahead of Europe in the pace of post-pandemic recovery. European operations have also been pressured by the strong dollar. In addition, spending on acquisitions has lowered European revenue by approximately \$900,000, leading to an operating loss for the unit.

Despite the challenging market conditions since the Jack's Flight Club acquisition, we expect improving conditions to enable

Travelzoo to expand its business by cross-promoting offers between Jack's Flight Club and Travelzoo members. We believe that the acquisition will ultimately help Travelzoo to introduce new membership options, including subscription-based Premium membership models over time. To that end, in March 2022, Travelzoo named Arveena Ahluwalia as global director of premium membership, to drive and manage the launch of such subscription-based products. Thus, with streamlined and more normalized operations, we expect Travelzoo to extract more value from the Jack's acquisition than it has to date.

In March 2022, Travelzoo announced a new metaverse division and a plan to launch Travelzoo META, a paid subscription-based service that provides members with exclusive access to metaverse travel experiences in an interactive, browser-based, computer-generated 3D environment that does not require the use of specialized virtual reality hardware. The service will work with content creators to make experiences exclusively available to Travelzoo META members to provide metaverse spaces and versions of destinations for its members. As such, Travelzoo META will complement real-world travel and should attract a new generation of members.

In our view, a recent survey by McKinsey validates the Travelzoo META opportunity, as virtual immersive travel was cited as the second-most sought-after experience in the metaverse, ranking only behind social connection. Thus, we see Travelzoo's first-mover advantage in this nascent market as representing an underappreciated potential long-term value driver.

The company launched Travelzoo META in May 2022 in a controlled test environment to a limited set of users, and is now expanding its launch. We like the product's modest upfront costs, as the new business is expected to be funded from membership fees.

## RECENT DEVELOPMENTS

In 2021, Travelzoo stock was virtually unchanged, versus a 27% advance for the S&P 500. Thus far in 2022, the stock has declined 46%, compared to a 20% decline for the index.

In October 2022, Travelzoo posted 3Q22 net income from continuing operations of \$0.06 per share, down from \$0.22 in the prior-year period. The global travel and entertainment industries are still in recovery mode, and demand among suppliers for the promotion of travel deals varies significantly. However, management noted signs of improving demand in the third quarter, and looks for stabilizing fundamentals going forward.

In June 2022, Travelzoo announced a 1 million share stock buyback authorization. In 3Q22, it repurchased roughly 200,000 shares of stock.

In June 2022, Travelzoo announced that Justin Soffer joined the company as global director for member acquisition, overseeing new member acquisition and providing support for the Travelzoo META.

In March 2022, Travelzoo appointed Arveena Ahluwalia as global director of premium membership, to drive and manage the launch of Travelzoo's paid subscription-based product. Ms. Ahluwalia has both start-up and corporate experience with consumer brands and in finance, most recently serving as COO for Evelyn & Bobbie and previously working with firms including Freshly Inc., Citi, Google, and UBS Investment Bank.

In March 2022, Travelzoo appointed Rhea Saran as global head of brand and content. Ms. Saran has extensive travel, luxury lifestyle, and consumer marketing experience. Most recently, she served on a team for the Saudi Arabian tourism project, Diriyah Gate Development Authority. Previously, she served as founding editor-in-chief of Conde Nast Traveler Middle East and held editorial positions with global brands -- including GQ magazine in India, and the U.S. edition of Conde Nast Traveler and Working Mother Media.

In March 2022, Travelzoo acquired the business unit of Secret Escapes in Spain, which nearly doubled the number of members in Spain, from 850,000 to approximately 1.5 million.

In August 2021, Travelzoo received the highest possible ranking for consumer satisfaction for the third year in a row by popular German magazine FOCUS-MONEY. In July 2021, Travelzoo received similar recognition from consumers in the online travel deal category in a national survey commissioned by BILD Zeitung, Germany's largest newspaper.

In March 2021, Travelzoo added 2 million new members, upon the exit of a European competitor from the U.S. market.

Across 2020, Travelzoo discontinued operations in the unprofitable Asia Pacific region to focus on its core North American and European markets. In June 2020, the company sold its Japan-based subsidiary, and entered into a licensing agreement, under which it retained ownership of the existing regional member base. Initial royalty revenues under this five-year agreement began being recognized in the fourth quarter of 2020. Similarly, in August 2020, Travelzoo sold its Singapore subsidiary and entered into a royalty bearing licensing agreement for use of Travelzoo's members in Australia, New Zealand and Singapore.

## EARNINGS & GROWTH ANALYSIS

We forecast revenues of \$69.5 million in 2022 and \$84.5 million in 2023, representing growth of 10% and 22%, respectively. We see 2022 revenues reflecting the early stages of recovery in the global travel industry, albeit with headwinds to more aggressive deal sourcing by vendors to Travelzoo due to pent-up consumer demand and vendor staffing challenges. In particular, Travelzoo has cited reduced capacity offered by airlines and hotels, which kept demand high and limited the need to offer deals. We expect these conditions to ease into 2023.

We are encouraged by the continued firming in advertising rates and the proportion of advertising in Travelzoo's revenue mix since the peak of the COVID-19 pandemic. While the redemption of previously purchased vouchers and lack of new voucher purchases contributed to less favorable revenue growth on a year-over-year basis, we think that the current revenue mix is contributing to a more favorable operating margin profile for Travelzoo moving forward.

We project gross margins of 86% in 2022 and 87% in 2023, up from 82% and 80% in 2021 and 2020, respectively. In late 2021, the product mix began to shift back towards advertising revenues and away from travel voucher sales. Vouchers had been more prevalent during the peak of the pandemic, but carry a lower margin due to increased transaction and processing-related costs. Following the company's operating losses in 2020 and 2021, and

the discontinuation of its unprofitable Asia Pacific business, we forecast a return to growth in 2022, with an operating margin of 9%, driven by increased consumer demand for travel and continued cost reductions. In 2023, we forecast an operating margin of 17%.

We forecast EPS from continuing operations of \$0.48 in 2022 and \$0.85 in 2023. We note that with only roughly 12.5 million shares outstanding, Travelzoo has significant leverage to drive bottom-line growth.

## FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Travelzoo is Medium-Low. As of September 30, 2022, the company had cash, cash equivalents, and restricted cash of \$20.5 million, compared to \$45.0 million at the end of 2021. The decline reflects payments to merchants following the redemption of travel vouchers. The sale of these vouchers had provided upfront cash to Travelzoo.

In our view, Travelzoo's cash balance, accounts receivable/deposits to payment processors, and prospects for a return to positive operating cash flow should enable the company to maintain a solid financial footing. To that end, we are encouraged by the recent announcement of a 1 million share stock buyback authorization. In 3Q22, the company repurchased approximately 200,000 shares of stock.

As of September 30, 2022, Travelzoo had negative working capital of \$17.4 million, compared to negative \$20.8 million at the end of the first quarter, and representing a current ratio of approximately 0.7. We note that Travelzoo had a current ratio above 1.0 between 2015 and the start of the COVID-19 pandemic, while carrying the unprofitable and now discontinued Asia Pacific operations.

We expect working capital to continue its improvement, as Travelzoo works through its merchant payables, noting that up to 10% of sold vouchers are ultimately not redeemed, and payment-processing deposits are returned to the company, as mentioned above. With Travelzoo's product mix shifting back towards advertising revenue, rather than voucher sales, and as the broader travel and entertainment industry's demand fundamentals stabilize, we expect Travelzoo's cash to payables ratio to improve significantly.

Net cash used by operating activities in 2021 was \$8.1 million, as compared with net cash provided of \$46.8 million in 2020. Net cash provided by investing activities in 2021 was \$104,000, compared to net cash provided of \$2.1 million in 2020, which was driven by proceeds from the sale of an equity investment in WeGo. Net cash used in financing activities was \$11.2 million in 2021, compared with cash used of \$7.0 million in 2020.

Travelzoo does not pay a dividend, and we do not expect one to be initiated in the near term, as the company focuses on integrating the Jack's acquisition and expanding its global footprint.

## MANAGEMENT

Ralph Bartel founded Travelzoo in May 1998. He has been a member of the board since inception and chairman since May 2017. Mr. Bartel served as CEO from 2008 to 2010, and currently serves as Travelzoo's chief talent officer. Mr. Bartel holds a Ph.D. in Communications from the University of Mainz, Germany; a

master's degree in journalism from the University of Eichstaett, Germany; and a Ph.D. in Economics and an MBA in finance and accounting from the University of St. Gallen, Switzerland.

Holger Bartel, has been Travelzoo's CEO since January 2016, and previously held the post in 1999-2007 and 2008-2010. Mr. Bartel also served as chairman between 2007 and 2009. Prior to joining Travelzoo, he was an engagement manager at McKinsey & Company. Mr. Bartel was a research fellow at Harvard Business School and holds a Ph.D. in Economics and an MBA in finance and accounting from the University of St. Gallen, Switzerland.

Travelzoo's board has five members. The board includes three independent directors. Importantly, independent directors, Michael Karg, Global Chief Operating Officer of Mindshare (Audit Committee) and Volodymyr Cherevko, Chief Transformation Officer of Haier Europe (Compensation, Nominating and Corporate Governance) chair the Board's key committees, which we view positively for Travelzoo's corporate governance.

## RISKS

Risks to the company include its status as a "controlled company," as Chairman Ralph Bartel, via investment vehicle Azzuro Capital (Travelzoo's largest shareholder), holds 36% of the common shares outstanding, as of September 2022. In addition, Chairman Ralph Bartel and CEO Holger Bartel are brothers.

Other risks include a protracted disruption from the pandemic, which initially lowered consumer demand for travel as well as the number of travel deals offered by suppliers. In addition, Travelzoo operates in a very competitive environment. Competitors include large internet portal sites, search engines, and travel search agents such as Kayak, Expedia, Groupon, and TripAdvisor. This competition has kept pressure on advertising rates. In addition, competitors may make strategic acquisitions or establish cooperative relationships to expand their businesses or to more comprehensive solutions. Travelzoo and its peers also face high customer acquisition costs.

## COMPANY DESCRIPTION

Founded in 1998, Travelzoo is a global Internet media company with more than 30 million members worldwide. Travelzoo pub-

lishes offers and experiences from more than 5,000 travel, entertainment and local-event companies, and aggregates deals on its technology platforms to enhance members' experiences.

## VALUATION

Over the past 52 weeks, TZOO shares have been volatile, trading between \$11 and \$4 (compared to a high near \$18 in early 2021). The shares have recently traded at the low end of this range, which we attribute to the residual impact of the pandemic on travel demand and deal trends; soaring inflation; and the stronger U.S. dollar, which has pressured results in Europe.

Despite volatile industry fundamentals, we believe that the current multiple of 6.2-times our 2023 EPS estimate does not fairly value Travelzoo's core business, which generated more than \$1.00 in EPS in 2019 and should return to positive operating cash flow in 2023. We note that the company's current market cap near \$70 million translates to less than \$3 per member, more than 90% below peak levels.

Although its initial contribution has been more modest than expected given the COVID-19 outbreak immediately following the transaction, we expect Jack's Flight Club to support cross promotion with the core Travelzoo user base, as pent-up consumer demand begins to translate into increased advertising rates and revenue growth. Further, we think the acquisition may help Travelzoo shift towards a subscription model, which could provide a more-stable and profitable revenue base and margin profile. We expect strengthening industry conditions across 2022, and look for Jack's to be an important driver of long-term growth.

We are encouraged by Travelzoo's recent appointment of a general manager for premium membership initiatives as well as member acquisition, and think that the newly announced metaverse product could represent a complementary long-term revenue driver, without significant ramp-up related expenses.

Based on these dynamics, we value the stock using a P/E multiple of 15, slightly below the average forward multiple of 16 for a basket of global interactive media service companies. Applying this multiple to our 2023 EPS estimate of \$0.85, we arrive at a fair value estimate for TZOO of \$13 per share, well above current levels above \$5.

Steve Silver,  
Argus Research Analyst

**INCOME STATEMENT**

<b>Growth Analysis (\$MIL)</b>	2019	2020	2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022E	2022E	Q1 2023E	Q2 2023E	Q3 2023E	Q4 2023E	2023E
Revenue	111.4	53.6	63.2	18.5	17.7	15.8	17.5	69.5	18.8	20.7	21.6	23.4	84.5
Gross Profit	99.5	43.0	51.7					60.0					73.4
SG&A	83.2	51.1	50.1					51.6					56.0
Product Development	6.9	3.1	2.6					2.0					3.0
Operating Income	9.4	-14.1	-1.0					6.4					14.5
Interest Expense	NA	NA	NA					NA					NA
Pretax Income	8.9	-13.6	3.0					8.9					14.7
Tax Rate (%)	54	NA	14					33					26
Net income	4.1	-10.0	1.2					6.0					10.7
Diluted Shares	12.0	11.3	12.4					12.6					12.6
EPS	0.34	-0.88	0.09	0.19	0.08	0.06	0.15	0.48	0.18	0.20	0.21	0.26	0.85
Dividend	NA	NA	NA					NA					NA
<b>Growth Rates (%)</b>													
Revenue	0	-52	18					10					22
Operating Income	15%	NM	NM					NM					128
Net Income	-11%	NM	NM					416					78
EPS	-8%	NM	NM					433					77
<b>Valuation Analysis</b>													
Price (\$): High	22.85	12.40	19.83					NA					NA
Price (\$):Low	8.72	3.04	8.67					NA					NA
PE: High	61.8	36.5	NA					NA					NA
PE: Low	23.6	8.9	NA					NA					NA
PS: High	2.5	1.3	4.6					NA					NA
PS: Low	0.9	0.3	2.0					NA					NA
Yield: High	NA	NA	NA					NA					NA
Yield: Low	NA	NA	NA					NA					NA
<b>Financial &amp; Risk Analysis (\$MIL)</b>													
Cash/Restricted Cash	20.8	64.2	45.0					NA					NA
Working Capital	1.1	-12.8	-22.5					NA					NA
Current Ratio	1.0	0.8	0.7					NA					NA
LTDebt/Equity (%)	NA	NA	NA					NA					NA
Total Debt/Equity (%)	NA	NA	NA					NA					NA
<b>Ratio Analysis</b>													
Gross Profit Margin	89%	80%	82%					86%					87%
Operating Margin	8%	NA	-2%					9%					17%
Net Margin	4%	NA	2%					9%					13%
Return on Assets (%)	12	NA	NA					NA					NA
Return on Equity (%)	33	NA	33					NA					NA
Op Inc/Int Exp	NA	NA	NA					NA					NA
Div Payout	NA	NA	NA					NA					NA

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