

Stockgroup Information Systems Inc. (TSXV: SWB; OTCBB: SWEB) – Q3 results were below expectations, but Q4 looks strong

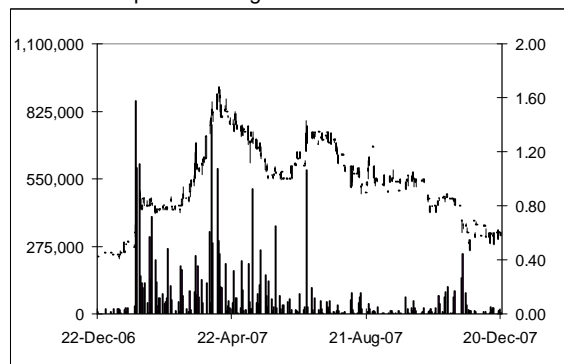
Sector/Industry: Technology Services/Financial/Internet

www.stockgroup.com

Market Data (as of December 21, 2007)

Current Price	C\$0.60
Fair Value	C\$1.65 (↓)
Rating*	BUY
Risk*	3 (Average)
52 Week Range	C\$0.41 -C\$1.68
Shares O/S	40,951,922
Market Cap	C\$24.57 mm
Current Yield	N/A
P/E	N/A
P/B	9.70
YoY Return	42.9%
YoY TSX-V	-5.2%

*see back of report for rating and risk definitions



Q3-FY2007 Highlights

- In October 2007, SWB launched a beta version of the next generation of StockHouse. The new version, which has a completely new look, has several additional features and functionalities. The most noteworthy new feature is that the website has a proprietary reputation and content ranking system which enables visitors to filter information based on the reputation of bloggers and quality of information. This new and unique feature is the internet's first and only investor reputation system.
- SWB posted their 19th quarter of YOY revenue growth in Q3-2007. The company's licensing and subscription (L&S) revenues were in line with expectations, but advertising revenues, which dropped for the first time in FY2007, fell below expectations.
- L&S revenue growth came from a solid organic growth rate of 42% in Q3-2007, and through acquisitions. One concern is that, we believe, revenues of the acquired divisions dropped by 23% YOY in Q3-2007.
- Although advertising revenues dropped YOY in Q3-2007, we have a positive outlook on Q4-2007, based on a significant YOY increase in traffic in October and November 2007.
- Also, in a recent report by comScore Media, StockHouse was ranked as the number one website for user engagement across Canada for the second consecutive year.

Key Financial Data (Financial Year-End Dec 31)

(US\$, 000's)	2004	2005	2006	2007E	2008E
Revenues	4,823	6,100	7,766	13,891	17,832
EBITDA	392	216	(622)	(4,306)	(3,745)
EBITDA Margin	8.1%	3.5%	-8.0%	-31.0%	-21.0%
Net Income	16	(59)	(791)	(5,184)	(4,636)
EPS (Basic)	0.00	(0.00)	(0.02)	(0.13)	(0.11)
Assets	2,842	3,290	3,460	5,149	3,759
Debt to Capital	0.0%	8.7%	15.1%	29.2%	n.a.
Free Cash Flow to Equity	417	389	(445)	(4,612)	(3,325)
ROE	1.0%	-4.0%	-61.6%	-958.1%	n.a.

Stockgroup Information Systems Inc. (SWB) is a provider of financial information, news, and analytical tools to financial services firms, corporations, and the media. It also provides investors with financial information through leading financial sites such as StockHouse.ca and Smallcapcentre.com.

Launched the next version of StockHouse

In October 2007, SWB launched a beta version of the next generation of StockHouse. The beta version, which has a completely new look, has several additional features and functionalities, including enhanced social networking tools, compared to the older version. One noteworthy feature of the new version is that it tackles a key problem of user-generated content – identifying and validating the quality of content. It is normally very difficult to evaluate the quality of content on social networking sites, as the content is user-generated, but the new version of StockHouse uses the company's proprietary reputation analytics and community ranking system to enable visitors to filter information based on the reputation of bloggers (members) and quality of information. Every user now has the capabilities to rank the reputation of bloggers and the quality of content available on the website. This new and unique feature makes StockHouse the internet's first and only investor reputation system. The company filed for a patent for the technology in Q3-2007. We believe this is a great improvement and has worked for sites such as ebay.

Management indicated that they expect the transition to the new website to be completed by the end of Q4-2007. As users of the new beta version since its launch, we were very pleased to see the vast improvement in the new version. We found the new website to be user-friendly, and believe that its additional features have the potential to drive more traffic.

19th quarter of YOY revenue growth

SWB posted their 19th quarter of YOY revenue growth in Q3-2007. Although revenues grew from \$1.89 million in Q3-2006, to \$3.48 million in Q3-2007, they were slightly below our expectations. The company's licensing and subscription (L&S) revenues were in line with expectations, but advertising revenues, which dropped for the first time in FY2007, fell below expectations. For the 9-month period in FY2007, the company generated \$10.29 million in revenues versus \$5.48 million in the same period in the previous year.

The table below shows the company's segmented revenues.

(in US\$ 1000's)	Q3 2006	% Total	Q3 2007	% Total	Growth
Advertising	943	49.9%	862	24.7%	-8.6%
L & S	946	50.1%	2,621	75.3%	177.1%
Total	1,889	100.0%	3,483	100.0%	84.4%

	2006 (9 mo)	% Total	2007 (9 mo)	% Total	Growth
Advertising	2,687	49.1%	2,877	28.0%	7.1%
L & S	2,788	50.9%	7,409	72.0%	165.7%
Total	5,475	100.0%	10,286	100.0%	87.9%

L&S revenue growth came primarily from the acquisition of two wireless financial data providers (MFD of TeleCommunication Systems Inc. and the wireless financial information assets of Semotus Solutions Inc (AMEX: DLK)) in the first half of 2007, and impressive organic growth of 42% in Q3-2007. The acquisitions, however, did not have any impact on the company's advertising revenues. One concern with regard to L&S revenues is that, we believe, the combined revenues of the acquired wireless financial data providers dropped by 23.1% YOY in Q3-2007, from \$1.66 million to \$1.28 million. In the next section, we take a look at the company's segmented revenues in more detail.

Licensing and Subscriptions (L&S) – solid organic growth; however revenues of the acquired divisions dropped YOY

Revenues in Q3-2007 were \$2.62 million versus \$0.95 million in Q3-2006. For the 9-month period, revenues increased from \$2.79 million to \$7.41 million. L&S revenues accounted for 75% (Q3-2006 – 51%) of the company's revenues in Q3-2007, and 72% of revenues in the 9-month period in FY2007 (51% in the comparable period in the previous year). The solid organic growth of 42% in Q3-2007 came from increased sales of StockStream Platinum, renewals of existing agreements, and services to the company's new and existing clients. Although revenues of the acquired divisions dropped by 23.1% YOY, they were in line with expectations, and we expect revenues from the wireless financial data providers to pick up in FY2008, as the company opens new channels.

In November 2007, the company announced they signed an agreement with Raymond James Ltd. to provide Raymond James's advisors and their clients with real-time streaming financial data and news. Raymond James has around 4,640 financial advisors serving 1.6 million accounts in 2,200 locations. We believe this agreement, with one of North America's leading independent investment dealers, will contribute to long-term revenue growth, while in the short-term, we do not expect a significant impact on revenues.

We have raised our revenue forecasts for FY2007, and FY2008, to \$9.36 million (up from \$9.18 million) and \$12.17 million (\$11.49 million), respectively.

Ad revenues were below expectations in Q3, but Q4 looks strong

Advertising revenues in Q3-2007 were \$0.86 million versus \$0.94 mm in Q3-2006, a decrease of 8.6% YOY. This is the first quarter that ad revenues dropped YOY in FY2007. Over the 9-month period, ad revenues were up YOY by 7.1%. Revenues for the 9-month period grew from \$2.69 million to \$2.88 million.

The following were three major reasons for the drop in revenues:

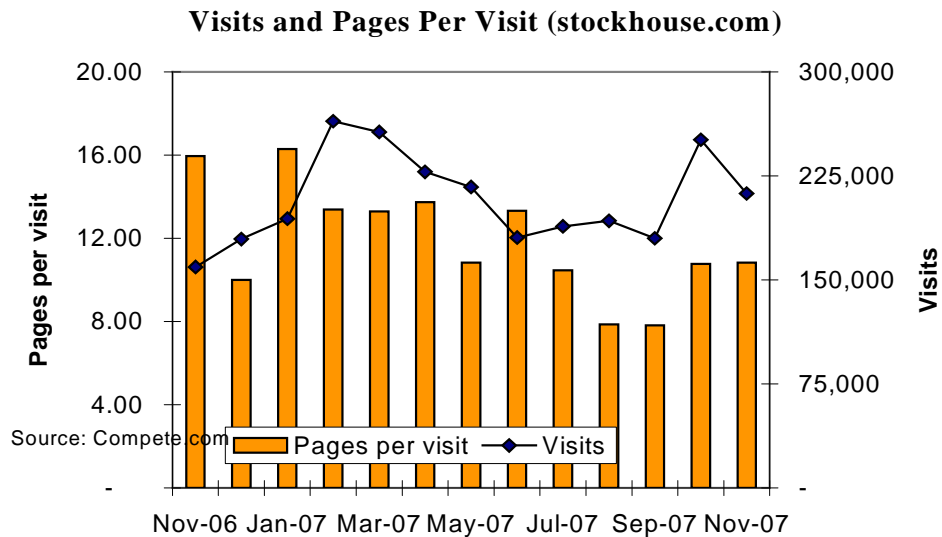
- Change in sales leadership – The company added a key sales member in Q3-2007. The change in leadership had a negative impact on revenues in the quarter. We expect to see the impact of the new leadership on revenues starting Q1-2008.
- The company had a higher percentage of ad network sales in Q3-2007, which is less profitable than direct or contextual advertising.
- Customers (advertisers) delayed purchasing in anticipation of the new version of StockHouse.

Even though revenues dropped in Q3-2007, we have maintained our positive outlook on ad revenues due to the following reasons.

- As mentioned earlier, we believe, the additional features of the **new version of StockHouse** will drive more traffic to the website.
- **Partnership with Yahoo! Canada** – In June 2007, the company announced they signed a deal with Yahoo! Canada (NASDAQ: YHOO). SWB will provide a selection of editorial content from the StockHouse website in a featured area of Yahoo! Canada Finance. SWB will also integrate Yahoo's latest search marketing platform, "Panama", into StockHouse. *(Yahoo's search marketing platform enables advertising clients to place their ads ahead*

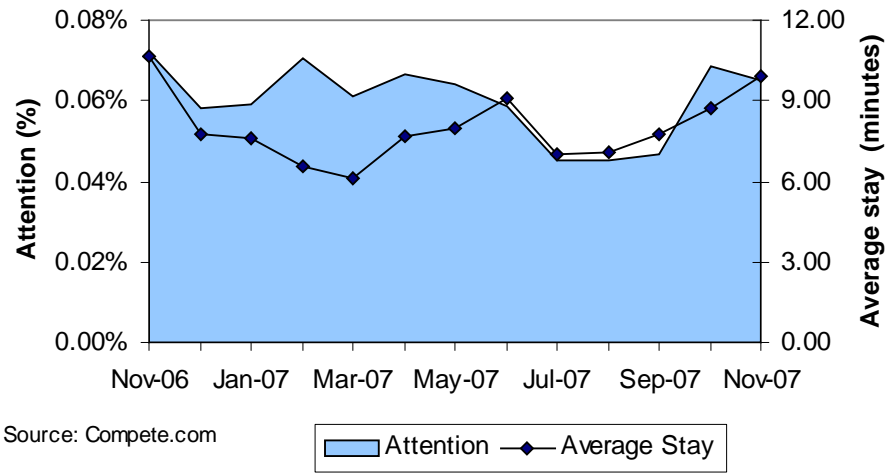
of other search results). SWB can generate more advertising revenues with this new feature available for clients in the StockHouse website. Also, as SWB’s editorial content will feature on the Yahoo! Canada Finance website, we believe, this deal has the potential to give significant exposure (and brand recognition) to SWB, and drive more traffic to StockHouse.

- The company intends to **increase its pipeline of direct advertising revenues** by adding more sales personnel and repositioning their ad network sales so that more inventories are available for direct sales.
- SWB intends to increase their ad network sales by adding a premium ad network for the U.S. market.
- In November 2007, the company launched their **StockHouse applications on Facebook and iGoogle**. As a result, users of Facebook and iGoogle, who enable the application, will now receive the latest financial information from Stockhouse. Like the partnership with Yahoo! Canada, we believe these two agreements will also lead to increased brand recognition and traffic to the StockHouse website.
- **Significant YOY increase in traffic in Q4-2007:** In October 2007, StockHouse had about one million unique visitors. For information on traffic in November 2007, we used data from Compete.com. According to Compete.com, although page views dropped (from 16.0 to 10.8) YOY, monthly visits increased by 33% YOY (from 159k to 212k) in November 2007, which we believe, is a very good sign for advertising revenues in Q4-2007 (shown on the chart below).



The average time spent per visitor and attention (time spent on Stockhouse as a percentage of the total time spent online) changed little YOY, which implies that the total time spent by all users on StockHouse increased YOY.

Attention (reach) and Average Stay (stockhouse.com)



Ranked No.1 for user engagement: In a recent report by comScore Media, StockHouse was ranked as the number one website for user engagement across Canada for the second consecutive year. According to comScore Media:

- StockHouse was the leading business and finance website for news and research in Canada over the 12-month period between October 2006 and September 2007.
- During August '07–October '07, visitors viewed 400% more pages, and spent 333% more average minutes than the average Business/Finance/News/Research category user.
- StockHouse was ranked number one in average minutes per person aged 35 and older in the Business/Finance - News and Research Category. Users spend more time per month visiting Stockhouse than on Google Finance, Globe Investor, TSX.com and MSN Money.

Based on all the above-mentioned factors, we expect SWB's advertising revenues to pick up in Q4-2007. However, we have reduced our ad revenue forecasts for FY2007, from \$4.95 million to \$4.53 million, since revenues in the first nine months of FY2007 were lower than expected. We have also reduced our revenue forecast for FY2008, from \$6.44 to \$5.66 million (which reflects 25% YOY growth).

All margins dropped YOY

Gross margins and EBITDA margins in Q3-2007, and the 9-month periods, were way below expectations, primarily due to increased expenses due to the acquisitions. The company is taking more time for consolidation, and renegotiation of some of the contractual costs the company inherited with the MFD acquisition - the primary reasons for the increase in costs.

The table below shows the company's gross margins in Q3-2007, and the nine-month period in FY2007, compared to their comparable periods in the previous year.

Margins	Q3 2006	Q3 2007	2006 (9 mo)	2007 (9 mo)
Gross	72.6%	50.4%	70.2%	55.4%
EBITDA	-13.6%	-60.8%	-16.6%	-35.5%
EBT	-13.0%	-65.0%	-16.1%	-39.2%
Net	-13.0%	-65.1%	-16.1%	-39.2%

Gross margins in Q3-2007, and the 9-month periods, were 50.4% (72.6% in Q3-2006), and 55.4% (70.2% in the comparable period in the previous year). Gross margins dropped primarily due to increases in costs for duplicate data feeds and exchange fees associated with the acquisition of MFD, offset by a decrease in costs due to the elimination of a primary data source.

In the most recent conference call, SWB's management indicated that they expect gross margins to improve gradually in FY2008 to 70%. However, we continue to be conservative, and have maintained our estimate of 60% for FY2008. We have reduced our gross margin forecasts for FY2007 from 60% to 56%. We expect the company will be able to increase gross margins in FY2008, through consolidation and integration, elimination of data feeds and duplication, and other cost cutting measures.

EBITDA margins in Q3-2007, and the 9 month period in FY2007, were -60.8% (-13.6% in Q3-2006) and -35.5% (-16.6% in the comparable period in FY2006). EBITDA margins dropped due to lower gross margins and significant increases in product development (for the new version of Stockhouse) and general and administrative (G&A) expenses (associated with the MFD acquisition), offset by a drop in sales and marketing expenses. G&A expenses and product development expenses, combined, accounted for 62% of the overall indirect costs for the 9-month period in FY2007. The majority of the increase in costs was due to increases in payroll (employees and consultants), addition of in-house human resources and legal functions and conversion of the back-end infrastructure to Microsoft(R).net platform architecture (which is now expected to be completed in Q1-2008 instead of Q4-2007).

	Q3 2006	Q3 2007	2006 (9 mo)	2007 (9 mo)
General and administrative/Sales	38.2%	52.9%	33.6%	41.7%
Sales and marketing/Sales	39.0%	34.1%	43.9%	34.5%
Research & Development / Sales	9.0%	24.3%	9.3%	14.8%
Total Costs / Sales	86.2%	111.2%	86.8%	90.9%

Total indirect expenses (sales and marketing, G&A and product development expenses) in the first 9 months of FY2007 were \$9.35 million (91% of revenues) versus \$4.75 million (87% of revenues) in the comparable period in the previous year. We have raised our estimate for total indirect costs in FY2007 from \$10.18 million (72% of revenues) to \$12.09 million (87% of revenues).

We expect margins to improve with revenues in FY2008. Also, research and development costs attributable to the completion of the new version of StockHouse will decrease in FY2008.

Net loss In Q3-2007, the company posted a net loss of \$2.23 million (EPS: -\$0.06) versus \$0.25 million (eps: -\$0.01) in the comparable period in the previous year. For the 9-month period in FY2007, the company posted a net loss of \$4.03 million (EPS: -\$0.10) versus \$0.88 million (EPS: -\$0.03) in the comparable period in the previous year.

We have lowered our EPS forecasts for FY2007 and FY2008, based on lower than expected ad revenues and higher than expected costs. Our revised forecasts for FY2007 and FY2008 are net losses of \$5.18 million (EPS: -\$0.13) (down from \$2.56 million; eps: -\$0.06) and \$4.64 million (EPS: -\$0.11) (from \$2.07 million, eps: -\$0.05).

Cash Flows In the 9-month period in FY2007, the company spent \$1.38 million in operations, while it had generated \$0.21 million from operations in the same period in FY2006. As for investing activities, the company spent \$0.71 million (of which \$0.44 million were for the two acquisitions). The company spent \$0.27 million on capital asset purchases (primarily related to computer equipment) in the 9-month period in FY2007. We have raised our forecast on capital asset expenses in FY2007 to \$0.35 million (up from \$0.18 million). Cash spent on operating and investing activities were funded by a private placement of \$4.15 million in the first nine months of FY2007.

Cash position At the end of September 2007, cash and working capital were \$4.13 million and \$2.09 million, versus \$2.01 million and \$1.00 million at the end of FY2006.

	2001A	2002A	2003A	2004A	2005A	2006A	Q3 2007
Working Capital	(3,003)	(211)	937	1,327	1,275	998	(14)
Current Ratio	11.3%	79.4%	207.6%	2.08	1.76	1.50	1.00
Debt / Capital	3804.0%	276.8%	3.0%	0.0%	8.7%	15.1%	12.1%
Interest Coverage Ratio (EBIT)	(0.89)	(0.32)	(1.22)	(2.01)	(0.13)	(0.03)	(0.01)

Total debt increased from \$0.22 million (debt to capital - 15.1%) to \$0.35 million (debt to capital - 12.1%). We estimate debt will decrease to \$0.23 million by the end of FY2007. The company is in a sound cash position for the next 6 months. However, our models suggest that the company will have to raise an additional \$2.30 million in the second half of FY2007 to fund its working capital.

Stock Options and Warrants: At the end of Sept 2007, SWEB had 2.68 mm stock options outstanding, with a weighted average exercise price of \$0.44 per share and time to maturity of 1.22 years.

Valuation Our DCF valuation on the company dropped from \$1.56 per share to \$1.52 per share as we dropped our short-term revenue forecasts and raised our short-term cost estimates.

DCF Valuation Model (in US\$)										
	2007F	2008F	2009F	2010F	2011F	2012F	2013F	2014F	2015F	Terminal
FFO	(4,049)	(3,503)	(2,692)	(1,116)	1,351	4,746	8,307	11,349	9,239	10,595
-increase in w/c	(213)	427	601	590	667	356	353	489	610	336
=CFO	(4,262)	(3,075)	(2,091)	(526)	2,018	5,103	8,660	11,838	9,849	10,930
-capex	(791)	(250)	(250)	(250)	(250)	(250)	(250)	(250)	(250)	(250)
- net debt repayment	(37)	(174)	(17)	-	-	-	-	-	-	-
=FCFE	(5,090)	(3,499)	(2,358)	(776)	1,768	4,853	8,410	11,588	9,599	10,680
PV	(4,948)	(3,037)	(1,827)	(537)	1,092	2,677	4,142	5,096	3,769	46,590
Discount Rate	12.00%									
Terminal Growth	3.00%									
Shares O/S	41,667									
Sum PV	53,016									
Cash	4,126									
PV Equity	57,142									
Value Per Share (in US\$)	\$1.37									
Value Per Share (in C\$)	\$1.52									

Based on our revised revenue forecasts for FY2007, the company is currently trading at a price to sales (P/S) ratio of 2, versus the industry average ratio of 4.9. Our revised valuation on the company based on the current industry average P/S is \$1.78 per share. Our valuation dropped from \$2.00 per share to \$1.78 per share due to lower revenue forecasts and as the industry average P/S dropped from 5.2 to 4.9.

Rating

Although advertising revenues declined in Q3-2007, our outlook for Q4-2007 is positive based on signs of solid growth in traffic in the first two months of Q4-2007. One of the major concerns in Q3-2007 was the significant increase in costs YOY. We expect costs as a percentage of revenues to decline in FY2008, through consolidation and integration, elimination of data feeds and duplication, and other cost cutting measures.

In summary, we have a positive outlook for Q4-2007, and FY2008, based on expected revenue growth and as costs as a percentage of revenues decline YOY. Based on our revised valuation models, we reiterate our BUY rating (Risk 3: Average), but lower our fair value estimate on the company from \$1.75 per share to \$1.65 per share. SWB's share price has dropped from \$1.10 per share to \$0.60 per share since our previous report in August 2007. We do not believe the drop in share prices reflects the company's fundamentals and growth potential, and therefore, we believe it is a good opportunity for investors to buy SWB's shares at current prices.

Risks

Stock market volatility affects SWB's revenue streams: SWB's sales are tied to public interest in stock markets. Their licensing and subscriptions business is driven by demand for market information from customers. The number of hits on the StockHouse website is directly linked with the fortunes of the stock market.

Threats from bigger players to replicate their business model: SWB faces a threat from bigger players, which may replicate its business model. Since online content providers thrive on innovation, SWEB could lose its edge once bigger players release similar models into the market. However, since StockHouse already has critical mass in user-generated content, we believe, entry barriers are high in this business.

Volatile Trading: As a small cap stock, investors may face liquidity problems

Appendix

CONSOLIDATED STATEMENT OF OPERATION

Year ended December 31

(expressed in US\$, 000's)

	2004A	2005A	2006A	2007F	2008F
REVENUE					
Revenues	4,823	6,100	7,766	13,891	17,832
Cost of revenues	911	1,459	2,259	6,112	7,133
Gross profit	3,912	4,640	5,507	7,779	10,699
EXPENSES					
Sales and Marketing	1,515	2,111	3,041	4,862	5,884
Product development	0	325	684	1,945	2,140
General and Administrative	2,005	1,988	2,404	5,279	6,419
Total Expenses	3,520	4,425	6,129	12,085	14,444
EBITDA	392	216	(622)	(4,306)	(3,745)
Amortization and Depreciation	393	275	217	959	923
EBIT	(1)	(59)	(839)	(5,265)	(4,668)
Interest income	24	36	66	92	37
Interest expense	(2)	(7)	(22)	(11)	(6)
Other income (expense)	(5)	(1)	8	-	-
Profit before effect of change in accounting principle	16	(31)	(787)	(5,184)	(4,636)
EBT	16	(31)	(787)	(5,184)	(4,636)
Taxes	0	(27)	(4)	0	0
Net Income	16	(59)	(791)	(5,184)	(4,636)
Basic and diluted earnings (loss) per share	0.00	(0.00)	(0.02)	(0.13)	(0.11)
Number of common shares outstanding	33,365	33,929	33,910	40,952	40,952

CONSOLIDATED BALANCE SHEET

As at December 31

(expressed in US\$, 000's)

	2004A	2005A	2006A	2007F	2008F
ASSETS					
Current					
Cash and cash equivalents	1,837	2,057	2,013	1,220	21
Net accounts receivable	596	760	814	1,389	1,783
Prepaid expenses & Marketable Securities	122	134	186	313	401
Total current assets	2,555	2,951	3,013	2,922	2,206
Intangible Assets				1,394	781
Goodwill				394	394
Property and equipment, net	287	339	447	439	379
Total Assets	2,842	3,290	3,460	5,149	3,759
LIABILITIES AND SHAREHOLDERS' EQUITY					
Current					
Bank indebtedness	0	0	0	0	0
Accounts payable and accrued liabilities	320	799	898	2,483	2,897
Accrued compensation	104	158	176	378	460
Deferred revenue	804	657	810	1,459	1,872
Current portion of capital lease obligation	0	64	130	174	17
Total current liabilities	1,228	1,677	2,015	4,494	5,247
Capital lease obligation	0	75	97	17	0
Long-term payables				32	32
Long-term deferred revenues		89	65	65	65
Total liabilities	1,228	1,841	2,177	4,608	5,344
Shareholders' equity (deficiency)					
Issued and outstanding shares	13,568	13,359	13,793	18,058	20,358
Additional paid-in capital	3,099	3,202	3,394	3,571	3,782
Accumulated Profit (Deficit)	(15,054)	(15,113)	(15,904)	(21,088)	(25,724)
Total shareholders' equity (deficiency)	1,614	1,449	1,284	541	(1,584)
Total Liabilities and Shareholder's equity	2,842	3,290	3,460	5,149	3,759

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended December 31

(expressed in US\$, 000's)

	2004A	2005A	2006A	2007F	2008F
OPERATING ACTIVITIES					
Net income (loss)	16	(59)	(791)	(5,184)	(4,636)
Add (deduct) non-cash items					
Amortization	393	275	217	359	310
Amortization of Intangible Assets				600	613
Stock based compensation	0	42	121	177	211
Funds from Operations	409	258	(453)	(4,049)	(3,503)
Net change in operating assets and liabilities	86	297	164	(213)	427
Cash provided by (used in) operating activities	495	555	(290)	(4,262)	(3,075)
FINANCING ACTIVITIES					
Net proceeds from issuance of common stock	0	0	343	4,146	2,300
Proceeds on exercise of warrants	0	42	-	-	-
Proceeds on exercise of stock options	59	25	190	119	-
Net proceeds from (repayments of) notes payable	0	0	-	32	-
Repayment of capital lease obligation	(39)	(21)	(103)	(37)	(174)
Share Buyback	0	(214)	(27)	-	-
Cash provided by financing activities	20	(169)	402	4,260	2,126
INVESTING ACTIVITIES					
Purchase of property and equipment	(78)	(166)	(156)	(350)	(250)
Acquisition of MFD				(225)	
Acquisition of Semotus				(216)	
Cash used in investing activities	(78)	(166)	(156)	(791)	(250)
Increase in cash and cash equivalents	437	220	(44)	(793)	(1,199)
Cash and cash equivalents, beginning of year	1,400	1,837	2,057	2,013	1,220
Cash and cash equivalents, end of year	1,837	2,057	2,013	1,220	21

Fundamental Research Corp. Equity Rating Scale:

Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk

Hold – Annual expected rate of return is between 5% and 12%

Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk

Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

Fundamental Research Corp. Risk Rating Scale:

1 (Low Risk) - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.

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