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Research Report – Update

Investors should consider this report as only a single factor in making their investment decision.

Nephros, Inc.

Rating: Speculative Buy

Howard Halpern

NEPH $8.55 — (NASDAQ)

November 12, 2019

	2016 A	2017 A	2018 A	***2019 E***	***2020 E***
Total Revenue (in millions)	$2.3	$3.8	$5.7	***$9.7***	***$15.3***
Earnings (loss) per share*	($0.56)	($0.14)	($0.49)	***($0.58)***	***($0.33)***

52-Week range*	$11.35 – $3.69	Fiscal year ends:	December
Shares outstanding a/o 11/01/19	8.0 million	Revenue/shares (ttm)*	$1.20
Approximate float	3.0 million	Price/Sales (ttm)	7.1X
Market Capitalization	$65.6 million	Price/Sales (2020) E	4.7X
Tangible Book value/shr*	$0.31	Price/Earnings (ttm)	NMF
Price/Book	NMF	Price/Earnings (2020) E	NMF

All per share figures adjusted for a 1-9 reverse stock split effective at the end of the day on 7/9/19

Nephros Inc., headquartered in South Orange, NJ, is a water purification company that develops and sells high performance filters and ultrafilters (filters with pore size below 0.01 microns) primarily to hospitals for the prevention of infection from waterborne pathogens and in dialysis centers for the removal of biological contaminants from water and bicarbonate concentrates. The company's 62.5% owned subsidiary, Specialty Renal Products, is a development stage company focused on improving therapies for patients with renal disease.

Key Investment Considerations:

Maintaining Speculative Buy rating and 12-month price target of $15.50 per share.

Nephros has substantial growth potential within the water purification market with their portfolio of filter and ultrafilter products. The primary growth opportunity to 2020 should be from increased customer penetration of US hospitals and dialysis centers, as well as increased usage from existing customers. We estimate NEPH's customers consist of approximately 600 US hospital/dialysis centers out of an estimated 12,000.

We believe NEPH's Specialty Renal Products subsidiary's 2nd generation Hemodiafiltration (a form of renal replacement therapy) system, once FDA 510(k) clearance is received, has the potential to generate annual revenue of approximately $15 million if the product only achieves approximately 1% market penetration.

NEPH reported (on 11-6-19) a 3Q19 loss of ($0.10) per share on a 79.5% sales increase to $3.1 million. We projected a loss of ($0.12) per share on sales of $3.1 million. In 3Q18, the loss was ($0.08) per share on sales of $1.7 million.

For 2019, we project a net loss of $4.4 million or ($0.58) per share on sales growth of 70.5% to $9.7 million. We previously projected a loss of $4.4 million or ($0.59) per share on sales of $9.6 million. Our forecast reflects 3Q19 results and an increase in average shares to 7.5 million from a previously forecasted 7.3 million.

For 2020, we project a net loss of $2.6 million or ($0.33) per share on revenue growth of 57.6% to $15.3 million. We previously projected a loss of $1.2 million or ($0.16) per share on sales of $14.4 million. Our net loss forecast reflects higher than anticipated costs associated with the launch of NEPH's waterborne pathogen diagnostics test device and its 2nd generation renal device. Higher than anticipated sales and marketing costs should stem from a more rapid sales ramp for the company's high performance filters and ultrafilters within existing customers, as well as introducing its product offerings to new commercial customers.

Please view our Disclosures pages 15 – 17.

Appreciation Potential

Maintaining Speculative Buy rating and 12-month price target of $15.50 per share. Our price target should be supported by 2H19 and 2020 growth in the company's customer base (primarily hospitals and dialysis centers) driving recurring revenue from the water filtration filter replacement cycle, as well as the 2H19 launch of its new waterborne pathogen diagnostics test device that will require a new test kit each time a test is performed.

Our rating reflects anticipated growth from Nephros' commercial water purification product portfolio that includes high performance filters and ultrafilters (filters with pore size below 0.01 microns), as well as from its AETHER® brand of water filters to expand its market to include companies in the hospitality/foodservice industries. Our rating should be reinforced once its Specialty Renal Products subsidiary receives FDA 510(k) clearance for its 2nd generation Hemodiafiltration (a form of renal replacement therapy that removes more middle-molecular-weight solutes) system. NEPH anticipates submitting the 2nd generation Hemodiafiltration product for 510(k) clearance in the 2Q20/3Q20 time frame.

Our 12-month price target of $15.50 per share implies shares could appreciate approximately 80% over the next twelve months. According to Thomson Reuters, the average trailing twelve-month and 2020 price-to-sales multiples for companies in the Healthcare Equipment and Supplies sectors are 3.6X (unchanged) and 3.5X (unchanged), respectively (on estimated 2020 sales growth of 7.5%). NEPH's trailing twelve-month and 2020 price-to-sales multiples are 7.1X and 4.7X (prior was 9.8X and 5.2X), respectively (on estimated 2020 sales growth of nearly 57.6%). We anticipate investors are likely to accord a sales multiple that more than doubles the industry due primarily to over 57% sales growth for NEPH compared to 7.5% for the industry. We applied a sales multiple of 8X (unchanged) to our 2020 sales per share forecast of $1.92 (prior was $1.95), to obtain a year ahead price target of approximately $15.50 per share.

A higher valuation of Nephros is likely to be supported by rapid sales growth (i.e., approximately 60% annualized total revenue growth to 2020 from 2016), a narrowing of operating losses, and receiving FDA 510(k) clearance for its 2nd generation Hemodiafiltration system in 2020. In 2020, we forecast NEPH's operating losses narrowing to $2.2 million from nearly $4 million in 2019. The company's cash burn should narrow to $1.2 million in 2020 from an estimated $3.1 million in 2019.

We believe Nephros, Inc. is most suitable for risk tolerant investors that seek exposure to a microcap company providing FDA cleared water filtration products.

Overview

Nephros Inc., headquartered in South Orange, New Jersey, is a commercial-stage water purification company that develops and sells high performance filters and ultrafilters (filters with pore sizes below 0.01 microns). The company operates a 62.5% owned subsidiary called Specialty Renal Products (SRP) that is a development stage medical device company focused on improving therapies for patients with renal disease. SRP's primary goal is to complete the development of a second-generation Hemodiafiltration (dialysis) System (HDF). Its first-generation product is the only US Food and Drug Administration 510(k) cleared medical device that enables nephrologists to provide HDF treatment to patients with end stage renal disease. HDF is a form of renal replacement therapy that when compared with standard hemodialysis, removes more middle-molecular-weight solutes.

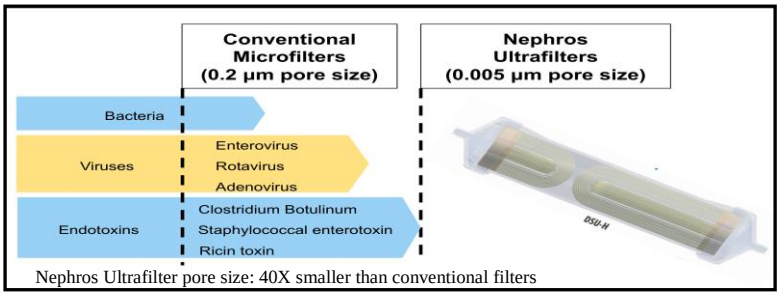
The company's medical device products are mostly classified as ultrafilters, and are primarily used in hospitals for the prevention of infection from water-borne pathogens (legionella, pseudomonas, and others), and in dialysis centers for the removal of biological contaminants from water and bicarbonate concentrate. Since the company's ultrafilters capture contaminants as small as 0.005 microns in size, they minimize exposure to a wide variety of bacteria, viruses, fungi, parasites, and endotoxins. NEPH expanded its commercial segment's NanoGuard® product line in December 2018 when it acquired the AETHER brand of water filters. The expanded product line should enable it to expand its customer base to the food service, convenience store, and hospitality industries, and to its existing hospital customers.

On August 14, 2019, the company's common stock began trading on the NASDAQ Capital Markets. The listing on NASDAQ aligns with the company's anticipated growth and commitment to maximize shareholder value.

Product Portfolio and Applications

The company develops and sells water filtration products used in both medical and commercial applications, employing multiple filtration technologies. The company's ultrafilters should have a competitive advantage compared to conventional microfilters based on pore size (see the picture on the right).

The company's product portfolio is broken down by target market.



Nephros Ultrafilter pore size: 40X smaller than conventional filters

Hospital and Healthcare Facilities

The primary purpose of NEPH's products for the hospital and healthcare facilities is the filtration of water for washing and drinking in order to enhance infection control. The company's filters produce water that is suitable for wound cleansing, cleaning of equipment used in medical procedures, and washing of surgeons' hands, etc. (NEPH's ultrafilter is pictured above on the right).

The company's product portfolio of filter/ultrafilters sold into hospitals and healthcare facilities (DSU-H, SSU-H, HydraGuard™, HydraGuard – F, and S100) have obtained FDA 510 (k) clearance and are marketed as either a dual-stage or single stage product, and/or in-line for protection from water borne pathogens. A competitive advantage Nephro's filters should have is its product life cycle, which is typically longer than conventional filters, thus reducing the annual cost of ownership. The reduced cost of ownership includes a reduction in replacement frequency that also lowers labor costs and allows for fewer physical trips into high-risk areas of a hospital such as intensive care units, neonatal intensive care units, and burn and transplant units. NEPH's offerings are also used to filter potable water that feed ice machines, sinks and showers, and sources that clean medical equipment, such as endoscope washers and surgical room humidifiers.

The company anticipates the addition of Legionella (a pathogenic group of gram-negative bacteria) risk prevention measures to Centers for Medicare & Medicaid Services (CMS) site inspections of hospitals and long term care facilities should increase the focus of infection control personnel and facilities engineers across the hospital industry. This focus should provide an opportunity for the company to market and expand its customer base within US hospitals and dialysis centers.

US Dialysis Centers

Nephros' FDA 510(k) cleared dialysis ultrafilters are designed to be used to filter water or bi-carbonate used in providing hemodialysis (a dialysis machine and a special filter called an artificial kidney, or a dialyzer, used to clean a patients blood) quality water or bicarbonate concentrate. The devices are not a complete water treatment system, but serve to remove biological contaminants. All dialysis clinics have dedicated water purification systems to produce water and bicarbonate concentrate, the two essential ingredients for making the liquid needed to remove waste material from the blood.

NEPH has FDA 510(k) clearance on its portfolio of medical device products for use in the dialysis setting. The company's ultrafilters (DSU-D and SSU-D) are sold to be used in water lines and bicarbonate concentrate lines leading into dialysis machines, and as a filter for portable reverse osmosis machines. The products can last up to 12-months.

The company has FDA 510(k) clearance to market its EndoPur 0.005-micron cartridge ultrafilter. The product offers single-stage protection from bacteria, viruses, and endotoxins and can last up to 12-months. It is primarily used to filter water following treatment with a reverse osmosis (RO) system typical in large RO systems that can provide ultrapure water to an entire dialysis clinic.

Commercial Facilities

The company markets a portfolio of proprietary products (under the NanoGuard® and AETHER® brands) for use in commercial, industrial, and food service settings.

The commercial NanoGuard product line provides ultrafiltration (0.005-micron) technology that filters bacteria and viruses from water. In December 2018, the company acquired the AETHER® brand of filters, which expanded its product line and water filtration and purification technologies to include improving odor, taste, and reducing scale and heavy metals from filtered water. The Aether filtration systems are primary sold to hotels, convenience stores, and quick service restaurants, which are new verticals for the company's offerings. The primary competition for Aether products is 3M's Cuno® brand and Pentair's Everpure® brand.

Specialty Renal Products

Nephros was founded based on its 1st generation Hemodiafiltration HDF device. The company's 1st generation device was developed as an alternative dialysis modality that combines the benefits of standard hemodialysis and HF into a single therapy by clearing toxins using both diffusion and convection. The company realizes that HDF is not widely used in the US, but is widely used in Europe.

In 2018, the company formed a new subsidiary, Specialty Renal Products, Inc. (which is 62.5% owned by NEPH) in order to drive the development of a second-generation Hemodiafiltration (HDF) system. The 2nd generation HDF system has been constructed and is being funded through funds directly raised into the subsidiary that includes the $3 million series A preferred stock financing in September 2018. Once FDA 510(k) clearance is received, marketing of the new HDF system will commence in the US.

The goal of the 2nd generation HDF system is to reduce setup and changeover time by 90%, space requirements by at least 80%, and system costs by 95%. The new system should also eliminate nightly maintenance and be easier to operate. In order to make the 2nd generation HDF more efficient and marketable to dialysis healthcare facilities, it is being designed as an attachment to an existing hemodialysis (HD) machine. The 2nd generation device needs disposable filters and tube sets in order to operate.

Growth Strategy

Sales Distribution Model

Since 2015, the company has shifted its sales model to emphasize building a network of value-added resellers for its target markets, hospitals, dialysis centers, and commercial establishments. Sales to commercial establishments will be supplemented by direct sales efforts stemming from the sales team of the company's December 2018 acquisition of Biocon's Aether brand of water filters. Over time the replacement cycle for NEPH's filters should provide a recurring revenue stream.

The company's established operations in the medical market has experienced in excess of 55% annualized total revenue growth (2016 to 2018) since the implementation of its reseller sales model. The reseller relationships began with small mom and pop companies that service the water and maintenance needs of medical facilities such as hospitals and their satellite facilities such as dialysis centers. Those service companies sell Nephros' filters into those facilities and once installed, they service them when replacement is required. The rapid sales growth is due to the company expanding to regional service providers to medical facilities and growth should continue as relationships are forged with national service providers. The company anticipates it can also grow outside of the medical facilities market with its existing group of reseller relationships.

Product Development

The company's product development strategy is to launch products over the next couple of years that can drive revenue growth. Before the end of 2019, NEPH plans to launch its waterborne pathogen diagnostics product that has the potential to serve existing and new customers in the hospital and medical facilities markets. This new product offering can serve to drive revenues in two ways, the one-time purchase of the device and through the recurring purchase of Nephros' collection filters and DNA/RNA test kits that are used each time a test is performed. The

device and process can provide results from a single liter water sample in approximately one hour compared to the current process for identifying water borne pathogens where the sample must be sent out to a lab and can take up to 10 days before receiving results.

NEPH's 2nd generation Hemodiafiltration (HDF) system will not be available until it receives 510(k) clearance from the FDA. The company anticipates the product should be launched in 2020. Once launched, management anticipates the company's HDF system has the potential to be used in approximately 50 sites (from existing relationships) without a significant investment to sales and marketing. The company believes a 1% market penetration could provide approximately $15 million in annual disposables revenues.

Projections

Basis of Forecast

The primary growth driver is an expansion of the company's reseller network, which in turn should increase the company's customers for its portfolio of water filtration filters. The leverage that the company should experience from a growing number of customers using its filters is that once a defined replacement cycle exists (depending on the type of filter purchased), a recurring revenue stream should be sustained during our forecast period.

In November 2019, NEPH announced it anticipates revenue of at least $9.5 million with the potential of reaching $10 million. Revenue growth is being driven by hospital customers and distribution partnerships.

We anticipate the company's core operations in 2020 could approach breakeven on a cash basis. However, the investments being made in the Specialty Renal Products subsidiary and spending to launch its waterborne pathogen diagnostics test device in 2H19 should result in operating losses of nearly $4 million and cash burn of $3.1 million in 2019. In 2020, we forecast operating losses narrowing to $2.2 million, with cash burn of approximately $1.2 million.

We anticipate gross margin expansion to 58% in 2020, up from an estimated 57.8% in 2019 and 56.3% in 2018. The gross margin improvement should be due primarily to the increase in recurring revenue from the replacement lifecycle of the company's water filters.

In 2020, we project operating expenses of $11.1 million, up from an estimated $9.6 million in 2019 due primarily to higher than anticipated costs associated with the launch of NEPH's waterborne pathogen diagnostics test device and its 2nd generation renal device. Sales and marketing costs are also likely to be higher than anticipated as the company ramps its support to increase sales of its high performance filters and ultrafilters within existing customers and introduces its product offerings to new commercial customers.

Operations – 2019

We project revenue growth of 70.5% to $9.7 million (prior was $9.6 million) due primarily to 3Q19 results and the increase in new customers and expansion of sales within existing customers, as well as sales to customers experiencing pathogen outbreaks, which are seasonal in nature.

Gross profit should increase 75.1% to $5.6 million due primarily to sales growth and gross margin of 57.8% compared to 56.3% in 2018.

We project operating losses increasing to nearly $4 million from $3 million as operating expenses increase by 53.8% to nearly $9.6 million. We anticipate SG&A expense increasing 41.5% to $6.4 million to support sales growth from the company's existing and new Aether brand filters. We anticipate R&D expenses more than doubling to $3.1 million from $1.5 million in 2018. The more than doubling of R&D expense compared to 2018 reflects more rapid spending to complete, test, and launch its waterborne pathogen diagnostics test device and 2nd generation Hemodiafiltration device.

Non-operating expense consists of interest expense of $186,000 and other expense of $31,000. In 2018, the company had interest expense of $168,000, other expense of $35,000, and a $199,000 loss on extinguishment of debt.

We project a net loss of $4.4 million or ($0.58) per share compared to a loss of $3.4 million or ($0.49) per share. We previously projected a net loss of $4.3 million or ($0.59) per share. The reduction in the loss per share is due to higher than anticipated average shares outstanding of 7.5 million compare to our prior forecast of 7.3 million.

We estimate the company's federal, state, and foreign net operating loss carryforwards were in excess of $82 million at September 30, 2019.

Finances – 2019
We project cash burn of $3.1 million and an increase in working capital of $201,000. The increase in working capital is due primarily to an increase in inventory and receivables, offset in party by increases in payables and accruals. Cash used in operations of $3.3 million, capital expenditures, and the repayment of debt should be partially offset by an approximate $2 million common stock offering. We project cash to decrease by $1.7 million to $2.9 million at December 31, 2019.

Operations – 2020
We project revenue increasing 57.6% to $15.3 million (prior was $14.4 million) due primarily to the company's customer base expanding to include companies within the food service, convenience store, and hospitality industries, as well as the launch of its waterborne pathogen diagnostic product into its existing hospital customers. The company's 2nd generation Hemodiafiltration device should generate revenue in 2H20 after FDA clearance is received. We also anticipate a higher base of recurring revenue than previously forecast due primarily to rapid sales growth in 2H19.

Gross profit should increase 58% to $8.9 million reflecting revenue growth and gross margin expansion to 58% compared to an estimated 57.8% in 2019. The improvement in gross margin reflects an increase in the number of replacement filters installed and sales from filter and assays for its waterborne pathogen diagnostic product.

We project the operating loss narrowing to $2.2 million from an estimated loss of $4 million in 2019 as operating expense margin improves to 72.6% from an estimated 98.6% in 2019. We anticipate operating expenses increasing by 16% to $11.1 million to support sales growth. We project SG&A expense increasing 22.8% to $7.9 million due primarily to higher compensation costs and the implementation of marketing initiatives to support the growth of newly launched products. We anticipate R&D expense flat at $3.1 million. We project non-operating interest expense of $160,000 compared to $186,000 due lower debt balances. We project a net loss of $2.6 million or ($0.33) per share. We previously projected a net loss of $1.2 million or ($0.16) per share. The increase in our loss forecast reflects higher than anticipated spending to support sales growth.

Finances – 2020
We project cash burn of $1.2 million and a decrease in working capital of $437,000. The decrease in working capital is due primarily increases in payables and accruals. Cash used in operations of $748,000, capital expenses and the repayment of debt should decrease cash by $1 million to $1.9 million at December 31, 2020.

3Q19 and 9M19 Results

3Q19
Total revenue increased 79.5% to $3.1 million compared to $1.7 million in the year-ago period. Revenue growth was due to increased medical device sales to new and existing customers and expansion into commercial markets.

Gross profit increased 91.1% to $1.8 million compared to $952,000 reflecting higher sales and expansion of gross margin to 58.8% from 55.2% in the year-ago period. Gross margin expansion was due primarily to a volume discount from its manufacturer.

Operating expenses increased 71.8% to $2.5 million from $1.5 million in 3Q18. R&D expenses for the water filtration and renal product segments increased $425,000 to $777,000. The increase in total R&D expense was due to increased spending on the development of the company's 2nd generation HDF product in its renal product segment (a $161,000 increase to $366,000) and new filter development increased $264,000 to $411,000 in the water filtration

segment. SG&A expenses increased 67.2% to $1.8 million due primarily to increases in headcount, professional fees, stock-based compensation, investor relations expenses, and increased other expenses related to rent and expanded warehouse capabilities. D&A expense was $44,000 versus $42,000 in 3Q18. The company had a change in fair value of contingent consideration of approximately $94,000 due to lower than expected Biocon performance.

Non-operating expense was $49,000 compared to $39,000 in the year-ago period. Interest expense increased to $48,000 from $32,000 due primarily to a higher debt balance and accretion of contingent consideration. Other expense decreased to $1,000 compared to $8,000 in 3Q18 due primarily to foreign currency transaction losses. The net loss was $804,000 or ($0.10) after a non-controlling interest loss of $60,000 compared to a loss of $566,000 or ($0.08) per share. In 3Q18, there was a non-controlling interest loss of $16,000. We projected a net loss of $851,000 or ($0.12) per share on revenue of $3.1 million.

9M19

Total revenue increased 76% to $7.2 million compared to $4.1 million in the year-ago period. Revenue growth was due to increased medical device sales to new and existing customers and expansion into commercial markets. Gross profit increased 86% to $4.2 million compared to $2.2 million reflecting higher sales and gross margin expansion to 58.3% from 55.2% in the year-ago period.

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Total Revenue	**$ 7.2**	**$ 4.1**	**76.0%**
Total Cost of Sales	3.0	1.8	**63.7%**
Gross Profit	$ 4.2	$ 2.2	**86.0%**
Total Operating Expenses	7.0	4.5	**55.4%**
Operating Income	(2.9)	(2.3)	**25.2%**
Total Other Income (Expense)	(0.2)	(0.4)	**NMF**
Pre-Tax Income	(3.0)	(2.7)	**14.1%**
Undeclared deemed dividend - Non-controlling interest	(0.2)	(0)	
Net Income (loss)	$ (3.2)	$ (2.7)	**39.9%**
Earnings (loss) per share	($0.43)	($0.40)	
Avg Shares Outstanding	7.4	6.8	
Margins			
Gross margin - combinded	58.3%	55.2%	
Operating Margin	(39.9%)	(56.1%)	
Pre-Tax Margins	(42.3%)	(65.3%)	
Tax Rate	(5.9%)	(0.6%)	

Source: company reports

Operating expenses increased 55.4% to $7 million from $4.5 million due primarily to R&D expenses more than doubling to $2.3 million from $993,000 in the year-ago period. SG&A expenses increased 37.2% to $4.7 million from $3.4 million. D&A expense was $142,000 compared to $123,000 in 9M18.

Non-operating expense was $171,000 compared to $374,000 in the year-ago period. Interest expense decreased to $140,000 from $146,000. The year-ago period included a $199,000 loss on extinguishment of debt.

The net loss was $3.2 million or ($0.43) after a non-controlling interest loss of $180,000 compared to a loss of $2.7 million or ($0.40) per share. In 9M18, there was a non-controlling interest loss of $16,000.

Finances

In 9M19, cash burn was $2.2 million with a $401,000 increase in working capital resulting in cash used in operations of $2.6 million. The increase in working capital was due primarily to increases in inventory and receivables, partly offset by an increase in accruals. Cash used in operations, acquisition costs, and repayment of debt more than offset nearly $2 million in gross proceeds from the issuance of common stock. Cash decreased by $726,000 to $3.9 million at September 30, 2019.

Capital Structure

On August 17, 2017, the company entered into a loan agreement with Tech Capital, providing for a secured asset-based revolving credit facility of up to $1 million, which is payable monthly based on the average daily outstanding balance at a rate equal to 3.5% plus the prime rate per annum (prime rate will not be less than 4.25%). At September 30, 2019, the outstanding balance was $982,000 and the annual interest rate was 8.5%. The company uses this revolving facility for working capital and general corporate purposes. The loan agreement has a term of 12-months, which automatically renewed on August 17, 2018 and will automatically renew for successive 12-month periods unless cancelled. NEPH granted to Tech Capital a first priority security interest in its assets, including its accounts receivable and inventory, to secure all of its obligations.

On March 27, 2018, NEPH entered into a secured promissory note with Tech Capital, LLC for a principal amount of approximately $1.2 million. At September 30, 2019, the principal balance was $879,000 million. The note matures on April 1, 2023 and the unpaid principal accrues annual interest at 8%.

Market Briefs

Hospitals

A 2019 statistical report published by the American Hospital Association estimates there are over 6,200 hospitals with approximately 931,000 beds that are staffed. IBISWorld estimates that the number of US hospitals could reach 6,100 in 2024, up from nearly 5,551 in 2018. Growth is likely to be attributable to the aging US population, as demand for hospital services should increase.

According to the US Office of Disease Prevention and Health Promotion, healthcare associated infections (HAI) at any given time affect approximately 1 out of every 25-hospital patients. These infections can lead to the loss of life and is estimated to cost the US health care system billions of dollars each year. One cause of HAI's is from waterborne bacteria and viruses. Bacteria and viruses can be present in the aging infrastructure of a healthcare facilities plumbing system. One strategic benefit that has the potential to benefit Nephros' efforts to sell its products to US hospitals (currently we estimate the company has 600 hospital customers) was the issuance in 2017 by the Center for Clinical Standards and Quality at the Centers for Medicare and Medicaid Services (CMS) in which CMS surveyors will review policies, procedures, and reports documenting water management implementation results to verify that facilities are compliant with existing requirements.

The US Office of Disease Prevention and Health Promotion's Healthy People 2020 initiative is driving additional awareness regarding HAI. HAIs occur in all types of care settings, including acute care hospitals, ambulatory surgical centers, dialysis facilities, outpatient care, and long-term care facilities such as nursing homes and rehabilitation facilities. The Healthy People 2020 initiative reflects the commitment of the US Department of Health and Human Services (HHS) to prevent HAIs.

Dialysis Centers

Dialysis clinics need to have dedicated water purification systems to produce water and bicarbonate concentrate, two essential ingredients for making dialysate (the liquid that removes waste material from the blood). According to the American Journal of Kidney Diseases, there are approximately 6,300 dialysis clinics in the United States. According to 2015 statistics from the National Institute of Diabetes and Digestive and Kidney Diseases, there are more than 661,000 Americans afflicted with kidney failure, of which 468,000 individuals are on dialysis, and roughly 193,000 live with a functioning kidney transplant. Nephros estimates there are over 100,000 hemodialysis machines in operation in the US. The company's 2nd generation HDF offering is likely to be marketed as an upgrade to existing hemodialyis machines, thus avoiding a large capital investment for a whole new HDF machine from larger competitors.

Hospitality/Food Services

IBISWorld has an all-encompassing report for what they call the US Accommodation and Food Services industry, which is primarily comprised of companies in the hospitality (hotels, casinos, etc.) and food services (restaurants, convenience stores, etc.). IBISWorld anticipates the number of establishments in 2023 for this industry of more than 1.2 million, up from under 1.1 million in 2017. While growth is good, the overall number of establishments is key to Nephros' growth as they have very little penetration in the market. A small increase in hospitality/food service customers should make a significant impact to top line results.

Competitive Landscape

The water filtration market has well established companies that manufacture point-of-use microfiltration products such as Pall Corporation (a subsidiary of Danaher Corporation), and that manufacture the Cuno® and Everpure® brands of water filtration and purification products, such as 3M and Pentair, respectively. Nephros believes it can compete within the water filtration market by developing and marketing products that are designed to meet critical and specific customer needs more effectively than devices on the market, offering filters and ultrafilters that have

unique attributes such as product reliability, user-friendliness (easy to install), and performance capabilities (extended life i.e., changing a filter once or twice a year compared to competitors offerings that need to be changed more often), and pursuing alliance and/or acquisition opportunities for joint product development and distribution.

The markets in which the company sells its commercial dialysis center products are highly competitive. The competition includes publicly traded companies such as Baxter International Inc., Fresenius Medical Care AG, Asahi Kasei Medical Co. Ltd., Terumo Medical Corporation and Toray Medical Co., Ltd., and international companies not publicly traded in the US such as B. Braun Melsungen AG, Nipro Medical Corporation Ltd., and Nikkiso Co., Ltd.

The company's 62.5% owned subsidiary, Specialty Renal Products, a development stage company focused on improving therapies for patients with renal disease, faces intense competition within the dialyzer and renal replacement therapy market. The company's success in this market will be dependant on its ability to meet the clinical goals of nephrologists, improve patient outcomes, and remain cost-effective for payers. The company competes with other suppliers of End-Stage Renal Disease (ESRD) therapies, supplies, and services. Suppliers include publicly traded companies Fresenius Medical Care AG and Baxter International, Inc., who are two of the primary machine manufacturers in hemodialysis.

Risks

In our view, these are the principal risks underlying the stock.

Operating Losses
Nephros Inc. has yet to turn profitable. At September 30, 2019, the company's accumulated deficit was $127.2 million, up from $124.2 million in 2018. Losses are likely to continue but diminish through our forecast period. The lack of profitability could result in the company's inability to execute its growth strategy and diminish its operations.

Compliance
The company's operations have a significant compliance burden under the FDC Act (set of laws giving authority to the US Food and Drug Administration (FDA) to oversee the safety of food, drugs, medical devices, and cosmetics) and other applicable statutes and regulations which govern the testing, labeling, storage, record keeping, distribution, sale, marketing, advertising and promotion of Nephro's medically approved products. A violation of the FDC Act or other regulatory requirements at any time during or after the product development and/or approval process, could subject NEPH to enforcement actions by the FDA or other agencies.

Product Liability
The production, marketing and sale of kidney dialysis and water-filtration products have liability risks in the event of product failure or claim of harm caused by the products operation. Voluntary recalls could subject the company to claims or proceedings by consumers, the FDA or other regulatory authorities, which would adversely impact future sales and revenues. Also, meritless claims of product liability may be costly to defend against. While the company does have product liability insurance, it may not be able to maintain this insurance on acceptable terms or at all.

Regulatory Approval
NEPH cannot ensure that any existing product(s) that have not yet been approved, or any new products developed in the future, will be approved for marketing. The clearance and/or approval processes are lengthy and uncertain and can require substantial financial resources, as well as management's time and effort. As a result, the company's global sales efforts may be slow to materialize and could drain financial resources to continue the development of new products for sale in the US.

Intellectual Property
The company's success depends in part on the ability to protect the intellectual property for its technology through patents. NEPH will only be able to protect its products and methods from unauthorized use by third parties to the extent that the products and methods developed are covered by valid and enforceable patents or are effectively maintained as trade secrets. The company has been granted 12 US patents that will expire at various times from 2019 to 2027, assuming they are properly maintained.

Licensing Agreement

In 2012, Nephros entered into a licensing and supply agreement with Medica S.p.A., an Italy-based medical product manufacturing company for the marketing and sale of certain filtration products based upon their proprietary Medisulfone ultrafiltration technology. The license and supply agreement with Medica expires on December 31, 2025. During the period (April 23, 2014 through December 31, 2025), the company will pay Medica a royalty rate of 3% of net sales of the filtration products sold, subject to reduction as a result of a supply interruption pursuant to the terms of the agreement.

510(k) Regulations

Before a new medical device can be introduced to the market, FDA clearance of a pre-market notification under Section 510(k) of the FDC Act or FDA clearance of a pre-market approval application under Section 515 of the FDC Act must be obtained. A 510(k) clearance will be granted if the submitted information establishes that the proposed device is substantially equivalent to a legally marketed medical device or to a medical device for which the FDA has not called for pre-market approval under Section 515. The Section 510(k) pre-market clearance process is generally faster and simpler than the Section 515 pre-market approval process. The company's filters and ultrafilters are medical devices that have gone through the 510(k) approval process.

Any devices cleared through the 510(k) process, modifications or enhancements that could significantly affect the safety or effectiveness of the device or that constitute a major change to the intended use of the device will require a new 510(k) pre-market notification submission. If the company seeks to obtain Section 510(k) pre-market clearance for any of its new or modified devices or filtration products, it would need to submit another 510(k) pre-market notification that could be costly and time consuming that may divert financial and management resources from products already approved and generating revenue in the US.

Shareholder Control

All executive officers and directors as a group, own 6.8% of the outstanding voting stock (March 2019). Two large investors own 56% of the company's outstanding voting stock. These owners could greatly influence the outcome of matters requiring stockholder approval, which decisions may or may not be in the best interests of the other shareholders.

Miscellaneous Risk

The company's financial results and equity values are subject to other risks and uncertainties, including competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

Trading Volume

Based on our calculations, the average daily-volume in 2018 was 41,100 shares. During the three months to November 11, 2019, volume decreased to 17,900. The company has a float of approximately 3 million shares and shares outstanding of 8 million. The company effected a reverse stock split (1-9) on July 9, 2019.

Nephros, Inc.
Consolidated Balance Sheets
FY2016 – FY2020E
(in thousands)

	FY16A	FY17A	FY18A	3Q19A	**FY19E**	**FY20E**
ASSETS						
Current assets:						
Cash	$ 275	$ 2,194	$ 4,581	$ 3,855	**$ 2,906**	**$ 1,885**
Accounts receivable, net	388	836	1,452	1,894	**1,616**	**1,783**
Investment in lease, net	27	20	-	-	**-**	**-**
Inventory, net	479	674	1,864	2,128	**2,726**	**2,986**
Prepaid expenses and other current assets	95	85	276	240	**305**	**229**
Total current assets	1,264	3,809	8,173	8,117	**7,554**	**6,883**
Property and equipment, net	70	52	91	85	**89**	**90**
Investment in lease, net and operating lease right-of-use assets	61	39	-	1,165	**1,165**	**1,165**
Intangible assets	-	-	590	559	**545**	**500**
Goodwill	-	-	748	759	**759**	**759**
License and supply agreement, net	1,262	1,072	938	837	**805**	**800**
Other assets	21	11	18	32	**39**	**39**
Total assets	$ 2,678	$ 4,983	$ 10,558	$ 11,554	**$ 10,956**	**$ 10,236**
LIABILITIES AND STOCKHOLDERS' EQUITY						
Current liabilities:						
Secured revolving credit facility	-	711	991	982	**1,000**	**1,021**
Secured note payable	-	-	195	207	**203**	**203**
Accounts payable	585	872	836	690	**1,045**	**1,427**
Accrued expenses	240	218	396	715	**970**	**1,375**
Contingent consideration	-	-	236	271	**329**	**329**
Operating lease liabilities	-	-	-	251	**373**	**497**
Deferred revenue	70	70	-	-	**-**	**-**
Total current liabilities	895	1,871	2,654	3,116	**3,920**	**4,852**
Secured note payable, net	-	-	843	672	**620**	**389**
Equipment financing debt, net	-	-	-	10	**10**	**10**
Contingent consideration, net	-	-	263	78	**78**	**50**
Long-term operating lease liabilities	-	-	-	956	**956**	**956**
Unsecured long-term note payable, net	838	954	-	-	**-**	**-**
Long-term portion of deferred revenue	278	208	-	-	**-**	**-**
Stockholders' equity:						
Common stock,$.001 par value; authorized 90,000,000 shares;	6	6	7	8	**8**	**8**
Additional paid-in capital	120,879	122,973	127,873	130,830	**130,615**	**131,615**
Accumulated other comprehensive income	67	77	71	63	**70**	**70**
Retained earnings (accumulated deficit)	(120,285)	(121,106)	(124,153)	(127,188)	**(128,324)**	**(130,714)**
Total stockholders' equity	667	1,950	3,798	3,713	**2,369**	**979**
Noncontrolling interest	-	-	3,000	3,009	**3,003**	**3,000**
Total liabilities and stockholders' equity	$ 2,678	$ 4,983	$ 10,558	$ 11,554	**$ 10,956**	**$ 10,236**
SHARES OUT	49,783	55,293	7,180	7,673	**7,965**	**7,985**

Source: Company reports and Taglich Brothers estimates

Nephros, Inc.
Annual Income Statement
FY2016 – FY2020E
(in thousands)

	FY16 A	FY17 A	FY18 A	**FY19 E**	**FY20 E**
Total Revenue - Product and License, royalty, other	$ 2,320	$ 3,809	$ 5,687	**$ 9,698**	**$ 15,280**
Total Cost of sales	1,026	1,517	2,484	**4,089**	**6,420**
Gross Profit	1,294	2,292	3,203	**5,609**	**8,860**
Operating Expenses:					
Research and development	1,079	1,002	1,539	**3,101**	**3,100**
Depreciation and amortization	230	218	163	**182**	**140**
Selling, general, and administrative	2,854	3,298	4,517	**6,393**	**7,850**
Change in fair value of contingent consideration	-	-	-	**(113)**	**-**
Total Operating Expenses	4,163	4,518	6,219	**9,563**	**11,090**
Operating Income (loss)	(2,869)	(2,226)	(3,016)	**(3,954)**	**(2,230)**
Loss on extinguishment of debt	-	-	(199)	**-**	**-**
Interest (expense) income	(167)	(298)	(168)	**(186)**	**(160)**
Other income (expense)	4	(74)	(35)	**(31)**	**-**
Total Other Income (expense)	(163)	(372)	(402)	**(217)**	**(160)**
Pre-Tax Income (loss)	(3,032)	(2,598)	(3,418)	**(4,171)**	**(2,390)**
Income Tax Expense (Benefit)	-	(1,789)	(93)	**-**	**-**
Net income (loss)	(3,032)	(809)	(3,325)	**(4,171)**	**(2,390)**
Undeclared deemed dividend - Non-controlling interest	-	-	(77)	**(240)**	**(240)**
Net income (loss) - attributable to Nephros, Inc.	$ (3,032)	$ (809)	$ (3,402)	**$ (4,411)**	**$ (2,630)**
Earning (loss) per share	$ (0.56)	$ (0.14)	$ (0.49)	**$ (0.58)**	**$ (0.33)**
Avg Shares Outstanding	5,398	5,882	6,847	**7,546**	**7,965**
EBITDA - Adjusted - includes renal subsidiary	$ (1,989)	$ (1,216)	$ (1,734)	**$ (2,243)**	**$ (730)**
Margin Analysis					
Gross margin	55.8%	60.2%	56.3%	**57.8%**	**58.0%**
Research & Development	46.5%	26.3%	27.1%	**32.0%**	**20.3%**
Selling, general, and administrative	123.0%	86.6%	79.4%	**65.9%**	**51.4%**
Operating margin	(123.7%)	(58.4%)	(53.0%)	**(40.8%)**	**(14.6%)**
Pre-tax margin	(130.7%)	(68.2%)	(60.1%)	**(43.0%)**	**(15.6%)**
Tax rate	0.0%	68.9%	2.7%	**0.0%**	**0.0%**
YEAR / YEAR GROWTH					
Total Revenues	N/A	64.2%	49.3%	**70.5%**	**57.6%**

Source: Company reports and Taglich Brothers estimates

Nephros, Inc.
Income Statement Model
Quarters FY2018A – 2020E
(in thousands)

	Q1 18 A	Q2 18 A	Q3 18 A	Q4 18 A	FY18 A	Q1 19 A	Q2 19 A	Q3 19 A	Q4 19 E	**FY19 E**	Q1 20 E	Q2 20 E	Q3 20 E	Q4 20 E	**FY20 E**
Total Revenue - Product and License, royalty, other	$ 985	$ 1,366	$ 1,724	$ 1,612	$ 5,687	$ 1,769	$ 2,309	$ 3,095	$ 2,525	**$ 9,698**	$ 2,900	$ 3,630	$ 4,900	$ 3,850	**$ 15,280**
Total Cost of sales	518	536	772	658	2,484	771	942	1,276	1,100	**4,089**	1,250	1,465	2,055	1,650	**6,420**
Gross Profit	467	830	952	954	3,203	998	1,367	1,819	1,425	**5,609**	1,650	2,165	2,845	2,200	**8,860**
Operating Expenses:															
Research and development	289	352	352	546	1,539	756	793	777	775	**3,101**	775	775	775	775	**3,100**
Depreciation and amortization	41	40	42	40	163	50	48	44	40	**182**	35	35	35	35	**140**
Selling, general, and administrative	1,260	1,091	1,069	1,097	4,517	1,503	1,403	1,787	1,700	**6,393**	1,850	1,925	2,100	1,975	**7,850**
Change in fair value of contingent consideration	-	-	-	-	-	(10)	(9)	(94)	-	**(113)**	-	-	-	-	**-**
Total Operating Expenses	1,590	1,483	1,463	1,683	6,219	2,299	2,235	2,514	2,515	**9,563**	2,660	2,735	2,910	2,785	**11,090**
Operating Income (loss)	(1,123)	(653)	(511)	(729)	(3,016)	(1,301)	(868)	(695)	(1,090)	**(3,954)**	(1,010)	(570)	(65)	(585)	**(2,230)**
Loss on extinguishment of debt	(199)	-	-	-	(199)	-	-	-	-	-	-	-	-	-	**-**
Interest (expense) income	(85)	(27)	(31)	(25)	(168)	(46)	(46)	(48)	(46)	**(186)**	(40)	(40)	(40)	(40)	**(160)**
Other income (expense)	(22)	(2)	(8)	(3)	(35)	(2)	(28)	(1)	-	**(31)**	-	-	-	-	**-**
Total Other Income (expense)	(306)	(29)	(39)	(28)	(402)	(48)	(74)	(49)	(46)	**(217)**	(40)	(40)	(40)	(40)	**(160)**
Pre-Tax Income (loss)	(1,429)	(682)	(550)	(757)	(3,418)	(1,349)	(942)	(744)	(1,136)	**(4,171)**	(1,050)	(610)	(105)	(625)	**(2,390)**
Income Tax Expense (Benefit)	-	-	-	(93)	(93)	-	-	-	-	-	-	-	-	-	**-**
Net income (loss)	(1,429)	(682)	(550)	(664)	(3,325)	(1,349)	(942)	(744)	(1,136)	**(4,171)**	(1,050)	(610)	(105)	(625)	**(2,390)**
Undeclared deemed dividend - Non-controlling interest	-	-	(16)	(61)	(77)	(59)	(61)	(60)	(60)	**(240)**	(60)	(60)	(60)	(60)	**(240)**
Net income (loss) - attributable to Nephros, Inc.	$ (1,429)	$ (682)	$ (566)	$ (725)	$ (3,402)	$ (1,408)	$ (1,003)	$ (804)	$ (1,196)	**$ (4,411)**	$ (1,110)	$ (670)	$ (165)	$ (685)	**$ (2,630)**
Earning (loss) per share	$ (0.23)	$ (0.10)	$ (0.08)	$ (0.09)	$ (0.49)	$ (0.20)	$ (0.14)	$ (0.10)	$ (0.15)	**$ (0.58)**	$ (0.14)	$ (0.08)	$ (0.02)	$ (0.09)	**$ (0.33)**
Avg Shares Outstanding	6,174	6,940	7,130	7,143	6,847	7,130	7,388	7,703	7,963	**7,546**	7,965	7,965	7,965	7,965	**7,965**
EBITDA - Adjusted - includes renal subsidiary	$ (773)	$ (394)	$ (314)	$ (253)	$ (1,734)	$ (909)	$ (485)	$ (209)	$ (640)	**$ (2,243)**	$ (635)	$ (195)	$ 310	$ (210)	**$ (730)**
Margin Analysis															
Gross margin	47.4%	60.8%	55.2%	59.2%	56.3%	56.4%	59.2%	58.8%	56.4%	**57.8%**	56.9%	59.6%	58.1%	57.1%	**58.0%**
Research & Development	29.3%	25.8%	20.4%	33.9%	27.1%	42.7%	34.3%	25.1%	30.7%	**32.0%**	26.7%	21.3%	15.8%	20.1%	**20.3%**
Selling, general, and administrative	127.9%	79.9%	62.0%	68.1%	79.4%	85.0%	60.8%	57.7%	67.3%	**65.9%**	63.8%	53.0%	42.9%	51.3%	**51.4%**
Operating margin	(114.0%)	(47.8%)	(29.6%)	(45.2%)	(53.0%)	(73.5%)	(37.6%)	(22.5%)	(43.2%)	**(40.8%)**	(34.8%)	(15.7%)	(1.3%)	(15.2%)	**(14.6%)**
Pre-tax margin	(145.1%)	(49.9%)	(31.9%)	(47.0%)	(60.1%)	(76.3%)	(40.8%)	(24.0%)	(45.0%)	**(43.0%)**	(36.2%)	(16.8%)	(2.1%)	(16.2%)	**(15.6%)**
Tax rate	0.0%	0.0%	0.0%	12.3%	2.7%	0.0%	0.0%	0.0%	0.0%	**0.0%**	0.0%	0.0%	0.0%	0.0%	**0.0%**
YEAR / YEAR GROWTH															
Total Revenues	34.2%	59.0%	88.2%	24.0%	49.3%	79.6%	69.0%	79.5%	56.6%	**70.5%**	63.9%	57.2%	58.3%	52.5%	**57.6%**

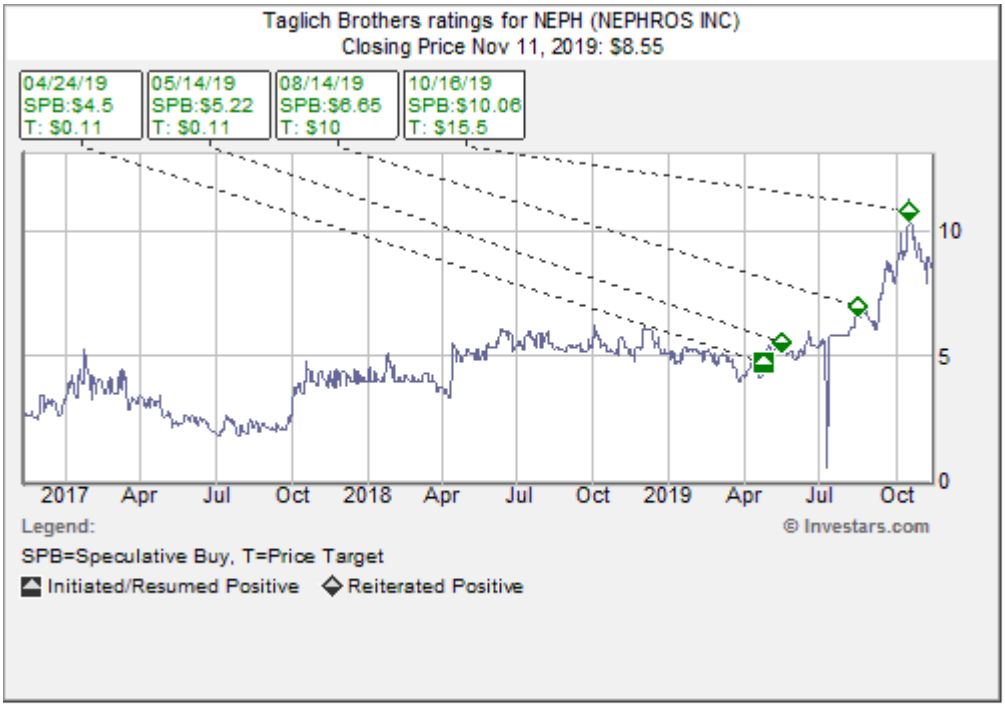
Source: Company reports and Taglich Brothers estimates

Nephros, Inc.
Cash Flow Statement
FY2016 – FY2020E
(in thousands)

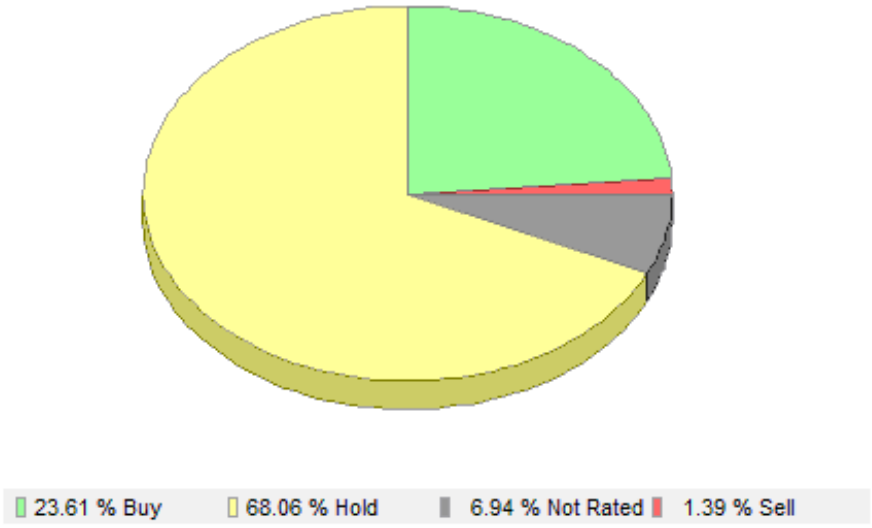
	FY2016A	FY2017A	FY2018A	9 Mos19A	**FY2019E**	**FY2020E**
Cash Flows from Operating Activities						
Net Income (loss)	$ (3,032)	$ (809)	$ (3,325)	$ (3,035)	**$ (4,171)**	**$ (2,390)**
Depreciation of property and equipment	19	28	29	20	**32**	**30**
Amortization of license and supply agreement	211	190	134	132	**176**	**175**
Non-cash stock-based comopensation, including stock options/restricted stock	551	772	985	662	**750**	**1,000**
Non-employee stock-based compensation	46	-	-	-	**-**	**-**
Loss on extinguishment of debt	-	-	199	-	**-**	**-**
Inventory reserve	27	-	70	37	**60**	**-**
Change in fair value of contingent consideration	-	-	-	(113)	**(37)**	**-**
Accretion of contingent consideration	-	-	-	41	**56**	**-**
Provision for bad debt expense	35	-	40	19	**19**	**-**
Amortization of debt discount	53	116	34	-	**-**	**-**
Loss on disposal of equipment	-	-	10	-	**-**	**-**
Loss on capital lease termination	-	-	11	-	**-**	**-**
Loss on foreign currency transactions	(4)	19	3	(2)	**6**	**-**
Cash earnings (burn)	(2,094)	316	(1,810)	(2,239)	**(3,109)**	**(1,185)**
Changes In:						
Accounts receivable	(17)	(416)	(484)	(461)	**(164)**	**(166)**
Inventory	(103)	(195)	(1,082)	(301)	**(862)**	**(260)**
Prepaid expenses and other current assets	(10)	30	(191)	21	**(29)**	**76**
Other assets	206	(10)	-	28	**(21)**	**-**
Accounts payable	(76)	268	(130)	(144)	**209**	**382**
Accrued expenses	51	-	35	456	**574**	**405**
Deferred revenue	(69)	(70)	-	-	**93**	**-**
(Increase)/decrease in Working Capital	(18)	(393)	(1,852)	(401)	**(201)**	**437**
Net cash provided by Operations	(2,112)	(77)	(3,662)	(2,640)	**(3,310)**	**(748)**
Cash Flows from Investing Activities						
Purchase of property and equipment	(45)	-	-	(14)	**(19)**	**(10)**
Biocon Acquisition, net	-	-	(991)	(137)	**(137)**	**-**
Cash Flows from Investing Activities	(45)	-	(991)	(151)	**(156)**	**(10)**
Cash Flows from Financing Activities						
Proceeds from issuance of common stock, net	-	1,179	3,778	1,992	**1,992**	**-**
Net proceeds (repayment) from secured revolving credit facility	-	711	280	(9)	**(100)**	**-**
Net proceeds (repayment) from equipment financing	-	-	-	13		
Proceeds from sale of subsidiary preferred shares to noncontrolling interest	-	-	3,000	-	**-**	**-**
Payments on secured note payable	-	-	(149)	(159)	**(335)**	**(231)**
Payment of contingent consideration	-	-	-	(78)	**(78)**	**(32)**
Proceeds from issuance of secured note	1,187	-	1,187	-	**-**	**-**
Repayment of unsecured long-term not payable	-	-	(1,187)	-	**-**	**-**
Proceeds from exercise of warrants and stock options	1	100	138	313	**313**	**-**
Net cash provided (used) by Financing	1,188	1,990	7,047	2,072	**1,792**	**(263)**
Effect of exchange rates	(4)	6	(7)	(7)	**(1)**	**-**
Net change in Cash	(973)	1,919	2,387	(726)	**(1,675)**	**(1,021)**
Cash Beginning of Period	1,248	275	2,194	4,581	**4,581**	**2,906**
Cash End of Period	$ 275	$ 2,194	$ 4,581	$ 3,855	**$ 2,906**	**$ 1,885**

Source: Company reports and Taglich Brothers estimates

Price Chart



Taglich Brothers Current Ratings Distribution



Investment Banking Services for Companies Covered in the Past 12 Months

Rating	#	%
Buy	2	10
Hold		
Sell		
Not Rated	1	25

Important Disclosures

As of the date of this report, we, our affiliates, any officer, director or stockholder, or any member of their families do not have a position in the stock of the company mentioned in this report. Taglich Brothers, Inc. does not currently have an Investment Banking relationship with the company mentioned in this report and was not a manager or co-manager of any offering for the company with in the last three years.

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Analyst Certification

I, Howard Halpern, the research analyst of this report, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities and issuers; and that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this report.

Public Companies mentioned in this report:

Asahi Kasei Corporation	(OTC: AHKSY)	3M Company	(NYSE: MMM)
Baxter International Inc.	(NYSE: BAX)	Pentair plc	(NYSE: PNR)
Danaher Corporation	(NYSE: DHR)	Terumo Corporation	(OTC: TRUMY)
Fresenius Medical Care AG & Co.	(NYSE: FMS)	Toray Industries, Inc.	(OTC: TRYIY)

Meaning of Ratings

Buy – The growth prospects, degree of investment risk, and valuation make the stock attractive relative to the general market or comparable stocks.

Speculative Buy – Long-term prospects of the company are promising but investment risk is significantly higher than it is in our BUY-rated stocks. Risk-reward considerations justify purchase mainly by high risk-tolerant accounts. In the short run, the stock may be subject to high volatility and could continue to trade at a discount to its market.

Neutral – Based on our outlook the stock is adequately valued. If investment risks are within acceptable parameters, this equity could remain a holding if already owned.

Sell – Based on our outlook the stock is significantly overvalued. A weak company or sector outlook and a high degree of investment risk make it likely that the stock will underperform relative to the general market.

Dropping Coverage – Research coverage discontinued due to the acquisition of the company, termination of research services, non-payment for such services, diminished investor interest, or departure of the analyst.

Some notable Risks within the Microcap Market

Stocks in the Microcap segment of the market have many risks that are not as prevalent in Large-cap, Blue Chips or even Small-cap stocks. Often it is these risks that cause Microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume which can lead to large spreads and high volatility in stock price. In addition, Microcaps tend to have significant company-specific risks that contribute to lower valuations. Investors need to be aware of the higher probability of financial default and higher degree of financial distress inherent in the microcap segment of the market.

From time to time our analysts may choose to withhold or suspend a rating on a company. We continue to publish informational reports on such companies; however, they have no ratings or price targets. In general, we will not rate any company that has too much business or financial uncertainty for our analysts to form an investment conclusion, or that is currently in the process of being acquired.