

Atossa Genetics

(ATOS-NASDAQ)

ATOS: Sales is picking up steam in 1Q13 following national rollout of ForeCYTE, progress made in reimbursement—Outperform

OUTLOOK

Atossa is a pure play breast health testing company with a focused growth strategy. The Company has recently launched FDA cleared MASCT System for NAF collection and two lab testing services, and will launch two new testing services in 2013.

We see total revenue growing at 96% CAGR from 2013 to 2018, with the Company turning profitable in 2015 with EPS of \$0.05. We see EPS at \$1.08 in 2018.

We think downside risk is low while upside potential is high at this time. We rate Atossa shares Outperform based on the Company's strong fundamentals.

Current Recommendation	Outperform
Prior Recommendation	N/A
Date of Last Change	12/19/2012
Current Price (05/14/13)	\$5.64
Twelve- Month Target Price	\$15.00

SUMMARY DATA

52-Week High	\$12.37
52-Week Low	\$3.80
One-Year Return (%)	N/A
Beta	0.29
Average Daily Volume (sh)	185,207

Shares Outstanding (mil)	13
Market Capitalization (\$mil)	\$73
Short Interest Ratio (days)	0.43
Institutional Ownership (%)	38%
Insider Ownership (%)	41%

Annual Cash Dividend	\$0.00
Dividend Yield (%)	0.00

5-Yr. Historical Growth Rates

Sales (%)	N/A
Earnings Per Share (%)	N/A
Dividend (%)	N/A

P/E using TTM EPS	N/A
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P/E using 2012 Estimate	N/A
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P/E using 2013 Estimate	N/A
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Zacks Rank	N/A
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Risk Level	N/A
Type of Stock	N/A
Industry	Med Instruments
Zacks Rank in Industry	N/A

ZACKS ESTIMATES

Revenue

(in millions of \$)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2012	0.05 A	0.22 A	0.11 A	0.10 A	0.48 A
2013	0.18 A	0.36 E	0.76 E	1.01 E	2.30 E
2014					9.70 E
2015					15.50 E

Earnings per Share

(EPS is operating earnings before non recurring items)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2012	-\$0.09 A	-\$0.10 A	-\$0.10 A	-\$0.11 A	-\$0.41 A
2013	-\$0.14 A	-\$0.13 E	-\$0.11 E	-\$0.11 E	-\$0.50 E
2014					-\$0.09 E
2015					\$0.05 E

Zacks Projected EPS Growth Rate - Next 5 Years %	N/A
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WHAT'S NEW

Atossa Genetics Reports 2013 First Quarter Financial Results

On May 15, 2013, Atossa Genetics, Inc. (ATOS) announced its 2012 financial results and corporate developments.

Total revenue for the three months ended March 31, 2013, were \$182,670, which included \$13,440 of product revenue from the sale of MASCT Systems and \$169,230 of diagnostic testing service revenue from the ForeCYTE breast health tests. This compares with total revenues of \$54,713 for the first quarter ended March 31, 2012. The year-over-year increase in total revenue was driven by the national rollout of the ForeCYTE test in January 2013.

Gross profit for the three months ended March 31, 2013, was \$116,206. This compares to gross profit of \$27,709 for the quarter ended March 31, 2012.

Total operating expenses were \$2.1 million for the three months ended March 31, 2013, consisting of G&A expenses of \$1.6 million, selling expenses of \$272,575 and research and development expenses of \$220,192. This compares to total operating expenses of \$1.1 million for the three months ended March 31, 2012, consisting of G&A expenses of \$601,452, selling expenses of \$70,435 and research and development expenses of \$417,990. The increase in G&A expenses of \$963,420, from the first quarter of 2012 to the first quarter of 2013, is attributed to the launch of the Company's MASCT System, ForeCYTE test and ArgusCYTE test and the related growth in expenses to hire additional staff and expand the Company's operations.

Net loss for the quarter ended March 31, 2013, was \$1.9 million, or \$(0.14) per share, compared with net loss of \$1.1 million, or \$(0.09) per share, for the first quarter ended March 31, 2012.

At March 31, 2013, Atossa had cash and cash equivalents of \$1.4 million.

First quarter financials were in line with our estimates in general. As the Company continues to roll out its ForeCYTE tests nationally, revenue growth will accelerate in the coming quarters.

\$30 Million Stock Purchase Agreement Provides Financing Flexibility

On Mar 28, 2013, Atossa entered into a \$30 million stock purchase agreement with Aspire Capital, LLC.

Under terms of the agreement, Aspire has made an initial purchase of \$1 million of Atossa common stock at a price of \$12.00 per share on March 27, 2013. In addition, after the SEC declares the registration statement related to the transaction effective, Aspire has committed to purchase up to an additional \$29 million of Atossa's common stock over the next three years at prices based on prevailing market prices over a period preceding each sale.

Atossa will control the timing and amount of any additional sales of common stock to Aspire and will know the sales price before directing Aspire to purchase shares. Aspire has no right to require any sales by Atossa, but is obligated to make purchases as Atossa directs, in accordance with the terms of the purchase agreement. Aspire has agreed to a long-only position. There are no limitations on use of proceeds, financial covenants, restrictions on future financings, rights of first refusal, participation rights, penalties or liquidated damages in the purchase agreement. The purchase agreement may be terminated by Atossa at any time, at its discretion, without any additional cost or penalty. Atossa has issued 250,000 shares of its common stock to Aspire Capital as a commitment fee in connection with entering into the purchase agreement.

Atossa also entered into a registration rights agreement with Aspire in connection with its entry into the purchase agreement that requires the Company to file a registration statement regarding the shares sold to Aspire Capital. Atossa will use the net proceeds from the sales of common stock for general corporate purposes and working capital requirements.

We think the agreement with Aspire provides added financial strength and flexibility to Atossa, allowing the Company to raise equity opportunistically based on market conditions and its working capital needs. Atossa presently does not expect to need to raise additional equity capital in the near term other than under this agreement.

Distribution Agreement With Millennium HealthCare Will Boost Atossa Topline for 2013

The Agreement

This morning (May 2, 2013), Atossa Genetics (ATOS) announced that it has signed an agreement with **Millennium HealthCare Inc.** (MHCC) for the distribution by Millennium Medical Devices of Atossa's ForeCYTE Breast Health devices, which consist of the patented MASCT pump and ForeCYTE patient collection kits.



Millennium has submitted an initial order for 10,000 ForeCYTE collection kits, which it intends to market to managed-care networks, healthcare clinics and physician practices in the New York Metro Area and Northern New Jersey.

Atossa's MASCT system is used by physicians and nurses to collect a small amount of nipple aspirate fluid for analysis by the National Reference Laboratory for Breast Health with the ForeCYTE Breast Health Test.

The Implications

We think this distribution agreement is a great achievement for Atossa as it will boost the Company's top line in the coming quarters.

The ForeCYTE Test provides Atossa with two revenue sources:

- Revenue from the sale of the MASCT System device and patient kits to physicians, breast health clinics, and mammography clinics; and

- Service revenue from the preparation and interpretation of the NAF samples sent to the Company's laboratory for analysis.

Atossa offers each component of the MASCT System for sale separately. The NAF sample collection device is currently priced at approximately \$250 per device and the patient kits are priced at approximately \$30 per kit. The cytology and molecular diagnostics testing and analysis services are billed to federal and/or state health plans at the reimbursement rates of either \$384 or \$1,275 per patient, depending on the complexity of the analysis performed. The Company expects that the substantial majority of patients will be billed at the \$384 rate. Some patients (approximately 10%) need more complex tests, which will be billed at the rate of \$1,275. This higher rate is only for those patients who have an initial test result that requires further analysis.

Atossa bills third-party payors at higher rates, as is customary for the industry.

Based on the above information, the initial order of 10,000 collection kits will bring about \$7.5 million in revenue for Atossa.

We think the distribution agreement with Millennium Healthcare represents an important milestone for the national rollout of ForeCYTE test.

In January 2013, Atossa initiated the national rollout of the ForeCYTE Breast Health Test in partnership with Clarity Women's Health. Clarity distributes the Clarity-branded ForeCYTE product line with major national distributors. These distributors collectively have more than 5,000 employee sales representatives and/or independent sales representatives selling their products to a target market of 33,000 obstetric-gynecologists in the United States.

Atossa, together with Clarity, is making steady progress in the national rollout of its ForeCYTE Test. Early responses from doctors and their patients are encouraging.

To help ensure that more doctors and their patients have access to the ForeCYTE and ArgusCYTE tests and that patients will receive insurance reimbursement for the laboratory costs associated with these tests, Atossa entered into two contracts with third parties to facilitate the reimbursement process from insurers, one with MultiPlan, Inc. in September 2012 and another with FedMed, Inc., in February 2013:

Progress Made in Reimbursement

On Mar 13, 2013, Atossa Genetics (ATOS) entered into a contractual agreement with **FedMed, Inc.**, one of the largest proprietary Preferred Provider Organization (PPO) networks in the U.S., for diagnostic laboratory testing.

FedMed is a National Provider Network and Healthcare Financial Services Organization. FedMed has developed innovative programs and services for the healthcare provider community in conjunction with large payors of healthcare services. FedMed's objective is to provide significant measurable benefits to providers not available from other provider networks and managed care organizations. Traditional networks and payors are eager to negotiate and take discounts, but less than eager to pay on time and quantify the value of their contracts. FedMed's programs have been created to specifically address these challenges.

FedMed's network is comprised of more than 550,000 providers, including 4,000 hospitals and more than 60,000 ancillary facilities, serving over 40 million Americans.

The agreement with FedMed is a great achievement for Atossa for its diagnostics testing. The agreement will give FedMed's participating providers and its clients' members greater access to Atossa's tests,

including the two launched products ForeCYTE Breast Health Test and the ArgusCYTE Breast Health Test.

The addition of Fedmed further expand Atossa's reimbursement network. Before FedMed, Atossa only has an agreement with **MultiPlan, Inc.** which was established in September 2012. MultiPlan is a leading provider of healthcare cost management solutions for diagnostic laboratory testing. Approximately 20% of Americans are covered by MultiPlan. The agreement with MultiPlan will give MultiPlan's participating providers and their patients access to Atossa's tests including the ForeCYTE and ArgusCYTE Breast Health Tests.

Going forward, we believe Atossa will make continued efforts to further expand its relationships with network providers to facilitate the reimbursement for its diagnostic testing.

INVESTMENT HIGHLIGHTS

- Atossa is targeting the rather large clinical lab testing market with a focus on breast health testing services, which has been growing rapidly in recent years due to rapid advancement in genomics and proteomics research. This market continues to grow dramatically due to the rapid growth of personalized medicine.
- Atossa launched two breast health testing services in late 2011; with two new testing tools expected to be launched in 2013. The Company holds numerous patents approved or pending and has built a strong portfolio which provides long term growth potential in the years to come.
- We think revenue growth will accelerate in the coming years thanks to the focused marketing strategy and continued new products/services offering. We model the top line growing from \$2.30 million in 2013 to \$66.5 million in 2018, an impressive CAGR of 96%. We think Atossa will become profitable in 2015 with EPS of \$0.05, which will grow to \$1.08 per share in 2018.
- Atossa has an appropriate growth strategy in place. Recent developments within the Company have made us believe this strategy will be well executed and we have a high confidence in management's ability to lead Atossa to the next level of growth in the next five years.
- Based on the Company's strong fundamentals, we think its shares are undervalued. We think downside risk is low at this point and upside potential is high. We encourage investors to accumulate Atossa shares at current level.

VALUATION AND RECOMMENDATION

We maintain our Outperform rating on Atossa Genetics and reiterate our 12-month price target of \$15.00 per share.

Atossa is an emerging medical diagnostics company with a focus on breast cancer detection. The Company has launched two breast health tests in late 2011 and will launch two more tests in 2013. Atossa also holds 179 issued patents and 50 pending patent applications directed to its products, services, and technologies. The Company has eleven 510(k)-cleared medical devices and two 510(k)-exempt medical devices. This strong intellectual property position provides long term growth for the Company in the years to come.

We think revenue will accelerate in the coming years thanks to its focused marketing strategy and continued new products/services offering. We see total revenue growing at an impressive 96%

compound annual growth rate (CAGR) from fiscal 2013 to 2018 according to our new financial model. We model that the Company will become profitable in fiscal 2015 with earnings per share (EPS) of \$0.05 based on total revenue of \$15.5 million. We forecast EPS will grow to \$1.08 per share based on revenue of \$66.5 million in fiscal 2018. This is impressive considering the relatively short history of the operations and the small size of the Company.

Based on Atossa's strong fundamentals, we think there is a lot of room for further appreciation of its share price. Currently, Atossa shares are trading at about \$5.50 per share which values the Company at \$74 million in terms of market cap based on 13.5 million shares outstanding. We think Atossa shares should trade at 35 x P/E multiple which is similar to the biotech industry average P/E ratio. If we use this P/E multiple, coupled with our estimated EPS of \$1.08 in 2018, discounted at 20% for five years, we come up with a price target of \$15.00 per share.

One wild card for Atossa valuation is that the Company could be an acquisition target for big players. The clinical lab testing industry is quite fragmented currently, and merger & acquisition activity is looming. We all know that big players LabCorp and Quest Diagnostics are increasingly acquiring smaller players in this field. Qiagen NV, a research service company based in Netherland, entered into molecular diagnostics market in 2007 by acquiring Digene Corp. Since then, Qiagen has been quite aggressive in acquisition of other small genetic/molecular testing companies.

With the increased activity in M&A in the industry, Atossa could be an easy target for acquisition. If acquired by big players, share price of Atossa may soar.

We are optimistic about the Company's prospect. With a rapidly growing market worldwide, combined with its unique technology and broad range of product offering, the Company is well positioned to boost its top line and bottom line in the coming years. We think at this time, downside risk for Atossa is relatively low while upside potential is high.

In the past one and a half months, share price of Atossa retreated dramatically from \$12.37 on March 19 to current \$5 per share on May 9, 2013.

The major reason for the retreat in our view is that investors are concerned about the end of lock up period which ended on May 7, 2013 related to its recent IPO.

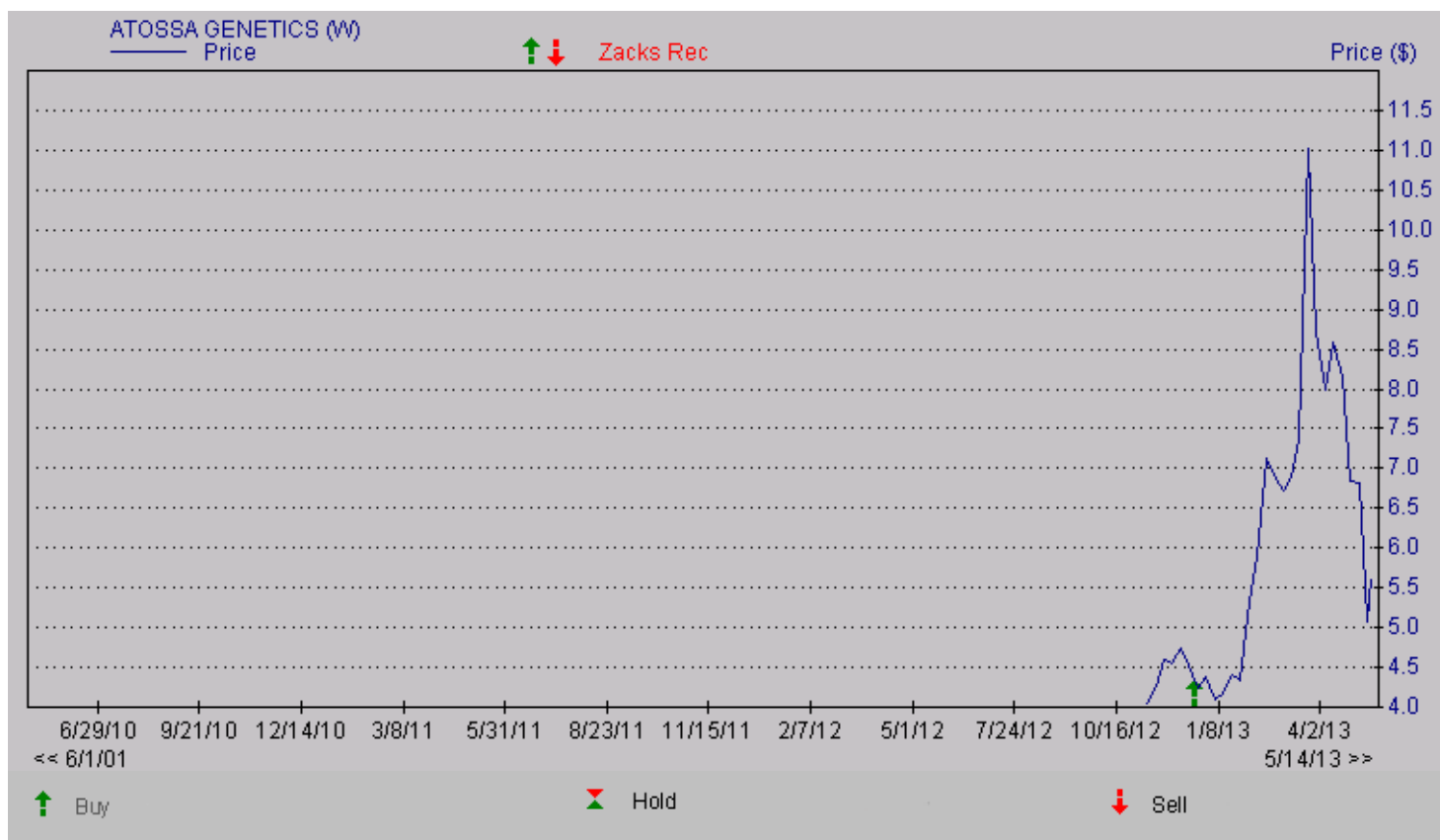
We think the retreat is not warranted and provides a good entry opportunity for both new and existing investors. The fundamentals of Atossa remain strong and there is lots of room for price appreciation in the next 12 months when the Company rolls out its two approved diagnostics nationally and launches two new products in 2013.

PROJECTED INCOME STATEMENT

	2012A (Dec)					2013E (Dec)					2014E (Dec)	2015E (Dec)	2016E (Dec)	2017E (Dec)	2018E (Dec)
\$ in million except per share data	Q1	Q2	Q3	Q4	FYA	Q1A	Q2E	Q3E	Q4E	FYE	FYE	FYE	FYE	FYE	FYE
Diagnostic Testing Services	\$0.05	\$0.22	\$0.10	0.10	\$0.48	\$0.17	\$0.35	\$0.75	\$1.00	\$2.27	\$9.50	\$15.00	\$25.00	\$40.00	\$65.00
Product sales	\$0.00	\$0.00	\$0.00	0.00	\$0.01	\$0.01	\$0.01	\$0.01	\$0.01	\$0.03	\$0.20	\$0.50	\$0.75	\$1.00	\$1.50
Total Revenues	\$0.05	\$0.22	\$0.11	\$0.10	\$0.48	\$0.18	\$0.36	\$0.76	\$1.01	\$2.30	\$9.70	\$15.50	\$25.75	\$41.00	\$66.50
YOY Growth	-	-	-	-	32164.5%	234.6%	59.1%	615.1%	898.0%	374.8%	322.2%	59.8%	66.1%	59.2%	62.2%
CoGS	0.00	0.02	0.02	0.03	0.07	0.07	0.03	0.08	0.10	0.27	1.16	2.02	3.86	6.15	9.98
Gross Income	\$0.05	\$0.21	\$0.09	\$0.07	\$0.42	\$0.12	\$0.33	\$0.68	\$0.90	\$2.03	\$8.54	\$13.49	\$21.89	\$34.85	\$56.53
Gross Margin	94.1%	92.0%	85.7%	70.6%	86.4%	63.6%	92.0%	90.0%	90.0%	88.2%	88.0%	87.0%	85.0%	85.0%	85.0%
SG&A	\$1.09	\$1.37	\$1.23	\$1.80	\$5.49	\$1.84	\$1.85	\$1.95	\$2.00	\$7.64	\$8.50	\$10.00	\$12.50	\$15.00	\$20.00
% SG&A	1996.6%	614.6%	1161.4%	1785.5%	1133.4%	1005.9%	521.1%	258.3%	199.0%	332.4%	87.6%	64.5%	48.5%	36.6%	30.1%
R&D	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.22	\$0.25	\$0.30	\$0.50	\$1.27	\$1.50	\$2.50	\$4.00	\$7.50	\$10.00
% Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Operating Income	(\$1.0)	(\$1.2)	(\$1.1)	(\$1.7)	(\$5.1)	(\$1.9)	(\$1.8)	(\$1.6)	(\$1.6)	(\$6.9)	(\$1.5)	\$1.0	\$5.4	\$12.4	\$26.5
Operating Margin	-	-	-	-	-	-	-	-	-	-	-	-	-	30.12%	39.89%
Other Net	(\$0.0)	(\$0.0)	(\$0.0)	(\$0.0)	(\$0.0)	\$0.0	(\$0.0)	(\$0.0)	(\$0.0)	(\$0.0)	(\$0.0)	(\$0.1)	(\$0.1)	(\$0.1)	(\$0.1)
Pre-Tax Income	(\$1.0)	(\$1.2)	(\$1.1)	(\$1.7)	(\$5.1)	(\$1.9)	(\$1.8)	(\$1.6)	(\$1.6)	(\$6.9)	(\$1.5)	\$0.9	\$5.3	\$12.3	\$26.5
Income taxes(benefit)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.5
Tax Rate	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Reported Net Income	(\$1.0)	(\$1.2)	(\$1.1)	(\$1.7)	(\$5.1)	(\$1.9)	(\$1.8)	(\$1.6)	(\$1.6)	(\$6.9)	(\$1.5)	\$0.9	\$5.3	\$12.3	\$26.0
YOY Growth	-	-	-	-	-	-	-	-	-	-	-	-	-	-	111.3%
Net Margin	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Diluted Shares Out	11.3	11.3	11.3	16.0	12.5	13.4	13.5	14.0	14.0	13.7	16.0	18.0	20.0	22.0	24.0
Reported EPS	(\$0.09)	(\$0.10)	(\$0.10)	(\$0.11)	(\$0.41)	(\$0.14)	(\$0.13)	(\$0.11)	(\$0.11)	(\$0.50)	(\$0.09)	\$0.05	\$0.27	\$0.56	\$1.08
One time charge	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Non GAAP Net Income	(\$1.0)	(\$1.2)	(\$1.1)	(\$1.7)	(\$5.1)	(\$1.9)	(\$1.8)	(\$1.6)	(\$1.6)	(\$6.9)	(\$1.5)	\$0.9	\$5.3	\$12.3	\$26.0
Non GAAP EPS	(\$0.09)	(\$0.10)	(\$0.10)	(\$0.11)	(\$0.41)	(\$0.14)	(\$0.13)	(\$0.11)	(\$0.11)	(\$0.50)	(\$0.09)	\$0.05	\$0.27	\$0.56	\$1.08

Source: Company filing and Zacks estimates

HISTORICAL ZACKS RECOMMENDATIONS



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