# KeyStone's Small-Cap Stock Report

Editor: Ryan Irvine, BBA (Finance)
Senior Analyst: Aaron Dunn, CFA

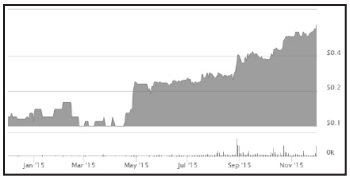
Independent Equity Advisors

## Lingo Media Corporation (LM:TSX-V)

**Current Price (November 30/2015): $0.74**

**RECOMMENDATION: SPEC BUY**

## UNDERFOLLOWED HIGH MARGIN EDUCATIONAL TECHNOLOGY MICRO-CAP POSTS BETTER-THAN-EXPECTED Q3, POISED FOR RECORD 2015, FAIR VALUE INCREASED – RATING MAINTAINED



Industry: Education Technology
Current Price: $0.74
Recommended: October 2015
Recommendation Price: $0.47
Market Cap: $20,781,056
Shares Outstanding: 28,082,509
Diluted: 36,121,677

**Focus BUY Portfolio**

**SELECTED QUARTERLY DATA**

| Income Statement | Q3 2015 | Q3 2014 |
|---|---|---|
| Revenues: | $1,203,201 | $222,468 |
| Earnings: | $631,730 | -$255,659 |
| Earnings Per Share: | $0.022 | -$0.009 |
| Fully Diluted EPS/PS: | $0.017 | -$0.007 |

**RATINGS**

**VALUE**

| | |
|---|---|
| P/E (ttm): | 10.14 |
| P/S (ttm): | 4.23 |
| P/B: | 6.54 |
| Current Ratio: | 3.88 |
| D/E: | 0.25 |

Lingo Media has coined itself an EdTech company, combining education with technology. Through its two distinct business units, the company develops, markets and supports a suite of English language learning solutions consisting of web-based software licensing subscriptions, online and professional services, audio practice tools and multi-platform applications. Lingo Media continues to operate its legacy textbook publishing business from which it collects recurring royalty revenues.

Since the beginning of 2015, Lingo Media's strategy has been to transition its business to online subscriptions and digital downloads that enable learners to bring your own device (BYOD) and look beyond paper-based textbook publishing. The company believes that these online subscription formats provide customers with an overall better learning experience, the flexibility to use the company's products on multiple platforms (i.e. beyond desktops to tablets and mobile extensions), and is a more economical and relevant way for Lingo Media to deliver its products to customers.

### REPORTED FINANCIAL HIGHLIGHTS

Lingo Media was recently recommended October of this year with the company's shares trading at $0.47. Today, following a strong set of Q3 2015 financials, we review the numbers and update our rating on the stock with it now trading at $0.74 or 57% higher than our original recommendation price and just below our Q2 near-term fair value of $0.75.

### THIRD QUARTER 2015 HIGHLIGHTS:

For the third quarter ended September 30, 2015, Lingo Media's revenue jumped 441% to $1.2 million from $222,468 in the same period of the prior year. As a result of the increased revenue, the company recorded a net (comprehensive) income of $631,730, or $0.023 per share basic, compared to a net loss ($255,659) in the same period of the prior year. The increase in revenue and net profit are primarily attributed to company's sales and marketing efforts in Online English Language Learning segment of its business.

**Online English Language Learning**
ELL Technologies earned revenue from its portfolio of products of $1.16 million for the quarter ended September 30, 2015, compared to $158,688 for the same period in 2014, an increase of 634%. This increase in sales is due to the company maximizing its sales efforts related to its ELL Technologies' redesigned suite of products. Since 2012, the company has


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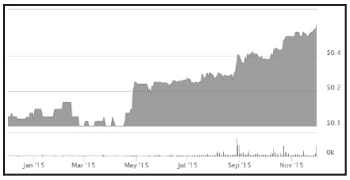
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completely redesigned the user interface, learning management system and the multi-browser delivery system for desktops and tablets for its ELL Technologies suite of products including Winnie's World, English Academy, Scholar, Campus Master and Business. The redesign has now been completed and full sales efforts have resumed and recorded a 634% increase in revenue in the 2015 third quarter compared to the same period in 2014.

- Partnered with Proloux, a subsidiary of the University of Guadalajara to provide accredited certification for ELL Technologies' software programs.
- Entered into an agreement with ISA Corporativo for advertising services throughout Mexico's metro stations in exchange for software licenses.
- Selected by Peruvian Navy to provide software licenses to ELL Technologies' training products.
- Secured software licensing contracts for ELL Technologies' programs with municipal government in Caldas Department, Colombia.
- Completed the development of ELL Technologies' Winnie's World, in HTML5 for the pre-kindergarten and kindergarten market.
- On September 30, 2015, awarded a large government contract with SENA, an organization under the Ministry of Labour of Colombia to build the world's largest digital library of English language learning resources.

**Print-Based English Language Learning (legacy business):**
Lingo Media earned royalty revenue of $39,155 for the three months period ended September 30, 2015, compared to $63,780 for 2014 from People's Education & Audio Visual Press. According to the company's current practice of recording revenues from PEP, Lingo Media recognizes no revenues from its print-based English language learning business in the first and third quarters as the sales from print-based products in China are reported semi-annually in the second and fourth quarters.

- Co-published 550 million units of PEP Primary English and Starting Line programs with People's Education Press in China.
- Conducted extensive teacher training initiatives and workshops.

## CONCLUSION

We were pleased with Lingo's Q3 numbers which bested market expectations in terms of both revenue and profitability and helped power the stock to new 4-year highs. With what


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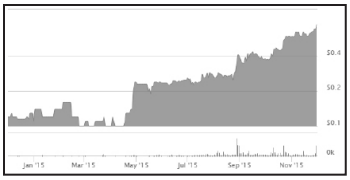
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is expected to be just over $5.5 million in sales for 2015, Lingo Media is truly a micro-cap company and a higher level of risk should be assigned to a company at this size. Having said this, the company reported only $2.5 million in sales last year, so the growth in 2015 is impressive. Add in strong margins, a better than expected Q3, strong projections for Q4, and Lingo Media is positioned for a record 2015. One concern at present is the company's relatively large accounts receivable position ($2.1 million). As yet, it does not appear to be a major concern given the fact that a significant percentage of the accounts are with large government organizations which tend to pay, but take longer to do so. We continue to monitor this.

The company has a small, but cash flow producing ($1.2-$1.6 in free cash flow annually) legacy business that is royalty based. This legacy print segment has five and a half years left on its contract, and it's recurring, growing in single digits. With a solid source of cash flow at present, the true focus and growth opportunity for Lingo Media is in the company's ELL Technologies business.

Lingo Media has undertaken a business transition which began to gather momentum during the second quarter of 2015. In fact since 2012, the company has completely redesigned its' proprietary user interface, learning management system and the multi-browser delivery system for desktops and tablets for its ELL Technologies suite of products including Winnie's World, English Academy, Scholar, Campus Master and Business. The redesign has now been completed and full sales efforts have resumed and produced a 634% increase in revenue in the third quarter 2015 compared to the same period in 2014. In Lingo Media's market, the key is to stay ahead of the curve technically. With the company's newly developed cutting edge technology, which is flexible and customizable and designed to work cross platform with cross browser capability and with availability in multiple countries with over 2,000+ hours of online training, management believes their ELL Technologies solutions are well positioned at the leading edge of the industry.

From a fundamental perspective, Lingo Media's shares currently trade at 10.4 times the company's earnings over the last 12-months – a reasonable, but not strikingly attractive multiple given the company's relatively small size. However, the company's shares appear to offer value if management is able to continue to hit or exceed targets as we witnessed in Q3 and produce a similar level of profitability in the upcoming Q4 as was achieved in Q2 2015. Management reported, in their Q2 2015 release, that during the second half of 2015, the


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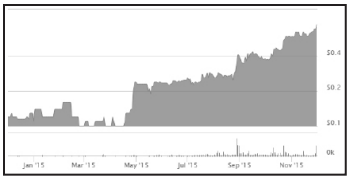
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company expects revenue growth and profitability to trend in a similar fashion as in the first half of 2015. The numbers reported in Q3 2015 greatly exceeded the first quarter of 2015 which bodes well for an even stronger second half of 2015. As such, we have revised our second half 2015 estimate higher to $1.75 million (from $1.3 million), or $0.062 per share basic, and $0.048 diluted per share in earnings. Our new estimate is $0.102 per share basic, or $0.08 per share in diluted earnings, for 2015. Management is currently looking for growth beyond this level in 2016 and we will look for further guidance at year's end. In the $0.74 range, Lingo Media has a low PE of around 7.4 based on our earnings estimate for 2015.

Given its small relative size and short history as a profitable entity under its new model, achieving a fair value estimate is extremely difficult and subject to a high degree of speculation. If we assign a PE of 9 to our expected 2015 EPS figure of $0.10 we arrive at near-term revised fair value in the range of $0.90. As such, Lingo Media's shares continue to hold upside potential from their current range for patient investors with an above average tolerance for risk.

As such, we maintain our SPEC BUY rating and the company's place in our Focus BUY Portfolio. As a micro-cap stock, we see the company as an appropriate investment only for those clients with an above average tolerance for risk. We would be patient and place limit orders initially below the $0.78 level.


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**BV (BV/Share): Book value (book value per share)**

Book value per common share calculated as total shareholder's equity less preferred equity, and divided by the number of common shares outstanding. Should the company decide to dissolve, the book value per common share indicates the dollar value remaining for common shareholders after all assets are liquidated and all creditors are paid.

**D/E: Debt-to-equity ratio**

A measure of a company's financial leverage calculated by dividing long term debt by shareholders equity. It indicates what proportion of equity and debt the company is using to finance its assets.

**Current ratio**

One of many ratios designed to evaluate short-term liquidity of a company. Calculated as current assets divided by current liabilities, this ratio gauges the level of cash resources relative to current liabilities as a measure of cash obligations.

**EBITDA**

Earnings before interest, taxes, depreciation, and amortization. EBITDA is calculated as revenue minus expenses (excluding tax, interest, depreciation, and amortization).

**EPS: Earnings per share**

A company's earnings available to common shareholders, also known as net income or net profit, divided by the number of shares outstanding.

**EV: Enterprise value**

Enterprise value is calculated as market capitalization less cash and equivalents, plus debt. Evaluation of EV relative to the company's trailing EBITDA is used in identifying potential takeover targets.

**FCF: Free cash flow**

Capital expenditures are subtracted from cash flow from operating activities to arrive at free cash flow, which intends to measure the cash available to a company after making all cash outlays necessary to maintain existing productive capacity (as measured by capital expenditures on a company's cash flow statement).

**Net working capital**

A measure of the company's ability to carry on its normal business comfortably and without financial stringency, to expand its operations without the need of new financing, and to meet emergencies and losses. Calculated by deducting current liabilities from the current assets.

**P/B: Price-to-book ratio**

Calculated as a stock's market value (current closing price) divided by its latest quarter's book value. While a lower P/B ratio could mean that the stock is undervalued, it could also serve as a sign of weak fundamentals, and as with most ratios, this varies a fair amount by industry.

**PEG ratio**

The price/earnings to growth, or PEG ratio is calculated as P/E ratio divided by a company's annual EPS growth. The PEG ratio is used to determine a stock's value while taking into account earnings growth.

**P/FCF: Price-to-free cash flow ratio**

Calculated as a company's current share price divided by its free cash flow per share (i.e., free cash flow divided by the number of company's shares outstanding) over the last four quarters (called "TTM," or "trailing 12 months" calculation). It is a measure of the market's expectations regarding a firm's future financial health.

**P/S: Price-to-sales ratio**

It is calculated as a stock's current market price divided by its sales (revenue) per share. When calculating this ratio, we use the company's revenue from its latest four quarters, or on a TTM basis.

**ROE: Return on equity**

A measure of a corporation's profitability, calculated as net income divided by shareholder's equity. ROE is often useful in comparing the profitability of a company to other firms in the same industry.

**Featured companies in KeyStone's Small-Cap Stock Report are evaluated on a scale of 1 to 5 on each of the following criteria:**

**Value:** 1 - poor investment value
5 - excellent investment value

**Growth:** 1 - poor growth potential
5 - excellent growth potential

**Risk/Liquidity:** 1 - high exposure to liquidity concerns
5 - low exposure to liquidity concerns

**Overall:** 1 - poor fundamental characteristics
5 - excellent fundamental characteristics

| Disclosure | | | | | |
|---|---|---|---|---|---|
| Stock Holding | | | | Other | |
| Companies | KeyStone | KeyStone Employees | Related Companies | Investment Banking Client | Related Company Business Relationship |
| Lingo Media Corporation | YES | YES | NO | NO | NO |


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