

## Company Update

# OCULUS INNOVATIVE SCIENCES, INC.

## 1Q12 Results Preview; Company in Great Shape

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### OCULUS INNOVATIVE SCIENCES, INC. (NASDAQ:CM – OCLS - \$1.53)

Price Target: \$3.50

Rating: Speculative Buy

#### COMPANY SNAPSHOT

Oculus is a healthcare company noted for its safe and effective tissue care products based upon the Microcyn® Technology platform which significantly reduces the need for antibiotics while reducing infections and accelerating healing. The Microcyn® Technology addresses the need for improved solutions in dermatology, oral care, cosmeceutical, wound care and other markets. It features a biocompatible, shelf-stable solution that is currently approved and commercialized in many of the world's largest markets. Several solutions derived from this platform have, in various studies, demonstrated the ability to treat antibiotic-resistant strains of bacteria (including MRSA and VRE), viruses; increase blood flow to the wound site; and reduce both inflammation and pain while assisting in faster wound closure.

#### KEY STATISTICS

|                       |               |
|-----------------------|---------------|
| Price as of 8/2/11    | \$1.53        |
| 52 Wk High – Low      | \$2.65 – 1.41 |
| Est. FD Shares Out.   | 26.5M         |
| Market Capitalization | \$40.5M       |
| 3 Mo Avg Vol          | 66,000        |
| Exchange              | NASDAQ:CM     |

#### COMPANY INFORMATION

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#### INVESTMENT HIGHLIGHTS

##### Update Summary

On Thursday, August 4<sup>th</sup>, after the close, Oculus is slated to release 1Q12 results, for the period ending June 30, 2011.

While we expect results to be in line with our expectations, ***we believe investors should focus on the Company's current positioning and trends, as Oculus is in great shape to achieve its objectives.***

##### Our Forecasts

Our model calls for \$2.975 million in revenue and a loss per share of **(\$0.05)**. We expect a blended gross margin of around 66%, which would be an improvement of 40 basis points from the full-year results for fiscal 2011. Revenue will likely be driven by the typical channels and we project that the geographic and product line source revenue mix will shift beginning in 2Q12. This is a direct result of the recently increased royalty rate to 30% from 20%, for *Innovacyn*.

##### Platform Positioning

We believe that Oculus is in great shape. The current platform is a proven anti-infective technology that reduces the need for antibiotics. The technology is buoyed by the all-encompassing agreement with AMNEAL which will likely bring quantifiable results, beginning later this year. New offerings such as *Puracyn* through *Innovacyn*, new partnerships, meaningful commercial activity in China, and the likely shift of current pending clearances to 510(k) clearance status for 1 or more products will only enhance Oculus' positioning. The pending products include Scar HydroGel, Allergen Shield HydroGel, and Oral indications.

To enhance its already diverse channels, Oculus recently announced a multi-year licensing agreement with Eloquest Healthcare, a wholly owned subsidiary of Ferndale Pharma Group, Inc., to market multiple Microcyn-based products in the United States under the Eloquest Healthcare brand, including Oculus' negative-pressure wound therapy solution and prescription wound care line. Marketing is slated to begin in early 2012.

# OCULUS INNOVATIVE SCIENCES, INC. (NASDAQ:CM – OCLS)

## Technology

**Oculus is well-positioned to become the global standard of care for the treatment and irrigation of open wounds and skin care.** The Company's highly effective anti-infective technology fills a serious need in the dermatology, oral care, and wound care markets.

Oculus is noted for its safe and effective tissue care products based upon the *Microcyn*® Technology platform which significantly reduces the need for antibiotics while reducing infections and accelerating healing. The *Microcyn*® platform technology generates stable, highly efficacious pH-neutral products based on the science of hypochlorous acid (HOCl), and is found only in trace amounts in the Oculus products. There have been some misleading reports regarding this HOCl concentration, which is also found in household bleach. Thus, investors could erroneously infer that the technology is nothing more than a bleach-based product, rather than complex chemistry in which Oculus has generated the only stable, non-toxic HOCl in a bottle.

The reports refer to an OCLS licensee's FDA-approved drug-like efficacy claims although it is approved for sale as a medical device offering. We should note that this licensee's offering and issues have no direct or indirect bearing on OCLS whatsoever, as this product provides negligible royalty streams to OCLS.

## Financial Positioning

**Oculus may be in the best financial position in many years. First, revenue from diversified sources is being generated at high growth rates. The *Innovacyn* line, effective July 1, will now generate 50% higher royalty rates, and new offerings down the line provide additional and diverse revenue streams.**

Importantly, the Company just enhanced its cash flow positioning via a recent loan and security agreement whereby the Company can borrow up to a total of \$2.5 million, in two tranches. Oculus has already borrowed \$1.5 million and if it meets certain milestones, has access to an additional \$1.0 million. According to the recently filed 8-K, the cash interest rate is 10%, with nine months of interest-only payments, to be followed by 30 months of a fixed principal and interest payment and a balloon payment at a 13% rate. Warrants are also attached to this agreement, including one warrant to purchase 226,325 shares at a price of \$1.657 per share.

In our view, Oculus' shares represent a tremendous opportunity for investors and that the stock is worth \$2.25 today, or 40% higher than Friday's closing price. With its projected hockey-stick type growth and upcoming milestone events, we believe that OCLS can reach \$3.50 in the next 6 months. Our preliminary 12-month target is \$5.00. We forecast 40% growth in revenue this year and 78% next year, plus meaningful operating profitability. Our methodology is based on a conservative 5x revenue multiple on estimated forward 12-month revenue forecasts. In addition, when valuing the Company based on operating income excluding non-cash compensation, FY13 results could appear to be stellar.

We rate these shares Speculative Buy.

## Company Update

**Analyst: Robert Goldman**

Rob Goldman has 20 years of investment and company research experience as a senior research analyst and as a portfolio and mutual fund manager. During his tenure as a sell-side analyst, Rob was a senior member of Piper Jaffray's Technology and Communications teams. Prior to joining Piper, Rob led Josephthal & Co.'s Washington-based Emerging Growth Research Group. In addition to his sell-side experience Rob served as Chief Investment Officer of a boutique investment management firm and Blue and White Investment Management, where he managed Small Cap Growth portfolios and *The Blue and White Fund*.

**Analyst Certification**

I, Robert Goldman, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report.

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