

Roka Bioscience (ROKA)

**1Q15 Recap - Results In-Line with Street & Below Wedbush
- Slight Improvement in Systems Sales - Cutting Estimates -
Lowering PT to \$3.50 - Maintain N**

- **Results in-line with consensus and below Wedbush estimates.** ROKA reported 1Q15 sales of \$1.5 MM and GAAP EPS loss of \$0.51 which missed our \$1.9 MM and (\$0.46) EPS loss estimate. 1Q15 results were in-line with Wall Street consensus estimates of \$1.4 MM and an EPS loss of (\$0.50).
- **Slight q/q improvement in system placements.** ROKA placed three total systems in 1Q15 which appeared to be roughly in-line with consensus expectations and five units below our model. Of note, the three systems were placed within the company's top 10 customers. We are lowering our 2015 and 2016 system placement estimates to 12 and 26 from 40 and 63, respectively.
- **Test utilization appears to be flattish q/q. Increased use of salmonella and E.coli tests appears to be offset by reductions in listeria utilization.** Pricing per test appears to be stable.
- **Listeria test issues still challenging the business. The new user friendly Listeria test is on-track for 3Q15 launch.** The new test development is complete and the company recently submitted it for AOAC approval. Of note, ROKA has received positive feedback from "several large" beta test customers. The company expects all customers to wait for AOAC approval before implementing the new listeria test. Management believes there is some pent up demand for the new listeria assay that may help compress the sales cycle, but did not quantify it.
- **GMs slightly better and opex in-line. Cash burn roughly in-line.**
- **Lowering 2015 and 2016 revenue & EPS substantially. Below consensus.**
- **Maintain NEUTRAL & lowering PT from \$9 to \$3.50.** We continue to be somewhat optimistic long term based on the best in class automation technology and the secular shift to molecular technologies. We arrive at our new 12-month \$3.5 price target through an EV/sales valuation framework where we assume a 7x 2016E EV/sales multiple with no cash and roughly 19 MM shares outstanding discounted back at 20%. Versus early stage life science tools, diagnostics and med tech group, ROKA is trading at a discount on a 2015E EV/sales multiple basis (2.8x vs. 3.6x).

May 8, 2015

Price
\$2.80

Rating
NEUTRAL

12-Month Price Target
\$3.50 (from \$9)

Zarak Khurshid
(415) 274-6823
zarak.khurshid@wedbush.com

Company Information

Shares Outst (M)	18
Market Cap (M)	\$51
52-Wk Range	\$2.75 - \$13
Cash/sh	3
Enterprise Value	11
LT Debt/Cap	0.124
2015 EV/Sales	3 x
Book Value/sh	3.9

Company Description

ROKA is an early stage diagnostics company focused on pathogen detection for food safety. The company's Atlas system and assay technologies represent a more accurate and more highly automated platform versus the competition.

FYE Dec	2014A	2015E			2016E		
REV (M)	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	\$0.8A	\$1.5A	\$2.0A	\$1.4A	\$2.4E	\$5.2E	\$3.2E
Q2 Jun	\$1.4A	\$1.6E	\$2.5E	\$1.5E	\$2.7E	\$6.3E	\$3.7E
Q3 Sep	\$1.5A	\$1.8E	\$3.3E	\$2.0E	\$3.0E	\$7.4E	\$4.5E
Q4 Dec	\$1.4A	\$2.0E	\$4.3E	\$2.6E	\$3.3E	\$8.6E	\$5.6E
Year*	\$5.1A	\$7.0E	\$12.0E	\$7.6E	\$11.4E	\$27.5E	\$16.3E
Change	132%	38%			64%		
	2014A	2015E			2016E		
EPS	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	(\$0.45)A	(\$0.51)A	(\$0.46)A	(\$0.50)A	(\$0.47)E	(\$0.42)E	(\$0.47)E
Q2 Jun	(\$0.40)A	(\$0.47)E	(\$0.47)E	(\$0.50)E	(\$0.46)E	(\$0.39)E	(\$0.46)E
Q3 Sep	(\$0.64)A	(\$0.47)E	(\$0.45)E	(\$0.49)E	(\$0.45)E	(\$0.35)E	(\$0.43)E
Q4 Dec	(\$0.40)A	(\$0.47)E	(\$0.43)E	(\$0.48)E	(\$0.45)E	(\$0.31)E	(\$0.40)E
Year*	(\$1.90)A	(\$1.92)E	(\$1.82)E	(\$1.97)E	(\$1.83)E	(\$1.47)E	(\$1.65)E
P/E	NM	NM			NM		
Change	543%	1%			-5%		

Consensus estimates are from Thomson First Call.

* Numbers may not add up due to rounding.



Source: Thomson Reuters

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Investment Thesis

ROKA is a pure play diagnostics company focused on the food safety industry. The company operates a razor/razorblade business model where it sells equipment and testing consumables directly to food processing plants and third party laboratories. ROKA's Atlas platform represents a more highly automated, accurate and flexible platform for detection of pathogens (e.coli, listeria and salmonella), which we believe will over time take share from incumbent players and become the gold standard. The commercial story remains early and the company began to see positive inflection with higher quality and higher volume customers in 1H14. In our view, ROKA is primarily an execution story and the company's strong management team, with a prior record of success, inspires confidence. ROKA represents long term play on the automation secular theme and the growing global need for better food safety. Near term the company is experiencing deceleration in growth due to disruption from its listeria test redevelopment (due to false positive issues). Our estimates are below consensus for 2015 and 2016 and we could become more bullish after the 3Q15 redeployment of the test and after we see signs of reacceleration.

We arrive at our 12-month \$3.50 price target through EV/sales valuation framework where we assume a 7x 2017E EV/sales multiple with no cash and roughly 19 MM shares outstanding discounted back at 20%. Versus early stage life science tools, diagnostics and med tech group, ROKA is trading at a discount on a 2015 EV/sales multiple basis (2.8 vs. 3.6).

Results

Figure 1: Results

	1Q:15	
	REV (m)	EPS
Actual	1.50	(\$0.51)
Wedbush	1.96	(\$0.46)
Consensus	1.40	(\$0.50)

Source: Company data, Wedbush Securities, Inc.

Figure 2: Catalysts/Pipeline

Catalyst/Milestones	Timing
Earnings (system placements and test utilization metrics)	Quarterly
Additional Large Lab Wins	2015
Large Beef Contract	2H15
Listeria user friendly (low fals positive test)	Mid-15
Listeria Non-Amplified Test Launch	2015
Min-Atlas Prototype Completion	2015
Next-Gen E.Coli test (faster)	2H15
Min-Atlas Commercial Launch	2016/2017
Potential multiplexed allergen testing	2017+

Source: Company data, Wedbush Securities, Inc.

Figure 3: Variance

	1Q14A	1Q15E	1Q15A	Δ Y/Y	Δ A/E
Product Revenue	828	1,962	1,511	82%	-23%
Total Revenues	828	1,962	1,511	82%	-23%
Cost of revenues	1,265	3,151	1,964	55%	-38%
Gross profit	(437)	(1,188)	(453)	4%	-62%
Gross Margins	-52.7%	-60.6%	-30.0%	-43%	-51%
Research and development	1,842	2,000	1,889	3%	-6%
General and administrative	2,255	5,200	5,113	127%	-2%
Selling and Marketing	2,793			-100%	NA
Amortization of intangibles	42	200	937	2131%	NA
Total operating expenses	6,932	7,400	7,939	15%	7%
Operating Income	(7,369)	(8,588)	(8,392)	14%	-2%
Interest income	(389)	27	(466)	20%	-1839%
Other	(603)	0	0	NA	NA
Income before taxes	(8,361)	(8,562)	(8,858)	6%	3%
Provision for income taxes	6	0	2	NA	NA
Tax Rate				NA	NA
Net income	(8,367)	(8,562)	(8,860)	6%	3%
Net Income	(8,367)	(8,562)	(8,860)	6%	3%
GAAP EPS -Basic	(\$0.48)	(\$0.48)	(\$0.51)	8%	6%
GAAP EPS -Diluted	(\$0.45)	(\$0.46)	(\$0.51)	13%	11%
Non-GAAP EPS -Diluted	(\$0.45)	(\$0.46)	(\$0.51)	13%	11%
Weighted average shares - basic	17,600	17,662	17,221	-2%	-2%
Weighted average shares - diluted	18400	18,464	17,221	-6%	-7%
Cash and Equivalents (pro forma)	32,699	62,860	49,900	53%	-21%
Debt	19,725	9,875	10,031	-49%	2%
Net Cash	12,974	52,985	39,869	207%	-25%
Net Cash/share	0.70511	2.9	2.3	228%	-19%

% of Rev.	1Q14A	1Q15E	1Q15A
Gross Margins	-53%	-61%	-30%
Research and development	222%	102%	125%
General and administrative	272%	265%	338%
Total operating expenses	837%	377%	525%
EBIT	-890%	-438%	-555%
Tax rate	0%	0%	0%
Net income	-1010%	-436%	-586%

Source: Company data, Wedbush Securities, Inc.

Risks

ROKA continues to burn cash and the path to profitability is murky. We estimate that the company has at least two years' worth of cash and may need to raise additional funds at some point in the next two years. ROKA has execution risk a sales cycles in the food testing business tend to be long and unpredictable. Additionally, the period of time between placement of and Atlas instrument and full implementation can take several months. In addition, the adoption curve is more difficult to predict relative to other diagnostics companies given the lack of close comparables.

Figure 4: Income Statement

	2012	2013	2014	1Q15	2Q15E	3Q15E	4Q15E	2015E	1Q16E	2Q16E	3Q16E	4Q16E	2016E
Product Revenue	105	2,183	5,057	1,511	1,625	1,785	2,035	6,956	2,359	2,701	3,023	3,345	11,428
Total Revenues	105	2,183	5,057	1,511	1,625	1,785	2,035	6,956	2,359	2,701	3,023	3,345	11,428
Cost of revenues	3,186	6,601	7,847	1,964	2,051	2,168	2,300	8,483	2,487	2,675	2,891	3,105	11,159
Gross profit	(3,081)	(4,418)	(2,790)	(453)	(427)	(383)	(264)	(1,527)	(128)	25	132	239	269
Gross Margins	-2934.3%	-202.4%	-55.2%	-30.0%	-26.3%	-21.4%	-13.0%	-22.0%	-5.4%	0.9%	4.4%	7.2%	2.4%
Research and development	9,584	7,568	7,934	1,889	2,000	2,000	2,000	7,889	2,000	2,000	2,000	2,000	8,000
G&A (plus S&M as of 2Q14)	16,052	7,264	16,308	5,113	5,400	5,500	5,600	21,613	5,800	5,800	5,800	5,800	23,200
Selling & Marketing	0	10,218	2,793					0					0
Amortization of intangibles	168	168	1,767	937	200	200	200	1,537	200	200	200	200	800
Total operating expenses	25,804	25,218	28,802	7,939	7,600	7,700	7,800	31,039	8,000	8,000	8,000	8,000	32,000
Operating Income	(28,885)	(29,636)	(31,592)	(8,392)	(8,027)	(8,083)	(8,064)	(32,566)	(8,128)	(7,975)	(7,868)	(7,761)	(31,731)
Interest income	(140)	(2,980)	(1,805)	(466)	(26)	(41)	(59)	(591)	(78)	(81)	(98)	(115)	(371)
Other	0	(53)	(785)	0	0	0	0	0	0	0	0	0	0
Income before taxes	(29,025)	(32,669)	(34,182)	(8,858)	(8,052)	(8,124)	(8,123)	(33,157)	(8,206)	(8,056)	(7,966)	(7,875)	(32,102)
Provision for income taxes	0	(3,092)	(1,952)	2	0	0	0	2	0	0	0	0	0
Tax Rate									0.0%	0.0%	0.0%	0.0%	0
Net income	(29,025)	(29,577)	(32,230)	(8,860)	(8,052)	(8,124)	(8,123)	(33,159)	(8,206)	(8,056)	(7,966)	(7,875)	(32,102)
Accretion of convertible preferred stock	(286)	-	0	0	0	0	0	0	0	0	0	0	0
Net Income	(29,311)	(29,577)	(32,230)	(8,860)	(8,052)	(8,124)	(8,123)	(33,159)	(8,206)	(8,056)	(7,966)	(7,875)	(32,102)
GAAP EPS -Basic	(\$8.05)	(\$0.30)	(\$1.96)	(\$0.51)	(\$0.47)	(\$0.47)	(\$0.47)	(\$1.92)	(\$0.47)	(\$0.46)	(\$0.45)	(\$0.45)	(\$1.83)
GAAP EPS -Diluted	(\$8.05)	(\$0.30)	(\$1.90)	(\$0.51)	(\$0.47)	(\$0.47)	(\$0.47)	(\$1.92)	(\$0.47)	(\$0.46)	(\$0.45)	(\$0.45)	(\$1.83)
Non-GAAP EPS -Diluted	(\$8.05)	(\$0.30)	(\$1.90)	(\$0.51)	(\$0.47)	(\$0.47)	(\$0.47)	(\$1.92)	(\$0.47)	(\$0.46)	(\$0.45)	(\$0.45)	(\$1.83)
Weighted average shares - basic	3,639	100,121	16,738	17,221	17,281	17,342	17,402	17,312	17,463	17,524	17,586	17,647	17,555
Weighted average shares - diluted	3,639	100,121	17,338	18,400	18,464	18,529	18,594	18,497	18,659	18,724	18,790	18,856	18,757
Cash and Equivalents	17,314	32,728	57,100	49,900	43,829	36,723	29,100	29,100	27,779	21,033	14,284	6,890	6,890
Debt	0	9,725	9,956	10,031	10,031	10,031	10,031	10,031	10,031	10,031	10,031	10,031	10,031
Net Cash	17,314	23,003	47,144	39,869	33,798	26,692	19,069	19,069	17,748	11,002	4,253	(3,141)	(3,141)
Net Cash/share		NA	2.6	2.2	1.8	1.4	1.0	1.0	1.0	0.6	0.2	(0.2)	(0.2)
% of Sales	2012	2013	2014	1Q15	2Q15E	3Q15E	4Q15E	2015E	1Q16E	2Q16E	3Q16E	4Q16E	2016E
Gross Margins	-2934%	-202%	-55%	-30%	-26%	-21%	-13%	-22%	-5%	1%	4%	7%	2%
Research and development	9128%	347%	157%	125%	123%	112%	98%	113%	85%	74%	66%	60%	70%
General and administrative	15288%	333%	322%	338%	332%	308%	275%	311%	246%	215%	192%	173%	203%
Sales and Marketing	0%	468%	55%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Total operating expenses	24575%	1155%	570%	525%	468%	431%	383%	446%	339%	296%	265%	239%	280%
EBIT	-27510%	-1358%	-625%	-555%	-494%	-453%	-396%	-468%	-344%	-295%	-260%	-232%	-278%
Tax rate	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Net income	-27915%	-1355%	-637%	-586%	-496%	-455%	-399%	-477%	-348%	-298%	-264%	-235%	-281%
Free Cash Flow	-27918%	-1493%	-464%	-447%	-360%	-332%	-286%	-350%	-238%	-206%	-184%	-167%	-195%
y/y Δ	2012	2013	2014	1Q15	2Q15E	3Q15E	4Q15E	2015E	1Q16E	2Q16E	3Q16E	4Q16E	2016E
Total Revenues	NA	1979%	132%	82%	17%	20%	50%	38%	56%	66%	69%	64%	64%
Cost of revenues	NA	107%	19%	55%	30%	-16%	-5%	8%	27%	30%	33%	35%	32%
Gross Margins	NA	-93%	-73%	-43%	99%	-71%	-84%	-60%	-82%	-104%	-120%	-155%	-111%
Sales and Marketing	NA	-21%	5%	3%	-10%	4%	3%	-1%	6%	0%	0%	0%	1%
General and administrative	NA	-55%	125%	127%	19%	19%	15%	33%	13%	7%	5%	4%	7%
Research and development	NA	NA	-73%	-100%	NA	NA	NA	-100%	NA	NA	NA	NA	NA
Total operating expenses	NA	-2%	14%	15%	11%	6%	0%	8%	1%	5%	4%	3%	3%
EBIT	NA	3%	7%	14%	15%	-3%	-9%	3%	-3%	-1%	-3%	-4%	-3%
Tax rate	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Net income	NA	1%	9%	6%	10%	-11%	9%	3%	-7%	0%	-2%	-3%	-3%

Source: Company data, Wedbush Securities, Inc.

Figure 5: Balance Sheet

	2012	2013	2014	Q1	Q2E	Q3E	Q4E	2015E	2016E
Current assets:									
Total Cash and Cash Equivalents	17,314	32,728	57,100	49,900	43,829	36,723	29,100	29,100	6,890
Accounts Receivable	30	277	670	713	812	893	1,018	1,018	1,672
Inventory	4,066	3,879	4,930	4,698	4,800	4,900	5,000	5,000	279
Prepaid expenses and other Current Assets	1,088	5,572	2,115	1,920	1,920	1,920	1,920	1,920	1,920
Total current assets	22,498	42,456	64,815	57,231	51,362	44,436	37,037	37,037	10,761
Property, Plant and Equipment	13,783	14,510	12,186	11,585	11,666	11,755	11,857	11,857	12,429
Intangible assets/Goodwill	1,512	1,344	26,516	25,219	23,519	21,719	19,819	19,819	11,019
Restricted cash and other non-current assets	624	804	308	663	890	1,401	1,899	1,899	(6,053)
Total assets	38,417	59,114	103,825	94,698	87,437	79,311	70,612	70,612	28,156
LIABILITIES AND STOCKHOLDERS' EQUITY									
Current liabilities:									
Accounts Payable and accrued expenses	3,333	1,226	1,134	645	1,428	1,426	850	850	877
Deferred revenue and Other Current Liabilities	1,733	7,639	12,776	12,561	12,561	12,561	12,561	12,561	12,561
Total current liabilities	5,066	8,865	13,910	13,206	13,989	13,987	13,411	13,411	13,438
Long-term liabilities:									
Long Term Debt	0	212	10,457	10,380	10380	10380	10380	10,380	0
Other long term liabilities	2,542	3,584	383	379	379	379	379	379	379
Total liabilities	7,608	12,661	24,750	23,965	24,748	24,746	24,170	24,170	13,817
Stockholders' equity:									
Preferred Stock	100,537	127,797	0	0	0	0	0	0	0
Common Stock, APIC, RE	(69,728)	(81,344)	79,075	70,741	62,689	54,565	46,442	46,442	14,340
Total liabilities and stockholders' equity	38,417	59,114	103,825	94,706	87,437	79,311	70,612	70,612	28,156

Source: Company data, Wedbush Securities, Inc.

Figure 6: Cash Flow Statement

	2012	2013	2014	Q1E	Q2E	Q3E	Q4E	2015E	2016E
Cash Flows from Operating Activities:									
Net (loss) income	(23,246)	(29,577)	(32,230)	(8,860)	(8,052)	(8,124)	(8,123)	(33,159)	(32,102)
Depreciation	2,045	2,437	4,248	1,600	1,700	1,800	1,900	7,000	8,800
change in FV of investor rights obligation	(4,996)	2,595	836	0	0	0	0	0	0
Loss on disposal/provision for inventory	2,197	1,118	167	0	0	0	0	0	0
Stock-based compensation expense	739	696	1,019	600	600	600	600	2,400	2,800
Deferred taxes	0	(3,127)	0	0	0	0	0	0	0
non-cash interest expense/impairment/deferred taxes	186	457	(2,912)	(800)	(800)	(1,000)	(1,000)	(3,600)	(4,000)
Change in working capital	(4,699)	(2,050)	2,662	(320)	581	(182)	(800)	(721)	4,093
Net cash provided by operating activities	(27,774)	(27,451)	(26,210)	(7,780)	(5,971)	(6,906)	(7,424)	(28,080)	(20,410)
Cash Flows from Investing Activities:									
Purchase of property and equipment	(5,929)	(3,410)	1,686	601	(100)	(200)	(200)	(600)	(1,800)
increase in restricted cash		0	(614)	0	0	0	0	0	0
Net cash used in investing activities	(5,929)	(3,410)	1,072	601	(100)	(200)	(200)	101	(1,800)
Cash Flows from Financing Activities:									
Proceeds from Issuance of Restricted Stock	0	4,672	0	0	0	0	0	0	0
proceeds from issuance of preferred stock	20,000	41,783	(15)		0	0	0	0	0
proceeds from issuance of common stock	0	20	65,000	0	0	0	0	0	0
costs of issuance/other	4	(199)	(7,045)	(21)	0	0	0	(21)	0
Net cash provided by financing activities	20,004	46,276	57,940	(21)	0	0	0	(21)	0
Net increase (decrease) in cash and cash equivalents	(13,699)	15,415	32,802	(7,200)	(6,071)	(7,106)	(7,624)	(28,000)	(22,210)
Cash and cash equivalents, beginning of period	31,013	17,314	32,728	57,100	49,900	43,829	36,723	57,100	29,100
Cash and cash equivalents, end of period	17,314	32,729	65,530	49,900	43,829	36,723	29,100	29,100	6,890

Source: Company data, Wedbush Securities, Inc.

Analyst Biography

Zarak Khurshid is a senior equity research analyst covering the Medical Diagnostics and Life Science Tools sectors. Prior to joining Wedbush in January 2010, Mr. Khurshid was Vice President and senior equity research analyst with Caris & Company where he covered the Medical diagnostics and Life Sciences Tools sectors from 2006 to 2010. Mr. Khurshid's aggressive risk/reward focused investment style is supported by data points from a diverse network of contacts from industry, hospitals, clinical labs, and academia. Mr. Khurshid was ranked #1 in the Life Science Tools and Services sectors and #4 on Wall Street for earnings accuracy in 2012 by *Starmine*. Prior to his start on Wall Street with Pacific Growth Equities in 2004, Mr. Khurshid was a Research Associate with Cytokinetics and an Associate Bioengineer with Aurora Biosciences. Mr. Khurshid received a BS in Bioengineering and a BA in Economics from the University of California, San Diego.

Analyst Certification

I, Zarak Khurshid, certify that the views expressed in this report accurately reflect my personal opinion and that I have not and will not, directly or indirectly, receive compensation or other payments in connection with my specific recommendations or views contained in this report.

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Outperform: Expect the total return of the stock to outperform relative to the median total return of the analyst's (or the analyst's team) coverage universe over the next 6-12 months.

Neutral: Expect the total return of the stock to perform in-line with the median total return of the analyst's (or the analyst's team) coverage universe over the next 6-12 months.

Underperform: Expect the total return of the stock to underperform relative to the median total return of the analyst's (or the analyst's team) coverage universe over the next 6-12 months.

The Investment Ratings are based on the expected performance of a stock (based on anticipated total return to price target) relative to the other stocks in the analyst's coverage universe (or the analyst's team coverage).*

Rating Distribution (as of March 31, 2015)	Investment Banking Relationships (as of March 31, 2015)
Outperform: 55%	Outperform: 31%
Neutral: 43%	Neutral: 3%
Underperform: 2%	Underperform: 0%

The Distribution of Ratings is required by FINRA rules; however, WS' stock ratings of Outperform, Neutral, and Underperform most closely conform to Buy, Hold, and Sell, respectively. Please note, however, the definitions are not the same as WS' stock ratings are on a relative basis.

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Wedbush Equity Research Disclosures as of May 8, 2015

Company	Disclosure
Roka Bioscience	1,3,4,5

Research Disclosure Legend

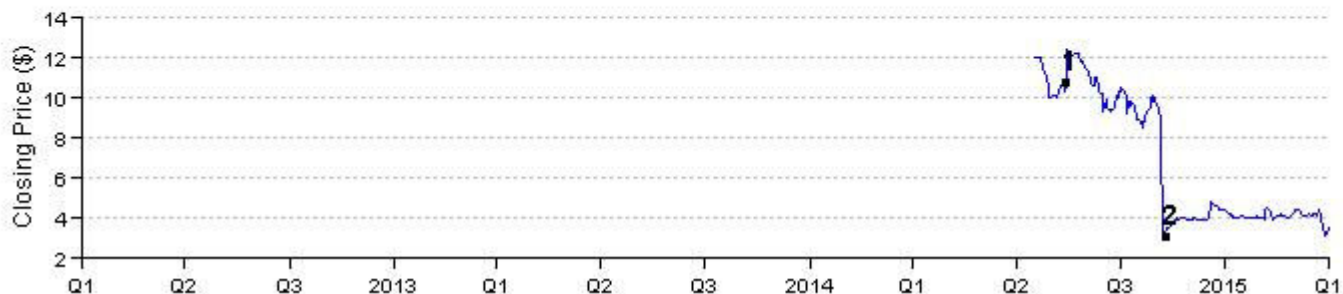
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ROKA

1) 08/11/14	2) 11/07/14
OUTPERFORM \$15	NEUTRAL \$9



* WS changed its rating system from (Strong Buy/Buy/Hold/Sell) to (Outperform/ Neutral/Underperform) on July 14, 2009.

Please access the attached hyperlink for WS' Coverage Universe: <http://www.wedbush.com/services/cmg/equities-division/research/equity-research> Applicable disclosure information is also available upon request by contacting Ellen Kang in the Research Department at (213) 688-4529, by email to ellen.kang@wedbush.com, or the Business Conduct Department at (213) 688-8090. You may also submit a written request to the following: Business Conduct Department, 1000 Wilshire Blvd., Los Angeles, CA 90017.

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RESEARCH DEPT. * (213) 688-4505 * www.wedbush.com

EQUITY TRADING Los Angeles (213) 688-4470 / (800) 421-0178 * EQUITY SALES Los Angeles (800) 444-8076
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WEDBUSH

EQUITY RESEARCH DEPARTMENT

(213) 688-4529

DIRECTOR OF RESEARCH

Mark D. Benson (213) 688-4435

MANAGER, RESEARCH OPERATIONS

Ellen Kang (213) 688-4529

RETAIL AND CONSUMER

Healthy Lifestyles

Phil Terpolilli (212) 833-1367

Leisure

James Hardiman, CFA CPA (212) 833-1362

Sean Wagner (212) 833-1363

Restaurants

Nick Setyan (213) 688-4519

Colin Radke (213) 688-6624

Specialty Retail: Hardlines

Seth Basham, CFA (212) 938-9954

John Garrett, CFA (213) 688-4523

Specialty Retail: Softlines

Morry Brown, CFA (213) 688-4311

Taryn Kuida (213) 688-4505

RETAIL CHANNEL CHECKING GROUP

Lupine Skelly (505) 417-5427

INDUSTRIAL GROWTH TECHNOLOGY

Environmental Services / Building Products

Al Kaschalk (213) 688-4539

John Garrett, CFA (213) 688-4523

Water and Renewable Energy Solutions

David Rose, CFA (213) 688-4319

James Kim (213) 688-4380

TECHNOLOGY, INTERNET, MEDIA & SOCIAL MEDIA

Communications & Cloud Infrastructure

Scott Thompson (212) 938-9933

Communications and Application Software

Shyam Patil, CFA (213) 688-8062

Andy Cheng (213) 688-4548

Enterprise Software

Steve Koenig (415) 274-6801

Jae Cho (212) 938-9937

Entertainment: Retail

Michael Pachter (213) 688-4474

Alicia Reese (212) 938-9927

Nick McKay (213) 688-4343

Entertainment: Software

Michael Pachter (213) 688-4474

Nick McKay (213) 688-4343

Financial Technology

Gil B. Luria (213) 688-4501

Aaron Turner (213) 688-4429

Internet: Media and Gaming

Michael Pachter (213) 688-4474

Nick McKay (213) 688-4343

Alicia Reese (212) 938-9927

Internet: Social Media, Advertising & Technology

Shyam Patil, CFA (213) 688-8062

Andy Cheng (213) 688-4548

Media

James Dix, CFA (213) 688-4315

Movies and Entertainment

Michael Pachter (213) 688-4474

Alicia Reese (212) 938-9927

Nick McKay (213) 688-4343

Semiconductors

Betsy Van Hees (415) 274-6869

Ryan Jue, CFA (415) 263-6669

HEALTHCARE

Biotechnology/Biopharmaceuticals

David M. Nierengarten, Ph.D. (415) 274-6862

Dilip Joseph (415) 273-7308

Robert Driscoll, Ph.D. (415) 274-6863

Heather Behanna, Ph.D. (415) 274-6874

Alison Macleod, Ph.D. (415) 273-7315

Emerging Pharmaceuticals

Liana Moussatos, Ph.D. (415) 263-6626

Kelechi Chikere, Ph.D. (415) 273-7304

Healthcare Services - Managed Care

Sarah James (213) 688-4503

Medical Devices

Tao Levy (212) 938-9948

Medical Diagnostics and Life Sciences Tools

Zarak Khurshid (415) 274-6823

EQUITY SALES

Los Angeles (213) 688-4470 / (800) 444-8076

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CORPORATE HEADQUARTERS

1000 Wilshire Blvd., Los Angeles, CA 90017-2465

Tel: (213) 688-8000 www.wedbush.com