TAGLICH BROTHERS

MEMBER: FINRA, SIPC | WWW.TAGLICHBROTHERS.COM

Research Update

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

Zynex, Inc.

Rating: Speculative Buy

Juan Noble

ZYXI $0.42 (ZYXI: OTC)

May 20, 2013

	2011A	2012A	*2013E*	*2014E*
Total revenues (in millions)	$ 34.1	$ 40.0	***$ 32.0***	***$ 35.3***
Earnings (loss) per share	$ 0.05	$ 0.05	***$ 0.02***	***$ 0.04***

52 - Week range	$1.01 – $ 0.40	Fiscal year ends:	December
Shares outstanding as of May 13, 2013	31.1 million	Revenue/share (ttm)	$1.23
Approximate float	12 million	Price/Sales (ttm)	0.3X
Market Capitalization	$13.1 million	Price/Sales (2014)E	0.4X
Tangible Book value as of Mar. 31, 2013	$0.36	Price/Earnings (ttm)	14.2X
Price/Book	1.2 X	Price/Earnings (2014)E	11.6X

Zynex, Inc., based in Lone Tree, Colorado, manufactures a line of electrotherapy devices that relieve pain while reducing reliance on drugs, and speeds rehabilitation and recovery of i mobility. The company also produces diagnostic devices and distributes electrotherapy systems manufactured by others. A substantial portion of revenue is recurring – device rentals and the sale of electrodes and batteries sent to patients using rented or purchased units.

Key Investment Considerations:

Reiterating Speculative Buy but lowering (12-month) price target to $0.50 from $1.10 due to a diminished earnings outlook.

Revenue gains have slowed, reflecting a drop in demand stemming from physician uncertainty over the impact of the Patient Protection and Affordable Care Act (PPACA), and a slowing in orders attributed to seasonal first quarter adjustment of health insurance deductibles. Due to slowing demand and curtailment of sales efforts we have reduced our revenue and earnings estimates for 2013 and 2014.

Zynex's gross margins, while compressed due to reduced overhead coverage, remains exceptionally high compared to the industry. But sharp increases in reimbursement costs and G&A have reduced the company's expense leverage and narrowed operating and pretax margins.

The US electrotherapy market is projected to grow to $820 million by 2016, up from $600 million in 2012, an IBISWorld forecast that has not changed recently due to concerns over the PPACA. But medical devices sold for at-home use may be adversely affected more than the broader medical device market.

For 2013 we project EPS of $0.02 per share on revenue of $32 million, down from our earlier projections of $0.07 EPS on revenue of $43 million. For 2014 we project EPS of $0.04 on revenue of $35.3 million, down from $0.09 EPS and revenue of $49.6 million projected earlier.

In 1Q13, Zynex lost $304,000, or ($0.01) per share, on revenue of $7.7 million. We projected 1Q EPS of $0.02 on revenue of $9.7 million. In the year-earlier quarter, the company earned $0.02 per share on revenue of $8.9 million.

See disclosures on pages 16 - 18

Investment Recommendation

Reiterating Speculative Buy but lowering (12-month) price target to $0.50 from $1.10 due to a diminished earnings outlook.

ZYXI is trading at 14.2X trailing EPS vs. the medical appliance/equipment industry's P-E of 24.6X, reflecting a discount that arguably stems from ZYXI's recent disappointing results, small float and light trading volume. We believe that within the next year, the stock will trade at around the same multiple on forward (2014) earnings. A 14X multiple on our 2014 EPS estimate of $0.04 per share, discounted by 4.7% to a year-ahead value, would value the stock at $0.48, implying stock price appreciation of 20% within the next 12 months.

ZYXI is a high-growth company that offers potentially attractive investment returns. But in our view, the stock's small float and low trading volume, a high concentration of stock ownership and potential reimbursement difficulties make it suitable mainly for highly risk-tolerant investors

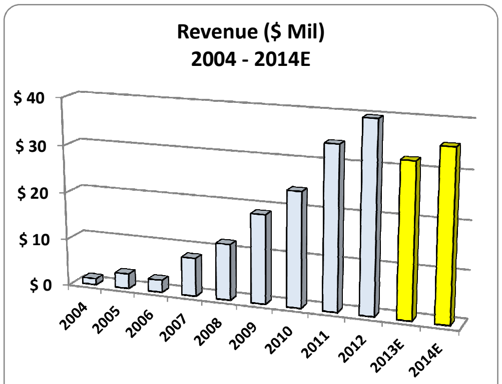
Recent Developments

Neurovirtual Marketing/Distribution Agreement On March 18, 2013 Zynex announced a marketing and distribution agreement with Neurovirtual (Doral, FL), a developer and global marketer of electroencephalography (EEG) and sleep diagnostic devices. Under the agreement Zynex has exclusive rights to sell, market and distribute Neurovirtual's EEG and sleep diagnostic devices in the US.

Overview

Zynex, Inc., headquartered in Lone Tree, Colorado, was founded in 1996 and became a publicly held company in 2004 through a reverse merger with a publicly held shell company. Zynex operated as a wholesaler of European-made electrotherapy devices until its first medical device was cleared by the Food and Drug Administration (FDA) in 1999. In 2003 Zynex's full line of electrotherapy devices and a stroke rehabilitation device were cleared by the FDA. In 2008 some of its major products were cleared for marketing in Europe.

Revenue has increased sharply, growing threefold in the three years through 2012. Profitability, however, has been less consistent despite a gross margin that significantly exceeds the medical device industry's gross margin of 50%. Although Zynex has been profitable since 2007, net income has fluctuated widely due mainly to sharp swings in operating expenses.



Source: Company reports and Taglich Brothers estimates

Now, revenue growth has stalled abruptly on an outlook that has become murky due to concerns over the impact of the Patient Protection and Affordable Care Act (PPACA). In 1Q13, hardware sales and rental revenue fell sharply. By our estimates, weakness will persist for through 2014. By then, the company could regain some of its lost growth momentum. .

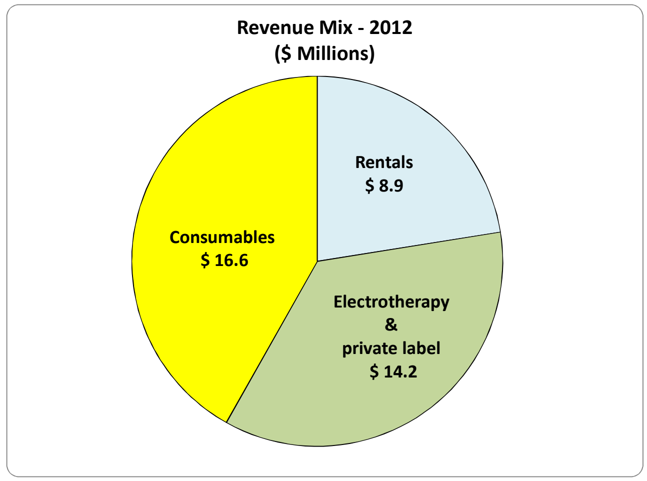
Zynex manufactures a line of pain management neuromodulator devices that reduce reliance on drugs and promotes rehabilitation and increased mobility. Zynex's non-invasive transcutaneous electrical nerve stimulation (TENS) and interferential current (IF) systems have been used to treat pain ranging from mild persistent problems such as sore muscles to acute postoperative pain.

The company's neuromuscular electrical stimulation (NMES) systems are used mainly by physical therapists to treat victims of trauma, stroke, or incidents that degrade muscle function, enabling stroke or spinal injury victims to regain lost mobility, functionality, speech, and memory.

In March 2012 Zynex expanded its product line with the acquisition a diagnostics business that manufactures electromyography (EMG) and photoelectric plethysmography (PPG) systems. The company's diagnostic devices are sold mainly overseas through distributors.

In addition to its own products, Zynex distributes private labeled electrical stimulation devices, electrodes and batteries produced by other US manufacturers. A substantial portion of revenue is recurring. Rentals and electrodes and batteries sold to patients using either rental or purchased units account for two-thirds of revenue.

Zynex's products are either purchased or rented on a monthly basis, mainly by patients, health care providers and distributors. Health insurers that cover patients generally determine, based on the anticipated time the device will be used, if devices will be rented or purchased. More than half of revenue consists of sales to patients covered by private health insurance plans. Patients also include Medicare and Medicaid beneficiaries. Returned rental units are refurbished and made available for future rentals. Rental margins and margins on consumables, typically around 80%, range significantly higher than the 50% margins on device sales.



At present, practically all of the company's revenue derives from electrotherapy systems but products that could potentially expand and diversify the company's target patient populations are in development. Zynex is developing electromyography (EMG), electroencephalography (EEG), sleep pattern, auditory and nerve conductivity neurological diagnosis devices for use in hospitals and clinics. Cardiac monitoring systems are also in development.

In the US, which accounts for most of its sales, the company sells its medical devices through a sales force that inlcudes independent sales representatives. Overseas, Zynex has distributors in Canada, Australia, Southeast Asia, the United Arab Emirates, the Netherlands, and Germany. An international sales manager oversees distributors covering Asia and the Middle East.

Strategy

The company plans to expand into new markets by developing new neurodiagnostic and cardiac monitoring products, and by making accretive acquisitions. In March 2012, Zynex acquired a device used by clinicians and therapists for surface electromyography (sEMG) muscle monitoring and rehabilitation. At this time, however, most of the company's revenue derives from the rental and sale of pain management devices and consumables.

Zynex is reevaluating the strategy for Zynex Medical, its largest business. Previously growth plans aimed to increase market penetration by sales force expansion, mainly through the recruitment of in-house sales representatives. In the aftermath of a disappointing 1Q13, the company reduced its sales force and its sales compensation.

Zynex now has 22 international distributors in Canada, Australia, Asia and the Middle East. In February 2012, the company formed a European subsidiary to focus on the European market, where several products have received regulatory clearance (CE mark) that could facilitate entry into other developed markets.

To respond more effectively to fluctuating volume, minimize capital expenditures, and spread the risk of quality deficiencies and supply interruptions, Zynex maximizes its use of contract manufacturers, of which there are a large number of qualified ones available in the US and overseas. Despite reliance mainly on contractors to process the bulk of the company's manufacturing requirements, Zynex has expanded its in-house production capability for certain TENS units.

Most of the company's technology – TENS was developed 30 years ago – is not patent protected. To keep its product knowledge proprietary, Zynex internally develops software for all of its products. All products are tested in-house to ensure quality and patient safety, and reduce the cost of warranty expenses.

2013 First Quarter Results

In 1Q13, Zynex incurred a loss of $304,000, or ($0.01) per share, on revenue of $7.7 million. We projected earnings of $0.02 per share on revenue of $9.7 million. In the year-earlier quarter, the company earned $0.02 per share.

1Q revenue dropped 14% to $7.7 million, a decline led by a 32% decrease in hardware sales to $2.1 million. Rentals, the company's highest margin revenue, fell 19% to $1.7 million. Consumables sales, driven mainly by the number of electrotherapy systems in service, were largely flat at around $3.8 million.

The decline in 1Q revenue reflects a drop in demand stemming from physician uncertainty over the impact of the Patient Protection and Affordable Care Act (PPACA), and a slowing in orders attributed to seasonal first quarter adjustment of health insurance deductibles. In response to potentially adverse changes in the outlook, Zynex, after building it up for years, cut its sales force, reduced sales compensation and began to train its sales representative to better cope with customer fears.

While changes relating to the sales force (and the decline in revenue) reduced sales/marketing expenses by almost 40% to $1.9 million, other expenses were up. Reimbursement and billing expenses increased 10% to $2.2 million due to additional investment made in personnel and systems deemed vital to negotiations with and collections from health insurers. G&A was up 15% to $1.4 million, reflecting the addition of administrative and regulatory staff to support the Zynex NeuroDiagnostics business acquired in 2012.

The gross margin for 1Q narrowed to 71.4% from

	Quarter ending Mar 31:			
($ Thousands)	**2013A**	***2013E***	**2012A**	**%+/-**
Revenue				
Rental	1,679	*2,227*	2,062	(19%)
Sales: electrotherapy/private label	2,091	*3,670*	3,058	(32%)
consumables	3,898	*3,833*	3,824	2%
Sales revenue	5,989	*7,502*	6,882	(13%)
Total revenue	7,668	*9,729*	8,944	(14%)
Cost of revenue				
Rental	301	*334*	258	17%
Sales	1,890	*1,575*	1,555	22%
Total	2,191	*1,910*	1,813	21%
Gross profit	5,477	*7,820*	7,131	(23%)
Operating expenses				
Sales/marketing	1,906	*3,405*	3,095	(38%)
Reimbursement & billing	2,231	*2,116*	2,034	10%
G&A	1,356	*1,168*	1,183	15%
Engineering & operations	340	*292*	333	2%
Total SG&A	5,833	*6,981*	6,645	(12%)
Operating income	(356)	*839*	486	(173%)
Interest income				
Interest expense	(130)	*(102)*	(93)	40%
Other income (expense)	(6)			NM
Pretax income	(492)	*737*	393	(225%)
Income tax	182	*(295)*	(73)	(349%)
Net income before minority interest	(310)	*442*	320	
Minority interest in earnings	6			NM
Net income	(304)	*442*	320	(195%)
Average shares outstanding	31,148	*32,750*	31,882	
Earnings (loss) per share	(0.01)	*0.02*	0.02	(152%)
Margin Analysis				
Gross margin - total	71.4%	*80.4%*	79.7%	
Rental	82.1%	*85.0%*	87.5%	
Sales	75.7%	76.0%	76.0%	
SG&A	76.1%	*71.8%*	74.3%	
Sales/marketing	24.9%	*35.0%*	34.6%	
Reimbursement & billing	29.1%	*21.8%*	22.7%	
G&A	17.7%	*12.0%*	13.2%	
Engineering & operations	4.4%	*3.0%*	3.7%	
Operating income	(4.6%)	*8.6%*	5.4%	
Net income	(4.0%)	*4.5%*	3.6%	
Tax rate	(37.0%)	*(40.0%)*	(18.6%)	

Source: Company reports and Taglich Brothers estimates

79.7% due mainly to compression in rental sales margins, which are the highest earned by the company, and reduced overhead coverage stemming from lower production volume. The gross profit for 1Q dropped 23% to $5.5 million due to gross margin compression and the decline in revenue. Due to the decline in gross profit and a loss of expense leverage, Zynex incurred an operating loss for 1Q.

Finances Zynex is moderately leveraged, with approximately 48% of tangible assets financed with (tangible) stockholders' equity. The balance sheet has become increasingly leveraged. At the end of 2009, 63% of tangible assets were financed with (tangible) stockholders' equity.

In 1Q13 cash earnings were nominal. Working capital increased by $1 million due mainly to reductions in payables and accruals, and increases in inventory and deposits, offset partly by a decrease in receivables. Cash of $993,000 used in operations was offset in part by additional bank borrowings. Cash dropped by $142,000 to $681,000 at the end of the quarter.

Credit Facility Under a December 2011 loan agreement with Doral Healthcare Finance, Zynex has an asset-backed revolving credit facility of up to $7 million at a variable interest rate equal to the LIBOR rate or 3% per annum + 3.75%, whichever is greater. The agreement matures on December 19, 2014.

The company may terminate the agreement at any time prior to the maturity date upon 30 days' notice and upon full payment of all outstanding obligations. If Zynex terminates the agreement after December 19, 2012 but before the maturity date, the company must pay a specified early termination fee. As of March 31, 2013, $6.6 million was outstanding under the agreement and $398,000 was available for borrowing.

As of March 31, 2013, the effective interest rate under the agreement was 8% (7% interest rate and 1% fees). The agreement contains restrictive and financial covenants for asset-backed credit facilities. As of March 31, 2013, the company was in compliance with all loan covenants.

Projections

Operations For 2013, we project EPS of $0.02 on revenue of $32 million, down from our earlier projections of $0.07 EPS on revenue of $43 million. We reduced our 2013 forecast to reflect 1Q results and expectations for reduced demand and orders due to the same factors that influenced 1Q, and increased spending on billing & reimbursement and G&A. In our view, demand and profitability in 2014 will also be adversely affected by the same factors. However, revenue growth momentum should partially recover, driving earnings growth to $0.04 per share on revenue of $35.3 million. We previously projected 2014 EPS of $0.09 on revenue of $49.6 million.

By establishing a rental business and manufacturing most of the products it markets, Zynex earns exceptional manufacturing margins that significantly exceed that of the industry. High gross margins are also supported by distribution of third-party manufacturers' consumables, mainly electrodes and batteries, that account for 40% of revenue (vs. 8% for the TENS segment of the neuromodulator market). But reimbursement & billing and G&A expenses are cutting more deeply into operating income. Market penetration has arguably decreased with the reduction in the number of sales representatives.

Pricing pressure from competing products and resistance from health insurers could limit pricing flexibility, exerting pressure on margins. Sales and marketing expense margins have been persistently high and have widened in recent quarters, constraining profit gains. The company's difficulty in adapting to new electronic claims filing processes has resulted in some reimbursement losses.

For 2013 we project a 19% decline in revenue to $32 million and gross margin compression to 76.7% from 2012's 77.9%. Gross profit will fall an estimated 20% to $24.6 million. Operating expenses should decrease by 17%, reflecting a 40% decline in sales/marketing but with expenses falling at a slower rate than gross profit, the operating margin for 2013 will narrow to 4% from 6.9%, reducing operating income by 53% to $1.3 million.

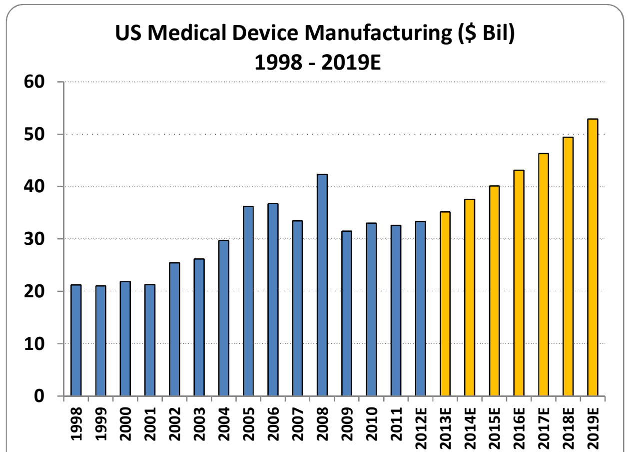
We project a partially recovery in revenue growth and profitability in 2014. We forecast a 10% rise in revenue to $35.3 million as demand recovers. An improvement in overhead coverage driven by an increase in volume should widen the gross margin to 78.1% from 76.7%. Gross profit gains and a recovery of expense leverage should widen the operating margin to 6.6% from 4%, increasing operating income by 81% to $2.3 million. So long as collections do not deteriorate, average borrowings should drop further, enabling Zynex to cut its interest expense 29% to $326,000. The increase in operating income and a reduction in interest expense should more than double pretax income to $2 million in 2014.

Finances DSO improved slightly in 1Q13 and turnover of inventory (which includes units held for rental) stayed at 1.4X. Inventory is generally high, as the independent sales representatives maintain supplies that enable them to rapidly fill orders.

We project cash earnings for 2013 and 2014 of $1.3 million and $2 million, respectively. An increase in 2014 working capital stemming from a rise in receivables and inventory will partly offset cash earnings. Cash from operations, $1.8 million in 2013 and $1.7 million in 2014, should cover projected capital expenditures. In both years, cash flow should enable Zynex to reduce its borrowings and interest expense. In 2013, cash will increase an estimated $92,000 to $915,000 at the end of the year. In 2014 cash will drop by $646,000 to $270,000 at the end of the year.

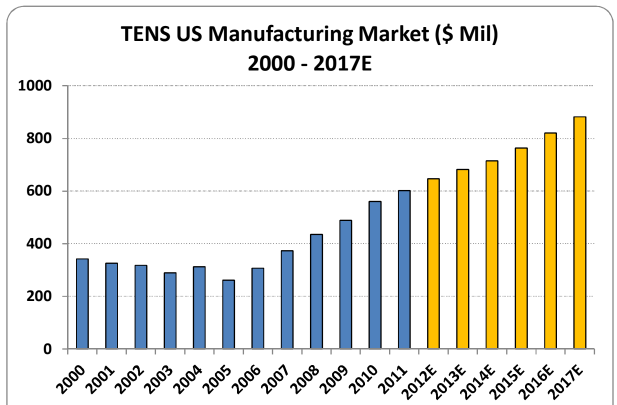
The US Medical Device Market

The US medical device manufacturing market for 2012 is estimated by IBISWorld at $33.4 billion, a figure projected to grow 6.8% a year to $53 billion by 2018. Between 1998 and 2006 the industry's CAGR was 4% but growth slowed dramatically in 2009 as a consequence of the recession. Despite the non-cyclical character of medical devices, industry growth slowed as hospital held equipment purchases in abeyance and patients deferred elective medical procedures. Future growth will be driven mainly by demographic trends, technological innovation and extension of health coverage by the Patient Protection and Affordable Care Act (PPACA) to up to 36 million previously uninsured patients by 2019.



Source: IBISWorld

With the aging of the population, the prevalence of age-related disease – cancer, cardiovascular disorders, stroke, diabetes, and degenerative spinal disorders – is expected to rise significantly, increasing the demand for pharmaceutical- and device-based therapy. Technological advances in device design, as seen earlier in cardiac rhythm management, coronary revascularization devices, spinal implants, orthopedic prostheses, and neuromodulation systems, will also drive the growth in demand.



Source: IBISWorld

Gains could potentially be offset in part by more stringent regulatory 510(k) review mandated by the Food and Drug Administration Reform Act of 2012, and pressure on pricing and industry profits as the PPACA goes into effect. The law will require all medical device manufacturers to pay, starting in 2013, 2.3% of the sales price of a device as an industry fee. Despite recent legislation that could tighten regulation, and more restrictive reimbursement by public and private payors, growth is expected to average 6.8% a year through 2019.

Neromodulation Devices This $6.5 billion segment of the US medical device market encompasses a wide range of devices that intervene in neural pathways to reduce pain and disorders stemming from illness and trauma that have impaired the central nervous system in some fashion. The neuromodulation segment includes electrotherapeutic devices, which apply an electrical impulse to an affected part of the anatomy. TENS systems fall within this group (which also includes cardiac rhythm management devices and other devices).

The US TENS market grew an average of 5.4% a year between 2000 and 2012. By IBISWorld's estimates, the US market for TENS in 2012 was $646 million, a figure that will increase an average of 6.4% annually to $882 million by 2017. However, growth could be constrained by the same regulatory factors that influence the broader medical device industry.

The higher prevalence of age-related disease and health disorders stemming from the growth in the elderly segment of the population will result in an increase in the number of patients suffering from chronic pain, driving growth in the demand for minimally invasive electrotherapy. Growing demand will drive the increase in prescriptions written by physical therapists and other clinicians, while Medicare and Medicaid coverage will ease patients' purchases of pain management devices.

Cost advantages to patients stemming from the wider availability of electrotherapy systems in the over the counter market and the reduced cost of smaller handheld systems should support the growth in patient demand. Over the counter purchases do not require a prescription, saving patients the expense of an office visit, and the lower cost of small units make them more attractively priced, provided they can deliver the same power of larger units. By IBISWorld's estimates, smaller and "mini' electrotherapy devices account for almost half of the TENS industry's sales.

Zynex's Electrical Nerve Stimulation Technology and its Product Line

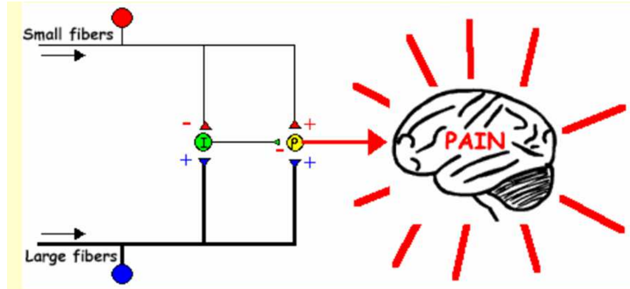
Zynex's principal products include pain management, rehabilitation and diagnostic technologies, some of them bundled in combination systems. In addition to the electrical nerve stimulation and diagnostic systems (table on page 9) that it manufactures, the company manufactures private label systems such as an electrical stimulator that manages female urinary incontinence and an electronic drug delivery device. Single-use supplies such as electrodes and batteries account for a sizable proportion of revenue.

Source: Physiomed

Electrotherapy devices are generally small, portable (hand-held in many cases), and relatively inexpensive. The TENS unit illustrated at right (not a Zynex product) is fairly typical. There are TENS systems that retail on the Internet for as little as $30.

Pain Mangement Electrical stimulation systems, also known as neurostimulation devices, range from Medtronic's PrimeAdvanced® and Restore™ implantables to the ubiquitous TENS (transcutaneous electrical nerve stimulation) system. TENS reduces pain by electrically stimulating nerve fibers that interfere with pain signals and by stimulating the production of pain-relieving endomorphins. Common pain relief applications for TENS include back and neck, RSD (complex regional pain syndrome), arthritis, shoulder pain, neuropathies, and other acute and chronic pain.

TENS therapy is delivered through a small, external portable battery-powered generator from which electrical impulses are coursed through electrodes placed on the skin, either directly over the painful area or at certain points along the nerve pathway.



I = "Inhibitory Interneuron"; P = "Projection Neuron"
- = inhibition (blocking); + = excitation (activation)

Source: Eric H. Chudler

The mechanism of action of TENS is explained by the gate-control theory (Melzack and Wall, 1965), illustrated at the right, as follows: in the absence of stimuli, both large and small nerve fibers are quiet and the inhibitory interneuron (I) blocks the signal in the projection neuron (P) that connects to the brain. The "gate is closed", so there is no pain sensed.

With non-painful stimuli, mainly the large nerve fibers are activated. Activation of the large nerve fibers also activates the projection neuron (P), but it also activates the inhibitory interneuron (I) which then blocks the signal in the projection neuron (P) that connects to the brain. The gate remains closed so there is no pain sensed.

With pain stimulation, small nerve fibers become active, activating the projection neurons (P) and blocking the inhibitory interneuron (I). Because activity of the inhibitory interneuron is blocked, it cannot block the output of the projection neuron that connects with the brain. So the gate is “open", and the brain senses pain. TENS aims to stimulate the large diameter nerve fibers, closing the gate and reducing pain.

The sensation produced by the electrical stimulation appears to "override" the pain messages and may stimulate the body to produce its own natural morphine-like substance, which minimizes pain.

PAIN MANAGEMENT/REHABILITATION	
TENS	TruWave ValuTENS (private label)
MNES	E-Wave
Combination:	
IF and NMES	IF 8000 and IF 8100
TENS, NMES and IF	NexWave, TruWave Plus
TENS and NMES	InWave
DIAGNOSTICS	
Electromyography	NM 900 NeuroSys/3 System
Photoelectric plethysmograph	MEDAC Sys/3 System

Source: Zynex, Inc.

Since it was developed more than 30 years ago TENS has been used to treat almost every type of pain, from mild persistent problems such as sore muscles to acute postoperative pain. Its most common use, however, has been in the treatment of chronic low-back pain, an application in which the American Academy of Neurology now says TENS is ineffective. Whether TENS suppresses or overrides pain signals, stimulates production of natural pain relieving chemicals, or is merely a placebo effect, it has provided pain relief in many cases. Its broad acceptance is based in part on its benign side effects profile. TENS is non-addictive, non-sedative, and can be used indefinitely without the problems associated with prolonged use of some pain medications.

Zynex’s pain management technologies include interferential (IF) current, which manages pain by a mechanism similar to TENS. Low-frequency electrical impulses directed at affected tissues intersect below the skin and induce the secretion of endorphins. IF penetrates tissue more deeply than TENS, achieving greater patient comfort and increased circulation. IF is often used to treat spasms, ligament sprains and strained muscles.

Rehabilitation Neuromuscular electrical stimulation (NMES) systems deliver electrical impulses to the surface over targeted muscles through electrodes. These electrical impulses cause muscles to contract as a form of exercise or physical therapy. NMES is used mainly by physical therapist to treat victims of trauma, stroke, or incidents that degrade muscle function. NEMS is also to diagnose the performance of nerves and muscles, and measure improvement after treatment.

NEMS is used in cases of chronic neuromuscular disorders such as cerebral palsy, spina bifida, club foot and some nonprogressive myopathies. It is also applied to healthy muscle to strengthen or maintain muscle mass during periods of enforced inactivity, increase range of motion, improve voluntary muscle control, and temporarily reduce spasticity.

Diagnostics Electromyography (EMG) tests the electrical activity of muscles to assess their health and the nerves that control them. EMG is often performed in tandem with nerve conduction studies. Detecting abnormal electrical activity in the muscles or nerves can help clinicians diagnose injuries or other disorders, such as nerve compression or injury (as in carpal tunnel syndrome), nerve root injury, and others, including alcoholic neuropathy, cervical spondylosis, and femoral nerve dysfunction. A very thin needle electrode inserted through the skin into the muscle detects electrical activity, which is displayed on a monitor, and may be heard through a speaker.

Photoelectric plethysmography (PPG) measures the intensity of light reflected from the skin surface and the red cells below to determine the blood volume of the target. That measurement enables a physician to determine erythrocyte volume and oxygen saturation. The diagnostic procedure utilizes a photosensitive cell to measure light reflected or passed through the tissue segment where a monitor is positioned. In a common application, the PPG sensor is placed over a fingertip. With each heartbeat, a surge of blood is forced through the vascular system, expanding the capillaries in the finger, changing the amount of electrical current that is translated into a signal. PPG can be used to assess the condition of patients suffering from hypertension, migraine headache or Raynaud's Disease.

In another application, PPG measures and records ear opacity through a tiny phototube and lamp clipped to the ear, measuring of the fullness of blood vessels. A PPG can be worn by aircraft pilots during high-altitude flights to signal oxygen insufficiency.

Competition

Zynex's competitors include large broad-line medical device manufacturers with substantial neurostimulation businesses, including Medtronic, which reported FY2011 neuromodulation revenue of $1.7 billion (FY ending April 2012) and St. Jude Medical, which reported 2012 neuromodulation revenue of $423 million. DJO Global's Recovery Science business, which includes direct competitor EMPI, reported 2011 revenue (latest released) of $343 million.

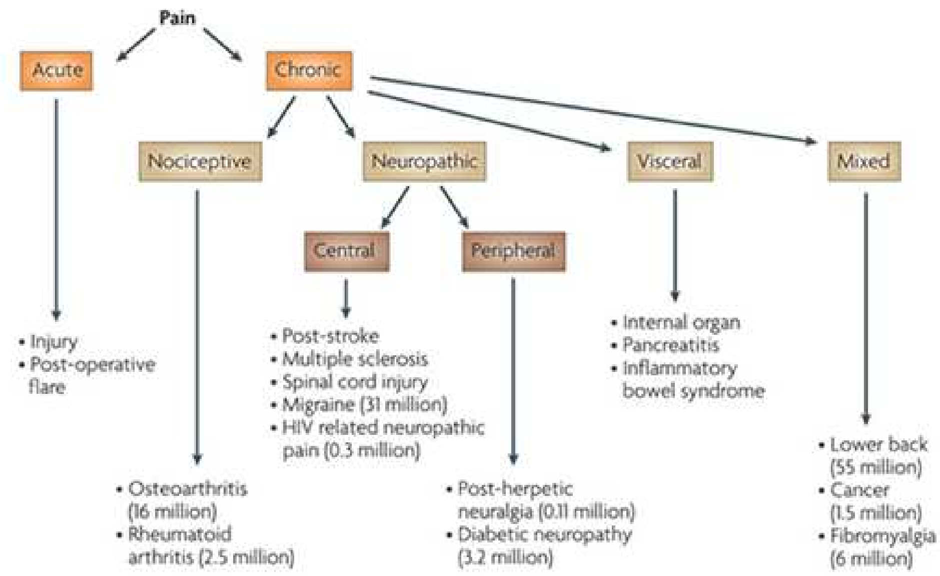
Neuromodulation revenue of Medtronic and St. Jude Medical, the high end of the market, were up 7% and 1% respectively. DJO's recovery science 2011 revenue was flat. Aside from the larger competitors in this industry segment, there are more than 40 US manufacturers of electrotherapy devices, most of which carry a wide variety of products sold to the physical therapy market. IBISWorld's TENS market data imply an average annual revenue of around $15 million per TENS manufacturer, making Zynex among the largest in this niche.

Competition is based on price, which is important to patients, clinicians and insurers. As all TENS devices perform the same function, based on largely dated technology, and are produced by a large number of manufacturers, they increasingly trade as commodities. Differentiating technology can also be an advantage. Despite limited potential for innovation in TENS devices, manufacturers try to differentiate their products. TENS systems are commonly differentiated by being bundled with another pain management modality, just as Zynex combines TENS with NMS and IF. Product innovations may make systems easier for untrained patients to use at home, or be mainly cosmetic, but in a commoditized market, novel features can underlie a slight competitive edge even if they do not enhance functionality.

Huge Patient Population

.

Patient population estimates by the Neuropathic Pain Network, MediZine and the American Cancer Society point to a combined US neuropathic and oncologic pain patient population of almost 8 million; we would estimate the worldwide figure at twice that number. Discounting the estimated global total by 25% to account for an overlap between neuropathic and oncologic pain patients, the estimated market would be around 12 million worldwide.



The chart above, compiled by Nature Reviews (August 2010) using data from the CDC, National Center for Health Statistics, and a number of medical foundations, shows the magnitude and breakdown of the potential market for pain management treatments.

Neuropathic Pain The Neuropathic Pain Network estimates that 1.5% of the US population − 4.6 million people − suffers from neuropathic pain. Research firm WWMR estimates that by 2018, there will be six million people in the US suffering from major neuropathic pain, a complex, chronic pain state that frequently accompanied by tissue injury and characterized by numbness, a shooting, stinging or burning pain, and a tingling or shock-like sensation. With neuropathic pain, the nerve fibers themselves may be damaged, dysfunctional or injured, sending incorrect signals to other pain centers. The impact of nerve fiber injury includes a change in nerve function both at the site of injury and areas around the injury.

Neuropathic pain diagnoses can be difficult to confirm, as there are no objective means of determining pain source, location, duration and intensity. But widely recognized causes include alcoholism, amputation, fibromyalgia, back, leg, and hip problems, chemotherapy, diabetes, facial nerve problems (trigeminal neuralgia), HIV infection or AIDS, multiple sclerosis, shingles and spine surgery. Neuropathic pain often responds poorly to standard pain treatments and may become more intense over time, potentially causing serious disability.

Oncologic Pain MediZine's Healthcom-munities.com points to studies showing that 30% of all cancer patients experience pain, with severity increasing as the disease progresses. An estimated 90% of patients with advanced cancer suffer severe pain. The American Cancer Society reported US cancer prevalence at 11 million in 2006. Extrapolating from the number of 2009 US cancer deaths, we surmise that of those 11 million, at least 565,000 are advanced or late-stage cases, of whom 510,000 are suffering severe pain. Cancer-related pain is either acute or chronic, each type being either tumor- or therapy-related. Acute pain stemming from tumor growth is best relieved by removing or reducing the tumor surgically or with radiation. The duration and intensity of acute pain caused by cancer therapy is predictable, as it ends when the treatment is over.

Chronic pain caused by tumor growth worsens as the disease progresses. Efforts to reduce chronic pain include removal or reduction of the tumor, analgesic drugs, neurosurgical anesthetic blocks and behavioral management. Examples of chronic cancer pain associated with therapy are pain after mastectomies or limb amputation. An increasing percentage of cancer patients suffer from chronic pain; an estimated one fourth of chronic cancer pain patients are referred to pain clinics.

Risks

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

Regulatory/Legal Zynex's devices must be cleared for US marketing by the FDA, mostly through the 510(k) review process, a relatively low regulatory hurdle that requires the company to demonstrate that a product under review is substantially equivalent to a similar device on the market (predicate device) before 1976. Devices sold in in the European Union (EU) must be CE (Conformite Europeenne) marked, showing that it meets EU health, safety, and environmental requirements.

The Patient Protection and Affordable Care Act (PPACA) of 2010, which must be fully implemented by 2019, contains provisions that will increase pressure on pricing and require medical device manufacturers to pay fees on their sales. The medical device industry has lobbied the US Senate in an effort to repeal or modify legislated fees. While that effort has had some initial success, the outcome is uncertain, as are the longer term ramifications of PPACA.

Intervening Technnology Zynex's technology is protected by trademarks and trade secrets, rather than patents. While the company keeps it software proprietary by developing and maintaining it internally, competitors could potentially develop more effective devices.

Reimbursement Applications for reimbursement are subject to disputes which can result in carriers' requests for refunds of previously paid claims. Refunds are frequently offset after review of the billings in question, and the sums refunded have been largely immaterial. Potential for refunds underlies some revenue uncertainty. Potential for refunds underlies some revenue uncertainty.

Reimbursement requests filed electronically must meet the more detailed requirements of a new coding system and be submitted under a revised processing system. Difficulty in conforming to the new requirements could result in delays or failure to secure reimbursement for products sold to health insurance pan beneficiaries.

Concentration of Receivables One private health insurance carrier accounted for 27% of net accounts receivable as of September 30, 2012. If this carrier proved to be especially problematical, reimbursements might be lost or delayed.

Competition The market for electrotherapy devices is fragmented and highly competitive. TENS and interferential current technologies have been on the market for more than 30 years and these devices increasingly tend to trade as commodities with limited pricing flexibility.

Concentration of stock ownership Thomas Sandgaard owns 57% of ZYXI shares. This concentration of ownership gives him disproportionate influence over management actions, potentially leading to decisions that may not be in the best interest of the stockholders at large.

Potential Dilution The sale of common shares to raise capital would dilute the ownership interests of current shareholders.

Microcap Concerns Shares of ZYXI have risks common to the stocks of other microcap (which we define as market capitalizations of $250 million or less) companies. These risks often underlie stock price discounts from the valuations of larger-capitalization stocks. Liquidity risk, typically caused by small trading floats and very low trading volume, can lead to large spreads and high volatility in stock price. The company has approximately 12 million shares in the float. Average daily volume is 13,500 shares.

Miscellaneous Risks The company's financial results and equity values are subject to other risks and uncertainties known and unknown, including but not limited to competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

Annual Income Statements
($ 000)
2010A –2014E

	2010A	2011A	2012A	2013E	2014E
Revenue					
Rental	8,533	9,892	8,917	7,743	8,403
Sales	15,552	24,256	30,749	24,268	26,883
Total	24,085	34,148	39,666	32,011	35,287
Cost of revenue					
Rental	802	1,842	1,283	1,167	1,239
Sales	4,400	5,529	7,487	6,277	6,485
Total	5,202	7,371	8,770	7,444	7,724
Gross profit	18,883	26,777	30,896	24,567	27,562
SG&A expenses					
Sales/marketing	6,331	9,340	13,340	7,992	8,822
Reimbursement & billing	6,261	7,969	8,944	8,925	9,704
G&A	3,246	4,278	4,702	5,290	5,646
Engineering & operations	1,484	2,089	1,173	1,070	1,059
Total SG&A	17,322	23,676	28,159	23,278	25,230
Operating income	1,561	3,101	2,737	1,290	2,332
Interest income	5	1			
Interest expense	(215)	(460)	(435)	(459)	(326)
Other income (expense)	(16)	2	31		
Pretax income	1,335	2,644	2,336	831	2,006
Income tax	(985)	(1,080)	(788)	(345)	(803)
Net income	350	1,564	1,548	486	1,204
Average shares outstanding	30,705	30,978	31,222	32,162	33,375
Earnings (loss) per share	0.01	0.05	0.05	0.02	0.04
Margin Analysis					
Gross margin - total	78.4%	78.4%	77.9%	76.7%	78.1%
Rental	90.6%	81.4%	85.6%	84.9%	85.3%
Sales	71.7%	77.2%	75.7%	74.1%	75.9%
SG&A					
Sales/marketing	26.3%	27.4%	33.6%	25.0%	25.0%
Reimbursement & billing	26.0%	23.3%	22.5%	27.9%	27.5%
G&A	13.5%	12.5%	11.9%	16.5%	16.0%
Engineering & operations	6.2%	6.1%	3.0%	3.3%	3.0%
Total SG&A	71.9%	69.3%	71.0%	72.7%	71.5%
Operating income	6.5%	9.1%	6.9%	4.0%	6.6%
Net income	1.5%	4.6%	3.9%	1.5%	3.4%
Tax rate	(73.8%)	(40.8%)	(33.7%)	(41.5%)	(40.0%)

Source: Company reports and Taglich Brothers estimates

Quarterly Income Statements
($ Thousands)
2012E - 2014E

	1Q12A	2Q12A	3Q12A	4Q12A	2012A	1Q13A	2Q13E	3Q13E	4Q13E	2013E	1Q14E	2Q14E	3Q14E	4Q14E	2014E
Revenue															
Rental	2,062	2,437	2,281	2,137	8,917	1,679	1,828	1,939	2,297	7,743	1,931	2,011	2,084	2,378	8,403
Sales: electrotherapy/private label pdts	3,058	3,622	3,783	3,689	14,152	2,091	2,717	2,837	3,136	10,780	2,509	2,988	3,121	3,449	12,068
consumables	3,824	3,967	4,038	4,768	16,597	3,898	2,954	3,104	3,531	13,488	4,396	3,249	3,383	3,787	14,816
Total sales	6,882	7,589	7,821	8,457	30,749	5,989	5,670	5,942	6,667	24,268	6,905	6,237	6,504	7,237	26,883
Total revenue	8,944	10,026	10,102	10,594	39,666	7,668	7,498	7,881	8,964	32,011	8,836	8,248	8,589	9,614	35,287
Cost of revenue															
Rental	258	273	279	473	1,283	301	238	330	299	1,167	270	302	287	380	1,239
Sales	1,555	1,513	1,937	2,482	7,487	1,890	1,361	1,426	1,600	6,277	1,674	1,497	1,577	1,737	6,485
Total	1,813	1,786	2,216	2,955	8,770	2,191	1,598	1,756	1,899	7,444	1,945	1,799	1,864	2,117	7,724
Gross profit	7,131	8,240	7,886	7,639	30,896	5,477	5,900	6,125	7,066	24,567	6,891	6,449	6,725	7,497	27,562
SG&A expenses															
Sales/marketing	3,095	3805	3,497	2,943	13,340	1,906	1,875	1,970	2,241	7,992	2,209	2,062	2,147	2,404	8,822
Reimbursement & billing	2,034	2047	2,425	2,438	8,944	2,231	2,062	2,167	2,465	8,925	2,430	2,268	2,362	2,644	9,704
G&A	1,183	1127	1,099	1,293	4,702	1,356	1,200	1,300	1,434	5,290	1,414	1,320	1,374	1,538	5,646
Engineering & operations	333	329	153	358	1,173	340	225	236	269	1,070	265	247	258	288	1,059
Total SG&A	6,645	7,308	7,174	7,032	28,159	5,833	5,361	5,674	6,409	23,278	6,318	5,897	6,141	6,874	25,230
Operating income	486	932	712	607	2,737	(356)	538	451	656	1,290	573	552	584	623	2,332
Interest income				3	3										
Interest expense	(93)	(81)	(119)	(142)	(435)	(130)	(112)	(113)	(103)	(459)	(85)	(77)	(79)	(83)	(326)
Other income (expense)		(7)	(6)	44	31	(6)									
Pretax income	393	844	587	512	2,336	(492)	427	338	553	831	488	475	504	539	2,006
Income tax	(73)	(371)	(229)	(115)	(788)	182	(171)	(135)	(221)	(345)	(195)	(190)	(202)	(216)	(803)
Net income before minority interest						(310)									
Minority interest in earnings						6									
Net income	320	473	358	397	1,548	(304)	256	203	332	486	293	285	303	324	1,204
Average shares outstanding	31,037	31,249	31,317	31,285	31,222	31,148	32,250	32,500	32,750	32,162	33,000	33,250	33,500	33,750	33,375
Earnings (loss) per share	0.01	0.02	0.01	0.01	0.05	(0.01)	0.01	0.01	0.01	0.02	0.01	0.01	0.01	0.01	0.04
Margin Analysis															
Gross margin - total	79.7%	82.2%	78.1%	72.1%	77.9%	71.4%	78.7%	77.7%	78.8%	76.7%	78.0%	78.2%	78.3%	78.0%	78.1%
Rental	87.5%	88.8%	87.8%	77.9%	85.6%	82.1%	87.0%	83.0%	87.0%	84.9%	86.0%	85.0%	86.3%	84.0%	85.3%
Sales	77.4%	80.1%	75.2%	70.7%	75.7%	68.4%	76.0%	76.0%	76.0%	74.1%	75.8%	76.0%	75.8%	76.0%	75.9%
SG&A	74.3%	72.9%	71.0%	66.4%	71.0%	76.1%	71.5%	72.0%	71.5%	72.7%	71.5%	71.5%	71.5%	71.5%	71.5%
Sales/marketing	34.6%	38.0%	34.6%	27.8%	33.6%	24.9%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Reimbursement & billing	22.7%	20.4%	24.0%	23.0%	22.5%	29.1%	27.5%	27.5%	27.5%	27.9%	27.5%	27.5%	27.5%	27.5%	27.5%
G&A	13.2%	11.2%	10.9%	12.2%	11.9%	17.7%	16.0%	16.5%	16.0%	16.5%	16.0%	16.0%	16.0%	16.0%	16.0%
Engineering & operations	3.7%	3.3%	1.5%	3.4%	3.0%	4.4%	3.0%	3.0%	3.0%	3.3%	3.0%	3.0%	3.0%	3.0%	3.0%
Operating income	5.4%	9.3%	7.0%	5.7%	6.9%	(4.6%)	7.2%	5.7%	7.3%	4.0%	6.5%	6.7%	6.8%	6.5%	6.6%
Net income	3.6%	4.7%	3.5%	3.7%	3.9%	(4.0%)	3.4%	2.6%	3.7%	1.5%	3.3%	3.5%	3.5%	3.4%	3.4%
Tax rate	(18.6%)	(44.0%)	(39.0%)	(22.5%)	(33.7%)	(37.0%)	(40.0%)	(40.0%)	(40.0%)	(41.5%)	(40.0%)	(40.0%)	(40.0%)	(40.0%)	(40.0%)

Source: Company reports and Taglich Brothers estimates

Zynex, Inc.

Annual Balance Sheets
($ 000)
2010A –2014E

	2010A	2011A	2012A	1Q13A	2013E	2014E
ASSETS						
Current assets						
Cash + equivalents	602	789	823	681	915	270
Accts receivable	7,309	10,984	12,224	11,234	10,226	11,272
Inventory	3,641	4,556	6,160	6,324	5,514	5,517
Prepaid expenses	145	293	243	256	170	187
Deferred tax asset	794	1,384	1,855	1,855	1,434	1,538
Other	41	42	57	228	50	50
Total	12,532	18,048	21,362	20,578	18,309	18,835
Fixed assets (net)	2,906	3,422	3,851	3,519	4,282	5,435
Deposits	174	170	171	170	175	175
Deferred financing fees	89	145	98	85	150	150
Intangibles			203	188	152	104
Goodwill			251	251	251	251
TOTAL ASSETS	15,701	21,785	25,936	24,791	23,319	24,950
LIABILITIES AND EQUITY						
Current liabilities						
Line of credit	1,270	3,289	5,906	6,602	5,500	5,000
Notes & other obligations - curr	93	131	144	151	140	140
Accts pay	1,313	2,189	2,057	1,675	2,068	2,146
Accruals	1,552	2,276	1,430	1,458	1,229	1,318
Income taxes payable	1,103	1,567	2,164	1,003	448	1,043
Deferred rent	221	296	371	390	325	325
Contingencies - curr			21	21	25	25
Total	5,552	9,748	12,093	11,300	9,735	9,997
Notes & other obligations (less curr)	327	258	114	144	200	200
Deferred rent	1,452	1,156	785	673	500	500
Deferred tax liability	188	483	786	786	500	500
Warranty liability			20	20	20	20
Contingencies - less curr			83	87	120	120
Shareholders' equity	8,182	10,140	12,055	11,781	12,244	13,611
TOTAL LIABILITIES AND EQUITY	15,701	21,785	25,936	24,791	23,319	24,950

Source: Company reports and Taglich Brothers estimates

Zynex, Inc.

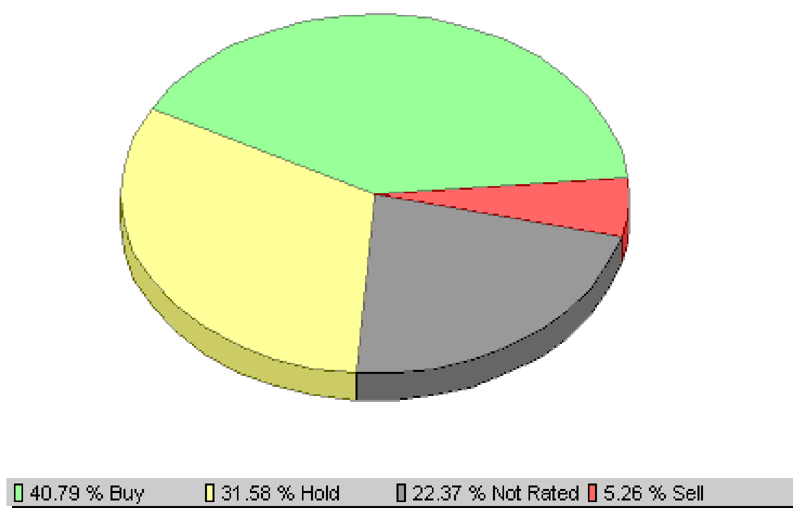
Annual Cash Flow Statements
($ 000)
2010A –2014E

	2010A	2011A	2012A	1Q13A	2013E	2014E
Operating activities				(quarter only)		
Net Income	350	1,564	1,548	(310)	480	1,204
Depreciation/ amortization	774	806	864	213	540	547
Accretion of contingency consideration			(31)	4	4	
Provision for losses - accts rec	317	1,190	485	136	376	320
Amortization of intangibles			48	15	51	48
Amortization - financing fees	71	91	50	13	13	
Stock based compensation - employees	267	267	166	36	171	180
Stock based compensation for services	79	79	20			
Provision for obsolete inventory	23	149	573	17	17	
Deferred rent	1,129	(221)	(296)	(93)	(318)	(300)
Net loss - disposal of equipment	18					
Deferred tax benefit	(281)	(295)	(168)			
Gain on value of derivative liability						
Changes in working capital	(3,412)	(3,992)	(4,138)	(1,024)	489	(305)
Net cash from operations	(665)	(362)	(879)	(993)	1,823	1,694
Investing activities						
Deposits						
Proceeds on lease termination	108					
Cash paid for domain name			(18)			
Capital expenditures						
Cash paid for acquisition			(245)			
Change in rental equip/inventory	(672)	(1,267)	(1,321)	192	(1,183)	(1,700)
Net - investing activities	(564)	(1,267)	(1,584)	192	(1,183)	(1,700)
Financing activities						
Decrease in overdraft						
Net change - line of credit	1,270	2,019	2,617	696	(406)	(500)
Deferred financing fees	(120)	(147)	(2)			
Payments - capital lease obligations	(182)	(104)	(131)	(37)	(142)	(140)
Proceeds - issuance of stock		48	13			
Repayment of shareholder loans						
Net cash from financing	968	1,816	2,497	659	(548)	(640)
Net change in cash	(261)	187	34	(142)	92	(646)
Cash - beginning	863	602	789	823	823	915
Cash - ending	602	789	823	681	915	270

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	1	4
Hold	1	14
Sell		
Not Rated		

Important Disclosures

At this writing, none of Taglich Brothers' affiliates, officers, directors or stockholders, or any member of their families have a position in the stock of Zynex, Inc. Taglich Brothers, Inc. does not have an investment banking relationship with Zynex, Inc. and was not a manager or co-manger of any offering for the company within the last three years.

All research issued by Taglich Brothers, Inc. is based on public information. In September 2012 the company paid an initial monetary engagement fee of US$4,500 to Taglich Brothers, Inc. representing payment for the first three months of creation and dissemination of research reports, after which the company will pay Taglich Brothers, Inc. a monetary fee of US$1,500 per month for a minimum of three more months for such services.

General Disclosures

The information and statistical data contained herein have been obtained from sources, which we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to change in figures or our views. This is not a solicitation of any order to buy or sell. Taglich Brothers, Inc. is fully disclosed with its clearing firm, Pershing, LLC, is not a market maker and does not sell to or buy from customers on a principal basis. The above statement is the opinion of Taglich Brothers, Inc. and is not a guarantee that the target price for the stock will be met or that predicted business results for the company will occur. There may be instances when fundamental, technical and quantitative opinions contained in this report are not in concert. We, our affiliates, any officer, director or stockholder or any member of their families may from time to time purchase or sell any of the above-mentioned or related securities. Analysts and members of the Research Department are prohibited from buying or selling securities issued by the companies that Taglich Brothers, Inc. has a research relationship with, except if ownership of such securities was prior to the start of such relationship, then an analyst or member of the Research Department may sell such securities after obtaining expressed written permission from Compliance.

Analyst Certification

I, Juan Noble, 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

ITT Corporation	(NYSE: ITT)	Qualmark	(OTC: QMRK)
Koninklijke Philips Electronics NV	(NYSE: PHG)	Siemens AG	(NYSE: SI)
Medtronic	(NYSE: MDT)	St. Jude Medical	(NYSE: STJ)

Meaning of Ratings

Buy - the company is undervalued relative to its market and peers. We believe its risk reward ratio strongly advocates purchase of the stock relative to other stocks in the marketplace. Remember, with all equities there is always downside risk.

Speculative Buy - We believe that the long run prospects of the company are positive. We believe its risk reward ratio advocates purchase of the stock. We feel the investment risk is higher than our typical “buy” recommendation. In the short run, the stock may be subject to high volatility and continue to trade at a discount to its market.

Neutral - We will remain neutral pending certain developments.

Underperform - We believe that the company may be fairly valued based on its current status. Upside potential is limited relative to investment risk.

Sell - We believe that the company is significantly overvalued based on its current status. The future of the company's operations may be questionable and there is an extreme level of investment risk relative to reward.

Dropping Coverage – we have discontinued research coverage due to the acquisition of the company, termination of research services, non-payment for such services, 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.