

### SELECTCORE LTD.

(\$0.07; TSX-V:SCG)

#### Recommendation

Speculative Buy

#### Risk

High

#### Price (March 11, 2010)

\$0.07

#### 52-Week Range

\$0.10 - \$0.015

#### Target Price Range (12 Mo.)

\$0.35-\$0.40

#### Shares O/S

102.9 million

#### Market Cap

\$7.2 million

#### Average Daily Volume

50-day: 233,400

200-day: 180,700

#### Year-End

December 31

C\$	BVPS	EPS
2007A	\$0.03	(\$0.03)
2008A	(\$0.04)	(\$0.08)
2009E	(\$0.03)	\$0.01
2010E	\$0.03	\$0.06

BVPS: Book Value Per Share

EPS: Earnings Per Share

#### Analysts

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Data Source: www.BigCharts.com

### UPFRONT

Although prepaid cards have been around for a while, SelectCore is the first to have a prepaid reloadable credit card that is sold to consumers through retail locations. Known as the Iridium MasterCard, it can be used at ATMs and for on-line purchases, and is accepted everywhere that MasterCard is. Given the adverse economic and financial environment, consumer credit has become difficult to acquire. This product is readily available, and easy to use and re-use. Its acceptance should generate significant revenue growth for the Company and at exceptional margins. In turn, this should lead, eventually, to an upwards multiple revision.

### RECOMMENDATION

We recommend SelectCore Ltd. as a Speculative Buy for risk-tolerant investors. Our 12-month Target Price range for the stock is \$0.35 to \$0.40, significantly above its current price.

### PROFILE

SelectCore Ltd. ("SelectCore" or the "Company") provides prepaid telecom and financial services for the credit-challenged and "un-banked" consumer markets. The Company offers products and services to consumers through its nation-wide retail channel and also provides wholesale solutions to its corporate clients.

## **THE COMPANY**

SelectCore offers prepaid telecom and prepaid financial solutions to a large and growing underserved market using its own network infrastructure and proprietary technology.

SelectCore provides services to both the consumer and wholesale market segments. The Company's consumer division offers a wide range of prepaid solutions, including wireless & long distance, internet, international mobile top-up, and credit card services through its established and growing retail network. Through its wholesale division, SelectCore provides a suite of solutions, including point-of-sale activation (POSA), transaction processing, long distance switching and termination, and call-center support to tier-1 corporate clients.

The Company was founded in 1999 and operates in major cities of Canada and the USA. Profit-100 ranked SelectCore as one of Canada's fastest growing companies in 2006 and 2007.

## **INVESTMENT CONSIDERATIONS**

### **Strengths**

- Large and growing underserved market;
- Strong growth in revenues and high operating margins;
- Well-established distribution channel providing access to credit-challenged target market;
- Existing network infrastructure with significant capacity and no major capex requirement; and
- 2010 expansion into the USA and the introduction of the Iridium MasterCard to be significant growth drivers.

### **Challenges**

- Majority of SelectCore's revenues are generated from sales of prepaid telecom products. There is no guarantee that distribution partners will continue to purchase the Company's products;
- Success will depend on the Company's ability to adapt to technology changes of: (1) service and product vendors; and (2) evolving trends and demand of customers;
- Expansion into the USA may not materialize or, if it does, may not be successful; and
- An economic slowdown could cause demand for the Company's products to decline.

## **CORPORATE STRATEGY**

Over the past 10 years, SelectCore has pursued an aggressive growth strategy in the prepaid telecom business, targeting the un-banked and credit-challenged. The Company deployed POS terminals using its own proprietary software to facilitate the delivery and activation of products and services. The flexibility and scalability of the platform allows for easy addition of new products and services.

SelectCore's objective is to leverage its existing technology, infrastructure, and retail channel that were established over the previous decade to:

- Become a leader in the prepaid financial services industry;
- Introduce new products and services (eg. Iridium MasterCard);
- Provide wholesale solutions to corporate clients;
- Offer the lowest fee products and services; and
- Expand into other markets (USA).

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## MARKET

The Canadian market for prepaid telecommunications services is a large and growing market, currently more than \$5 billion. There is also a \$10 billion plus market for stored-value cards and a \$5 billion market for remittance. A poor economy over the last 18 months has seen financial institutions tighten credit requirements, limiting access to credit for low to moderate income individuals.

A large and growing underserved market and the current economic situation provide much opportunity for SelectCore. The Company targets the 20% of the Canadian population that is credit-challenged, which includes teens, new immigrants, and un-banked and poor-credit individuals. SelectCore's products and services empower these consumers with convenience, security, and freedom to be self-banked.

In addition, the Company provides a growing suite of wholesale solutions aimed at tier-1 corporate clients, including some of Canada's largest grocery store chains, telephone companies, and retailers. This business segment generates high margins for SelectCore, from 20% to up to 100%. SelectCore is the first company to develop a point of sale activation (POSA) solution exclusively for the independent retail chain. Other products and services the Company provides to the wholesale business segment include transaction processing, long distance switching and termination, and call centre support.

## IRIDIUM MASTERCARD

On February 9, 2010, SelectCore launched the Iridium MasterCard, a reloadable prepaid credit card that is accepted for purchases, and ATM and online use. The Iridium MasterCard is accepted everywhere MasterCard is accepted - at more than 28.5 million locations and 1 million bank machines worldwide. The Iridium MasterCard can be purchased from authorized store locations across Canada for \$3.99 and used instantly. The Company intends to roll the product out to its top 4,000 locations across Canada. A personalized version with added security can be purchased for \$9.99. There is no application, credit check, ID or personal bank account required. The Iridium MasterCard will be reloadable up to a \$5,000 balance.

Benefits to the cardholder from the Iridium MasterCard will include a low fee structure, online purchases and account access, text message alerts, bill payments, global remittance, ATM cash access, and direct payroll deposits.

Management has secured funding for Iridium's program launch and expansion. This program should be a significant revenue generator for the firm with a projected 700,000 plus cards sold over the next 3 years. The Iridium MasterCard is expected to be a high-margin business segment (approximately 75%). The Company will earn revenue through card sales, interchange fees on merchant transactions, float interest, POS transaction fees, ATM transactions, monthly service fees, remittance fees, breakage, and other miscellaneous fees.



## FINANCIAL REVIEW AND PROJECTIONS

The Company's year-end is December 31. Abridged financial statements for the last three years (2006-2008) as well as projections for 2009 and 2010 are provided overleaf.

### (1) Q3/2009 versus Q3/2008

For the third quarter of 2009, the Company reported earnings of \$0.01 per share compared with a minor loss for the same period in 2008. Revenues rose 16.6% to \$23.1 million in Q3/2009 from \$19.8 million for the same period in 2008. The increase in revenue is primarily from the Company's internally developed and proprietary POSA solution for prepaid wireless and prepaid long distance service. The significant increase in EBITDA margin reflects the benefit of a foreign exchange gain of \$249,000 in Q3/2009 compared to a foreign exchange loss of \$172,000 in Q3/2008.

(\$000s)	<u>Q3/2009</u>	<u>Q3/2008</u>
Revenue	23,064	19,779
Gross Profit	1,418	1,061
Gross Profit Margin	6.1%	5.4%
EBITDA	506	30
EBITDA Margin	2.2%	0.2%
Net Profit (Loss)	595	(481)
Net Profit Margin	2.6%	N/A
EPS	\$0.01	(\$0.00)
Avg. Shares O/S (000)	102,363	100,363

### (2) 9M/2009 versus 9M/2008

The latest results brought earnings for the first nine months of 2009 to \$0.02 per share compared with a loss of \$0.02 per share for the first three quarters of 2008. Revenues increased 24% to \$63.9 million. Again, the strong growth in revenues was primarily from the Company's internally developed and proprietary POSA solution for prepaid wireless and prepaid long distance service. The improvement in the EBITDA margin for the nine month period in 2009 also reflects a foreign exchange gain of \$331,000 versus a foreign exchange loss of \$172,000 for the same period in 2008.

(\$000s)	<u>9M/2009</u>	<u>9M/2008</u>
Revenue	63,876	51,507
Gross Profit	3,797	3,016
Gross Profit Margin	5.9%	5.9%
EBITDA	868	(100)
EBITDA Margin	1.4%	N/A
Net Profit (Loss)	727	(1,918)
Net Profit Margin	1.1%	N/A
EPS	\$0.01	(\$0.02)
Avg. Shares O/S (000)	102,363	97,506

**COMMENT:** Year-to-date net profit of \$727,000, compared to a loss of \$1,918,000 for the same period in 2008, has been achieved as a result of the growth in sales, cost reductions, and a foreign exchange gain on the US\$ loan facility.

**(3) Financial Statements**

	Year Ending December 31:			12Mo:	Year Ending December 31:	
	2006	2007	2008	Sept 30 2009	2009E	2010E
<b>Statement of Income/(Loss):</b>						
Revenue	37,645,919	47,762,218	70,638,397	83,007,646	90,400,000	134,200,000
Cost of Sales	(36,929,821)	(45,668,990)	(66,912,358)	(78,500,694)	(85,000,000)	(122,300,000)
Gross Profit	716,098	2,093,228	3,726,039	4,506,952	5,400,000	11,900,000
Gross Profit Margin	1.9%	4.4%	5.3%	5.4%	6.0%	8.9%
SG&A	(1,141,062)	(3,481,663)	(3,624,734)	(3,489,336)	(3,800,000)	(5,100,000)
Stock-based Compensation	(174,082)	(422,025)	(150,039)	(97,962)	(150,000)	(250,000)
EBITDA	(599,046)	(1,810,460)	(48,734)	919,654	1,450,000	6,550,000
EBITDA Margin	-1.6%	-3.8%	-0.1%	1.1%	1.6%	4.9%
Amortization	(26,940)	(420,450)	(1,064,873)	(490,204)	(250,000)	(400,000)
Non-cash items adjustments	0	0	(4,916,008)	(4,916,008)	0	0
Other Income/(Expenses)	0	(115,289)	(1,088,072)	64,869	290,000	(100,000)
EBIT	(625,986)	(2,346,199)	(7,117,687)	(4,421,689)	1,490,000	6,050,000
Interest Expense	(49,991)	(7,418)	(365,584)	(416,337)	(250,000)	(300,000)
EBT	(675,977)	(2,353,617)	(7,483,271)	(4,838,026)	1,240,000	5,750,000
Future Income Taxes (Payable)/Recovery	(23,955)	0	0	0	0	0
Net Income/(Loss)	(699,932)	(2,353,617)	(7,483,271)	(4,838,026)	1,240,000	5,750,000
Total Shares Outstanding	74,758,409	96,553,462	102,362,985	102,362,985	102,862,298	102,862,298
Weighted Average Shares Outstanding	36,544,969	80,344,691	97,823,301	102,362,985	102,404,652	102,862,298
Earnings (Loss) Per Share	(\$0.02)	(\$0.03)	(\$0.08)	(\$0.05)	\$0.01	\$0.06
<b>Statement of Cash Flow:</b>						
Net Income (Loss)	(699,932)	(2,353,617)	(7,483,271)	(4,838,026)	1,240,000	5,750,000
All Non-Cash Items	238,837	879,263	6,130,920	5,104,174	400,000	650,000
Cash Flow from Operations	(461,095)	(1,474,354)	(1,352,351)	266,148	1,640,000	6,400,000
Capital Expenditures	(27,717)	(159,446)	(725,172)	(271,745)	(205,000)	(95,000)
Other Investing Items	977,018	(2,787,591)	0	77,058	(1,000)	(45,000)
Free Cash Flow	488,206	(4,421,391)	(2,077,523)	71,461	1,434,000	6,260,000
Working Capital Changes	125,553	1,671,666	(1,832,688)	(193,515)	(348,545)	(2,276,400)
Equity Financing	43,205	2,985,413	0	0	30,500	0
Debt Financing/Capital Leases	(37,366)	(9,406)	2,276,243	122,054	130,000	100,000
Change in Cash	619,598	226,282	(1,633,968)	0	1,245,955	4,083,600
Cash, Beginning of the Period	47,658	667,256	893,538	(893,538)	(740,430)	505,525
Cash, End of the Period	667,256	893,538	(740,430)	(893,538)	505,525	4,589,125
<b>Balance Sheet:</b>						
	As at December 31:			September 30:	December 31:	
	2006	2007	2008	2009	2009E	2010E
Cash	667,256	893,538	0	0	505,525	4,589,125
Accounts Receivable	1,994,180	3,066,386	4,437,541	5,550,385	5,600,000	5,000,000
Other Current Assets	272,296	1,556,684	1,607,504	2,988,779	2,990,000	3,000,000
Capital Assets	252,713	941,131	900,142	884,399	885,000	950,000
Intangibles	0	3,290,777	57,444	38,694	39,000	30,000
Other Assets	399,226	1,463,295	0	0	0	100,000
Total Assets	3,585,671	11,211,811	7,002,631	9,462,257	10,019,525	13,669,125
Bank Overdraft	0	0	740,430	0	0	0
Current Liabilities	3,292,564	8,295,389	7,754,735	10,139,961	10,150,000	8,500,000
Current Portion of Long-Term Debt	7,253	8,172	19,214	2,446,361	2,450,000	2,000,000
Deferred Revenue	0	0	38,033	0	0	0
Debt/Capital Leases	30,818	44,393	2,309,594	8,368	8,400	8,000
Total Liabilities	3,330,635	8,347,954	10,862,006	12,594,690	12,608,400	10,508,000
Shareholders' Equity	255,036	2,863,857	(3,859,375)	(3,132,433)	(2,588,875)	3,161,125
Total Liabilities & Equity	3,585,671	11,211,811	7,002,631	9,462,257	10,019,525	13,669,125
Book Value (S.E.) Per Share	\$0.00	\$0.03	(\$0.04)	(\$0.03)	(\$0.03)	\$0.03

**NOTE:** See COMMENT on this financial table on the next page.

**COMMENT:** (1) *The consistent improvement in gross profit margin over the period 2006-2008 is directly related to the increase in revenue from the Company's point of sale activation (POSA) system. We expect a 6% gross profit margin for 2009 which is a slight improvement from the 5.9% profit margin year-to-date. For 2010, we expect profit margins to increase to 8.9% as a result of high margins generated from the Iridium MasterCard business segment.*

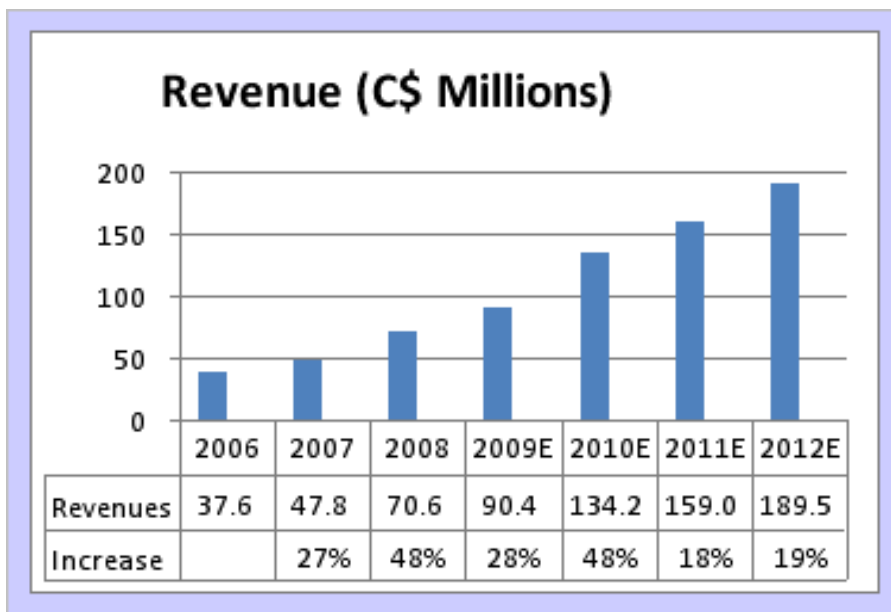
(2) *SelectCore has a very robust and highly scalable network completely paid for in full. Taking this into consideration, we estimate SelectCore's capital expenditures to be approximately \$95,000, the bulk of which will be used to expand the Company's processing and delivery footprint in the USA and to support the Iridium MasterCard launch.*

(3) *In 2008, SelectCore wrote down property and equipment, intangible assets, and goodwill obtained through the acquisition of Canquest Communications (Canada) Inc. and its subsidiary, Canquest Communications (Wireless) Inc. due to deterioration of performance and corresponding reduction in the value of that line of business. The write-downs had a negative impact on the book value of the Company in the order of \$0.05 per share. We expect an improvement in the book value to (\$0.03) and \$0.03 per share in 2009 and 2010, respectively.*

**(4) Yearly Trends and Projections**

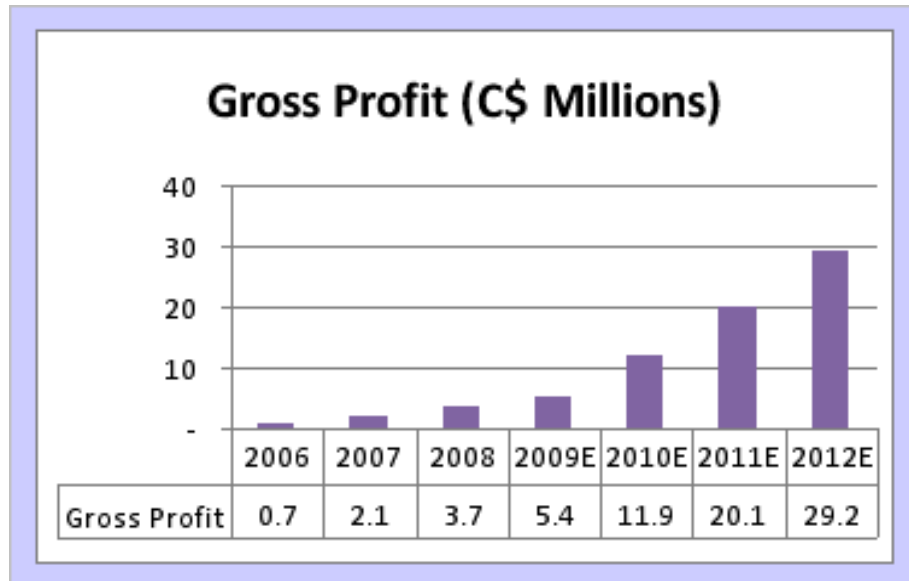
Profit-100 ranked SelectCore as one of Canada's fastest growing companies in 2006 and 2007 with revenues of \$37.6 million and \$47.8 million respectively. The Company continues on a high-growth path with proforma 2009 revenues expected to be \$90.4 million.

The increase in revenue is primarily from the Company's internally developed and proprietary POSA solution for prepaid wireless and prepaid long distance service. This is expected to contribute to future revenue increases in the near term, but longer-term revenue increases are expected to come from the Iridium MasterCard program along with revenues generated from the expansion into the USA. Historical and projected revenues are presented in the following chart:



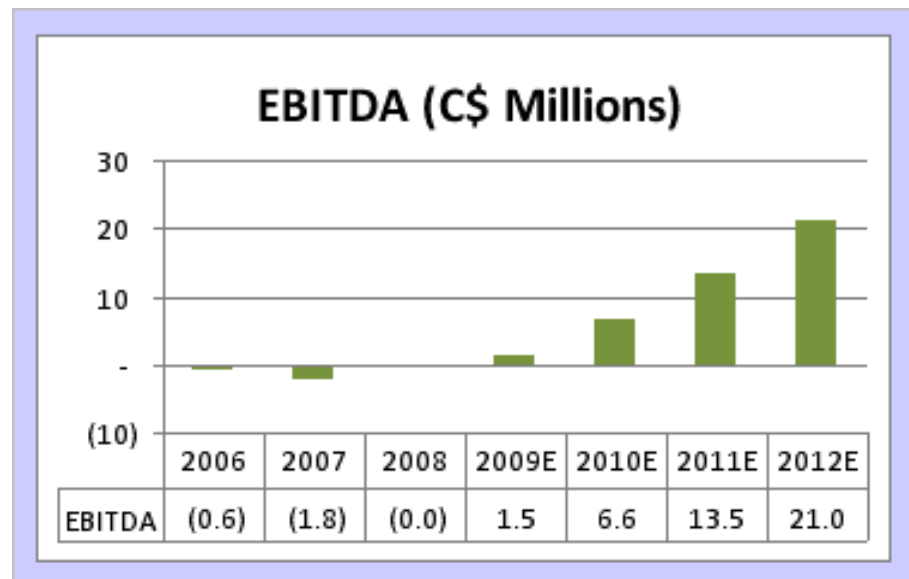
Source: eResearch and Company

The Company has also seen an increase in its gross profit margin from 1.9% (\$0.7 million) in 2006 to 6.0% (\$5.4 million, pro forma estimate) in 2009, and ratcheting up over the ensuing years.



Source: eResearch and Company

The Company's EBITDA increased from (\$0.6) million in 2006 to \$1.5 million (pro forma estimate) in 2009. The EBITDA is expected to be \$21.0 million (EBITDA margin of 11.1%) by 2012. The expected increase in the EBITDA margin will be the result of lower cap-ex spending and increased margin provided by the Iridium MasterCard.



Source: eResearch and Company

**COMMENT:** We expect gross margins for the Company to continue to trend up as the Company leverages existing technology and infrastructure with little or no cap-ex in future introductions of services and products, and expansions into other markets.

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## COMPETITION

A comparable based valuation for SelectCore was not performed as adequate public companies to gauge SelectCore's value were not found. Publicly trading companies operating in the prepaid telecom and prepaid financial services space tend to be larger players. Companies in this industry of similar size to SelectCore operate privately and, thus, adequate data is not available.

A few of the companies operating in this sector are listed below:

**Incomm** – Incomm provides technology to the prepaid long-distance industry. Partnered with retailers and product providers, the company provides stored-value gift and prepaid products, services, and technologies. Incomm is a large private company that was founded in 1992 and is headquartered in Atlanta.

**VendTek Systems Inc. (TSX-V:VSI)** – VendTek develops and licenses transaction automation software and supporting technologies for the prepaid telecom and financial services industries. The company was founded in 1988 and became a publicly-listed company in Canada in 1999. As of the date of this report, VendTek shares have not resumed trading due to ongoing restatement of financial statements required by the British Columbia Securities Commission.

**Euronet Worldwide Inc. (NASDAQ:EEFT)** – Euronet provides electronic payment and transaction processing solutions for financial institutions, retailers, service providers, and individual consumers. The company was founded in Budapest, Hungary in 1994, and became a publicly-listed company in the USA in 1997. Euronet's market cap of approximately US\$1 billion makes it an inadequate company for comparable purposes.

**Mint Technology Corp. (TSX-V:MIT)** – Mint provides prepaid financial products and services tailored to their clients needs. The company's technology delivers an improved means to handle and manage financial transactions. Mint also provides clients with payment methods that include chip, internet, data mining, and mobile phone load and remittance technologies.

**Blackhawk Network** and **Coinstar, Inc.** are also competitors of SelectCore, but to a lesser extent, and were determined to be inappropriate for comparables for reasons similar to the companies considered above.

## VALUATION

### 1. Discounted Cash Flow Valuation

With almost all of SelectCore's capital expenditures behind them, we expect growth in the Company's cash flow going forward. In addition, we expect stronger near-term cash flow reflecting the Company's launch of the Iridium MasterCard. In our valuation, we assume a 3-year high-growth period in which cash flow will increase by 15% per annum, after which the Company's growth in cash flow will be at a more sustainable level. The table below illustrates a range of values for SelectCore based on varying discount and terminal growth rates. We used a range of discounts from 12% to 20% in increments of 2%, and terminal growth rates ranging from 1% to 5%, which provided a matrix of values for SelectCore ranging from \$0.27 to \$0.71 per share.

The following table shows the discounted cash flow valuation range using a cash flow growth rate of 15% in the first three years, and then the terminal growth rate set out in the table below:

		Discount Rate				
		20%	18%	16%	14%	12%
Terminal Growth	1%	0.27	0.31	0.35	0.41	0.49
	2%	0.28	0.32	0.37	0.43	0.53
	3%	0.29	0.33	0.39	0.46	0.57
	4%	0.31	0.35	0.41	0.50	0.63
	5%	0.32	0.37	0.44	0.54	0.71

On a discounted cash flow basis, we believe an appropriate range for the Company's stock is \$0.33 to \$0.46 per share.

### 2. Multiple of Earnings

For 2010, we forecast EPS of \$0.055 per share. Based on a 6x-8x forward P/E multiple, SelectCore has a fair value range of \$0.33 to \$0.44 per share.

### 3. Multiple of Cash Flow

For 2010, we forecast cash flow per share of \$0.06. Based on a 5x-7x forward P/CF multiple, SelectCore has a fair value range of \$0.30 to \$0.42 per share.

## TARGET PRICE

With due consideration to all of the factors involved in assessing the estimated value of SelectCore, we have chosen a 12-month Target Price range for the stock of \$0.35-\$0.40 per share.

**COMMENT:** *We believe that the Company's stock is significantly undervalued based on analysis of both discounted cash flow and multiples of earnings and cashflow and, therefore, provides attractive capital gains potential over the intermediate term.*

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## APPENDIX 1: MANAGEMENT AND DIRECTORS

**Martin Bernholtz**, Chairman, Director

**Keith McKenzie**, Chief Executive Officer, Director

**Ryan Deslippe**, President, Director

**Jannet Wang**, Chief Financial Officer

**Mohammad Abu-Leil**, Chief Operating Officer & VP Sales

**Derek Robertson**, VP Operations

**Dan Devolder**, Director of IT Operations

**Debbie Villeneuve**, Manager, Sales Operations

**Randy Khalaf**, Director

**Mike Rohrer**, Director

## APPENDIX 2: SHARE STRUCTURE

Current Issued and Outstanding	
Shares	102,862,298
Options	5,965,000
Warrants	0
	<hr/>
Fully Diluted	108,827,298

The Management and Board of SelectCore own approximately 40% of the shares outstanding. In addition, Mavrix Fund Management Inc. and Camlin Asset Management own approximately 13-14% and 10%, respectively.

## APPENDIX 3: CORPORATE INFORMATION

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## ANALYST CERTIFICATION

Each Research Analyst who was involved in the preparation of this Research Report hereby certifies that:

- (1) the views, opinions, and recommendations expressed in this Research Report reflect accurately the Research Analyst's personal views concerning any and all securities and issuers that are discussed herein and are the subject matter of this Research Report; and
- (2) the fees, earnings, or compensation, in any form, payable to the Research Analyst, is not and will not, directly or indirectly, be related to the specific views, opinions, and recommendations expressed by the Research Analyst in this Research Report.

### **eResearch analysts on this report:**

**Shash Patel, B.Sc. (Act. Sc.), MBA:** Shash Patel has been involved with investment research for more than six years, as a securities analyst and trader, and as a pension and benefits specialist. He joined eResearch in September 2009.

**Bob Weir, B. Comm, B.Sc., CFA:** Bob Weir has 43 years of investment research and analytical experience in both the equity and fixed-income sectors, and in the commercial real estate industry. He joined eResearch in 2004 and has been its President, CEO, and Managing Director, Research Services since May 2005. Prior to joining eResearch, Mr. Weir was at Dominion Bond Rating Service (DBRS), latterly as Executive Vice-President responsible for supervising the firm's 34 analysts and conducting the day-to-day management affairs of the company.

## **eRESEARCH ANALYST GROUP**

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#### **Oil & Gas**

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Achille Desmarais

Eric Eng

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Bill Campbell

Bob Leshchyshen

Shash Patel

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Perry Siu

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George Cargill

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Tony Hayes

Kirsten Marion

Shash Patel

Oliver Schatz

Graham Wilson

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## eResearch Recommendation System

<b>Strong Buy:</b>	Expected total return within the next 12 months is at least 40%.
<b>Buy:</b>	Expected total return within the next 12 months is between 10% and 40%.
<b>Speculative Buy:</b>	Expected total return within the next 12 months is substantial, but Risk is High (see below).
<b>Hold:</b>	Expected total return within the next 12 months is between 0% and 10%.
<b>Sell:</b>	Expected total return within the next 12 months is negative.

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## eResearch Risk Rating System

A company may have some, but not necessarily all, of the following characteristics of a specific risk rating to qualify for that rating:

<b>High Risk:</b>	<p><i>Financial</i> - Little or no revenue and earnings, limited financial history, weak balance sheet, negative free cash flows, poor working capital solvency, no dividends.</p> <p><i>Operational</i> - Weak competitive market position, early stage of development, unproven operating plan, high cost structure, industry consolidating, business model/technology unproven or out-of-date.</p>
<b>Medium Risk:</b>	<p><i>Financial</i> - Several years of revenue and positive earnings, balance sheet in line with industry average, positive free cash flow, adequate working capital solvency, may or may not pay a dividend.</p> <p><i>Operational</i> - Competitive market position and cost structure, industry stable, business model/technology is well established and consistent with current state of industry.</p>
<b>Low Risk:</b>	<p><i>Financial</i> - Strong revenue growth and earnings over several years, stronger than average balance sheet, strong positive free cash flows, above average working capital solvency, company may pay (and stock may yield) substantial dividends or company may actively buy back stock.</p> <p><i>Operational</i> - Dominant player in its market, below average cost structure, company may be a consolidator, company may have a leading market/technology position.</p>

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## eResearch Disclosure Statement

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