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Ongoing costly and well-publicized security breaches in the U.S. and overseas continues to increase demand for information security software and solutions. It hardly seems a day goes by that a prominent company or government agency around the world announces a hacking incident that compromises private employee or customer data.

The massive scope and severity of security breaches continues to provide fertile ground for venture-backed startups and other emerging technology companies pioneering innovative solutions. Several emerging information security companies have popped up on our radar screen having recently completed successful initial public equity offerings.¹ One of the emerging publicly traded companies we've been analyzing and tracking closely in this segment over the past year is StrikeForce Technologies. The company has been gaining some traction in the market as consumers, businesses and government agencies beef up their defense against hackers.

IMPROVING OUTLOOK

StrikeForce has two core information security products in the marketplace currently – *ProtectID*® and *GuardedID*®. These products offer customers state-of-the-art identity theft protection, keystroke encryption and anti-keylogger protection that are not prevented by anti-scam and anti-virus signature based solutions. We have provided in-depth analysis of StrikeForce's core product offerings in previous reports.² Our research shows they provide a compelling and cost-effective solution to other competing products in the marketplace.

In our initial report on StrikeForce, published last summer, we noted that market conditions were becoming increasingly favorable for *ProtectID* and *GuardedID*. Against this market backdrop, we identified two key strategic initiatives: 1) accelerating top line growth, and 2) cleaning up the company's balance sheet to reduce its heavy debt load.

StrikeForce has been working diligently over the past year to increase its penetration in the market. On its recent earnings call with investors, management stated that the company was on track to grow revenues to \$1–\$1.5 million this year, more than double or triple what the company booked in 2011.³ Noteworthy was the fact that nearly three-quarters of the \$184,600 of sales during Q1 were of a monthly and increasing recurring nature. Driving recurring sales are the over 4 million and counting downloads of *GuardedID* and over 10 million end users of *ProtectID*.

The large share of recurring sales increases our confidence that the company will continue to drive top line growth in the quarters ahead. Management's intention of accelerating top line growth through direct sales, as well as leveraging its existing and new channel partners in the U.S. and overseas, is an important element in the company's strategy. StrikeForce currently has channel partnerships with at least eight companies that were publicly announced, including Intersections and WhiteSky in the U.S., DW Consulting Consortium and Managed Services Center in the UK/Europe, and Terrestrial Five in New Zealand (see exhibit on next page for complete list of channel partners that

¹ See: [Research 2.0 blog](#) "Information Security Update 1Q2012."

² See: [StrikeForce Technologies Research Note](#), February 22, 2012.

³ A Webex replay of the StrikeForce earnings call is available at this link:
<http://www.strikeforcetech.com/video/SFOR-2012-q1-investor-review.wmv>.

were publicly announced). We expect the company to sign up additional channel partners in the future.

8-K CONFUSION

The acceleration of top line growth is creating a favorable cash flow dynamic for StrikeForce that has not been seen throughout the history of the company. StrikeForce is likely to become cash flow positive later this year. In the past, not having the requisite cash to finance operations, management had to continually tap the private and/or public debt and equity markets to sustain the company – sometimes at significantly discounted and/or dis-

terms of the equity facility were contained in a SEC Form 8-K dated May 3, 2012.⁴

Auctus agreed over a period of 36 months to commit to purchase up to \$6,000,000 of StrikeForce’s common stock with a specified pricing structure based on the company’s then-current share price.

The terms of the equity facility stated that StrikeForce would be able to raise capital at a 10% discount to the lowest closet bid price for the five consecutive trading days after a drawdown notice. The terms further specified

StrikeForce Technologies Channel Partners			
Company	Type	Location	Agreement Signed
Intersections	OEM	VA, US	January 10, 2008
WhiteSky	OEM	CA, US	May 27, 2010
Datanet 2000	Distributor	NJ, US	March 1, 2011
Veratad Technologies, LLC	Distributor	NJ, US	October 3, 2011
Managed Services Center	Distributor	London, Europe	October 5, 2011
DW Consulting Consortium Ltd.	Master Distributor	London, Europe	October 5, 2011
STRATEGIC MicroSystems	Reseller	NJ, US	January 1, 2012
Terrestrial Five, Inc.	Reseller	Auckland, NZ	February 12 2012

Source: StrikeForce Technologies

tressed valuations.

The lack of positive cash flow during its operating history has taken a toll on StrikeForce’s balance sheet. Management has indicated its desire to shore up the company’s capital structure, but it is not clear at this juncture precisely how or when it will be done.

In the meantime, the company has put in place an equity facility to ensure it has sufficient operating growth capital in the future if and when needed. StrikeForce recently finalized an equity facility with Auctus Private Equity Fund, LLC whereby the parties entered into a drawdown equity financing agreement and a registration rights agreement. The

that a drawdown would not exceed the lesser of \$150,000 or the value of 200% of the average daily volume for the prior ten trading days multiplied by the average of the closing best bid prices for the prior ten trading days. The terms of the facility further stated that Auctus would immediately cease reselling any StrikeForce equity within a pricing period if the per share price fell below a minimum floor set in each notice by the company.

Management indicated on its recent earnings call that the S-1 filing associated with the Auctus equity facility would be limited to 40 million shares. They also stated that the objective of the equity facility was solely for insurance purposes and not to be

⁴ See StrikeForce Form 8-K at this link: http://xml.10kwizard.com/filing_raw.php?repo=tenk&page=8252038

utilized unless absolutely necessary.

While the terms of the equity facility contained in the 8-K were specified in detail, there appeared to be a good deal of confusion in the investor community following its release. Based on what management stated on its earnings call, it appears some investors thought the facility would require the company to issue shares at a par value of \$0.0001 per share. While such a misunderstanding by investors is difficult to fathom in light of what the 8-K actually says, it would help explain the sharp decline in the company's stock price following release of the document.

VALUATION AND SUMMARY

StrikeForce's financial condition has improved over the past year. Revenues are on track to double or triple and management believes the business will become cash flow positive sometime in late Q3 or Q4 of this year. The company posted a net loss in the first quarter of 2012 of \$297,943 versus a net loss of nearly \$2 million a year ago. Management's guidance for the top line in 2012 is consistent with the projection in our valuation model published in our previous report.

Despite the substantive progress the company has made over the past several months the share price has declined from \$0.017 at the start of the year to \$0.009 today.

There are a couple of potential developments to keep an eye on that could provide a further boost to the top line beyond the projections in our model. One is related to a key patent. StrikeForce engaged a company to leverage its "out-of-band" authentication patent (#7,870,599) for additional potential revenues.

While it is possible that the company could experience additional licensing revenue associated with this development, management has given no guidance to what revenues, if any, might be generated in conjunction with this activity. All we can note at the present time is that any potential royalties/revenues related to the patent would have a favorable impact on the top and bottom lines beyond what we have modeled.

Another development to watch is related to new product launches. StrikeForce is gearing up to re-

lease new products targeted at Apple's computers, iPads and iPhones and Google's Android devices. The company has developed and is testing a version of *GuardedID*® to work on the Macintosh with keystroke encryption and real-time anti-keylogging features. Management projects to move it to market by the fourth quarter of 2012.

Additionally, StrikeForce has also developed a new mobile application that will first be deployed to the iPhone/iPad and then also to Android phones/tablets. This new mobile application will provide an OTP Authenticator to be used for consumers and enterprises, a secure browser feature, a password vault and a random password generator. Management projects release of these products by year-end.

Management's financial guidance is in line with the projections in our valuation model. We are not inclined to make any further adjustments at the present time. Our estimate of intrinsic value of StrikeForce remains at \$0.08/share, well above the current share price.

While prospects for the company's business has brightened over the past year, considerable business risks remain. We continue to believe that the company would benefit significantly from a capital account restructuring that dramatically reduced its debt load. We expect management to seek to explore options to address this key issue in the months ahead.

The market for security software is dynamic, crowded and competitive. The structure of the market makes it challenging for emerging companies such as StrikeForce to grow and prosper. StrikeForce's current valuation more than reflects the challenging business environment. Management's recent financial guidance gives cause for optimism, but much work remains to be done to shore up the company's finances. StrikeForce's strategic decision to design and sell security software for Apple's Macs, iPads and iPhones and Google's Android devices is on target. It will be interesting to see what kind of reception these products receive in the market after they are launched later this year. The timing of these products seems propitious with the huge and growing popularity of Apple's and Google's products with consumers, as well as enterprises and government

agencies with BYOD (Bring Your Own Device) becoming an important issue to be addressed by corporate information security personnel.

StrikeForce Technologies has operated as a standalone business since its inception, but has benefited from the formation of various partnerships. We have seen a good deal of consolidation in the information security sector over the past several years and expect this trend to continue. Given the dynamics of the security segment, we would not be surprised to see StrikeForce or its products acquired by a larger, more diversified company in the future.

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