



### COMPANY UPDATE / ESTIMATE CHANGE TARGET CHANGE

#### Key Metrics

FB - NASDAQ - as of	5/4/17	\$150.85
Price Target		\$170.00
52-Week Range	\$108.23 -	\$153.60
Diluted Shares Outstanding (mm)		2,944
Market Cap. (\$mm)		\$444,102
1-Mo. Average Daily Volume		18,823,780
Institutional Ownership		71.9%
Debt/Total Capital (net)	Q1'17	0%
ROE		20.8%
Book Value / Share		\$19.78
Price / Book Value		7.6x
Dividend Yield		0.0%
LTM EBITDA Margin		52.0%

#### GAAP EPS FY 12/31

	Prior	Current		Prior	Current
	2016A	2017E		2018E	2018E
1Q	\$0.60	\$1.04	A	\$0.98	\$1.09
2Q	\$0.71	\$1.01		\$1.18	\$1.28
3Q	\$0.81	\$1.07		\$1.24	\$1.31
4Q	\$1.21	\$1.40		\$1.56	\$1.61
Year	\$3.33	\$4.52		\$4.96	\$5.30
P/E	45.3x	33.4x			28.5x

\*Columns may not equal due to rounding

#### Revenue (\$mil)

	Prior	Current		Prior	Current
	2016A	2017E		2018E	2018E
1Q	\$5,382	\$8,032	A	\$9,549	\$ 9,745
2Q	\$6,436	\$8,818		\$10,906	\$10,978
3Q	\$7,011	\$9,337		\$11,519	\$11,572
4Q	\$8,809	\$11,142		\$13,591	\$13,612
Year	\$27,638	\$37,329		\$45,564	\$45,906

Facebook Inc – is the world's largest social network, with almost 2 billion monthly active users. Facebook connects users with friends and family and allows users to share information. A majority of Facebook revenue is derived from mobile advertising, of which Facebook has become the market leader. Other Facebook brands include Instagram, WhatsApp, Messenger and Oculus. Facebook launched in 2004, by Founder, CEO & Chairman, Mark Zuckerberg and is headquartered in Menlo Park, California.

### Facebook Inc.

FB - NASDAQ – Long-term Buy - 3

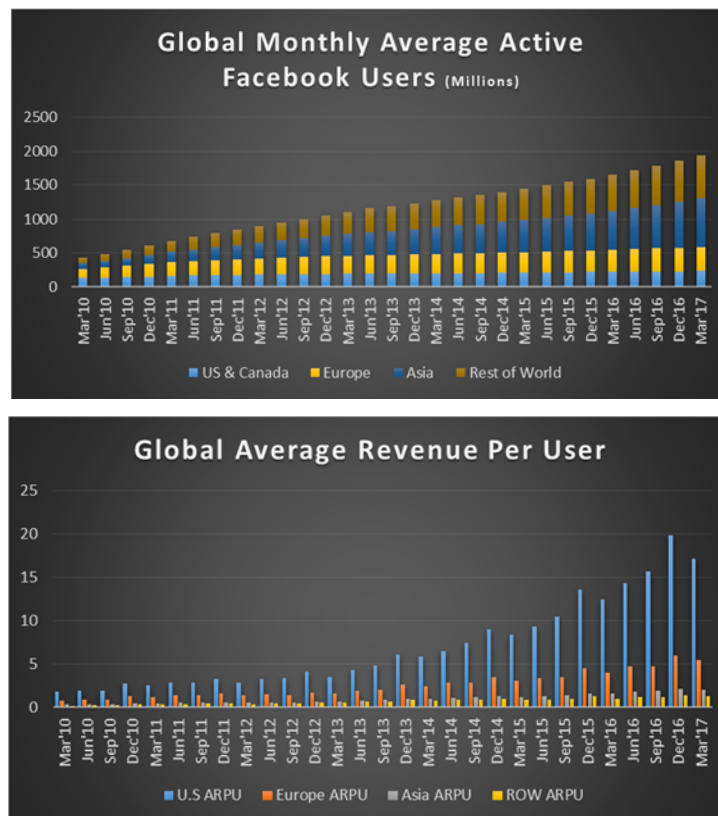
#### Facebook Reports Record Q1 Results; Increasing PT to \$170

- Key Metrics.** Facebook ended Q1 with a record 1.936 billion monthly active users vs. our estimate of 1.895 billion, up a better than expected 17% y/y. Daily active users totaled 1.284 billion vs. 1.090 billion last year. Engagement was flat at 66% DAUs/MAUs for the 5<sup>th</sup> consecutive quarter. The average revenue per user (ARPU) during the quarter was \$4.23 vs. our estimate of \$4.15, up 27% y/y. Mobile ad revenue represented 85% of ad revenue, up from 82% last year. The CPM (cost per thousand impressions) increased 14%, up from 3% last quarter, while ad impressions increased 32% y/y. Advertiser count totaled ~5 million, up ~67% y/y while our estimated average revenue spend per advertiser decreased 9%. We view the 9% decrease as positive as the total advertiser base tied for its fastest growth rate in Facebook's history as a public company and we assume more advertisers with smaller budgets were added.
- Results.** Management began reporting GAAP earnings that were significantly above consensus and close to non GAAP estimates which caused initial confusion. The company reported GAAP EPS of \$1.04, up 74% y/y on revenue of \$8.03 billion, up 49% y/y. Ad revenue of \$7.857 billion increased 51% y/y. Gross margin increased to a Q1 record 85.6%, while operating margin reached a Q1 record 41.4%, increasing 410 bps y/y due to the higher revenue base. Non GAAP EPS was \$1.23 vs. our estimate of \$1.09; we will no longer provide non GAAP figures as FB believes stock based compensation is a key and ongoing part of total compensation. Facebook's cash balance was a record \$32.3 billion, or \$11 per share; the company has no debt. Operating cash flow totaled a record \$5.05 billion, while free cash flow was \$3.78 billion, an increase of over 100% y/y. Facebook repurchased \$228 million of FB shares in Q1.
- Outlook.** Expense guidance was reiterated at 40%-50% growth for FY'17. We expect advertising revenue growth to decelerate throughout FY'17 from lower ad load despite strength from video, Instagram, Messenger, and WhatsApp. We increase our outlook on improving ad rates despite concerns of lower ad load growth and higher expenses in FY'17. Our Q2'17 EPS estimate increases to \$1.01 on revenue of \$8.8 billion. We raise our FY'17 outlook based on higher ARPU, increasing advertiser count, and continued growth in global users across products. We expect FY'17 & FY'18 EPS of \$4.52/\$5.30 on revenue of \$37.3/\$45.9 billion, respectively.
- Opinion.** We raise our FYE'18 price target to \$170 and maintain our Long-term Buy rating.

**Note Important Disclosures on Pages 7-8**  
**Note Analyst Certification on Page 7**

### ADDITIONAL DISCUSSION

From a geographic and total user basis, the Asia region monthly active user (MAU) base of 716 million was the largest and experienced the fastest user growth, up 27% y/y, an improvement from last quarter's 25% growth rate and last year's 20% growth rate. Asia ad revenue increased 60% y/y as ARPU increased 27%, up one percentage point on a sequential basis. Rest of World (ROW) segment MAUs of 632 million increased 19% y/y, in line with growth from last quarter and an improvement from 18% y/y in the year ago quarter. **ROW ARPU increased 40% y/y, significantly above the 11% growth rate during the year ago quarter.** ROW revenue increased a strong 66% y/y vs. 35% in the year ago quarter. **The U.S. & Canada region experienced the slowest growing user count at 5%, while average revenue per user increased 37% y/y to \$17.07, a significant slowdown vs. 46% growth last quarter and 49% in the year ago period.** Monetization continues to improve as Facebook's total average revenue per user was \$4.23 vs. \$3.32 last year, growth of 27% y/y. This was a result of the average price per ad increasing 14% y/y vs. 3% last quarter while ad impressions increased 32%, down from 49% as ad load growth begins to decelerate as expected.



Source: Company data

### OUTLOOK

We continue to believe Facebook has an industry leading advertising position due to the network effect of the social media company's 2 billion monthly active user base and other company-owned brands such as fast growing Instagram's 700 million MAUs, Messenger's 1.2 billion MAUs, WhatsApp's 1 billion MAUs, and the Oculus virtual reality platform. We expect continued monetization improvement in near-term results from an increasing advertiser count, which now exceeds 5 million advertisers, and only a slight decrease in ad spend per advertiser, which we view as healthy given the significant increase in the number of advertisers who may initially allocate a smaller budget to Facebook. Results are expected to benefit from enhanced video advertising, Instagram monetization, and continued global user growth. However, advertising revenue growth rates are expected to slow as ad load growth slows. Longer-term growth potential includes improved ad campaign management tools, Messenger, WhatsApp, Video, Facebook Live, Marketplace, artificial intelligence, and the Oculus virtual reality platform.

Management again noted FY'17 expense growth guidance of 40%-50%, which may be weighing on shares following the release of strong quarterly results. We also believe the light APRU growth in North America was a weak area. We continue to expect strong advertising revenue growth from Facebook Video, Instagram, and platform growth from Messenger and WhatsApp. We increase our outlook as we expect improved monetization despite concerns of lower ad load growth and higher expenses in FY'17. Our Q2'17 EPS estimate increases to \$1.01 on revenue of \$8.8 billion, an increase from our prior EPS view of \$0.92 on revenue of \$8.6 billion. We raise our FY'17 outlook based on higher ARPU, increasing advertiser count and spend, healthy user engagement, continued growth in global users across products and a lower tax rate. We project FY'17 EPS of \$4.52, representing y/y growth of 36%, an increase from our prior view of \$4.27. We forecast FY'18 EPS of \$5.30 on revenue of \$45.9 billion. This compares to our prior EPS view of \$4.96 on revenue of \$45.5 billion. We note a significant decrease in earnings growth as management continues to spend aggressively.

## VALUATION

In our opinion, shares of FB represent a long-term investment opportunity suitable for aggressive growth investors. The company is a generator of significant free cash flow and due to the global scale of the business it has been highly profitable with industry leading operating metrics. We continue to recommend shares of FB as we view Facebook and Alphabet as leading beneficiaries of the shift of advertising dollars away from traditional media and onto mobile and video ad platforms. We note shares may continue to be more volatile near term as investors accept Facebook's reiterated heavy expense guidance for FY'17.

**We maintain our Long-term Buy rating and increase our FYE'18 price target to \$170 from \$165 per share.** Facebook posted another quarter of consistently strong operating results including strong revenue growth, free cash flow generation, global user, and ARPU growth. We continue to hold Facebook's management team in high regard and believe they can execute on Facebook's well communicated long-term strategy.

We derive our FY'18 price target of \$170 by multiplying our increased FY'18 GAAP EPS estimate of \$5.30 by our forward P/E multiple of 32x, which is above our prior 28x multiple. **Our forward P/E multiple increases due to Facebook management's decision to begin reporting higher quality GAAP results vs. non GAAP results reported previously. These GAAP metrics are growing faster than the prior non GAAP metrics we previously incorporated into our valuation of FB shares.** We were previously lowering the multiple used in our share price calculation as revenue growth begins to slow over our investment timeframe while expenses are set to rise. We believe a 32x multiple appropriately reflects the company's current reporting structure and future growth prospects. Our price target of \$170 offers a potential total return of 13% based on yesterday's closing price through our FYE'18 investment timeframe. Our price target does not include Facebook's \$32.3 billion cash position which can be used for share repurchases, future acquisitions, and growth initiatives should opportunities arise.

## SUITABILITY

We assign shares of FB a suitability rating of 3 on our scale of 1-4 (1 = most conservative, 4 = most aggressive). A 3 rating is given based on Facebook's limited history as a public company while also incorporating the company's industry leading market position and management team; expanding product set; global reach; solid balance sheet; and significant free cash flow generation. We believe a suitability rating of 3 incorporates these attributes. Shares of FB are suitable for aggressive growth oriented investors seeking long-term capital appreciation, in our view.

## RISKS & CONSIDERATIONS

Risks to our valuation include but are not limited to:

- Ad load growth is expected to materially slow as the mobile news feed product reaches saturation.
- The ability to grow and/or retain the Facebook user base and their current level of engagement.
- Loss of advertising dollars, as advertising revenue generates a majority of Facebook revenue. We highlight ad blockers as one such potential threat to PC and ad mobile revenue.

- The inability by Facebook to further monetize mobile products, as users shift usage patterns.
- The threat of a new social network, website or app that could draw internet users away such as Snap Inc.
- The lack of adoption of the Facebook platform, and/or the lack of innovation and new products from platform partners.
- The threat of a Facebook infrastructure failure, causing site downtime, or ad server downtime, which could materially affect revenue.
- The unlawful distribution of user information, or the hacking of user information by an outside party and other privacy concerns that may drive users away from the site or create an unwillingness of users to share additional information.
- Regulations and restrictions imposed on Facebook by U.S. or foreign governments (China).
- The loss of key Facebook executives including COO Sheryl Sandberg, and CEO Mark Zuckerberg, who have a majority voting interest in the stock.
- Higher expenses due to legal fees resulting from patent lawsuits.

*Additional information is available upon request.*

Other stocks mentioned: Alphabet (GOOGL-\$954.72 – Neutral), and Snap Inc. (SNAP-\$22.59).

## Facebook Inc. Consolidated Statement of Income (in millions except per share data)

	2011	2012	2013	2014	2015	2016	Q1'17	Q2'17E	Q3'17E	Q4'17E	2017E	2018E
Advertising revenue	\$ 3,154	\$ 4,279	\$ 6,986	\$ 11,492	\$ 17,080	\$ 26,885	\$ 7,857	\$ 8,648	\$ 9,172	\$ 10,967	\$ 36,644	\$ 45,276
Payments and other fees revenue	557	810	886	974	847	753	175	170	165	175	685	630
<b>Total Revenue</b>	<b>\$ 3,711</b>	<b>\$ 5,089</b>	<b>\$ 7,872</b>	<b>\$ 12,466</b>	<b>\$ 17,927</b>	<b>\$ 27,638</b>	<b>\$ 8,032</b>	<b>\$ 8,818</b>	<b>\$ 9,337</b>	<b>\$ 11,142</b>	<b>\$ 37,329</b>	<b>\$ 45,906</b>
Cost of revenue	860	1,364	1,875	2,153	2,866	3,788	1,159	1,226	1,288	1,371	5,044	6,065
Research and development	388	1,399	1,415	2,666	4,817	5,908	1,834	2,160	2,241	2,451	8,687	10,617
Marketing and sales	427	896	997	1,680	2,724	3,768	1,057	1,235	1,387	1,582	5,260	6,714
General and administrative	280	892	781	973	1,295	1,730	655	750	766	836	3,006	3,609
<b>Total Costs and Expenses</b>	<b>\$ 1,955</b>	<b>\$ 4,551</b>	<b>\$ 5,068</b>	<b>\$ 7,472</b>	<b>\$ 11,702</b>	<b>\$ 15,194</b>	<b>\$ 4,705</b>	<b>\$ 5,370</b>	<b>\$ 5,681</b>	<b>\$ 6,240</b>	<b>\$ 21,996</b>	<b>\$ 27,006</b>
<b>Income from Operations</b>	<b>\$ 1,756</b>	<b>\$ 538</b>	<b>\$ 2,804</b>	<b>\$ 4,994</b>	<b>\$ 6,225</b>	<b>\$ 12,444</b>	<b>\$ 3,327</b>	<b>\$ 3,448</b>	<b>\$ 3,655</b>	<b>\$ 4,903</b>	<b>\$ 15,333</b>	<b>\$ 18,901</b>
Interest and Other Income	(61)	(44)	(50)	(84)	-31	90	81	80	85	90	336	360
<b>Income Before Provision for Income Taxes</b>	<b>\$ 1,695</b>	<b>\$ 494</b>	<b>\$ 2,754</b>	<b>\$ 4,910</b>	<b>\$ 6,194</b>	<b>\$ 12,534</b>	<b>\$ 3,408</b>	<b>\$ 3,528</b>	<b>\$ 3,740</b>	<b>\$ 4,993</b>	<b>\$ 15,669</b>	<b>\$ 19,261</b>
Provision for income taxes	695	441	1254	1,970	2,505	2,794	344	547	598	824	2,313	3,587
<b>Net Income</b>	<b>\$ 1,000</b>	<b>\$ 53</b>	<b>\$ 1,500</b>	<b>\$ 2,940</b>	<b>\$ 3,689</b>	<b>\$ 9,740</b>	<b>\$ 3,064</b>	<b>\$ 2,981</b>	<b>\$ 3,142</b>	<b>\$ 4,169</b>	<b>\$ 13,356</b>	<b>\$ 15,674</b>
Net Income Attributable to Participating Securities	332	21	9	15	19	26	5	6	6	7	24	27
<b>Net Income After Participating Securities</b>	<b>\$ 668</b>	<b>\$ 32</b>	<b>\$ 1,491</b>	<b>\$ 2,925</b>	<b>\$ 3,670</b>	<b>\$ 9,714</b>	<b>\$ 3,059</b>	<b>\$ 2,975</b>	<b>\$ 3,136</b>	<b>\$ 4,162</b>	<b>\$ 13,332</b>	<b>\$ 15,647</b>
Basic Shares Outstanding	1,294.00	2,006.00	2,420	2,614	2,803	2,863	2,891	2,913	2,928	2,939	2,918	2,976
Diluted Shares Outstanding	1,508.00	2,166.00	2,517	2,664	2,857	2,916	2,944	2,933	2,944	2,967	2,947	2,955
Basic EPS	\$ 0.52	\$ 0.02	\$ 0.62	\$ 1.12	\$ 1.31	\$ 3.39	\$ 1.06	\$ 1.02	\$ 1.07	\$ 1.42	\$ 4.57	\$ 5.26
<b>Diluted EPS</b>	<b>\$ 0.46</b>	<b>\$ 0.01</b>	<b>\$ 0.59</b>	<b>\$ 1.10</b>	<b>\$ 1.28</b>	<b>\$ 3.33</b>	<b>\$ 1.04</b>	<b>\$ 1.01</b>	<b>\$ 1.07</b>	<b>\$ 1.40</b>	<b>\$ 4.52</b>	<b>\$ 5.30</b>
<b>Y/Y Percentage Change</b>												
Revenue	88%	37%	55%	58%	44%	54%	49%	37%	33%	26%	35%	23%
Cost of Revenue	74%	59%	37%	15%	33%	32%	38%	34%	31%	31%	33%	20%
Total operating expenses	132%	153%	-1%	49%	51%	37%	44%	51%	58%	48%	50%	25%
Total costs and expenses	108%	133%	11%	47%	57%	30%	40%	46%	46%	47%	45%	23%
Operating income	70%	-69%	421%	78%	25%	100%	66%	26%	17%	7%	23%	23%
Net income	65%	-95%	2730%	96%	25%	164%	76%	45%	32%	17%	37%	17%
Diluted EPS	64%	-97%	3910%	85%	17%	159%	74%	44%	31%	16%	36%	17%
Diluted share count	14%	44%	16%	6%	7%	2%	1%	1%	1%	1%	1%	0%
<b>Percentage of Revenue</b>												
Advertising revenue	85.0%	84.1%	88.7%	92.2%	95.3%	97.3%	97.8%	98.1%	98.2%	98.4%	98.2%	98.6%
Payments revenue	15.0%	15.9%	11.3%	7.8%	4.7%	2.7%	2.2%	1.9%	1.8%	1.6%	1.8%	1.4%
Cost of Revenue	23.2%	26.8%	23.8%	17.3%	16.0%	13.7%	14.4%	13.9%	13.8%	12.3%	13.5%	13.2%
Gross Margin	76.8%	73.2%	76.2%	82.7%	84.0%	86.3%	85.6%	86.1%	86.2%	87.7%	86.5%	86.8%
Total costs and expenses	52.7%	89.4%	64.4%	59.9%	65.3%	55.0%	58.6%	60.9%	60.9%	56.0%	58.9%	58.8%
Operating income	47.3%	10.6%	35.6%	40.1%	34.7%	45.0%	41.4%	39.1%	39.2%	44.0%	41.1%	41.2%
Net income attributable to Class A and Class B common stockholders	18.0%	0.6%	18.9%	23.5%	20.5%	35.1%	38.1%	33.7%	33.6%	37.4%	35.7%	34.1%

Source: Company data &amp; Hilliard Lyons estimates.

## Facebook Inc. Consolidated Balance Sheets (in millions except per share data)

	2012	2013	2014	2015	Q1'16	Q2'16	Q3'16	Q4'16	2016	Q1'17
<b>Assets</b>										
Cash and cash equivalents	\$ 2,384	\$ 3,323	\$ 4,315	\$ 4,907	\$ 6,456	\$ 5,108	\$ 6,038	\$ 8,903	\$ 8,903	\$ 7,104
Marketable securities	7,242	8,126	6,884	13,527	14,165	18,185	20,102	20,546	20,546	25,202
Accounts receivable, net	719	1,109	1,678	2,559	2,348	2,801	3,070	3,993	3,993	3,415
Income tax refundable	451	-	-	-	-	-	-	-	-	-
Prepaid expenses and other	471	512	793	659	843	916	1,118	959	959	1,209
<b>Total current assets</b>	<b>11,267</b>	<b>13,070</b>	<b>13,670</b>	<b>21,652</b>	<b>23,812</b>	<b>27,010</b>	<b>30,328</b>	<b>34,401</b>	<b>34,401</b>	<b>36,930</b>
Property and equipment, net	2,391	2,882	3,967	5,687	6,467	7,104	7,899	8,591	8,591	9,462
Goodwill and intangible assets, net	1,388	1,722	21,910	21,272	21,096	20,922	20,787	20,657	20,657	20,486
Other assets	57	221	637	796	700	703	660	1,312	1,312	1,836
<b>Total assets</b>	<b>15,103</b>	<b>17,895</b>	<b>40,184</b>	<b>49,407</b>	<b>52,075</b>	<b>55,739</b>	<b>59,674</b>	<b>64,961</b>	<b>64,961</b>	<b>68,714</b>
<b>Liabilities and stockholders' equity</b>										
Accounts payable	65	87	176	196	149	130	260	302	302	170
Developer partners payable	169	181	202	217	216	232	239	280	280	278
Accrued expenses and other current liabilities	423	555	866	1,449	1,389	1,770	2,018	2,203	2,203	2,400
Deferred revenue and deposits	30	38	66	56	55	79	78	90	90	80
Current portion of capital lease obligations	365	239	114	7	-	-	-	-	-	-
<b>Total current liabilities</b>	<b>1,052</b>	<b>1,100</b>	<b>1,424</b>	<b>1,925</b>	<b>1,809</b>	<b>2,211</b>	<b>2,595</b>	<b>2,875</b>	<b>2,875</b>	<b>2,928</b>
Capital lease obligations, less current portion	491	237	119	107	-	-	-	-	-	-
Long-term debt	1,500	-	-	-	-	-	-	-	-	-
Other liabilities	305	1,088	2,545	3,157	3,116	3,145	2,964	2,892	2,892	3,598
<b>Total liabilities</b>	<b>3,348</b>	<b>2,425</b>	<b>4,088</b>	<b>5,189</b>	<b>4,925</b>	<b>5,356</b>	<b>5,559</b>	<b>5,767</b>	<b>5,767</b>	<b>6,526</b>
<b>Stockholders' equity:</b>										
Common stock and additional paid in capital	10,094	12,297	30,225	34,886	36,129	37,405	38,756	38,227	38,227	38,639
Accumulated other comprehensive loss	2	14	(228)	(455)	(276)	(374)	(372)	(703)	(703)	(626)
Retained earnings	1,659	3,159	6,099	9,787	11,297	13,352	15,731	21,670	21,670	24,175
Total stockholders' equity	11,755	15,470	36,096	44,218	47,150	50,383	54,115	59,194	59,194	62,188
<b>Total liabilities and stockholders' equity</b>	<b>15,103</b>	<b>17,895</b>	<b>40,184</b>	<b>49,407</b>	<b>52,075</b>	<b>55,739</b>	<b>59,674</b>	<b>64,961</b>	<b>64,961</b>	<b>68,714</b>

Source: Company data

### Analyst Certification

I, Stephen Turner, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

### Important Disclosures

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

### Suitability Ratings

- 1 - A large cap, core holding with a solid history
- 2 - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks
- 3 - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage
- 4 - Speculative, due to small size, inconsistent profitability, erratic revenues, volatility, low trading volume or a narrow customer or product base

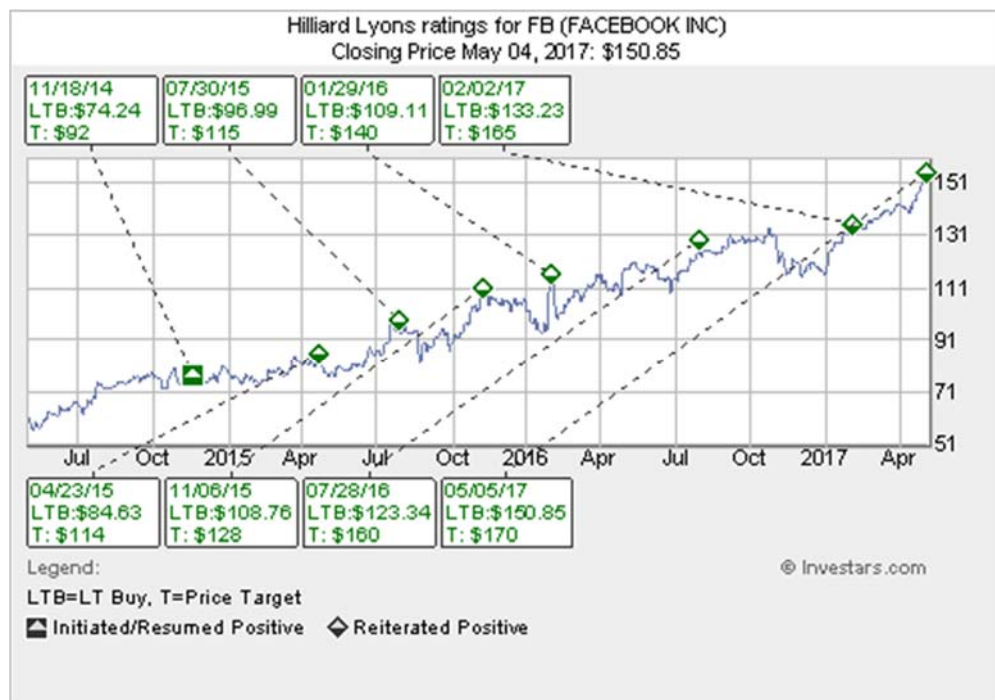
### Investment Ratings

**Buy** - We believe the stock has significant total return potential in the coming 12 months.

**Long-term Buy** - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

**Neutral** - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

**Underperform** - We believe the stock is vulnerable to a price setback in the next 12 months.



Note: Price targets accompanying Buy ratings reflect a one year time period while price targets accompanying Long-term Buy ratings generally reflect a two to three year time period.

	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
<b>Rating</b>				
<b>Buy</b>	36	30%	14%	86%
<b>Hold/Neutral</b>	71	58%	6%	94%
<b>Sell</b>	15	12%	7%	93%

As of 5 April 2017

### Other Disclosures

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