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**CyberDefender Corp. (CYDE – 3.37)**

**Q3 Results. LiveTech Driving Growth.**

November 17, 2010

James D. Ragan, CFA

YE 12/31	Gross Rev (mm)	GAAP Rev (mm)	EPS	P/E	Shares Out.(mm): 27.0	Price Target: \$8.00
2011E	97.88	73.38	\$0.06	55x	Ent Value (\$mm):\$90	Rating: BUY
2010E	63.32	46.43	(\$0.51)			Dividend: none
2009	28.97	25.97	(\$0.64)			

52-wk Px Range: \$3.00-\$4.90

\* Crowell, Weedon estimates..

9/30/10 Bal. Sheet: Cash/Investments: \$5.3mm (\$2.8mm unrestricted), Total Assets: \$19.4mm, Total Debt: \$4.5mm

Recommendation: BUY rated, Price Target \$8. Portfolio Suitability: Aggressive Growth.

CyberDefender's (CYDE) third quarter (Q3) was highlighted by strong year/year and sequential growth. Q3 gross sales of \$18.6mm increased 90% from \$9.8mm last year (and 49% from \$12.4mm in Q2) and GAAP revenue increased 187% to \$12.7mm year/year (and 31% sequentially). Growth was driven by ongoing consumer adoption of CYDE's Live Technical Support service (LiveTech), which comprised 63% of gross revenue. The Company's accelerated Q3 growth was attributed to completing the transition to domestic, in-house sales and tech support, and effective consumer marketing programs produced with strategic partner Guthy-Renker Corp. Demand for an integrated home computer security solution incorporating security software with access to live technical support remains high, and should continue to grow as consumers are educated about alternatives to taking their home computers to physical repair locations.

Based upon the strength of the services business, which has driven higher than expected gross sales, and also a higher component of deferred revenue and refunds, we have made adjustments to our model. Slightly higher expense levels could push profitability to Q2 or Q3 of next year, but we estimate that CYDE will be cash flow positive throughout 2011. We reiterate our Buy rating and \$8.00 target.

**Services Business Driving Growth.** Gross revenue from CYDE's LiveTech increased to \$11.7mm in Q3, an increase of 67% from \$7.0mm in Q2, and up 300% year/year. Driving the growth has been better-trained in-house call-center reps, and an increase in revenue per order (\$150 in Q3'10 vs. \$80 last year).

**Deferred Revenue was \$14.2mm.** CYDE sells its software and LiveTech under 1-3 year licenses that are paid for either up front, or under a 3-payment option. A portion of the revenue is recognized immediately and the balance deferred over the life of the license. As of 9/30/10 deferred revenue was \$14.2mm, up 17% sequentially and 46% year/year. Deferred revenue will be recognized into GAAP revenue in future periods.

**Guidance Reflects Strong Growth.** Management expects continued growth in Q4 led by LiveTech penetration. Gross sales are estimated in a range of \$20.0mm-\$21.5mm (up 104%-119% year/year) and the Company's GAAP revenue range is \$13.5mm-\$15.0mm (up 80%-100% year/year). We estimate gross sales and GAAP revenue of \$20.5mm and \$14.5m, respectively.

This material does not constitute an offer to sell or the solicitation of an offer to buy any security. This information has been obtained from sources of which Crowell, Weedon & Co. believes to be reliable, but is not guaranteed by us as to accuracy or authenticity. It does not purport to include all the information available on the companies mentioned. The reader is referred to the regular statistical services, company reports, and any official prospectuses for further details.

**Valuation.** Our 12-month valuation range for CYDE is \$6.39 - \$9.29 per share, leading to a midpoint price target of \$8.00. As a high growth software and service provider with strong gross margins, CYDE has focused on optimizing its revenue model and building its infrastructure to support more growth. Therefore, we believe it is appropriate to value the company based upon Enterprise Value multiples of current and estimated revenue. We have looked at other high growth software and service providers to compare relative revenue multiples.

We believe that using Gross Receipts less refunds (adjusted gross receipts) is the best gauge of company revenue or sales. Our model uses our 2010, and forward four quarter, estimates for adjusted gross receipts. For comparison we have performed the same analysis on GAAP revenue. The valuation matrix is listed in the table below. Our 2010 and forward four quarter adjusted gross revenue estimates are \$51.9mm and \$75.4mm, respectively. And our respective 2010 and forward four quarters GAAP revenue estimates are \$46.4mm and \$67.2mm. We used 40.6mm shares outstanding for valuation purchases, assuming conversion of outstanding warrants that will raise cash theoretically available for share repurchase (modified treasury stock method). In addition, we assume that debt and cash will be equal making Enterprise Value equal to Equity Value. In prior models we have used gross receipts without the refund adjustment, which is a higher sales number. However, due to the growth in the LiveTech segment (higher sales value with a higher deferred component) refunds have trended higher. We believe backing out the refunds gives an accurate picture of “net” sales.

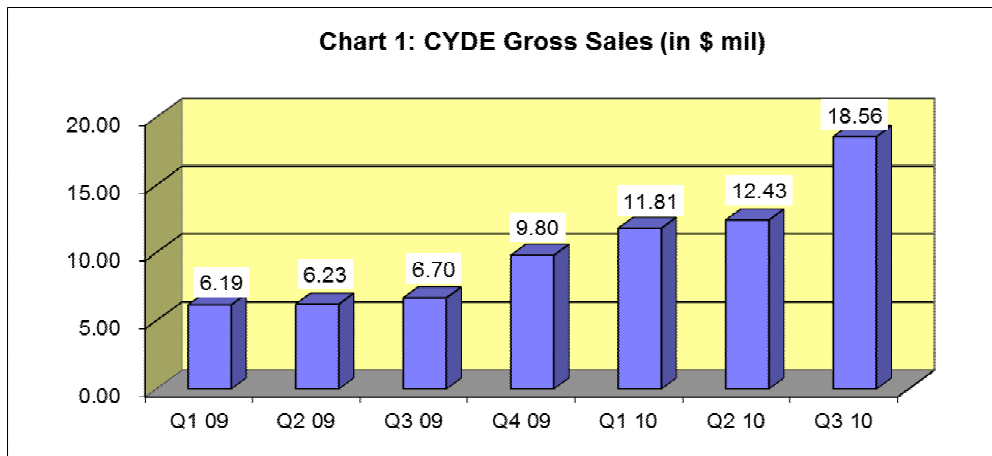
**CYDE Revenue Multiples Valuation Matrix**

shares used for valuation (mm) 40,570

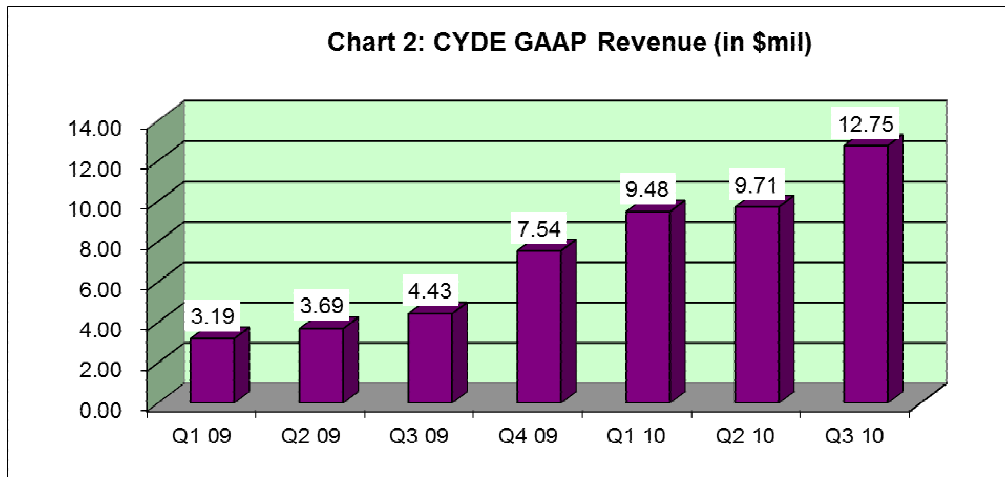
	2010		Fwd 4 Qtrs	
Est. Gross Receipts (less refunds)	51,860		75,375	
Multiple	5.0	6.0	4.0	5.0
Equity Valuation (mm)	259,300	311,160	301,500	376,875
Share Price Valuation	\$6.39	\$7.67	\$7.43	\$9.29
Est. GAAP Revenue	46,425		67,220	
Multiple	5.0	6.0	4.0	5.0
Equity Valuation (mm)	232,125	278,550	268,880	336,100
Share Price Valuation	\$5.72	\$6.87	\$6.63	\$8.28

source: Crowell Weedon estimates

**Quarterly Results.** CYDE reported Q3 GAAP revenue growth of \$12.7mm, up 188% from \$4.4mm and 31% above the Q2 2010 GAAP revenue of \$9.7mm. Gross sales, which add deferred revenue and refunds to GAAP revenue, increased 175% year/year to \$18.6mm, and were 89% above \$12.4mm of gross sales in Q2. Charts 1 & 2 below show the quarterly progression of gross sales and GAAP revenue over the past seven quarters.



Source: company filings



Source: company filings

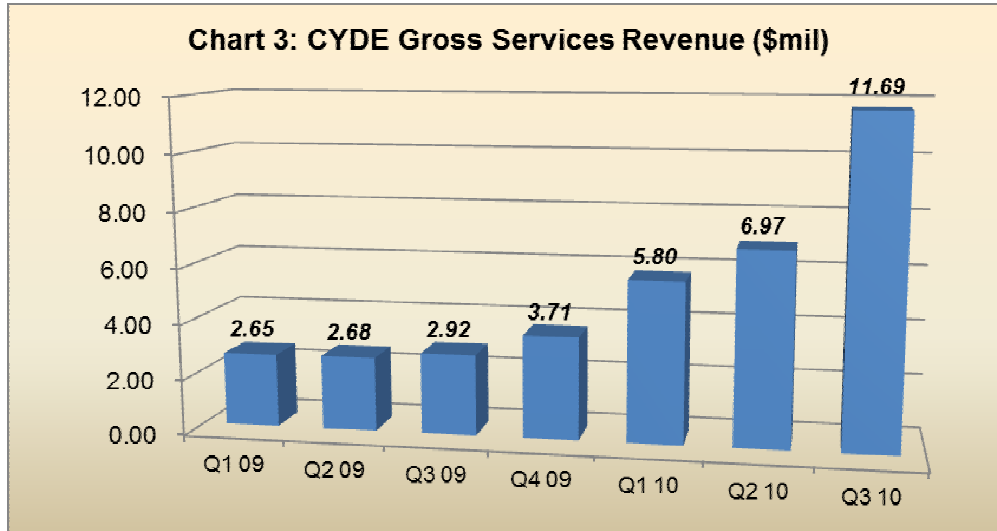
CYDE's accelerated Q3 growth (both year/year and sequentially) growth was attributed to completing the transition to domestic, in-house sales and tech support, effective consumer marketing programs produced with strategic partner Guthy-Renker Corp., and strong consumer adoption of LiveTech (CYDE's technical support service offering). In early 2010 CyberDefender initiated expansion efforts to establish necessary infrastructure to support anticipated growth. This included several key management additions as well as changes to the call center operations. Cyber has successfully increased its roster of in-house representatives who are better-trained and equipped with state of the art telecommunications, sales and customer service software. Q3 saw the benefits of those efforts as both software and services posted sequential increases in gross sales.

Q2 gross margin of 54.2% compared to 58.7% in Q2, and declined due to the increased mix of services revenue, which has a lower gross margin than software. GAAP advertising expense was \$4.3mm (34% of GAAP revenue) in Q3 compared to \$3.4mm (35.1% of GAAP revenue) in Q2. Actual media expenditures (ads back capitalized costs) were \$5.8mm vs. \$5.0mm in Q2. The Q3 ratio of gross sales to media outlays was 3.2x in Q3 compared to 2.5x in the prior quarter.

SG&A expenses in Q3 increased to \$4.7mm from \$3.7mm in Q2, but as a percentage of net revenue declined to 37.1% from 38.3%. The increase was tied to the growth in the in-house call center, which has supported higher sales, and also higher variable expenses such as interchange fees. Q3 operating loss was \$2.9mm, compared to -\$2.7mm in Q3 2009 and -\$2.4mm in Q2 2010. However, the increase in deferred revenue was a positive to cash flow, leading to an improvement in adjusted EBITDA (EBITDA plus changes in deferred revenue, deferred charges and stock compensation). We estimate CYDE's Q3 adjusted EBITDA was negative \$2.4mm, compared to -\$3.0mm in Q2. We estimate adjusted EBITDA will remain slightly negative in Q4, and turn positive in Q1 of 2011.

CYDE's Q3 EPS loss was \$0.18, compared to -\$0.15 last year and -\$0.19 in the previous quarter. The loss was above our -\$0.07 estimate primarily due to higher than expected deferred revenue, lower gross margin due to the mix of higher services, and higher spending levels to support the call center transition. Each of these developments, in our view, is a positive, and we believe that CYDE has exceeded expectations over the past several quarters.

**LiveTech has exceeded expectations.** CYDE's services segment, LiveTech, has increased gross sales substantially in 2010. Chart 3 below shows quarterly gross sales for services over the past seven quarters. Q3 services gross sales were \$11.7mm, representing a 67% sequential increase from Q2 (\$7.0mm) and triple the level one year ago (\$2.9mm in Q3 2009). We believe that CYDE's integrated security solution that combines security software with live technical support availability is unique, and sets the company apart from the competition. The Company has emphasized its LiveTech segment in 2010, and the sales results have exceeded expectations.



Source: company reports, and Crowell, Weedon adjustments

Several factors contributed to LiveTech's impressive growth. First was effective television and radio ads prompting potential customers to contact CyberDefender through the web URLs MaxMySpeed.com, DoubleMySpeed.com, and MyCleanpc.com. Second was the addition of well-trained domestic call-center employees who have improved the conversion rates upselling CYDE's higher dollar value technical support products. Third, was an expansion of multi-year licenses that offer consumer PC support for one, two, or three years. Multi-year licenses offer consumers a per-year discount, but generate higher sales dollars up front for CYDE.

**Multi-year Licenses.** CYDE offers consumers live technical support services 24/7 provided on-line by CYDE technicians located in Los Angeles, New York, or Utah. One-year protection sells for \$240 for one PC, or \$300 for up to five PCs. A two year license sells for \$379 and \$420, and three years of protection is priced at \$500 (one pc) and \$600 (up to 5 PCs). (Prices do change as the company optimizes its service offering.) CYDE is paid up-front for the licenses, although the Company offers a "3 easy payment" option for multi-year licenses, spread equally over three months.

**Refunds and Chargebacks.** CYDE's GAAP revenue reflects gross sales less deferred sales and refunds. As a direct consumer marketer, CYDE has a 30-day refund policy and expects a certain percentage of gross sales to be refunded. The product might not meet the consumer's expectations, the consumer might have second thoughts about the cost, or sometimes the credit card payment is rejected. The Company believes that 10%-20% refunds/chargebacks are typical for direct response consumer products. In Q3 the rate was 20%, at the high end of that range and compared to 18% in Q2. We attribute the higher rate to an increase in dollar per sale and multi-year licenses. In Q3 revenue per order increased to \$150, from \$80 one year ago, and multi-year licenses comprised 60% of gross services sales. We use gross sales less refunds for valuation purposes, as we believe that represents the best measure of net revenue.

**Estimates.** For Q4 we estimate gross sales of \$20.5mm, representing 109% year/year growth and 10% sequentially. Our GAAP revenue estimate is \$14.5mm, compared to \$12.7mm in Q3 and \$7.5mm in Q4 2009. That would take 2010 full year gross sales and GAAP revenue to \$63.3mm and \$46.4mm, respectively. In 2011 we estimate a 55% increase in gross sales to \$97.9mm, and GAAP revenue of \$73.4mm, up 58%.

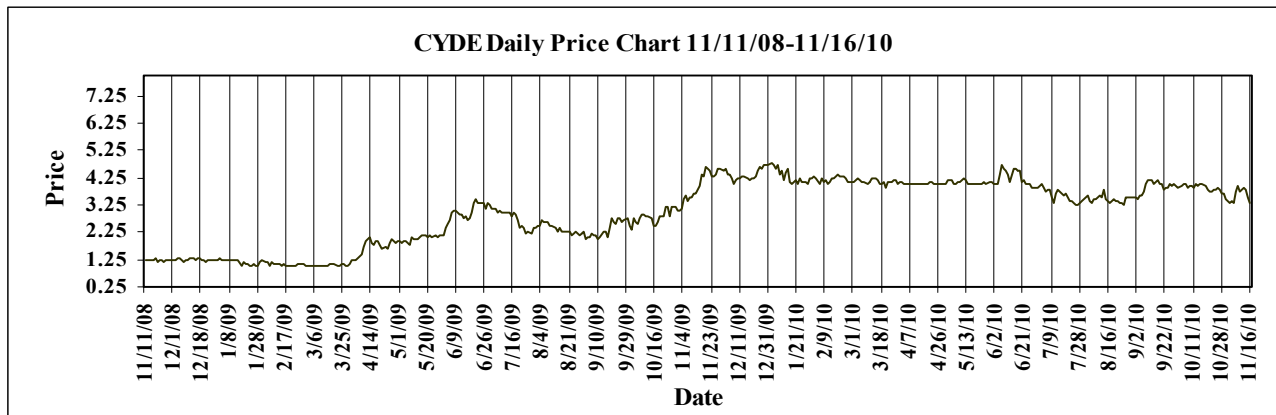
**(Additional Information is Available Upon Request)**

	Q109	Q209	Q309	Q409	Year 09A	Q1'10A	Q2'10A	Q3'10A	Q4'10E	Year 10E	Q1'11E	Q2'11E	Q3'11E	Q4'11E	Year 11E
	Mar	Jun	Sep	Dec		Mar	Jun	Sep	Dec		Mar	Jun	Sep	Dec	
<b>Revenue Detail</b>															
Gross Sales	6,191	6,231	6,742	9,808	28,972	11,813	12,429	18,560	20,515	63,317	22,056	23,477	25,320	27,024	97,877
Refunds/Chargebacks	(865)	(1,119)				(1,495)	(2,255)	(3,732)	(3,975)	(11,457)	(3,813)	(4,061)	(4,145)	(4,171)	(16,190)
Change in Deferred Rev (incr)	(2,134)	(1,428)				(841)	(462)	(2,082)	(2,051)	(5,436)	(2,037)	(1,939)	(2,128)	(2,200)	(8,304)
GAAP Revenue	3,192	3,686	4,427	7,536	18,841	9,477	9,713	12,746	14,489	46,425	16,207	17,477	19,047	20,653	73,384
<b>Income Statement</b>															
Net Sales (GAAP Rev)	3,191.6	3,686.6	4,427.4	7,536.2	18,841.9	9,477.3	9,712.6	12,746.0	14,489.0	46,424.9	16,206.6	17,476.9	19,047.3	20,652.8	73,383.6
Cost of Sales	679.7	753.3	1,018.4	1,731.1	4,182.5	3,155.1	4,013.8	5,834.0	5,027.5	18,030.3	4,748.0	5,138.9	5,636.7	6,070.2	21,593.8
Gross Profit	2,511.9	2,933.3	3,409.0	5,805.2	14,659.4	6,322.3	5,698.8	6,912.0	9,461.5	28,394.6	11,458.7	12,337.9	13,410.6	14,582.6	51,789.8
Advertising	3,743.7	3,408.3	3,545.1	2,384.4	13,081.5	3,067.9	3,407.2	4,328.0	5,501.3	16,304.4	6,029.3	6,628.2	7,118.4	7,556.8	27,332.7
Product Development	299.7	365.5	464.8	721.9	1,851.9	752.1	963.4	742.0	811.4	3,268.9	810.3	821.4	819.0	826.1	3,276.9
SG&A Expense	1,251.6	1,566.0	1,612.3	2,136.8	6,566.7	2,877.2	3,722.4	4,730.0	4,491.6	15,821.2	4,456.8	4,544.0	4,533.3	4,543.6	18,077.7
Investor Relations/consult	1,220.0	1,346.2	490.3	147.3	3,203.8	165.1	0.0	0.0	0.0	165.1	0.0	0.0	0.0	0.0	0.0
Dep/Amort	10.3	9.8	9.0	8.0	37.1	20.2	54.9	52.0	53.6	180.7	53.5	52.4	53.3	55.8	215.0
Other Op Expense															
Total Operating Exp.	6,525.3	6,695.8	6,121.5	5,398.4	24,741.0	6,882.5	8,147.9	9,852.0	10,857.8	35,740.3	11,349.9	12,046.0	12,524.0	12,982.3	48,902.2
Operating Income	(4,013.4)	(3,762.5)	(2,712.5)	406.7	(10,081.6)	(560.2)	(2,449.1)	(2,940.0)	(1,396.3)	(7,345.7)	108.8	291.9	886.6	1,600.2	2,887.5
Derivative Sec Valuation	109.1														
Loss on Registr. Rights															
Interest Expense	(912.5)	(1,052.9)	(843.2)	(921.3)	(3,729.9)	(1,320.5)	(2,446.6)	(2,036.0)	(394.3)	(6,197.4)	(119.3)	(119.3)	(119.3)	(119.3)	(477.0)
Interest Income	0.0	0.1													
Pretax Income	(4,816.9)	(4,815.4)	(3,555.6)	(514.6)	(13,811.5)	(1,880.7)	(4,895.7)	(4,976.0)	(1,790.6)	(13,543.1)	(10.5)	172.7	767.3	1,481.0	2,410.5
Income Taxes (credit)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Net Income	(4,817.1)	(4,815.6)	(3,555.8)	(514.8)	(13,811.7)	(1,880.9)	(4,895.9)	(4,976.0)	(1,790.8)	(13,543.3)	(10.7)	172.5	767.1	1,480.8	2,410.3
Diluted EPS	(\$0.27)	(\$0.24)	(\$0.15)	(\$0.02)	(\$0.64)	(\$0.07)	(\$0.19)	(\$0.18)	(\$0.07)	(\$0.51)	(\$0.00)	\$0.00	\$0.02	\$0.04	\$0.06
WA Shares	17,991	20,392	23,620	24,459	21,616	25,758	26,427	27,027	27,527	26,685	37,777	38,927	39,427	40,360	39,123
<b>Components of GAAP Revenue</b>															
Rev from Prod Sales	1,700	2,000			3,700	4,400	3,600	6,061	6,568	20,629	6,772	7,264	7,849	8,663	30,548
Rev from Services	900	1,100			2,000	4,000	4,900	6,567	7,281	22,748	8,560	9,297	10,261	11,032	39,151
Rev from Other Sources	592	300			892	1,077	1,000	600	640	3,317	874	916	937	958	3,685
<b>Components of Gross Receipts</b>															
Software Revenue	6,191	6,231	6,742	9,808	28,972	11,813	12,429	18,560	20,515	63,317	22,056	23,477	25,320	27,024	97,877
Services Revenue	2,475	2,501	2,666	4,402		4,092	3,504	4,110	4,923	16,629	5,530	5,917	6,213	6,523	24,182
Ancillary Revenue	2,646	2,679	2,916	3,706		5,802	6,967	11,692	12,295	36,756	13,810	14,777	16,090	16,895	61,572
Renewals Revenue	606	584	461	983		856	569	552	640		874	916	937	958	
	464	467	699	718		1,063	1,389	2,200	2,657		1,842	1,867	2,081	2,648	
<b>Expense and Revenue %</b>															
Gross Profit % of GAAP Rev	78.7%	79.6%	77.0%	77.0%	77.8%	66.7%	58.7%	54.2%	65.3%	61.2%	70.7%	70.6%	70.4%	70.6%	70.6%
Advertising as % Rev	117.3%	92.5%	80.1%	31.6%	69.4%	32.4%	35.1%	34.0%	38.0%	35.1%	37.2%	37.9%	37.4%	36.6%	37.2%
Product Development % Rev	9.4%	9.9%	10.5%	9.6%	9.8%	7.9%	9.9%	5.8%	5.6%	7.0%	5.0%	4.7%	4.3%	4.0%	4.5%
SG&A Expense % Rev	39.2%	42.5%	36.4%	28.4%	34.9%	30.4%	38.3%	37.1%	31.0%	34.1%	27.5%	26.0%	23.8%	22.0%	24.6%
Investor Relations % Rev	38.2%	36.5%	11.1%	2.0%	17.0%	1.7%	0.0%	0.0%	0.0%	0.4%	0.0%	0.0%	0.0%	0.0%	0.0%
Dep/Amort as % Rev	0.3%	0.3%	0.2%	0.1%	0.2%	0.2%	0.6%	0.4%	0.4%	0.4%	0.3%	0.3%	0.3%	0.3%	0.3%
Other Op Expense															
Total Oper Exp. As % Rev	204.5%	181.6%	138.3%	71.6%	131.3%	72.6%	83.9%	77.3%	74.9%	77.0%	70.0%	68.9%	65.8%	62.9%	66.6%
Operating Margin	-125.7%	-102.1%	-61.3%	5.4%	-53.5%	-5.9%	-25.2%	-31.1%	-9.6%	-15.8%	0.7%	1.7%	4.7%	7.7%	3.9%
Interest Exp. As % of Rev	-28.6%	-28.6%	-19.0%	-12.2%	-19.8%	-13.9%	-25.2%	-16.0%	-2.7%	-13.3%	-0.7%	-0.7%	-0.6%	-0.6%	-0.7%
Pretax Income as % Rev.	-150.9%	-130.6%	-80.3%	-6.8%	-73.3%	-19.8%	-50.4%	-39.0%	-12.4%	-29.2%	-0.1%	1.0%	4.0%	7.2%	3.3%
Ad Exp as % of Gross Receipts	60.5%	54.7%	52.6%	24.3%	45.2%	26.0%	27.4%	23.3%	26.8%	25.8%	27.3%	28.2%	28.1%	28.0%	27.9%
Prod Develop as % GR	4.8%	5.9%	6.9%	7.4%	6.4%	6.4%	7.8%	4.0%	4.0%	5.2%	3.7%	3.5%	3.2%	3.1%	3.3%
SG&A Exp as % GR	20.2%	25.1%	23.9%	21.8%	22.7%	24.4%	29.9%	25.5%	21.9%	25.0%	20.2%	19.4%	17.9%	16.8%	18.5%
<b>Cash Flow-EBITDA</b>															
Operating Income						A	A	E	E	E	E	E	E	E	E
Dep/Amort						(560)	(2,449)	(2,940)	(1,396)	(7,346)	109	292	887	1,600	2,888
Stock Comp						20	55	52	54	181	53	52	53	56	215
Add Change in Def Rev						91	299	159	181	731	203	218	238	258	917
less Change in Def Charges						841	461	2,081	2,051	5,434	2,037	1,939	2,128	2,200	8,304
Other						(1,716)	(1,342)	(1,764)	(899)	(5,720)	(883)	(768)	(647)	(597)	(2,895)
Adjusted EBITDA						(1,323)	(2,976)	(2,412)	(9)	(6,720)	1,519	1,734	2,659	3,518	9,429

## Disclosure Section

### References to Past Performance Are Not An Indicator Of Future Potential Returns

I, James Ragan certify that the views expressed in this note/report accurately reflect my personal views and that no part of my compensation was or will be directly or indirectly related to any recommendations.



Source: Bloomberg daily closing prices

**Ratings History:** 9/9/10 (\$3.73) Initiate Buy. Price target \$8. 11/17/10 (\$3.37) Buy, price target \$8.

#### Risks to Achieving Target Price

1. CYDE should be considered a high-risk, emerging growth investment. Prior to 6/9/10 the shares traded on the OTCBB.
2. CYDE has not been profitable in its history. The company will likely access the capital markets to support its growth outlook.
3. CYDE operates in a highly competitive industry against several well-capitalized competitors. Its products and services could be duplicated, leading to price competition and/or loss of market share.

#### Crowell, Weedon & Co. makes a market in CYDE

**Ratings Key:** **Buy/Add:** Buy new positions or Add to existing portfolio positions. We believe the security's 12-18 month reward-to-risk profile is **attractive**. Security appears **under valued** based on our analysis. **Hold/Neutral:** We believe that the security has strong attributes, but **concerns exist** that offset the conviction of a Buy/Add and Sell/Reduce opinion. Security appears **fairly valued** based on our analysis. **Sell/Reduce:** Sell positions or Reduce exposure to portfolio positions. We believe the security's 12-18 month reward-to-risk profile is **unattractive**. Security appears **over valued** based on our analysis.

Department	#	%	Growth	%	Income	%
Total Buys	41	79%	33	80%	8	73%
Total Holds	8	15%	5	12%	3	27%
Total Sells	3	6%	3	7%	0	0%
Total Companies	52	100%	41	100%	11	100%
As of:	11/15/2010					

Distribution of recommendations

Partners of and/or the firm of Crowell, Weedon & Co. in the normal course of business have a position in all of the securities mentioned in this report

The analyst who prepared this report owns CYDE shares.

**\*\*Crowell, Weedon & Co. regularly acts as a co-manager and/or syndicate participant in offerings of securities. Crowell, Weedon will participate and seek to participate in a like manner in the future when given the opportunity.**