

Costar Technologies, Inc.

Letter from the President and Chief Executive Officer



OTC: CSTL.PK
www.costartechnologies.com



August 28, 2017

Dear Shareholders,

I am very pleased with our team at Costar Technologies, Inc. and their accomplishments and dedication as they managed through a very tough security environment in 2016.

Our Costar Video Systems segment made significant progress this past year in replacing revenue from its largest customer, which experienced a major reduction in its new store openings. We realigned our salesforce to increase our focus on smaller, non-concentrated customers. The CohuHD segment's revenue rebounded as our new RISE product line was released in the third quarter of 2015 and the federal government passed a transportation bill in December 2015 that allocates approximately \$305 billion in funding over five years. All of these factors contributed to increased growth and profitability in 2016.

Our RISE product line continues to expand as CohuHD focusses on a new RISE low cost pan, tilt and zoom dome to meet market pricing while maintaining margins and a new RISE dual-headed thermal and visual camera for border applications.

The Company generated \$0.6 million of net income in 2016. In 2016, the CohuHD segment sales increased 26% to \$17.5 million from \$13.9 million in 2015 with net income increasing to \$1.1 million from (\$0.0) million the prior year. The Costar Video Systems segment sales increased 6% to \$21.0 million from \$19.7 million in 2015, with net income increasing to \$2.7 million from \$2.5 million in the prior year. The improvement in net income was primarily due to a 14% increase in revenue with a 12% increase in gross profit margins due to long term strategic investments made by the Company. SG&A expenses increased 17% as the Company continued to build its team, as we are committed to continuing to grow and increase profits next year and for years thereafter.

We must continue to invest to grow, while staying competitive and responsive. We believe that growth is achievable, provided we strategically approach the market.

Competition from Chinese manufacturers for commodity security products is at the highest level I have ever seen. The focus from these manufacturers has been to provide low price products to

distributors in a “race to the bottom” strategy, as opposed to servicing the integrator market that requires exceptional sales support, technical support, and system solutions. Our focus and investment has been in the integrator market, which continues to pay dividends as we strategically expand the integrator segment of our business. We have a tested team who is rewarded only when they deliver for our customers.

As part of our growth strategy, we are continuing our transition from legacy analog products to network video products. Network video products provide new opportunities for us to design “niche” accessories that allows Costar to offer a complete video solution for our customers. The network segment of our product line grew at a rate of 91% last year.

We are also continuing to grow through thoughtful strategic acquisitions. In December 2016, we acquired Innotech Security, a value-added manufacturer of customized video and security surveillance systems for major U.S. retailers, restaurant chains and public venues requiring high quality surveillance security. We acquired Innotech to expand our footprint in the security and surveillance industry. Costar and Innotech serve different integrator and retail customers, which means the acquisition creates many cross-selling opportunities.

Our board of directors continues to be an integral part of the governance, development and operating activities of our business. The board consistently provides strong leadership and direction and is a guiding force in helping maximizing value for our shareholders. I am grateful for the board’s strong commitment and their wise stewardship of the company.

Sincerely,

James D. Pritchett
President and Chief Executive Officer

Cautionary Statement Regarding Forward Looking Statements

This document contains forward-looking statements that involve risks and uncertainties, as well as assumptions, that if they never materialize or prove incorrect, could cause the results of Costar Technologies to differ materially from those expressed or implied by such forward-looking statements. Forward-looking statements generally are identified by the words “expects,” “anticipates,” “believes,” “intends,” “estimates,” “should,” “would,” “will,” “strategy,” “potentially,” “plan” and similar expressions. All statements other than statements of historical fact are statements that could be deemed forward-looking statements. The risks, uncertainties and assumptions include developments in the marketplace for our products, competition, related products and services and general economic conditions, as well as other risks and uncertainties. Accordingly, we cannot give assurance that any of the events anticipated by the forward-looking statements will transpire or occur, or if any of them do so, what impact they will have on the results of operations or financial condition of Costar Technologies.

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COMPANY FINANCIAL INFORMATION

A Copy of our Annual Report is available upon request and will be mailed to you at no charge.
Please send requests to:

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It can also be downloaded from our website at www.costartechnologies.com.