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Deer Valley Corp. (OTC-BB: DVLY)

Reason for Report: Initiation of Coverage
**RATING
Speculative Buy**
Recent Price: \$1.90

Market Data

Market Capitalization (mln)	\$12.97
Enterprise Value (mln)	\$11.67
Basic Shares Outstanding (000s)	6,825
Fully Diluted Shares Outstanding (000s)	6,825
Average Volume (90 Day)	9,304
Institutional Ownership	N/A
Insider Ownership	N/A
Exchange	OTC-BB

Balance Sheet Data

Shareholders' Equity (mln)	\$8.802
Price / Book Value	1.6x
Cash (000s)	\$4,580
Working Capital (000s)	\$4,425
Long-term Debt (000s)	3,284
Total Debt to Capital	.18:1

Company Overview

Deer Valley Corporation, through its wholly owned subsidiary, Deer Valley Homebuilders, Inc., engages in the production, sale, and marketing of manufactured homes in the southeastern and south central United States. It manufactures and sells single and multi-section manufactured homes. The company offers approximately 22 models of manufactured homes with various decors marketed under the Deer Valley brand name. It sells its products through a network of independent dealers and retail centers. The company was founded in 2004 and is based in Tampa, Florida.

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Summary and Investment Recommendation

- **Initiating Coverage with a Speculative Buy Rating and a 12-Month Price Target of \$2.60.**

We are initiating coverage of Deer Valley Corp. with a Speculative Buy rating. After entering the manufactured housing industry through acquisition, management is now focused on driving organic revenue growth and enhancing shareholder value. This industry is not well followed or understood by Wall Street, which we believe provides a relatively undiscovered niche for opportunistic investors.

- **Manufactured Housing Projected to Post Double Digit Growth for Next Several Years.**

The manufactured housing industry is a key contributor to the availability of affordable housing in the U.S. and is expected to grow at attractive rates over the next several years. Through improved standards and more uniform regulation, the industry is moving beyond past misconceptions to merge more into the mainstream of the U.S. housing market. We believe 10-12% overall industry growth is likely for the next 3-5 years.

- **Strong Management Team with a Solid Growth Strategy**

We believe that Deer Valley management has competitive advantages in its focused strategy, a strong growth-oriented operating team, a conservative financial management approach, and a history of dramatic growth. These factors combined should allow it to continue growing faster than the overall market over our forecast horizon. We believe that although industry conditions are mixed at best as we approach fall, we note that Deer Valley is maintaining its backlog and highly efficient production.

- **Industry Consolidation**

After a long malaise, the industry appears poised for improvements and potential consolidation over the next few years, which should provide a more constructive macro environment for well positioned and managed competitors going forward. Recent acquisitions by major industry players Clayton Homes and Champion Enterprises emphasize the trend toward consolidation.

Review & Estimates, In mlns except per share data (fiscal year ends Dec. 31st)

	FY2005A	FY2006E	FY2007E	FY2008E
Revenues	\$35.717	\$70.914	\$82.347	\$90.582
EBIT	3.416	5.430	6.821	7.874
Net Income	3.367	3.503	4.389	5.059
Operating EPS Full Year-Diluted	3.85	1.41	0.17	0.20
Operating Income	3.429	5.511	6.921	7.974
Fully Diluted P/E	N/A	N/A	19	14.62
Q1 EPS	\$0.50	\$(1.14)	0.03E	0.03E
Q2 EPS	0.83	(1.22)	0.05E	0.06E
Q3 EPS	1.10	(0.63)E	0.05E	0.06E
Q4 EPS	1.42	(0.02)E	0.05E	0.05E

Please see analyst certification and required disclosures on page 17 of this report.

Company Overview

Investment Summary

We are initiating coverage of Deer Valley with a Speculative Buy rating and a \$2.60 price target. After recently changing its name from Cytation Corp. to Deer Valley following a series of transactions to bring the entity public, Deer Valley is emerging as a producer of high-end manufactured housing following its acquisition of Deer Valley Homebuilders in 2004. The manufactured housing business is recovering from a long stretch of harsh conditions which should provide an improved macro backdrop for well managed competitors to benefit. Although this entity is relatively new, the management team has a long proven track record of performance that adds to our confidence level on this stock.

Solid Organic Growth Opportunity

The Company was born into a depressed market that is still weak compared to more normal periods, despite a post-hurricane Katrina surge in FEMA business. Deer Valley's advantages include specialization in the high end of the market and development of strong relationships with a high-quality independent dealer network that position the Company to thrive despite the difficult overall market. We believe this strategy and approach positions the company not only to grow faster than the overall market but to earn above-average financial returns through disciplined financial management. In addition to attractive organic growth opportunities we expect management to expand operations going forward either through plant expansion or possibly acquisition of underperforming competitors or facilities in certain circumstances.

Market Recovery Expected to Continue

Looking at the high end segment targeted by Deer Valley and excluding the single-wide FEMA (non HUD code) type units that do not apply to this analysis, we see conditions as improving but with some variability. For 2005 the Manufactured Housing Institute (MHI) reported shipments of about 95,700 multi-section units (projected growth of 11.4% in 2006). MHI projects 52,000 single-wide units for 2005, which is actually up 25% excluding FEMA units. MHI issued an estimate for 2006 of 145,800 units, comprised of 106,600 multi-section units and just over 39,000 single-wide units. We think there could be faster growth in certain market sub sectors served by Deer Valley and expect the Company to be able to grow faster than the overall market, in part through potential capacity expansion. An estimated market share of less than 1% of the total available leaves a very large growth opportunity available for Deer Valley.

As discussed in more detail later in this report, we believe the shares could trade at 15-18X our FY2007 operating EPS estimate of \$0.17 given the differentiated product offering and above market revenue growth rates. Although the manufactured housing industry faces a number of challenges for most operators, we believe that Deer Valley can grow at faster rates than the overall market due to its differentiated strategy, focused approach, and tight financial management regimen.

Well Developed Loyal Dealer Network

We view the Company's decisions to forego the seemingly attractive short-term revenue available from lower end FEMA units in order to be a consistent reliable supplier of its core products to the dealer network as an important strategic decision that has improved Deer Valley's competitive position immensely. While competitors rushed to grab the short-term gratification of FEMA revenue, this deprived dealers of product and established Deer Valley as a trusted partner that can be counted on to provide product consistently. We believe this will serve the Company well over the longer term as expansion occurs.

Top Flight Management Group

We believe Deer Valley also has a distinct advantage in its experienced cohesive management team that has been together in this and prior assignments for a considerable period of time. Management has demonstrated the ability to run fiscally responsible tightly controlled operations that run on plan and consistently achieve or exceed objectives. We believe this is an outstanding and above average group for a company of this size and age.

Balance Sheet Strength and Financial Flexibility

Deer Valley has accomplished a strong record of growth and profitability while also employing conservative financial management practices. The Company has been able to avoid taking on debt, tightly control expenses, and generate strong internal cash flow. The combination of these factors leaves Deer Valley with a debt-free balance sheet (excluding mortgages on real estate) and the financial flexibility to grow at above-market rates. With the opening of the Company's second plant, management has demonstrated the ability to quickly ramp production and revenue without excessive working capital expenditures or large incremental investments.

Manufactured Housing Industry Overview

The Manufactured Housing industry of today has its roots in the pre-WWII evolution of what were originally travel trailers. Over many years, mobile units evolved into prefabricated units that were designed for semi-permanent or permanent placement on a fixed site. As far back as the 1930s trends toward extended living periods in what were, at that time, essentially large mobile travel trailers began to emerge; with year-round living in various trailer types beginning to become more accepted. As the U.S. entered World War II, the supply of housing in cities near facilities manufacturing for the war effort such as shipyards and munitions plants became tight and trailers were a practical solution for the short-term need. Prior to the war, most commercially built trailers were used for travel or vacations. In contrast, during and after the war the vast majority were used for permanent or semi-permanent housing. The federal government bought over 30,000 house trailers and built a large number of trailer parks with the capacity to accommodate them. After the war, many of these units ended up transitioning to use on college campuses as veterans returning from service took advantage of GI Bill benefits. The term “mobile home” had been originated in the early 1950s by an industry pioneer named Elmer Frey at a time when the recreational trailer industry and the mobile or manufactured home industry clearly emerged as separate market segments. By the 1960s, the target customer group for manufactured housing was becoming younger and more motivated by housing alternatives that were lower in cost than conventional site-built homes. Customers were also becoming much more interested in homes that looked more like and had the “feel” of conventional homes, including more features, more floor space, and suitability for year-round occupation.

These developing views resulted in many changes and design innovations, including initially wider units (10 feet in the early stages and progressing to the current 16 foot width) and double-wide sectional units that offered floor plans that were very similar to those of site-built homes. The industry exhibited strong growth through the early 1970s driven by new models and mobile home park improvements that expanded target markets through increased product appeal. The industry’s all time high water mark was hit in 1973, when an aggregate of approximately 580,000 units were shipped. As the industry grew and gained increasing acceptance there was a corresponding increase in scrutiny from critics and detractors calling for increased regulations or restrictions. Certain perceptions and stigmas from the early days of manufactured housing caused critics to argue that manufactured homes were of inferior quality and that lower prices were a result of improper practices and shortcuts by industry participants. While any industry has some instances of misbehavior, these perceptions were the exception rather than the norm and the industry took proactive steps to prevent ongoing issues by cooperating in the development of construction standards in the early 1960s. In 1963 collaboration with the American National Standards Institute (ANSI) resulted in the propagation of a construction code for manufactured housing companies that while initially voluntary had by 1973 been adopted by 45 states, which had the effect of solidifying the code as a de facto industry standard. Unfortunately, although rare, isolated incidents continue to occur in which manufacturers violate the intent of the HUD standards.

As the industry continued to gain credibility and the appeal of low cost housing increased, demand for mortgage financing increased. This prompted the Veterans Administration (VA) in 1969 to extend mortgage guarantees to mobile/manufactured home loans. The industry actively sought to expand government involvement in hopes that new construction regulations would be enacted resulting in uniform national standards that would ensure a place in the market for manufactured housing. The first major Congressional action in this area came in 1974 when Congress passed the National Mobile Home Construction & Safety Standards Act, which was essentially the genesis of standards referred to even today as the “HUD Code.” The 1974 legislation charged the U.S. Department of Housing & Urban Development (HUD) with development and implementation of standards to regulate single family mobile and manufactured homes. This was a critical event in the process of manufactured homes being defined and treated as buildings rather than any kind of vehicle or equipment. The Housing Act of 1980 incorporated changes in terminology to replace the expression “mobile home” with the modern language “manufactured home” in all federal legislation and publications, which had the practical effect of all homes being built to HUD Code after June 15, 1976 being classified as manufactured homes.

The most recent significant legislative/regulatory changes applicable to the industry came in late 2000 with the Manufactured Housing Improvement Act of 2000 (Public Law No. 106-569), which established a private sector committee to work in an advisory capacity to the Secretary of HUD at least bi-annually to keep HUD code current with developments in the industry and markets. This legislation clarified the scope of federal authority regarding regulation of preemption of HUD code requirements. The preemption of HUD Code prohibits imposition by state or local government entities of manufactured housing code that differs from the federally mandated HUD code. The benefits of this legislation include dispute resolution program requirements for states, increased standardizations, and clarity of regulatory authority across jurisdictions.

Manufactured Housing Products

Most products of today’s manufactured housing industry bear little resemblance to early mobile homes, and indeed many high end offerings can be virtually indistinguishable from a conventional site-built home. Many misconceptions and misunderstandings exist among the general public today about both facts and terminology relating to manufactured housing. The Manufactured Housing Institute (MHI) recognizes five primary categories of manufactured housing of which two types (HUD Code and Modular) represent the majority of units produced today.

Manufactured or HUD Code Homes

The category of HUD Code homes is the largest and is the type of manufactured home that most closely compares with traditional site-built homes. Deer Valley specializes in this type of home, constructed in accordance with the Federal Manufactured Home Construction and Safety Standards promulgated by the U.S. Department of Housing and Urban Development, better known as the “HUD Code.” This is the only kind of federally regulated construction code in the U.S. and applies only to the manufactured product itself. Any improvements added to the structures after transportation to the destination site, such as garages or decks, are subject to state or local building codes. These homes are built entirely in the factory, transported to the site, and installed under federal (HUD) building code. HUD regulations supersede (or preempt) state and local government regulations that might otherwise apply to manufactured housing. This is generally viewed by industry participants as a positive factor that allows a level playing field and an environment where participants will not be surprised by more (or less) stringent codes in certain isolated jurisdictions.

This preemptive status is a significant factor that contributes to making manufactured homes affordable, due to the specific tailoring of the HUD code to be compatible with factory production methods in wide use by the industry. Uniform standards are imposed for major design and construction elements including structural characteristics, heating, plumbing, air conditioning, insulation, energy efficiency, fire safety, and transportation procedures to the ultimate destination site. Having a pre-defined set of specifications to work within allows the industry to produce quality product at lower cost per square foot of living space than traditionally constructed homes.

Modular Homes

A modular home is a factory-produced home that is built to state, local, or regional code at the final destination, as opposed to the federal HUD regulations. Similar to HUD code units, these homes are moved from the factory to the destination and installed. This category is the fastest growing segment in the industry. It offers a great degree of design flexibility, but also a high degree of manufacturing challenges. To date Deer Valley has not entered this market, but we believe this is a possible future expansion opportunity for the Company.

Pre-Cut Homes

Pre-cut homes are factory built homes that are assembled at the destination site from building materials that have been factory processed to meet state, local, or other applicable building codes as well as design specifications and transported to the destination for assembly. Examples of pre-cut homes include kits, log, and dome homes.

Panelized Homes

The panelized home category is not much different from pre-cut varieties, but additional processing or assembly is conducted at the factory to produce a panel constructing a complete wall with structural elements including windows, doors, wiring, and outside siding. State or local building codes apply to this category.

Mobile Homes

This is a legacy product that is not relevant for this report, although units still exist that were manufactured prior to June 15, 1976, when the HUD Code went into effect. Other products that could fit in this category include FEMA units that do not meet HUD code and so-called “Park” models that are less than 400 square feet in size and therefore do not fall under the HUD code umbrella.

The Production Process

Manufactured housing is produced today in a controlled assembly line production process that allows for tight quality control, highly efficient production, and economies of scale. Volume purchasing of materials including taking full advantage of accelerated payments purchase discounts is a tactic that Deer Valley employs effectively to reduce costs compared with many competitors. With just-in-time delivery, rapid inventory turnover, and high plant capacity utilization, Deer Valley enjoys significant advantages that reduce storage space requirements and cost. The series of processes required to produce the finished product can be carefully planned in advance to improve economies of scale and reduce waste, contributing significantly to the affordability of the finished product. The production process is broken down into a series of specific steps or stations at which certain components are added to the unit. A factory production line process requires up to two-thirds less labor than traditional on-site construction and allows inspections to occur simultaneously at critical points of the assembly process, contributing further to cost reductions. The fact that production occurs in a factory facilitates adherence to quality assurance practices.

In view of dramatic needs in major target markets like the Gulf Coast, including a lack of infrastructure, severe labor shortage in the area, and lack of services, Deer Valley has a significant advantage operating in a factory located elsewhere for delivery to the region. A key reason for this is the fact that it is much easier to hire workers to work inside in a stable area away from the gulf coast than it would be to build on site in the area. Factory production eliminates exposure to potentially harsh weather

conditions that may be present during traditional outdoor construction. The assembly time required in the factory for a single-section home is typically about 120 worker-hours, but can often be finished in a single day depending upon the specific manufacturer, although in smaller plants larger units may take several days to finish.

The primary assembly line stations in a typical factory might be as follows¹:

Sub-floor Framing Station

HUD code homes of the type produced by Deer Valley begin with a metal chassis which is delivered to the factory already assembled, including axles and wheels. Modular homes do not require a metal chassis. Deer Valley builds its own chassis from raw steel and purchased parts. One of the first steps of home construction is placing camber in the metal chassis. Camber is a bend in the steel of the chassis. The amount of camber depends on the weight of the home being constructed. When the weight of the home is placed on the chassis, its camber will hold the structure level. Without the camber, the chassis would sag around the wheels and the home would not sit straight. At the chassis station, a sub-floor frame of wood is constructed on a jig next to where the chassis has been rolled. Heating ducts and other utility lines are run through the sub floor. Insulation is added, and the entire sub floor is then covered with a bottom enclosure. The sub floor is then flipped over onto the metal chassis and bolted to it.

Floor Finishing Station

At the next station, plumbing connections that will project above the floor and into fixtures, such as toilet and bath, are attached. The sub floor frame is then covered with plywood, OSB (oriented strand board), or particleboard sheets which have been cut to accommodate the plumbing connections. Cut outs are also made for HVAC (heating, ventilation, and air conditioning) fixtures. In some factories, part of the finished floor covering, such as vinyl sheeting for kitchen and bath areas, may be added at this station, but carpeting is added later.

Interior Wall Assembly Station

The wood frames that will become the interior walls of the home are assembled on jigs next to where the chassis, with floor attached, has now been rolled. Often the walls have their electrical wiring added and one of their finished surfaces of drywall or other paneling applied before the whole assembly is lifted off the jig and onto the floor. It is then attached to the floor.

In many factories, kitchen cabinets are purchased from a supplier and shipped to the factory, while some plants build their own cabinets in a separate shop. Regardless of their source, the cabinets are attached to the interior walls at this station. Plumbing fixtures, water heater, and furnace are also added at this point, so that when the home leaves the station it has a fairly finished interior but no exterior walls.

Exterior Wall Assembly Station

At the next station the home pulls up alongside jigs where the exterior walls are assembled. Again, electrical wiring is pulled through the wall frames, and insulation and inside wall surface panels are also applied while on the jig. The finished wall assembly is then lifted up and attached to the waiting home using metal fastener plates and/or metal straps. Depending on the interior design of the home, some or all of the kitchen cabinets may be added at this point in the assembly process. Other interior finishing work may also be completed at this station, including sealing joints between panels, attaching face plates over electrical outlets, and installing doors, moldings and closet fixtures.

Roof Assembly Station

The roof of a manufactured home, like that found on many site-built homes, consists of a series of bow-shaped or triangular trusses. The trusses are pre-assembled, as with site-built homes, and then placed on a jig where they are tied together with other pieces of wood to create the roof structure. Any wiring and insulation is then added, and the exterior sheathing is attached. The finished roof assembly is then lifted off the jig and hoisted on top of the home, where it is fastened with metal plates and/or straps. In addition to these connections—tying the wall, floor and roof panels together—manufactured housing construction incorporates metal straps which run up one exterior wall, over the roof, and down the other exterior wall. These straps will be used to help tie the home to a foundation system when it gets to its final home site. On most homes, manufacturers use the same type of composition shingles found on site-built homes. The outer finished surface, as well as the interior ceiling, is applied before the home leaves the roof assembly station.

Exterior Siding Station

The home arrives at the next station looking like a big padded box with doors and windows in it. The padding, of course, is the insulation that already has been applied. At this station the exterior wall surfaces are added. Exterior finishes on today's manufactured homes are similar to those found on many site-built homes. Many home designs have overhanging eaves, which

¹ Source Manufactured Housing Educational Institute

would then be applied at this station. Since some of these roof sections project well over the side walls of the home, they may be attached with hinges so they can be folded up on the roof when being transported on the highway and then hinged down at the home site. These, and other joints between multi-sectional homes, are finished at the site.

Interior Appointments Station

At this last station, finishing touches are put on the interior of the home. Carpeting may be added and additional interior joint fastening attended to. If the home has a multi-sectional design, the open faces between sections must be enclosed temporarily in plastic to protect it once outside the factory doors. Some temporary framing elements may be inserted into the openings onto which the plastic is attached.

Inspections & Certification

An important element of any building code scheme is the enforcement that assures its integrity. The manufactured home enforcement program mandated by HUD is a comprehensive system designed specifically for the factory production process. The HUD enforcement system begins with oversight by the Design Approval Primary Inspection Agency (DAPIA). The DAPIA (a third party inspection agency) has the following authority and mandates: approving the engineering design of the home; approving the manufacturer's quality assurance manual; and coordination with the other third-party inspection agency, known as the IPIA. The Production Inspection Primary Inspection Agency (IPIA) has the responsibility to make sure the production facility programs and procedures are in accordance with the DAPIA-approved quality assurance manual and conduct inspections of homes. Because factory construction differs from that of the construction site, the manufactured home enforcement system is specifically tailored for differences in the process. The ultimate objective, however, remains to ensure a high degree of safety in the design and construction of the products. The HUD enforcement system relies on a cooperative federal/state program to ensure compliance with the Federal Manufactured Home Construction and Safety Standards (the HUD Code).

The Department of Housing and Urban Development enforces the HUD Code through a third party monitoring contractor. Uniformity and consistency can be maintained better in the HUD enforcement system because of two key factors. First, the inspections take place in the factory and follow after the manufacturer's in-house inspection and quality assurance teams. This allows for comprehensive redundant inspections and saves time spent traveling to remote home sites. Efficiency is increased by reducing travel and minimizing paperwork. Second, consistency is maintained because the home is inspected by a third party during the construction process. The enforcement procedure is much less susceptible to individual interpretations, as would be the case with on-site inspections in a wide variety of jurisdictions nationwide.

Prior to shipping from the factory, each home will have a numbered certification label affixed to the exterior of each section of the home certifying to the buyer that the home has been inspected in compliance with HUD procedures and that it meets the HUD building code. Only when all inspectors are satisfied with the home's compliance can the certification label be attached to the unit. This label provides consumers a high degree of assurance that homes have been properly tested and inspected according to strict regulations and codes.

Market Conditions Improving But Erratically

The manufactured housing industry has been through a very difficult period that started in about 1998 when shipments reached their most recent peak. The manufactured housing industry downturn is generally attributed to a number of factors coming together, including a tightening of credit standards, restricted availability of retail and wholesale financing, excessive industry capacity, and inventory levels. Statistics from the Manufactured Housing Institute (MHI) show that shipments for the industry reached just over 372,000 in 1998 and declined all the way through 2004 to an annual low of 130,802. Annual volume subsequently recovered somewhat to an annual volume in 2005 of 146,744 with considerable remaining volatility from month to month. The data available year to date for 2006 (through April) shows monthly shipments running at an average rate of about 10,950, compared with an average for the first four months of the prior year of about 10,450 monthly, an increase of 4.8%. 2005, which was the first year of increased shipments for the industry since 1998, benefited from a one-time increase in shipments related to hurricane relief that can not be counted on to recur. This volume increase, however, was driven in large measure by shipments of a specific product type directly to the federal government known as FEMA homes. Single-wide FEMA type units were up over 200% in the last quarter of 2005, and although this provided significant financial benefit to those manufacturers who chose to divert capacity to this business, the longer-term impacts may be more questionable. Assembly lines are generally unable to produce more than one type of unit on a production run, and FEMA homes are incompatible with the normal production runs of many suppliers, requiring that capacity be changed over to take advantage of the short-term revenue opportunity. This comes at the cost of reduced or suspended production of more conventional units that would have been sold through the normal distribution network. Distributors deprived of product flow may have suffered significant financial damage and possibly moved to other suppliers like Deer Valley that demonstrated a longer-term commitment to more conventional non-FEMA units. Without FEMA-driven volume it is estimated that shipments would have been virtually flat for 2005.

Emerging Megatrend

We believe that there is an increasingly important secular trend driven by a number of powerful factors that should produce rapidly increasing demand for manufactured homes going forward. Although a prime example is the Gulf Coast region following last year's hurricanes, we see similar influences in other areas of the country. A key common driver is the difficulty or outright inability of contractors to hire skilled craftsmen in the construction trades in the specific end markets needing housing. This, in combination with the ongoing devastation and lack of infrastructure in many areas with urgent housing needs, is contributing to an increasing demand for housing product manufactured in remote areas where skilled labor is available and production can occur in a highly quality-controlled factory setting. The ability to produce inside a factory as opposed to outdoors in harsh variable climatic conditions can not be underestimated as a favorable differentiator for manufactured housing. In addition, a factory process eliminates the need to coordinate and manage a large group of sub-contractors that may introduce quality and reliability issues to the equation. We expect this trend to gain strength over time and ultimately be a factor in returning the industry to more healthy conditions over time. Deer Valley is carefully evaluating the optimal ways for the Company to appropriately support and participate in the reconstruction of the Gulf Coast and to be ready to react to any similar events in the future.

MH Industry Unit Shipments

	1998	1999	2000	2001	2002	2003	2004	2005	2006
January	26,362	26,784	21,180	12,396	14,435	10,436	8,713	10,019	11,677
February	27,549	28,770	22,806	13,124	13,258	9,620	8,832	9,773	10,254
March	31,813	34,205	26,341	16,110	13,925	10,435	11,282	11,119	11,816
April	33,266	33,148	22,662	15,715	15,216	11,416	11,370	10,917	10,037
May	31,397	30,550	24,783	17,707	16,245	11,473	10,587	10,913	
June	33,567	32,887	24,430	17,776	14,824	11,750	11,899	11,926	
July	31,805	26,799	18,081	14,912	13,707	11,366	10,033	9,335	
August	32,556	30,890	23,637	19,840	15,861	11,923	11,886	12,146	
September	32,710	28,875	19,606	16,960	14,321	11,815	12,720	12,863	
October	35,185	28,239	19,214	19,700	15,708	12,744	12,888	17,432	
November	30,110	25,675	16,248	16,189	11,555	9,435	11,112	16,034	
December	27,243	21,849	11,562	12,800	9,436	8,524	9,490	13,997	
Annual Total	372,843	348,671	250,550	193,229	168,491	130,937	130,802	146,744	

Source: MHI

Weakness Concentrated In Markets Outside Deer Valley Geographies

MHI statistics indicate that many of the industry's weakest areas are in the Midwest US, an area not currently served by Deer Valley. Industry observers are generally constructive on the prospects for improvement, and MHI estimates show continuing growth into 2006.

Available 2006 Results Encouraging

MHI and many economists point to the following factors as contributors to forecasts for growth in 2006: upward pressure on prices spilling over from conventional housing, contained inflation resulting in modest interest rate increases, relatively strong job growth, manufactured housing contributions to permanent rebuilding in the Gulf region, and reacceleration of multi-floor units in the first quarter as production capacity is converted back from FEMA units.

Market Breakdown by Geography

Deer Valley currently sells into 13 states primarily in the Southeastern United States.

The following statistics from MHI show placements of multi-section homes by Region for the last several years:

(data in 000's)	Total US	Northeast	Midwest	South	West
1999	213.0	9.7	35.2	133.3	34.9
2000	190.3	10.6	34.4	113.4	31.9
2001	139.3	8.3	27.0	80.0	24.0
2002	128.7	8.7	25.7	72.0	22.2
2003	106.0	7.8	20.0	57.0	21.3
2004	90.9	7.6	16.4	46.6	20.2
2005	87.3	6.7	13.0	45.2	22.4

Industry Growth Drivers

Affordability

The lower price has historically been one of the key selling points for manufactured homes, and some would argue that the advantage has been increasing as housing prices have spiked higher in recent years. The appeal is obviously greatest for low and moderate income prospective homeowners, as traditional housing prices have increasingly risen out of many buyers' reach. Interest rates also figure into the total cost equation, and low rates have actually been working against manufactured housing for the last few years as traditional home financing became more affordable. Rising interest rates should contribute to increasing the relative affordability of manufactured homes going forward.

Manufactured Home Pricing & Market Share (Multi Section –US Total)

	2001	2002	2003	2004	2005
Average Price	\$55,200	\$56,100	\$59,700	\$63,300	\$68,400
MH Total % Sales	N/A	N/A	10.7%	9.8%	10.3%

Improved Utility & Functionality

Over time, early issues and perceptions regarding the size and quality of manufactured homes have been mitigated to a significant degree by a number of factors that have closed the gap with traditional site-built homes. Historic factory production limitations and transportation issues have been overcome in recent years, allowing the industry to move beyond smaller one-story units, which were often less attractive to prospective buyers, to the larger designs available today. Modern design and production techniques have dramatically improved the appearance and functionality of today's manufactured homes, placing them much closer to site-built options.

Lower Industry-wide Inventories and Work Off of Repossessions

A very large pool of repossessed manufactured homes through the early 2000s served as a major inhibitor to manufactured housing shipment levels. This condition has been steadily improving with a continuing trend toward fewer repossessed units and higher recoveries that has contributed to the health of the industry. Repossessions appear to have peaked in 2002, and a significant portion of this problem has been removed at this point. Due to the segment served by Deer Valley, we view this issue as a relatively minor one for them. Statistics also indicate that dealers today carry much lower inventory of HUD Code units as a common business practice than was the case at past industry peaks, allowing the manufacturers to move product more quickly and avoid having to carry significant inventory.

Improved Underwriting & Loan Performance

The surge in repossessions and underperforming loans in the late 1990s and early 2000s appears to have resulted in some turnover in financing sources and improved underwriting discipline that should drive better loan performance and potentially contribute to better access to funding through the securitization market going forward. Access to securitization and lower repossession experience would improve liquidity and lower financing costs for the industry.

Financing Manufactured Housing

It is common practice for manufacturers and MH retailers to maintain relationships with conventional lenders who provide two basic types of consumer financing in the manufactured housing industry: (1) chattel or personal property loans for purchasers of a home with no real estate involved and (2) land/home or mortgage loans that finance the land, home, and all improvements on the property. Most states classify manufactured homes as personal property rather than real property for purposes of taxation and lien perfection, and interest rates for manufactured homes are generally higher and the terms of the loans shorter than for site-built homes. Financing for the purchase of manufactured homes is often more difficult to obtain than conventional home mortgages. There are two types of mortgage loans — conforming and non-conforming. Conforming loans conform to Federal Housing Administration, Department of Veterans Affairs, Federal Home Loan Mortgage Corporation (Freddie Mac), and Federal National Mortgage Association (Fannie Mae) requirements. Generally, the type of required foundations installed conforms to federal requirements, and the borrower must meet certain criteria. Non-conforming loans are financed by banks or mortgage lenders that do not require a specific foundation type. Deer Valley sells all of its production to dealers and does not become directly involved in buyer financing as some integrated manufacturers do. The Company's sales are made to dealers either through floor plan financing arrangements with a financial institution or on a cash basis. When a manufactured home is purchased, Deer Valley receives payment either directly from the dealer or from a financial institution which has agreed to finance dealer purchases. As customary in the manufactured housing industry, many financial institutions which finance dealer purchases require the execution of a repurchase agreement which provides that, in the event a dealer defaults on its repayment of the financing arrangement, Deer Valley agrees to repurchase the manufactured home from the financing institution, in accordance with a declining repurchase price schedule that is mutually agreed upon. We do not view this as a significant risk because of the negotiated discount repurchase price structure, contractual allowances for recovery of any required repair costs, and the fact that Deer Valley has ready buyers for any spare capacity that may be available. Because the Company does not build significant inventories of either finished goods or raw materials and

produces against specific product orders. Deer Valley minimizes demand for working capital and does not carry significant inventories.

Company Overview

The Company, as it is currently organized, began in January 2006 with the acquisition by the predecessor entity Cytation Corporation of 100% of the outstanding stock of Deer Valley Homebuilders through a special entity called Deer Valley Acquisitions (DVA) that was set up specifically to complete the acquisition. A recent recapitalization and name change resulted in the current Deer Valley Corporation. For approximately a year prior to the acquisition, Cytation had no active business operations while management was in the process of raising capital and identifying potential acquisition targets. Deer Valley is an Alabama corporation with its headquarters located in Guin, Alabama. The Company is engaged in the production, sale and marketing of manufactured homes in the southeastern and south central U.S. housing markets. Deer Valley currently operates two manufacturing facilities, one located in Guin, Alabama and one located in Sulligent, Alabama. The Company uses a team of regional sales directors and approximately 80 independent dealers to market its manufactured homes in over 110 retail locations. Deer Valley is currently selling manufactured homes in 13 states through its network of independent dealers and retail centers.

The Company's specialty is high-end, feature rich homes constructed in accordance with the Federal Manufactured Home Construction and Safety Standards promulgated by the U.S. Department of Housing and Urban Development, discussed earlier in this report as the "HUD Code." Management has historically concentrated production and marketing efforts on multi-section homes and, appropriately in our view, resisted the urge to chase fleeting short-term profits by participating in the short-term demand for FEMA-related units. That said, management has been evaluating a number of potential expansion strategies which have resulted in the addition of (non-FEMA) single-wide units to the product line. By following what we view as prudent long-term strategies combined with financial discipline, the Company has been able to successfully launch its business through an efficient manufacturing and production facility that achieved profitability in the first full month of production and has maintained profitability ever since. We believe additional contributing factors include flexible product designs, a dedicated manufacturing organization, an experienced and capable sales team, superior after-market trim out, service and support group, stringent cost controls, and attention to dealer relations. Deer Valley homes are often sold as part of a land-home package and may be financed by a conventional mortgage. Multi-section homes often have an external appearance similar to more traditional site-built homes, which are built according to local building codes, but are competitively priced when compared to site-built homes.

Deer Valley Production Operations

The Company currently produces all of its units at two manufacturing facilities. The Company began operations with its first plant in Guin, Alabama, consisting of an approximately 118,000 square foot facility. Manufacturing is now conducted under controlled conditions in two indoor facilities, the first of which is located on 25.5 acres in Guin, Alabama, which has approximately 107,516 square feet of floor space, a frame shop with 10,800 square feet, a material shed with 23,172 square feet of space and an office facility consisting of 11,250 square feet of space. In addition, in February 2006, the Company opened a 65,992 square foot plant in Sulligent, Alabama. The two plants employ an average of 375 employees, who generally work one shift per day, five days per week. As discussed in some detail earlier in this report, construction is based upon an assembly line system that involves moving a unit through the plant, stopping at a number of work stations where various components and sub-assemblies are attached. While manufactured homes are constructed with many of the same components and building materials used in site-built homes, Deer Valley operates cost-efficient assembly line manufacturing processes which enable production of quality homes at a much lower cost per square foot than a traditional site-built home. A Deer Valley home is built with residential features, including 1/2 inch drywall, Thermopane™ brand windows, enhanced insulation, oak cabinets, cultured marble vanities, and two inch by six inch exterior wall construction standards. Each section is permanently attached to a steel support chassis, and various components are later added, including floors, interior and exterior walls, roof, cabinets, ceilings, and windows. It takes approximately 2½ days to complete construction of a home. Once the home has been assembled and quality review testing has been completed, the home is ready to be transported to a dealer location or for installation and hookup to a homebuyer's utility systems.

The Guin plant quickly ramped up to a profitable operating level within its first 30 days of operations and is now running at what management views as 100% capacity. Similarly, the Sulligent plant also achieved profitability within the first 30 days and currently runs at its designed capacity of five floors daily. Production volume of manufactured homes is measured within the industry in terms of "floors," which essentially amount to building blocks or sub-components that can be combined and configured in a variety of ways to compose multi-level or larger complete homes than can be manufactured and transported conveniently. The original plant can produce 7-8 floors per day, or approximately 1,680 floors on an annual basis, with one floor per day translating into approximately \$6mm in annual revenue. Deer Valley concentrates exclusively at this time on HUD Code units and we expect that to continue in the foreseeable future. The Company has no plans at this time to expand beyond a single shift, five day work week production run. With both plants running at or near full capacity, however, management is considering alternatives to expand capacity in other ways.

Because all of Deer Valley’s manufactured homes are constructed in accordance with HUD Standards, the manufacturing facilities are subject to strict oversight and monitoring by the U.S. Department of Housing and Urban Development, using independent third-party inspection agencies for enforcement. Each home complies with the HUD Standards and has a special label affixed to the exterior of the home indicating that the home has been designed, constructed, tested, and inspected to comply with stringent federal standards set forth in these HUD Standards. As required by the National Manufactured Home Construction and Safety Standards Act of 1974, homes may not be shipped from the factory unless in compliance with HUD Standards and having received a certification label from an independent third-party inspector. Manufacturing facilities must meet performance standards for heating, plumbing, air conditioning, thermal and electrical systems, structural design, fire safety, and energy efficiency. The Company also conducts its own in-plant inspection and quality assurance programs.

Upon completion, Deer Valley contracts with an independent trucking company to transport the home to either a retail sales center or a customer’s site. All transportation costs are borne by the independent retailer or other independent installer, who is responsible for placing the manufactured home on the customer’s site, joining the interior and exterior seams, and providing any utility hookups.

The total number of factory homes built and sold by Deer Valley, square footage, and retail price range in 2005 are shown below:

Type of Homes Sold	Number of Homes Sold	Square Feet	Retail Price Range (excluding land)
Multi-Section Homes	1,385 floors or 842 units	1,560 - 2,580	\$59,000 to \$119,000

Deer Valley Product Offerings

The Company currently offers 22 different models of manufactured homes with a variety of decors that are marketed under the Deer Valley brand name. Deer Valley homes are designed as primary residences ready for immediate occupancy. The homes, many of which are customized at the factory to the home buyer’s specifications, are constructed in one or more sections and transported by independent trucking companies to dealer locations or to a customer’s site. Deer Valley currently builds and sells multi-section manufactured homes, with 100% of the manufactured homes produced in 2005 consisting of multi-section units. Deer Valley offers a wide variety of different floor plans ranging in size from approximately 1,560 to 2,580 square feet with many customizable features available. Management believes that the Company’s willingness and ability to offer factory trim-out services and customize floor plans and design features to match homebuyer preferences is a significant favorable differentiator from most competitors. The pictures below depict representative finished products that can be difficult to distinguish from a traditional site-built home.



Deer Valley
MANUFACTURED HOMES, LLC

The Charleston
DV-8403



Deer Valley
MANUFACTURED HOMES, LLC

The Charleston
DV-8403



Each home typically includes three to five bedrooms, a great room which functions as a living room, family room, and dining room, a kitchen, two or three bathrooms, and features central air conditioning and heating, a water heater, a dishwasher, a refrigerator, a microwave, a cook top/range, and an oven. Deer Valley offers a wide range of colors, moldings, and finishes as well as optional features including fireplaces, wood floors, and modern kitchen counter-tops. Designs are continually updated and improved in consultation with sales representatives and the independent dealer network. The Company also utilizes computer-aided and other design methods in an effort to continuously improve home designs and to permit customers to customize their purchases. Deer Valley has traditionally focused on high end manufactured homes with rich feature sets comparable to site-built homes.

In addition to offering the consumer options specified in the preceding paragraph, Deer Valley generally offers extensive customization of floor plan designs and exterior elevations to meet specific customer preferences. The extent of customization of the home performed by Deer Valley varies to a significant degree with the price of the home. In the higher price range of the market, the home buyer is often less sensitive to the price increase associated with significant design modifications. The Company's experience in producing customized homes on a cost-effective basis has allowed it to offer customized homes and factory provided trim-out services and walk-through inspections of the home.

Competition

The manufactured housing industry, which has suffered through a difficult environment for the last several years, is highly competitive at both the manufacturing and retail levels. Competition is traditionally based upon numerous factors including total price to the dealer, customization to homeowners' preferences, product features, quality, warranty repair service, and the terms of dealer and retail customer financing. Deer Valley has many competitors, ranging from very large, established, and well-financed companies to small, specialized manufacturers. Numerous firms produce manufactured and modular homes in the southeastern and south central United States, many of which have direct overlap with Deer Valley markets. In addition, certain of Deer Valley's competitors provide retail customers with financing from captive finance subsidiaries. Deer Valley is not integrated at this time, meaning that the Company does not own retail outlets or endeavor to provide financing.

Manufactured homes also compete with other forms of housing, including site-built and prefabricated homes. Historically, manufactured housing has had a price advantage over these other forms of housing. That advantage has deteriorated, however, as the credit market in the manufactured housing industry has, at both the retail and wholesale levels, continued to tighten, while interest rates for site-built houses in recent years have been at historic lows, thus increasing the competitive pressures on manufactured housing.

The capital requirements and barriers to entry as a producer in the manufactured housing industry are relatively low, however, Deer Valley believes that the qualifications for obtaining inventory financing, which are based upon the financial strength of the manufacturer and each of its dealers, have recently become more difficult to meet due to the exit of certain major financial institutions from the market and efforts of the Company's competitors to add dealers to their sales networks.

A partial list of the largest competitors in the manufactured housing industry is shown in the table below:

Company	Symbol	Market Cap.	Estimated Market Share	Price/TTM Sales
Clayton Homes	Subsidiary of Berkshire Hathaway BRK.B	N/A	23%	Acquired for \$1.7 bil – Revenue was \$1.2 bil
Fleetwood Enterprises	FLE	\$460mm	18	0.2X
Champion Enterprises	CHB	\$530mm	13	0.4X
Skyline Corp.	SKY	\$320mm	6	0.6X
Palm Harbor Homes	PHHM	\$340mm	6	0.45X
Cavalier Homes	CAV	\$65mm	4	0.2X
Southern Energy Homes	Recently Acquired by Clayton	\$107mm	4	Acquisition price 0.42X TTM Sales
Cavco Industries	CVCO	\$210mm	3	1.1X
Deer Valley Homebuilders	DVLY	\$13mm	< 1%	0.43X

Source: Company reports & Harbinger Research estimates.

Competitive Advantages

Quality Combined With Competitive Prices

Cost control and a manufacturing facility with stringent quality control standards allow Deer Valley to provide a high-quality product at an attractive value. Multi-section homes sold for an average retail price ranging from \$59,000 to \$119,000 in 2005, excluding land costs. Deer Valley's objective is to have every customer provide word of mouth referrals due to a favorable buying experience. By focusing on the fastest-growing sector of the manufactured housing industry, giving attention to detail,

using quality components, and offering factory-provided trim-out options and service capabilities, the Company has differentiated itself competitively.

Concentration on High-end Feature-rich HUD Code Homes

By focusing manufacturing efforts exclusively on HUD Code homes on a cost-effective basis and by relying upon a strong network of regional independent dealers, the Company has been able to minimize administrative and marketing expenses while providing customers with a competitively priced product which maximizes the value/price relationship.

Experienced Cohesive Management Team with Extensive Industry Experience

The management team is made up of seasoned industry veterans in key leadership positions whose interests are closely aligned with those of shareholders. The core of this group has been together as an operating group for the last several years.

A Strong Network of Independent Dealers

Deer Valley has devoted considerable effort and resources to building a strong network of independent dealers who operate in a highly fragmented industry consisting of approximately 8,000 dealers in the United States. The Company does not own any company retail stores and does not provide any financial or insurance-related services which could significantly increase Deer Valley's administrative expenses. The Company cultivates close relationships with independent dealers and carefully monitors service responsibilities to customers. The Company endeavors to be extremely responsive to any dealer need or issue for which that the company can offer assistance. A side benefit is that in its entire time in business Deer Valley has never had a material dealer or customer dispute that was not resolved promptly.

Management Team

Charles G. Masters – CEO, President, and Chairman of Deer Valley Corporation

Mr. Masters was the founder of Deer Valley Acquisitions Corporation and led the smooth transition from a private to a public company. Since its inception in July 2005, he has served as its Chief Executive Officer. In March 1998, Mr. Masters founded and has since served as CEO and CFO of Bumgarner Enterprises, Inc., an oil and gas development and a business consulting firm. Since 2001, Mr. Masters has also served as Director, CEO, and CFO of Ranger Industries, Inc., a public company which is the sole shareholder of Bumgarner Enterprises. Mr. Masters has founded and served as the CEO and CFO of several private companies involved in the development of military electronic communications and test equipment, pioneering the introduction of microprocessors into point of sale equipment, medical equipment, artificial intelligence devices, and the development of laser scanners. Mr. Masters received a B.S. degree in electrical engineering (1961) from Duke University, a M.S. degree in electrical engineering (1964) from the University of Pittsburgh and a M.S. degree in materials science and engineering (1966) from Johns Hopkins University.

Joel Stephen Logan, II – Director, President, and General Manager of Deer Valley Homebuilders, Inc.

Mr. Logan has extensive experience in the manufactured home industry and provided key leadership bringing the Deer Valley Homebuilders team from a start up to the strong company it is today. Since 2004, Mr. Logan has served as General Manager and President for Deer Valley Homebuilders, Inc. From 1996 until 2003, Mr. Logan worked as President of Pinnacle Homes of Alabama, a manufactured housing company. Mr. Logan holds a B.S. in business administration from Mississippi State University.

Charles L. Murphree, JR. – Director, VP, and Regional Sales Director of Deer Valley Homebuilders, Inc.

Since April 2004, Mr. Murphree has worked as Regional Sales Director and Vice President of Deer Valley Homebuilders, Inc. From 2003 until 2004, Mr. Murphree served as Plant Manager for Clayton Homes, Inc. From 2000 through 2003, Mr. Murphree worked as General Manager of the Energy and LifeStyle Divisions of Southern Energy Homes, Inc. Mr. Murphree received a B.S. in business administration from the University of Alabama.

John Steven Lawler – Director and Director of Finance of Deer Valley Homebuilders, Inc.

Since April 2004, Mr. Lawler, a certified public accountant, has worked as Director of Finance for Deer Valley Homebuilders, Inc. From 2001 until 2004, he served as ERP and IT Project Manager for Cavalier Homes, Inc. From 1999 until 2001, Mr. Lawler worked as the ERP Team Leader for Financial Accounting for Cavalier Homes, Inc. Mr. Lawler holds a B.S. in business administration from the University of Alabama.

Independent Board of Directors

Hans Beyer, Director

Since February 2005, Mr. Beyer has served as a partner for Saxon Gilmore Carraway Gibbons Lash & Wilcox, P.A. At SGCG & W, P.A., he oversees and manages complex legal matters. Since September 2005, Mr. Beyer has served as the Senior Vice President of Mirabilis Ventures, Inc., where he oversees private equity investments. In addition, Mr. Beyer is President and Founder for Daedalus Consulting, Inc., which provides consulting advice on business matters. From 2003 to February 2005, Mr. Beyer was a partner at Buchanan Ingersoll, P.C. Prior to 2002, Mr. Beyer was the founder and President

of the Law Firm of Hans Christian Beyer, P.A. Mr. Beyer holds a B.A. from the University of Michigan and a J.D. from the University of Michigan Law School.

John Giordano, Director

For the past five years, Mr. Giordano has served as Chair of the Business, Tax, and Corporate Finance Practice Group at Bush Ross, P.A., a Tampa, Florida law firm. He is regularly involved in complex business-related transactions; has extensive experience in a broad range of areas, including federal and state securities law, corporate finance, mergers, acquisitions, and tax law; and has acted as general corporate counsel for numerous Florida-based public and private corporations. Mr. Giordano attended the University of Florida, where he received a B.S., a J.D., and an L.L.M. in taxation.

Dale Phillips, Director

For the past five years, Mr. Phillips has served as a director and Vice President of Finance for RE Purcell Construction Co., Inc., a paving and utility contractor. He is also a director and Vice President for Dalmari, Inc. Mr. Phillips holds an A.S. (1968) in business management from Champlain College and a B.A. (1971) in accounting from Castleton State College.

Financial Overview

Although management has pursued growth in an aggressive manner, the tactical approach to financing the venture has been quite conservative in our view and has been an important element in positioning the Company for future growth in a difficult market environment for many competitors. Several examples of prudent financial management practices stand out and demonstrate the focus of management on tight financial controls. Deer Valley as it is currently constituted was organized without taking on debt, which greatly increases the financial flexibility over firms with large debt burdens. Working capital elements are managed to maximize cost efficiency and beneficial relationships with vendors by combining cash payment for purchases to take all available discounts with timely vendor payments to ensure that deliveries can be obtained early in tight operating circumstances. The aggressive pursuit of purchase discounts, which are often negotiated higher and always taken, should allow Deer Valley to benefit from a lower sustained cost structure than many competitors. This is related to the Company's operations, which run at near capacity due to a variety of value-added strategies that are also differentiated from competitors that often are only able to run their facilities part time. In our view, this management team has demonstrated a differentiated approach that gives us additional confidence in the Company's ability to continue above market growth rates on a sustainable basis.

Risks**Industry Downturn**

In recent years, the manufactured housing industry experienced a prolonged and significant downturn as consumer lenders began to tighten underwriting standards and curtail credit availability in response to higher than anticipated rates of loan defaults and significant losses upon the repossession and resale of homes securing defaulted loans. According to the Manufactured Housing Institute, domestic shipments of manufactured homes peaked in calendar year 1998 with the shipment of 372,843 homes, before declining to a total of 130,802 manufactured homes in calendar year 2004. The manufactured housing industry's share of new single-family housing starts also increased to 24% in calendar year 1997 before declining to 7.5% of all new single-family housing starts in calendar year 2004. Other causes of the downturn include a reduced number of consumer lenders in the traditional chattel (home-only) lending sector and higher interest rates on home-only loans. These factors have resulted in declining wholesale shipments, excess manufacturing and retail locations, and surplus inventory.

Cyclical Trends

The manufactured housing industry is highly cyclical and is influenced by many national and regional economic and demographic factors, including:

- the availability of consumer financing for homebuyers;
- the availability of wholesale financing for retailers;
- consumer confidence;
- interest rates;
- demographic and employment trends;
- income levels;
- housing demand;
- general economic conditions, including inflation and recessions; and
- the availability of suitable home sites.

Intense Competition

The manufactured housing industry is highly competitive. The Company estimates that there are approximately 100 manufacturers in the U.S. in its industry and approximately 8,000 retail sales centers that sell manufactured homes. The ten largest manufacturers are estimated to account for approximately 80 percent of the sales in the manufactured housing market.

Geographic Concentration

In 2005, 100% of Deer Valley's revenues were generated from the southeastern and south central regions of the U.S. A decline in the demand for the manufactured housing in these states and regions and/or a decline in the economies of these regions could have a material adverse affect on sales and results of operations.

Government Regulations

Deer Valley's manufactured homes are subject to a number of federal, state, and local laws. Construction of manufactured housing is governed by the National Manufactured Housing Construction and Safety Standards Act of 1974 ("1974 Act"). In 1976, HUD issued regulations under the 1974 Act establishing comprehensive national construction standards. The HUD regulations cover all aspects of manufactured home construction, including structural integrity, fire safety, wind loads, thermal protection, plumbing, and electrical work. Such regulations preempt conflicting state and local regulations. Deer Valley's manufacturing facilities and the plans and specifications of its manufactured homes have been approved by a HUD-designated inspection agency. An independent, HUD-approved third-party inspector checks each of Deer Valley's manufactured homes for compliance during at least one phase of construction. In 1994, HUD amended manufactured home construction safety standards to improve the wind force resistance of manufactured homes sold for occupancy in coastal areas prone to hurricanes. Failure to comply with the HUD regulations could expose Deer Valley to a wide variety of sanctions, including closing Deer Valley's plants. Management believes its manufactured homes meet or surpass all present HUD requirements.

Manufactured, modular, and site-built homes are frequently built with particleboard, paneling, and other products which contain formaldehyde resins. Since February 1985, HUD has regulated the allowable concentration of formaldehyde in certain products used in manufactured homes and requires manufacturers to warn purchasers concerning formaldehyde-associated risks. Deer Valley currently uses materials in its manufactured homes which meet HUD standards for formaldehyde emissions and which otherwise comply with HUD regulations. In addition, certain components of manufactured homes are subject to regulation by the Consumer Product Safety Commission (CPSC), which is empowered to ban the use of component materials believed to be hazardous to health and to require the manufacturer to repair defects in components of its homes. The CPSC, the Environmental Protection Agency, and other governmental agencies are evaluating the effects of formaldehyde. In February 1983, the Federal Trade Commission adopted regulations requiring disclosure of manufactured homes' insulation specifications.

On-site installations of Deer Valley's manufactured homes are also subject to local zoning and housing regulations. Utility connections are subject to state and local regulation, and must be complied with by the dealer or other person installing the home. A number of states require manufactured and modular home producers to post bonds to ensure the satisfaction of consumer warranty claims. Several states have adopted procedures governing the installation of manufactured and modular homes. Deer Valley has complied with these requirements in Alabama, Mississippi, Louisiana, Arkansas, Georgia, Florida, Tennessee, Kentucky, Indiana, Illinois, Missouri, Oklahoma, and Texas. Many of these states require that companies renew their compliance or notify the state after a change in ownership. Deer Valley is taking the steps necessary to remain in compliance with these state laws.

Valuation Analysis

In its relatively brief history as a public entity Deer Valley has built an impressive track record of strong revenue growth and disciplined financial management that we expect to continue over our forecast horizon. Although some convertible preferred stock and a modest amount of long-term debt were issued to bring the Company public, we view the capital structure as appropriate given the strong track record to date and the growth prospects available over the next several years. In the near-term there is a depressing effect on earnings available to common shareholders and reported EPS throughout 2006. This short-term effect results from the GAAP accounting treatment of a non-recurring, non-cash item related to the valuation of the beneficial conversion features of the preferred stock sold by the Company during the first and second quarter of 2006. As part of the transaction to become public, the share count has increased significantly and some additional expenses have been incurred in order to position the Company for long-term success. This has rendered the absolute levels of prior period EPS and the growth trajectory incomparable and requires us to focus on earnings potential going forward. Over time, we expect the Company to grow into its higher outstanding share count and work past the short-term effects of preferred share issuances. One catalyst to accelerate this process and increase the revenue base would be a capacity expansion either through an acquisition or startup of a new factory, both of which we believe are being evaluated as options by management.

Due to these short-term factors and in the interest of a comparable analysis of the cash generating capacity of the business we use operating earnings in combination with a discounted cash flow analysis (DCF) to arrive at our firm valuation. Our DCF model, which uses approximately a 16% weighted average cost of capital, produces a target valuation of approximately \$2.30 per share. If we apply a multiple of 18X our FY2007 operating EPS estimate of \$0.17 we arrive at a price target of \$3.06. We combine these metrics to arrive at a blended target price of \$2.60, implying 30% upside potential from recent prices and supporting our rating of Speculative Buy.

Investment Conclusion

We believe that Deer Valley Corp. represents a potentially attractive opportunity at recent prices due to the very strong management team, improving near term industry dynamics, and a substantial long-term growth opportunity. In addition to the factors discussed in this report, we believe there are a number of additional catalysts that could accelerate the revenue growth rate and increase the scale of Deer Valley's operations. Although the Company began with an exclusive emphasis on multi-section homes, Deer Valley has recently added single-wide units to the product line, and we believe these are currently available on dealer lots. Additional growth opportunities, including capacity expansion and the possibility of entering the modular home segment, are expected to drive continued growth. We view the manufactured housing industry as an attractive secular growth opportunity for risk-tolerant equity investors.

Deer Valley Corp.		INCOME STATEMENT																							
(in \$, except EPS)		- Fiscal Year Ending December 31st -																							
	FY	Q1	Q2	Q3	Q4	FY	Q1	Q2	Q3	Q4	FY	Q1	Q2	Q3	Q4	FY	Q1	Q2	Q3	Q4	FY				
	2005	2006A	2006A	2006E	2006E	2006E	2007E	2007E	2007E	2007E	2007E	2008E	2008E	2008E	2008E	2008E	2008E	2008E	2008E	2008E	2008E	2008E			
Revenue	35,717,073	12,913,079	18,962,394	19,331,442	19,718,071	70,914,987	17,192,473	22,055,639	21,772,813	21,326,631	82,347,157	18,911,721	24,261,093	23,949,874	23,459,185	90,581,872	18,911,721	24,261,093	23,949,874	23,459,185	90,581,872	18,911,721	24,261,093	23,949,874	23,459,185
Cost of Sales	29,292,051	10,895,389	15,705,761	16,002,017	16,308,000	58,911,166	14,289,753	18,306,097	18,071,269	17,701,021	68,348,140	15,696,728	20,136,707	19,678,386	19,471,123	75,182,954	15,696,728	20,136,707	19,678,386	19,471,123	75,182,954	15,696,728	20,136,707	19,678,386	19,471,123
Total cost of goods sold	29,292,051	10,895,389	15,705,761	16,002,017	16,308,000	58,911,166	14,289,753	18,306,097	18,071,269	17,701,021	68,348,140	15,696,728	20,136,707	19,678,386	19,471,123	75,182,954	15,696,728	20,136,707	19,678,386	19,471,123	75,182,954	15,696,728	20,136,707	19,678,386	19,471,123
Gross Profit	6,425,021	2,017,690	3,246,634	3,329,426	3,410,071	12,003,821	2,922,720	3,749,442	3,701,344	3,625,610	13,999,017	3,214,993	4,124,386	4,071,479	3,988,061	15,398,918	3,214,993	4,124,386	4,071,479	3,988,061	15,398,918	3,214,993	4,124,386	4,071,479	3,988,061
Operating Expenses:	2,996,022	1,249,327	1,662,644	1,686,697	1,719,411	6,307,078	1,719,247	1,720,023	1,719,361	1,719,366	6,877,998	1,805,389	1,806,481	1,808,467	1,806,557	7,224,694	1,805,389	1,806,481	1,808,467	1,806,557	7,224,694	1,805,389	1,806,481	1,808,467	1,806,557
Selling, general and administrative	-	36,065	49,207	50,000	50,000	186,372	50,000	50,000	50,000	50,000	200,000	50,000	50,000	50,000	50,000	200,000	50,000	50,000	50,000	50,000	200,000	50,000	50,000	50,000	50,000
Depreciation, amortization & other op. exp.	-	1,285,992	1,701,951	1,735,697	1,769,411	6,492,450	1,769,247	1,770,023	1,769,361	1,769,366	7,077,998	1,855,389	1,856,481	1,858,467	1,856,557	7,424,694	1,855,389	1,856,481	1,858,467	1,856,557	7,424,694	1,855,389	1,856,481	1,858,467	1,856,557
Total Operating Expenses:	2,996,022	1,285,992	1,701,951	1,735,697	1,769,411	6,492,450	1,769,247	1,770,023	1,769,361	1,769,366	7,077,998	1,855,389	1,856,481	1,858,467	1,856,557	7,424,694	1,855,389	1,856,481	1,858,467	1,856,557	7,424,694	1,855,389	1,856,481	1,858,467	1,856,557
Operating Income	3,428,999	732,298	1,544,683	1,593,729	1,640,660	5,511,371	1,153,473	1,979,418	1,931,983	1,856,144	6,921,018	1,359,604	2,267,905	2,215,011	2,131,704	7,974,224	1,359,604	2,267,905	2,215,011	2,131,704	7,974,224	1,359,604	2,267,905	2,215,011	2,131,704
Other Income:	12,563	6,243	25,002	25,002	25,002	81,249	25,002	25,002	25,002	25,002	100,008	25,002	25,002	25,002	25,002	100,008	25,002	25,002	25,002	25,002	100,008	25,002	25,002	25,002	25,002
Interest Income	(74,903)	(13,867)	(21,799)	(30,000)	(30,000)	(95,665)	(30,000)	(30,000)	(30,000)	(30,000)	(120,000)	(30,000)	(30,000)	(30,000)	(30,000)	(120,000)	(30,000)	(30,000)	(30,000)	(30,000)	(120,000)	(30,000)	(30,000)	(30,000)	(30,000)
Other, net	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total Other Expense net	(62,341)	(7,624)	3,204	(4,998)	(4,998)	(14,416)	(4,998)	(4,998)	(4,998)	(4,998)	(19,992)	(4,998)	(4,998)	(4,998)	(4,998)	(19,992)	(4,998)	(4,998)	(4,998)	(4,998)	(19,992)	(4,998)	(4,998)	(4,998)	(4,998)
Pre-tax Income	3,366,658	724,674	1,547,887	1,588,731	1,635,662	5,496,955	1,148,475	1,974,420	1,926,985	1,851,146	6,901,026	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706
Income Taxes	-	261,173	559,422	578,298	595,381	1,994,274	418,045	718,689	701,422	673,817	2,511,974	493,077	823,698	804,445	774,121	2,895,341	493,077	823,698	804,445	774,121	2,895,341	493,077	823,698	804,445	774,121
Net Income	3,366,658	463,501	988,465	1,010,433	1,040,281	3,502,681	730,430	1,255,731	1,225,562	1,177,329	4,389,053	861,529	1,439,209	1,405,569	1,352,585	5,058,892	861,529	1,439,209	1,405,569	1,352,585	5,058,892	861,529	1,439,209	1,405,569	1,352,585
Preferred Dividends	-	113,086	128,696	128,696	128,696	499,174	128,696	128,696	128,696	129,696	515,784	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Beneficial Conversion	-	1,491,243	2,079,488	5,206,289	911,586	(8,777,030)	801,734	1,127,035	1,096,866	1,047,633	3,873,269	861,529	1,439,209	1,405,569	1,352,585	5,058,892	861,529	1,439,209	1,405,569	1,352,585	5,058,892	861,529	1,439,209	1,405,569	1,352,585
Net Income Available to Common Shares	-	(1,140,828)	(1,219,719)	(4,324,962)	(911,586)	(5,775,923)	1,148,475	1,974,420	1,926,985	1,851,146	6,901,026	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706
Reported Pre-tax Income	-	724,674	1,547,887	1,588,731	1,635,662	5,496,955	1,148,475	1,974,420	1,926,985	1,851,146	6,901,026	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706	7,954,232	1,354,606	2,262,907	2,210,013	2,126,706
<i>Weighted Average Shares Outstanding</i>																									
Basic	873,996	1,000,000	1,000,000	6,825,640	6,825,640	3,912,820	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640
Diluted	873,996	1,000,000	1,000,000	6,825,640	6,825,640	3,912,820	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640	6,825,640
<i>Earnings Per Share from Continuing Operations:</i>																									
Basic	\$3.85	(\$1.14)	(\$1.22)	(\$0.63)	\$0.13	(\$1.48)	\$0.09	\$0.17	\$0.16	\$0.15	\$0.57	\$0.13	\$0.21	\$0.21	\$0.20	\$0.74	\$0.13	\$0.21	\$0.21	\$0.20	\$0.74	\$0.13	\$0.21	\$0.21	\$0.20
Diluted	\$3.85	(\$1.14)	(\$1.22)	(\$0.63)	\$0.02	(\$1.48)	\$0.02	\$0.03	\$0.03	\$0.03	\$0.10	\$0.02	\$0.04	\$0.04	\$0.03	\$0.13	\$0.02	\$0.04	\$0.04	\$0.03	\$0.13	\$0.02	\$0.04	\$0.04	\$0.03
Operating EPS	\$3.85	\$0.73	\$1.54	\$0.23	\$0.04	\$1.41	\$0.03	\$0.05	\$0.06	\$0.05	\$0.17	\$0.03	\$0.06	\$0.05	\$0.05	\$0.17	\$0.03	\$0.06	\$0.06	\$0.05	\$0.17	\$0.03	\$0.06	\$0.06	\$0.05

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Analyst Highlight

Michael R. Anderegg, CFA, Senior Research Analyst

Information Security and Data Storage

In addition to his position as a Senior Research Analyst at Harbinger Research, Mr. Anderegg is currently President of MRA Research, an independent research and trading systems consulting firm. He holds the CFA Charter and is a member of the San Francisco and Twin Cities analyst societies. His most recent research position was Research Analyst covering the Network Security Software and Storage Industries for a sell-side technology research boutique in San Francisco. His previous employers include leading companies such as IDS-American Express, GE Capital and First American Asset management. His 20 years of financial analysis, management and investment experience includes fixed income trading, treasury management, private placements, equity analysis, and portfolio management.

He earned an MBA in Finance from the University of Minnesota and a BA in Economics from Hamline University. Mr. Anderegg is also a member of the Technical Securities Analysts Association of San Francisco.

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