

August 13, 2008

Key Metrics

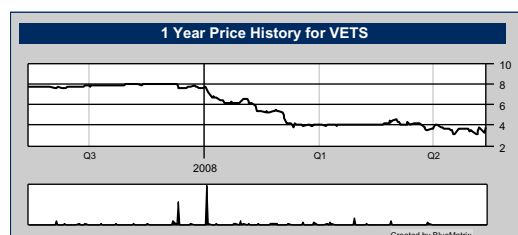
VETS - NASDAQ	\$3.75
Pricing Date	08/12/2008
Price Target	\$7.50
52-Week Range	\$8.04-\$3.00
Shares Outstanding (mm)	23.7
Market Capitalization (\$mm)	\$88.9
3-Mo Average Daily Volume	17,393
Institutional Ownership	42%
Debt/Total Capital	53.4%
ROE	NM
Book Value/Share	\$1.00
Price/Book	3.8x
Dividend Yield	NM
LTM EBITDA Margin	NM

EPS(\$) FY: December

	2007A	Prior 2008E	Curr. 2008E	Prior 2009E	Curr. 2009E
1Q-Mar	(0.21)	--	(0.13)A	--	--
2Q-Jun	(0.12)	(0.07)E	(0.08)E	--	--
3Q-Sep	(0.15)	--	(0.04)E	--	--
4Q-Dec	(0.16)	--	(0.01)E	--	--
FY	(0.64)	--	(0.26)E	--	0.28E
P/E	NM		NM		13.4x

Revenue(\$mm)

	2007A	Prior 2008E	Curr. 2008E	Prior 2009E	Curr. 2009E
1Q-Mar	17.4	--	17.8A	--	--
2Q-Jun	17.7	20.0E	19.0E	--	--
3Q-Sep	17.7	--	25.8E	--	--
4Q-Dec	16.4	--	29.1E	--	--
FY	69.3	92.7E	91.7E	--	150.8E



Company Description: Pet Rx Corporation (www.petdrx.com) Pet DRx Corporation provides primary veterinary and specialty care services to companion animals through a network of veterinary hospitals in California. Its services include general medical treatment for pets, including preventive care, such as vaccinations, examinations, spraying, and dental care; and a range of specialized diagnostic and medical services, such as x-ray, ultra-sound internal medicine, surgery, cardiology ophthalmology, dermatology, oncology, and other services.

Pet DRx Corporation

Rating: Buy

2Q08 Preview; Earnings Expected to Improve to (\$0.08); Buy

Investment Highlights:

- **Pet DRx plans to announce 2Q08 results after the close on Thursday, August 14, with a conference call to follow at 5:00 p.m. ET.** The dial-in number is (800) 232-9476 and the access code is 58134999.
- **Lowering our revenue estimates based on timing of acquisitions.** We are reducing our revenue expectations for 2Q08 by \$1mm to \$19mm based on the timing of certain acquisitions. Accordingly, our EPS estimate has been reduced by (\$0.01) to (\$0.08).
- **EPS of (\$0.08) expected to show significant improvement from LY.** We expect a 2Q08 EPS loss of \$0.08 per share to improve significantly from last year's actual 2Q07 loss of \$0.59 per share. On a pro forma basis, assuming acquisitions occurred as of January 1, 2007, we estimate EPS improve from (\$0.12).
- **New acquisitions should benefit "Hub and Spoke" business model.** Looking forward, we believe Pet DRx Corporation's "hub and spoke" network should continue to grow with additional acquisitions. Already, in 3Q08 the company completed the acquisition of Valley Animal Medical Center in Coachella Valley, CA. With the acquisition, Pet DRx Corporation increased its veterinary hospitals in Coachella Valley to eight. Further, in 3Q08, the company announced the signing of a definitive agreement to acquire a veterinary hospital in San Diego, CA, and signed letters of intent to acquire two additional veterinary hospitals in San Diego, CA, and San Jose, CA.
- **New store acquisitions trending slightly behind forecasts; long term growth plan appears on track.** While we are not reducing our 2H comparable store sales expectations and believe the acquisition pipeline remains strong, closings appear to be moving slower than anticipated and possibly will be weighted toward Q408-Q109 as opposed to Q308-Q408; therefore, our second-half projections could prove aggressive at this point. With that said, we continue to believe the company's long-term strategy to expand through acquisition remains intact and we maintain our Buy rating on the shares.

EQUITY RESEARCH

PetDRx (PDXC.OB)

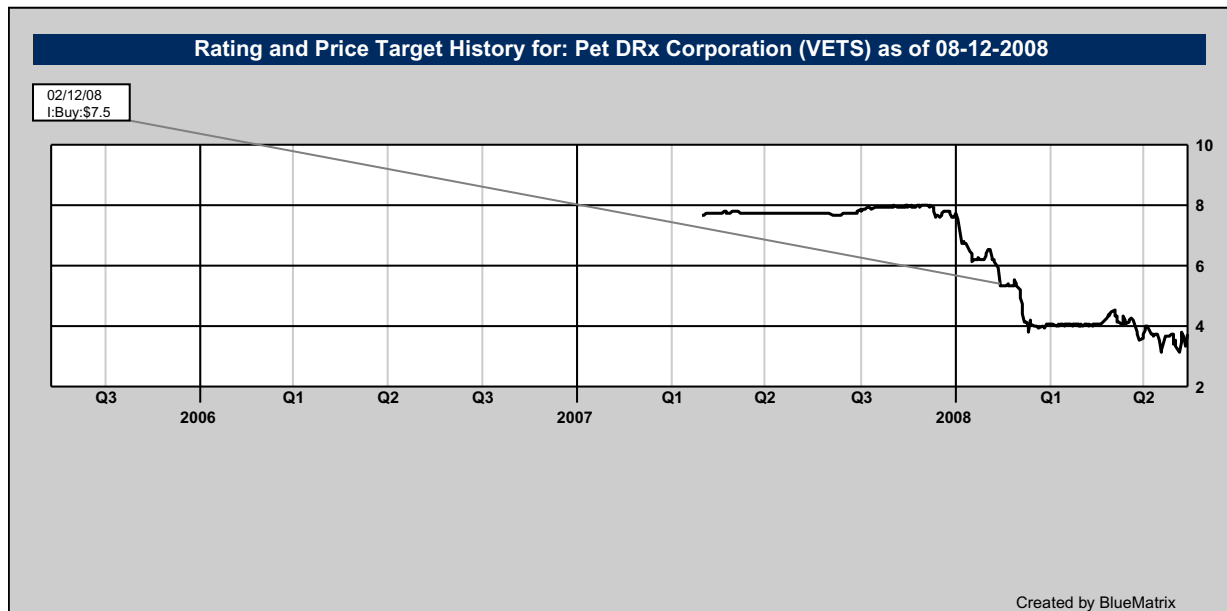
(In Millions, Except Per Share Data)

Quarter End	FY* 2006	Q1* Mar-07	Q2* Jun-07	Q3* Sep-07	Q4* Dec-07	FY* 2007	Q1 Mar-08	Q2E Jun-08	Q3E Sep-08	Q4E Dec-08	FYE 2008	FYE 2009
Sales	70.3	17.4	17.7	17.7	16.4	69.3	17.8	19.0	25.8	29.1	91.7	150.8
<i>% Increase</i>	NA	NA	NA	NA	NA	-1.4%	2.3%	7.2%	45.8%	77.1%	32.4%	64.4%
Cost of Goods Sold	67.4	17.1	16.9	16.2	15.6	65.9	16.1	16.3	21.9	24.7	79.1	125.4
<i>As % Sales</i>	95.9%	98.0%	95.3%	91.7%	95.2%	95.0%	90.4%	86.0%	85.0%	85.0%	86.3%	83.2%
<i>% Increase</i>	NA	NA	NA	NA	NA	-2.3%	-5.6%	-3.3%	35.1%	58.1%	20.2%	58.5%
Gross Profit	2.9	0.4	0.8	1.5	0.8	3.4	1.7	2.7	3.9	4.4	12.6	25.7
<i>Margin</i>	4.1%	2.0%	4.7%	8.3%	4.8%	5.0%	9.6%	14.0%	15.0%	15.0%	13.7%	17.0%
SG&A	4.7	4.5	3.0	3.7	3.4	14.6	3.8	3.7	3.6	3.4	14.5	14.0
<i>As % Sales</i>	6.7%	25.9%	16.9%	21.0%	20.4%	21.1%	21.3%	19.5%	14.0%	11.7%	15.8%	9.3%
<i>% Increase</i>	NA	NA	NA	NA	NA	NA	-16.2%	23.5%	-3.2%	1.5%	-0.7%	-3.4%
Operating Profit	(1.8)	(4.2)	(2.2)	(2.2)	(2.6)	(11.2)	(2.1)	(1.0)	0.3	1.0	(1.9)	11.7
<i>Margin</i>	-2.6%	-23.9%	-12.2%	-12.7%	-15.6%	-16.1%	-11.7%	-5.5%	1.0%	3.3%	-2.1%	7.8%
<i>% Increase</i>	NA	NA	NA	NA	NA	NA	50.1%	52.0%	112.0%	137.6%	83.1%	NA
Interest Expense	4.3	1.1	1.1	1.1	1.0	4.3	1.2	1.2	1.2	1.2	4.8	4.6
Other Income	2.0	0.7	0.7	0.0	0.0	1.3	0.2	0.4	0.0	0.0	0.6	0.0
Pretax Profit	(4.1)	(4.6)	(2.6)	(3.4)	(3.6)	(14.1)	(3.0)	(1.8)	(0.9)	(0.2)	(6.0)	7.1
<i>Margin</i>	-5.9%	-26.3%	-14.7%	-19.0%	-21.7%	-20.4%	-16.9%	-9.7%	-3.6%	-0.8%	-6.6%	4.7%
<i>% Increase</i>	NA	NA	NA	NA	NA	NA	34.1%	29.5%	72.4%	93.4%	57.4%	NA
Taxes(benefit)	0.2	0.2	0.2	0.0	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0
<i>Rate</i>	-5.1%	-3.6%	-6.3%	-0.4%	0.0%	-2.4%	-0.3%	0.0%	0.0%	0.0%	-0.2%	0.0%
Net Income--Oper.	(4.4)	(4.7)	(2.8)	(3.4)	(3.6)	(14.5)	(3.0)	(1.8)	(0.9)	(0.2)	(6.0)	7.1
<i>Margin</i>	-6.2%	-27.2%	-15.6%	-19.1%	-21.7%	-20.9%	-17.0%	-9.7%	-3.6%	-0.8%	-6.6%	4.7%
<i>% Increase</i>	NA	NA	NA	NA	168.7%	NA	36.2%	33.7%	72.5%	93.4%	58.3%	NA
EPS--Operations	(0.20)	(0.21)	(0.12)	(0.15)	(0.16)	(0.64)	(0.13)	(0.08)	(0.04)	(0.01)	(0.26)	0.28
<i>% Increase</i>	NA	NA	NA	NA	NA	NA	36.3%	33.9%	72.5%	93.6%	58.9%	NA
Shares Out. Diluted	21.6	22.7	22.7	22.7	22.5	22.5	22.8	22.8	22.8	23.0	22.8	25.0

Source: Company reports and Morgan Joseph estimates

* Pro Forma adjustments give effect as if XLNT acquired operations January 1, 2006

Required Disclosures



Price Target

Our price target is \$7.50.

Valuation Methodology

Our \$7.50 price target is based off of a 2x multiple on our 2008 sales projection. We derive our \$7.50 price target off of a 2x price-to-sales multiple, which is based off of recent acquisition activity within the veterinarian health care industry. Recent trends suggest to us that individual hospitals (similar to the compensation paid by PetDRx for its 26 acquisitions) are closing at a multiple of roughly 1x sales. Larger deals that include multiple hospitals have utilized a multiple closer to 2x sales. Thus, based off of our expectation that PetDRx should add roughly 15 to 20 hospitals in 2008 and expand sales by upwards of \$100mm, we believe 2x sales is a more appropriate multiple at this point.

Risk Factors

- **Growth strategy is highly dependent upon acquisitions.** Pet DRx's growth strategy is primarily dependent upon identifying and acquiring hospitals within geographically targeted territories. If the company cannot implement this growth strategy, results could be adversely affected and investors' growth expectations could fail to be met.
- **Long-term growth could be dependent upon generating additional financing.** As mentioned above, we believe Pet DRx has the capacity to add 20 to 30 acquisitions with current cash balances. Should the company fail to generate additional financing, long-term revenue gains could fall short of expectations.
- **Change of ownership could negatively impact core customer base.** While we believe the company targets hospitals with established customer bases and typically retains key employees, there is no guarantee that past customer traffic will translate to future business.
- **Some competitors are larger than Pet DRx.** Some of Pet DRx's competitors generate superior sales and production rates to that of the company. Should larger competitors outspend or significantly reduce price points to attain market share, sales and earnings could be negatively impacted.
- **An inability to attract and retain skilled personnel may cause disruption in business.** As the pet population is expected to grow, the need for skilled veterinarians should increase and become more competitive. If Pet DRx is unable to retain an adequate number of skilled veterinarians, the company could lose customers and subsequent revenue streams.
- **An economic downturn could negatively impact the business.** While the pet-care industry has proven to be relatively recession resistant, Pet DRx's business could be adversely impacted by negative or unfavorable trends in the general economy.

- **The possible implementation of pet insurance could adversely affect its business.** While more expansive options for pet insurance could increase the number of customers capable of utilizing veterinarians, fees associated with various administrative requirements related to the submission and processing of claims could result in delayed payments and reduced profits. One of the key advantages to the pet health industry relative to human health care is that for the most part, pet health is largely a "cash" business, where receivables are generally low. Once insurance carriers are involved in claims processing, we believe the potential for receivables default may increase, ultimately hurting the company's bottom line.

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Rating	Investment Banking Services/Past 12 Mos.	
	Percent	Percent
BUY [B]	56.82	36.00
HOLD [H]	42.05	29.73
SELL [S]	1.14	0.00

Meaning of Ratings

- A) Buy means reasonable outperformance relative to the market over 12-18 months.
- B) Hold means market-type risk adjusted performance; potential source of funds.
- C) Sell means expected to underperform the market.

Other Disclosures

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