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## Better Choice Company Inc. (NYSE AM: BTTR)

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### Buy: Halo Elevate Launched. Reiterate Buy and \$10 Price Target

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Better Choice hit another important milestone with the launch of Halo Elevate, a super-premium pet food that will be available in over 2,000 retail outlets in the United States. We reiterate our \$10 target based on an EV/sales multiple of 4x our 2023 sales estimate of \$80 million. We expect growth in the company's e-commerce, brick and mortar and international segments will result in top-line growth of over 40% this year and rapidly expanding margins.

Management delivered on another important milestone with the launch of Halo Elevate, a super-premium pet food brand available in over 2,000 retail outlets in the United States. Halo Elevate includes 39 SKUs of dry and wet food for dogs and will be available at Petco, Pet Supplies Plus and neighborhood pet stores.

The company's goal is to increase sales from brick-and-mortar outlets from about \$15 million annually to \$25 million annually. The Halo Elevate launch is critical to achieving this goal. Previously, the company had indicated Halo Elevate would be available at 600 Pet Supplies Plus stores beginning in April and at 900 Petco stores beginning June/July. The launch announcement is consistent with, or a bit better, than that goal. Better Choice has targeted sales of \$200 per week per store twelve months after launch, which equates to \$21 million in annual sales for the 2,000 stores now committed to carry Halo Elevate.

International sales are projected to reach \$14 to \$15 million this year, about 30% of total sales and up from \$8.6 million in 2020. Better Choice is targeting 30% top line growth for the next few years in international markets and \$25 million in sales withing five years. The company has \$100M in purchase agreements to support this goal and plans to enter additional markets in the coming quarters.

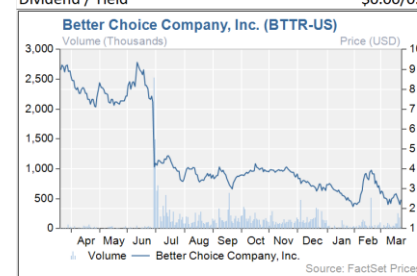
We project gross margins to improve this year. Margins were pressured in 2021 by supply issues, inability of the company's manufacturing partner to keep up with demand and cost increases. Two new manufacturing partners have been signed and have begun production. This and price increases are expected to result in significantly improved gross margin beginning this quarter.

We believe pet food sales will be less impacted than other major consumer expenditures by the Fed's tighter monetary policy. The pandemic has changed work-from-home habits for a generation and increased the number of pets and demand for pet food, particularly demand for premium food. We believe a mix shift to premium food is driven by the humanization of pets, greater time at home, lower birth rates and substantial cash balances on consumer's balance sheets.

**Valuation:** An EV/Sales multiple of 4x applied to our 2023 revenue estimate results in a price target range of \$10 to \$12 per share. The low end of the range assumes exercise of the company's warrants. Our \$10 price target uses the 4x EV/Sales multiple and assumes exercise of the company's warrants.

**Risks:** Risks to achieving our price target include an interruption in the economic recovery, less expansion in the domestic retail channel than we project, Asian distributors not meeting their minimum purchase obligations, cost increases impacting margins and greater time and resources needed to meet sales objectives.

Current Price	\$2.46		
Price Target	\$10.00		
Estimates	F2020A	F2021E	F2022E
Revenues (\$000s)	\$ 42,590	\$ 46,165 E	\$ 64,769
1Q March	\$ 12,226	\$ 10,830 A	\$ 13,149
2Q June	\$ 9,941	\$ 10,989 A	\$ 16,109
3Q September	\$ 11,135	\$ 13,200 A	\$ 17,385
4Q December	\$ 9,288	\$ 11,146 E	\$ 18,127
	F2020A	F2021E	F2022E
EBITDA (\$000s)	\$ (16,634)	\$ (10,845)E	\$ (4,563)
1Q March	\$ (5,591)	\$ (2,183)A	\$ (2,672)
2Q June	\$ (9,071)	\$ (2,471)A	\$ (1,284)
3Q September	\$ (1,306)	\$ (2,876)A	\$ (452)
4Q December	\$ (666)	\$ (3,315)E	\$ (155)
EV/Sales	1.2 x	1.1 x	0.8 x
EV/EBITDA	(3.0) x	(4.5) x	(10.8) x
<b>Stock Data</b>			
52-Week Range	\$2.11	-	\$9.72
Shares Outstanding (mil.)	29.2		
Market Capitalization (mil.)	\$72		
Enterprise Value (mil.)	\$49		
Debt to Capital	1%		
Cash (mil.)	\$33		
Cash/Share	\$1.14		
Average Three Months Trading Volume (K)	350		
Insider Ownership	32.6%		
Institutional Ownership	29.1%		
Short interest (mil.)	0.3%		
Dividend / Yield	\$0.00/0.0%		



We think the company has significant growth potential. Apart from the pet food market's two mega, mass-market suppliers, Nestlé's Purina and Mars which serve about 45% of the global pet food market, the rest of the market is highly fragmented. We believe this offers opportunities for well-managed and well-financed companies, such as Better Choice, to gain share organically and through acquisitions. We expect the pet food market will grow far in excess of nominal growth in the U.S. driven by increased pet ownership, higher income, and migration to bigger houses, on larger lots. The pandemic has boosted growth as more people work from home and have more opportunity to care for pets.

The company is led by an experienced and deep management team with a history of success in consumer products and pet food. Recent additions include experienced e-commerce and marketing talent. We also believe the company has the financial resources necessary to accomplish its goals, with over \$33 million in cash.

The company is re-launching its offering to the brick-and-mortar distribution channel this year and has signed an agreement to launch in 600 Pet Supplies Plus stores in Q1, 900 Petco stores in Q2/Q3 and through its distribution agreement with Phillips Pet Food & Supplies more than 500 independent pet food stores as early as March. We expect additional specialty and independent store launches for the Halo Elevate brand. This product re-launch is expected to drive revenue growth sharply higher in this channel over our forecast horizon.

Better Choice has also signed minimum purchase agreements with its Asian distributors valued at \$100 million over the next 4-5 years. This is a key component of our revenue projections. Demand for pet food and increased pet ownership is increasing in international markets, particularly in China, where household pet ownership is much lower than the level in the U.S.

### Financial model

The company's long-term financial model is a gross margin of 40% to 45%, contribution margin of 20% to 25% and long-term EBITDA margin of 10% to 15%. We believe the company can exit 2023 at or near these target ranges. The company was at the low end of the gross margin target range in 2020 but experienced cost pressure, supply constraints and shortfalls by its manufacturing partner. However, price increases and new manufacturing partners should alleviate much of the issues faced recently.

	2020	2021E	Target
Annual sales (\$M)	\$42.6	\$46.2	\$85 net/\$100 gross
Gross margin	40%	36%	40%-45%
EBITDA	\$(16.6)	\$(10.8)	10%-15%

Source: Better Choice and Dawson James Securities estimates

The company also has a goal of achieving \$100 million in gross annual sales within the next 3 years. This would equate to about \$85 million in net sales (gross sales less allowances and discounts), or a 25% CAGR from 2020. As mentioned above, higher growth is expected from the brick-and-mortar and international channels, with still strong growth from e-commerce and DTC.

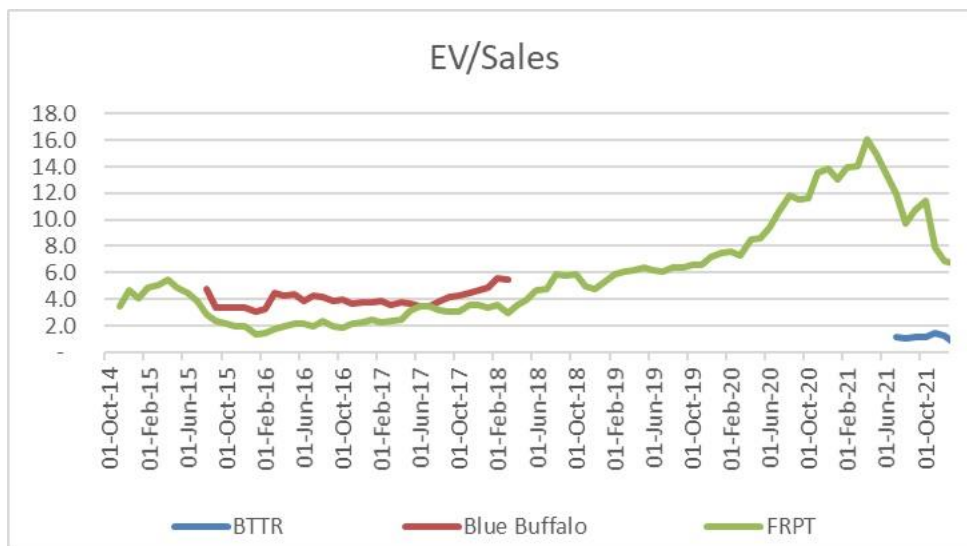
### Valuation

Freshpet is the closest and most relevant comp to Better Choice. There are retailers in the pet business, but their margin and growth profiles are much different from Better Choice's. The pet food businesses of J.M. Smucker, General Mills, Colgate, Spectrum Brands and Nestlé are parts of larger businesses and have much lower expected growth relative to Better Choice.

The chart below shows historical EV/Sales data for Freshpet, Blue Buffalo (while it was public) and Better Choice. Blue Buffalo had a similar growth, margin and market focus to Better Choice, so we believe its multiple history is relevant to where we believe Better Choice's shares could trade.

From August 2015 through March of 2018, the average EV/Sales based on forward-12-month sales estimates for Blue Buffalo was 4.0x. During this same period, Freshpet's shares traded at an average EV/Sales of 2.5x. From March 2018, when Blue Buffalo was acquired, through February 2020, when the pandemic began to have an impact on the market, Freshpet's shares traded at an average EV/Sales of 5.9x, and since March 2020, have traded at an average of 11.8x.

We believe the Blue Buffalo and Freshpet pre-pandemic average multiples are the most relevant for Better Choice's valuation. Growth is similar, as are margins. An EV/Sales multiple of 4x applied to our 2023 Better Choice revenue estimate results in a price target range of \$10 to \$12 per share. The low end of the range assumes exercise of the company's warrants. Our \$10 price target uses the 4x EV/Sales multiple and assumes exercise of the company's warrants.



Source: FactSet and Dawson James Securities estimates

### Risk Analysis

Risks to achieving our price target include an interruption in the economic recovery, less expansion in the domestic retail channel than we project, Asian distributors not meeting their minimum purchase obligations, cost increases impacting margins and greater time and resources needed to meet sales objectives.

**Exhibit 1. Income Statement**

(\$ in 000's) (except per share data)	31-Dec-19 2019 A	31-Dec-20 2020 A	31-Mar-21 Q1 21 A	30-Jun-21 Q2 21 A	30-Sep-21 Q3 21 A	31-Dec-21 Q4 21 E	31-Dec-21 2021 E	31-Dec-22 2022 E	31-Dec-23 2023 E
Revenue	15,577	42,590	10,830	10,989	13,200	11,146	46,165	63,928	79,910
COGS	9,717	26,491	6,556	7,089	8,762	7,356	29,763	39,205	45,863
Gross Profit	5,860	16,099	4,274	3,900	4,438	3,790	16,402	24,723	34,047
Gross margin	38%	40%	39%	35%	34%	34%	36%	39%	43%
G&A	19,782	25,966	4,551	3,530	3,727	3,500	15,308	14,560	15,142
Share-based comp	10,280	8,940	2,525	332	660	660	4,177	2,000	2,400
Sales and marketing	10,138	7,892	2,336	3,235	4,018	4,018	13,607	16,715	17,383
Other	1,097	623	0	0	0	0	0	0	0
Impairment	889	0	0	0	0	0	0	0	0
Opex	42,186	43,421	9,412	7,097	8,405	8,178	33,092	33,275	34,926
Operating Income	(36,326)	(27,322)	(5,138)	(3,197)	(3,967)	(4,388)	(16,690)	(8,552)	(879)
Interest Expense	670	9,247	835	2,234	79	79	3,227	316	316
Loss on extinguishment of debt	0	88	394	(851)	0	0	(457)	0	0
Loss on acquisitions	147,376	0	0	0	0	0	0	0	0
Change in fair value of warrant liability	90	22,678	6,483	(29,356)	(590)	0	(23,463)	0	0
Net Income	(184,462)	(59,335)	(12,850)	24,776	(3,456)	(4,467)	4,003	(8,868)	(1,195)
Preferred dividends	109	103	0	0	0	0	0	0	0
Net to common	(184,571)	(59,438)	(12,850)	24,776	(3,456)	(4,467)	4,003	(8,868)	(1,195)
Basic Shares	5,540	8,181	9,588	11,127	29,467	29,241	19,856	30,241	32,241
Diluted Shares	5,540	8,181	9,588	21,389	29,467	29,241	22,421	30,241	32,241
Basic EPS	\$ (33.32)	\$ (7.27)	\$ (0.22)	\$ 2.23	\$ (0.12)	\$ (0.15)	\$ 0.20	\$ (0.29)	\$ (0.04)
Diluted EPS	\$ (33.32)	\$ (7.27)	\$ (0.22)	\$ 1.16	\$ (0.12)	\$ (0.15)	\$ 0.18	\$ (0.29)	\$ (0.04)
Depreciation and Amortization	171	1,748	411	413	431	413	1,668	1,652	1,652
Stock Comp	10,280	8,940	2,544	313	660	660	4,177	2,000	2,400
EBITDA	(25,875)	(16,634)	(2,183)	(2,471)	(2,876)	(3,315)	(10,845)	(4,900)	3,173
Margin	NM	-39.1%	-20.2%	-22.5%	-21.8%	-29.7%	-23.5%	-7.7%	4.0%

Source: Better Choice Company Inc. and Dawson James Securities estimates



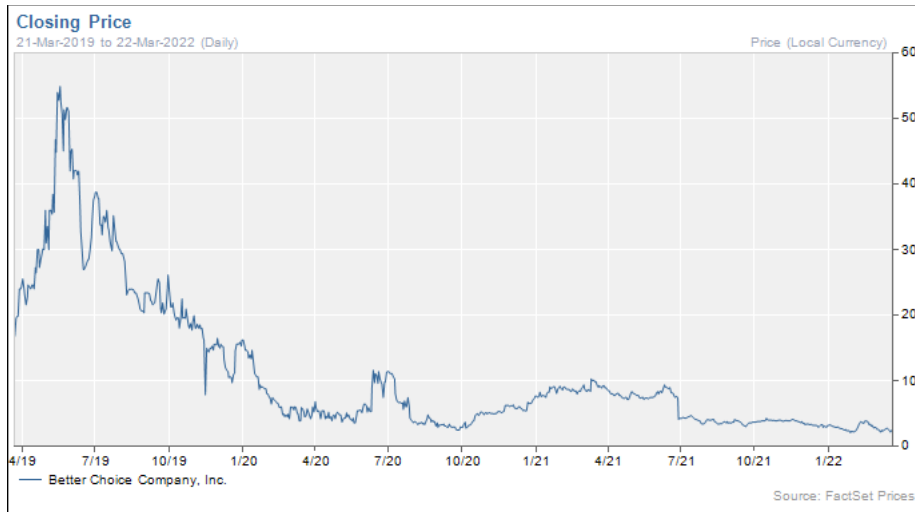
**Exhibit 2. Balance Sheet and Cash Flow Statement**

(\$ in 000's)	31-Dec-19 2019	31-Dec-20 2020	31-Dec-21 2021 E	31-Dec-22 2022 E	31-Dec-23 2023 E
Cash	2,361	3,926	21,567	12,540	13,302
Restricted Cash	173	63	7,213	7,213	7,213
A/R	5,824	4,631	5,573	8,643	10,804
Inventory	6,580	4,869	6,130	8,643	10,084
Prepaid expenses and other	2,641	4,074	3,146	4,879	6,099
<b>Current Assets</b>	<b>\$ 17,579</b>	<b>\$ 17,563</b>	<b>\$ 43,629</b>	<b>\$ 41,919</b>	<b>\$ 47,502</b>
PP&E	417	252	168	168	168
Right-of-use assets	951	345	68	68	68
Intangible assets	14,641	13,115	11,586	10,059	8,532
Goodwill	18,614	18,614	18,614	18,614	18,614
Other assets	1,330	1,364	114	114	114
<b>Total Assets</b>	<b>\$ 53,532</b>	<b>\$ 51,253</b>	<b>\$ 74,180</b>	<b>\$ 70,942</b>	<b>\$ 74,998</b>
Short term loan	16,061	7,826	780	780	5,559
Line of credit	4,819	0	0	0	4,846
PPP loans	0	190	0	0	0
Other liabilities	500	47	0	0	0
A/P	4,049	3,137	3,417	5,300	6,625
Accrued liabilities	4,721	3,003	1,357	2,104	2,631
Deferred revenue	311	350	0	0	0
Operating lease	345	173	52	52	52
Warrant derivative liab.	2,220	39,850	0	0	0
<b>Current Liabilities</b>	<b>\$ 33,026</b>	<b>\$ 54,576</b>	<b>\$ 5,606</b>	<b>\$ 8,236</b>	<b>\$ 19,712</b>
Notes payable	16,370	18,910	0	0	0
Term loans	0	0	4,779	4,779	0
Line of credit	0	5,023	4,846	4,846	0
PPP loans	0	662	0	0	0
Operating lease liab.	641	184	19	19	19
Series E Cv. Preferred	10,566	0	0	0	0
<b>Total Stockholders' Equity</b>	<b>(7,071)</b>	<b>(28,102)</b>	<b>58,930</b>	<b>53,062</b>	<b>55,267</b>
<b>Total Liabilities &amp; Equity</b>	<b>\$ 53,532</b>	<b>\$ 51,253</b>	<b>\$ 74,180</b>	<b>\$ 70,942</b>	<b>\$ 74,998</b>
	31-Dec-19 2019	31-Dec-20 2020	31-Dec-21 2021 E	31-Dec-22 2022 E	31-Dec-23 2023 E
Net Income	(184,571)	(59,438)	4,003	(8,868)	(1,195)
Depreciation and amort.	171	1,748	1,668	1,652	1,652
Share-based comp.	10,280	8,940	4,177	2,000	2,400
Working Capital and other	153,151	41,245	(22,617)	(4,686)	(2,970)
<b>Operating CF</b>	<b>\$ (20,969)</b>	<b>\$ (7,505)</b>	<b>\$ (12,769)</b>	<b>\$ (9,902)</b>	<b>\$ (113)</b>
Capex	(110)	(151)	(155)	(125)	(125)
Acquisitions	(20,097)	0	0	0	0
<b>Investing Activities</b>	<b>\$ (20,207)</b>	<b>\$ (151)</b>	<b>\$ (155)</b>	<b>\$ (125)</b>	<b>\$ (125)</b>
Equity	20,333	19,101	40,583	1,000	1,000
Debt	19,431	(9,990)	(2,867)	0	0
<b>Financing</b>	<b>\$ 39,764</b>	<b>\$ 9,111</b>	<b>\$ 37,716</b>	<b>\$ 1,000</b>	<b>\$ 1,000</b>
<b>Change in Cash</b>	<b>\$ (1,412)</b>	<b>\$ 1,455</b>	<b>\$ 24,791</b>	<b>\$ (9,027)</b>	<b>\$ 762</b>

Source: Better Choice Company Inc. and Dawson James Securities estimates

## **Important Disclosures:**

### **Price Chart:**



### **Price target and ratings changes over the past three years:**

Initiated – Buy – August 31, 2021 – Price Target \$10.00  
 Update – Buy – October 19, 2021 – Price Target \$10.00  
 Update – Buy – November 11, 2021 – Price Target \$10.00  
 Update – Buy – February 11, 2022 – Price Target \$10.00  
 Update – Buy – March 23, 2022 – Price Target \$10.00

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Current as of... 15-Mar-22

	<b>Company Coverage</b>		<b>Investment Banking</b>	
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Market Outperform (Buy)	31	74%	4	13%
Market Perform (Neutral)	11	26%	0	0%
Market Underperform (Sell)	0	0%	0	0%
Total	42	100%	4	10%

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