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Better Choice Company Inc. (NYSE AM: BTTR)

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Buy: Q4 Results. Reiterate Buy and \$10 Price Target

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Q4 results were a bit lower than we forecast, but Q1 is expected to be much higher than anticipated. We reiterate our \$10 target based on an EV/sales multiple of 4x our 2023 sales estimate of \$82 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.

Q4 revenue of \$11.0 million was in line with our \$11.1 million estimate, while continued supply chain issues, and the transition to new manufacturing partners resulted in lower-than-expected gross margin. The company guided to gross sales growth of 40%, or over \$18.5 million, which should translate into net sales exceeding \$15 million in Q1. Gross margin is modeled to improve as the year progresses due to changes in manufacturing partners and price increases.

Halo Elevate, a super-premium pet food brand, will be 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 amount of shelf space allocated for Halo Elevate by its retail partners has increased and this is another good sign for the launch. 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 grew 227% in Q4 and 71% for the year. International sales are projected to exceed \$20 million this year, up over 35%. Better Choice is targeting 30% top line growth for the next few years in international markets and \$25 million in annual sales within five years. The company has \$100M in purchase agreements to support this goal and plans to enter additional markets in the coming quarters.

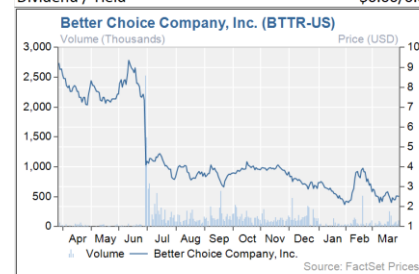
We project gross margins to improve this year. Margins were pressured in 2021 by supply issues, inability of the company's manufacturing partner to keep up with demand and cost increases. Two new manufacturing partners have been signed and have begun production. This and price increases are expected 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	\$2.51		
Price Target	\$10.00		
Estimates	F2021A	F2022E	F2023E
Revenues (\$000s)	\$ 46,006	\$ 64,311 E	\$ 82,159
1Q March	\$ 10,830	\$ 15,383 E	\$ 19,500
2Q June	\$ 10,989	\$ 15,473 E	\$ 19,841
3Q September	\$ 13,200	\$ 16,949 E	\$ 21,686
4Q December	\$ 10,987	\$ 16,506 E	\$ 21,133
	F2021A	F2022E	F2023E
EBITDA (\$000s)	\$ (11,475)	\$ (3,126)E	\$ 5,843
1Q March	\$ (2,183)	\$ (1,443)E	\$ 718
2Q June	\$ (2,471)	\$ (1,102)E	\$ 1,056
3Q September	\$ (2,876)	\$ (202)E	\$ 2,048
4Q December	\$ (3,945)	\$ (379)E	\$ 2,021
EV/Sales	1.2 x	0.9 x	0.7 x
EV/EBITDA	(4.8) x	(17.6) x	9.4 x
Stock Data			
52-Week Range	\$2.11	-	\$9.72
Shares Outstanding (mil.)	29.4		
Market Capitalization (mil.)	\$74		
Enterprise Value (mil.)	\$55		
Debt to Capital	1%		
Cash (mil.)	\$29		
Cash/Share	\$0.99		
Average Three Months Trading Volume (K)	152		
Insider Ownership	32.5%		
Institutional Ownership	28.9%		
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 GDP 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 almost \$29 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, 900 Petco stores and through its distribution agreement with Phillips Pet Food & Supplies more than 500 independent pet stores. The company expects Halo Elevate will be available in more than 1500 pet stores by the end of April and more than 2000 stores by the end of July. 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.

Q4 Results

Q4 21						
(\$ in 000's)						
	Actual		Estimates		Delta	% Delta
Revenue	\$	10,987	\$	11,146	\$ (159)	-1%
COGS		8,231		7,356		
Gross Profit		2,756		3,790	(1,034)	-27%
Gross margin		25.1%		34.0%		
SG&A		7,110		8,178		
Opex		7,733		8,178	(445)	-5%
Operating Income	\$	(4,977)	\$	(4,388)	\$ (589)	-13%
Interest Expense		69		79		
Pretax Income	\$	(5,046)	\$	(4,467)	\$ (579)	-13%
Taxes		37		0		
Net to common	\$	(5,083)	\$	(4,467)	\$ (616)	-14%
Diluted Shares		29,241		29,241		
Diluted EPS	\$	(0.17)	\$	(0.15)		
Depreciation and Amortization		409		413		
Stock Comp		623		660		
EBITDA	\$	(3,945)	\$	(3,315)	\$ (630)	-19%
Margin		-35.9%		-29.7%		
		2022E		2023E		
		Old	New	Old	New	
Revenue (\$M)	\$	64.8	\$ 64.3	\$ 80.7	\$ 82.2	
EPS	\$	(0.28)	(0.23)	(0.02)	\$ 0.05	
EBITDA (\$M)	\$	(4.6)	\$ (3.1)	\$ 3.6	\$ 5.8	

Source: Better Choice and Dawson James Securities estimates

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.

	2021A	2022E	Target
Annual sales (\$M)	\$46.0	\$64.3	\$85 net/\$100 gross
Gross margin	33%	39%	40%-45%
EBITDA	\$(11.5)	\$(3.1)	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.

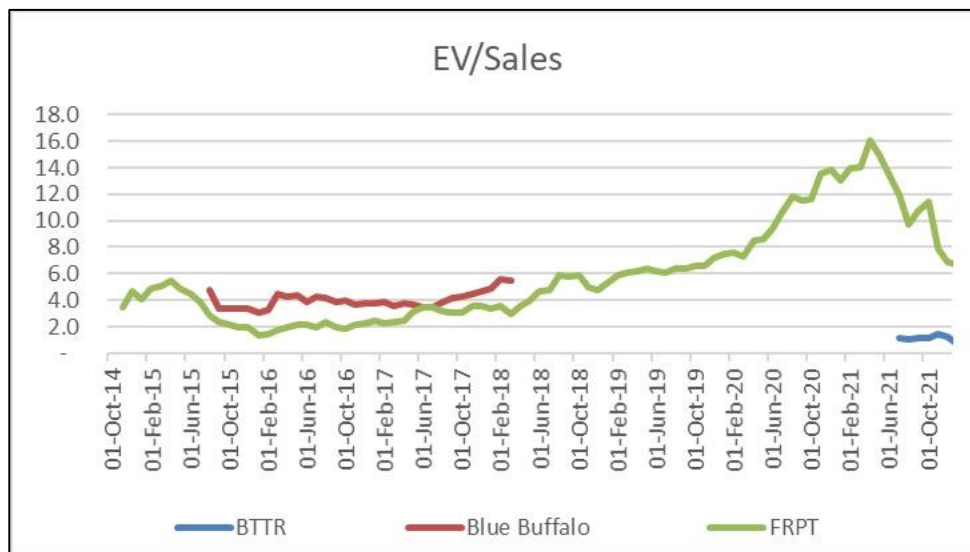
Valuation

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-Dec-21 2021 A	31-Mar-22 Q1 22 E	30-Jun-22 Q2 22 E	30-Sep-22 Q3 22 E	31-Dec-22 Q4 22 E	31-Dec-22 2022 E	31-Dec-23 2023 E
Revenue	15,577	42,590	46,006	15,383	15,473	16,949	16,506	64,311	82,159
COGS	9,717	26,485	30,638	9,845	9,593	10,169	9,904	39,511	47,208
Gross Profit	5,860	16,105	15,368	5,538	5,880	6,780	6,603	24,800	34,951
Gross margin	38%	38%	33%	36%	38%	40%	40%	39%	43%
SG&A	34,487	34,487	28,507	7,394	7,394	7,394	7,394	29,578	30,761
Share-based comp	10,280	8,940	4,140	500	500	500	500	2,000	2,400
Impairment	889	0	0	0	0	0	0	0	0
Opex	45,656	43,427	32,647	7,894	7,894	7,894	7,894	31,578	33,161
Operating Income	(39,796)	(27,322)	(17,279)	(2,356)	(2,015)	(1,115)	(1,292)	(6,778)	1,791
Interest Expense	670	9,247	3,217	69	69	69	69	276	276
Loss on extinguishment of debt	0	88	(457)	0	0	0	0	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	(23,463)	0	0	0	0	0	0
Net Income	(184,462)	(59,335)	3,387	(2,425)	(2,084)	(1,184)	(1,361)	(7,054)	1,515
Preferred dividends	109	103	0	0	0	0	0	0	0
Net to common	(184,571)	(59,438)	3,387	(2,425)	(2,084)	(1,184)	(1,361)	(7,054)	1,515
Basic Shares	5,540	8,181	19,856	29,303	29,615	30,115	30,615	29,912	31,865
Diluted Shares	5,540	8,181	22,421	29,303	29,615	30,115	30,615	29,912	31,865
Basic EPS	\$ (33.32)	\$ (7.27)	\$ 0.17	\$ (0.08)	\$ (0.07)	\$ (0.04)	\$ (0.04)	\$ (0.24)	\$ 0.05
Diluted EPS	\$ (33.32)	\$ (7.27)	\$ 0.15	\$ (0.08)	\$ (0.07)	\$ (0.04)	\$ (0.04)	\$ (0.24)	\$ 0.05
Depreciation and Amortization	171	1,748	1,664	413	413	413	413	1,652	1,652
Stock Comp	10,280	8,940	4,140	500	500	500	500	2,000	2,400
EBITDA	(29,345)	(16,634)	(11,475)	(1,443)	(1,102)	(202)	(379)	(3,126)	5,843
Margin	NM	-39.1%	-24.9%	-9.4%	-7.1%	-1.2%	-2.3%	-4.9%	7.1%

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

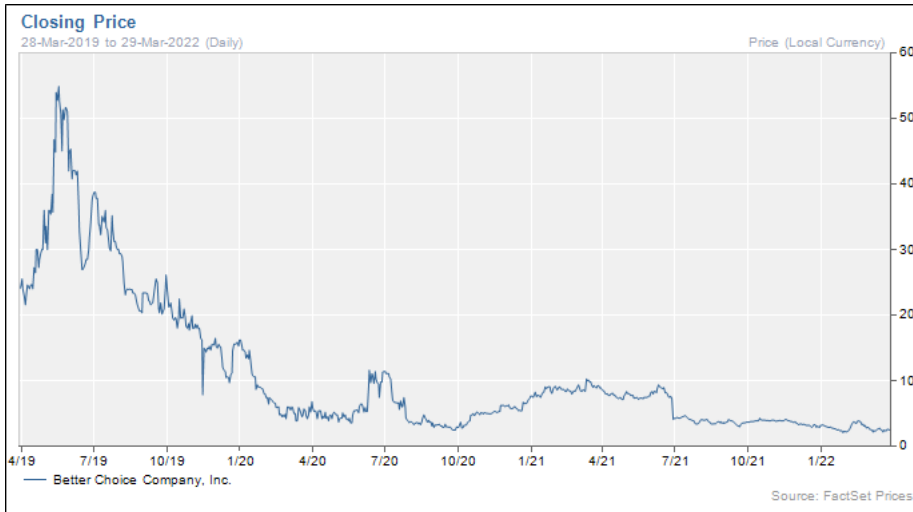
Exhibit 2. Balance Sheet and Cash Flow Statement

(\$ in 000's)	31-Dec-19 2019	31-Dec-20 2020	31-Dec-21 2021	31-Dec-22 2022 E	31-Dec-23 2023 E
Cash	2,361	3,926	21,729	16,249	20,014
Restricted Cash	173	63	7,213	7,213	7,213
A/R	5,824	4,631	6,792	10,346	13,245
Inventory	6,580	4,869	5,245	6,399	7,646
Prepaid expenses and other	2,641	4,074	2,940	4,417	5,655
Current Assets	\$ 17,579	\$ 17,563	\$ 43,919	\$ 44,623	\$ 53,773
PP&E	417	252	369	369	369
Right-of-use assets	951	345	56	56	56
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	116	116	116
Total Assets	\$ 53,532	\$ 51,253	\$ 74,660	\$ 73,837	\$ 81,460
Short term loan	16,061	7,826	855	855	5,414
Line of credit	4,819	0	0	0	4,856
PPP loans	0	190	0	0	0
Other liabilities	500	47	0	0	0
A/P	4,049	3,137	4,553	6,840	8,757
Accrued liabilities	4,721	3,003	1,879	2,823	3,614
Deferred revenue	311	350	0	0	0
Operating lease	345	173	54	54	54
Warrant derivative liab.	2,220	39,850	0	0	0
Current Liabilities	\$ 33,026	\$ 54,576	\$ 7,341	\$ 10,572	\$ 22,696
Notes payable	16,370	18,910	0	0	0
Term loans	0	0	4,559	4,559	0
Line of credit	0	5,023	4,856	4,856	0
PPP loans	0	662	0	0	0
Deferred Tax	0	0	24	24	24
Operating lease liab.	641	184	5	5	5
Series E Cv. Preferred	10,566	0	0	0	0
Total Stockholders' Equity	(7,071)	(28,102)	57,875	53,821	58,736
Total Liabilities & Equity	\$ 53,532	\$ 51,253	\$ 74,660	\$ 73,837	\$ 81,460
	31-Dec-19 2019	31-Dec-20 2020	31-Dec-21 2021	31-Dec-22 2022 E	31-Dec-23 2023 E
Net Income	(184,571)	(59,438)	3,387	(7,054)	1,515
Depreciation and amort.	171	1,748	1,664	1,652	1,652
Share-based comp.	10,280	8,940	4,140	2,000	2,400
Working Capital and other	153,151	41,245	(21,049)	(2,953)	(2,677)
Operating CF	\$ (20,969)	\$ (7,505)	\$ (11,858)	\$ (6,355)	\$ 2,890
Capex	(110)	(151)	(353)	(125)	(125)
Acquisitions	(20,097)	0	0	0	0
Investing Activities	\$ (20,207)	\$ (151)	\$ (353)	\$ (125)	\$ (125)
Equity	20,333	19,101	40,181	1,000	1,000
Debt	19,431	(9,990)	(3,017)	0	0
Financing	\$ 39,764	\$ 9,111	\$ 37,164	\$ 1,000	\$ 1,000
Change in Cash	\$ (1,412)	\$ 1,455	\$ 24,953	\$ (5,480)	\$ 3,765

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
 Update – Buy – March 30, 2022 – Price Target \$10.00

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- 2) **Neutral:** the analyst believes the price of the stock is fairly valued for the next 12-18 months;
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Current as of... 15-Mar-22

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
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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