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Better Choice Company Inc. (NYSE AM: BTTR)

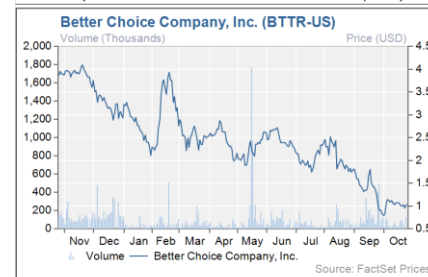
October 26, 2022

Buy: Increasing Balance Sheet Flexibility.

Better Choice amended its credit facility to improve its balance sheet flexibility. Shares of Better Choice have been beaten down with the general market downturn and we believe offers exceptional value at current levels.

Investment Highlights

| | | | |
|---|-------------|--------------|------------|
| Current Price | \$1.03 | | |
| Price Target | \$10.00 | | |
| Estimates | F2021A | F2022E | F2023E |
| Revenues (\$000s) | \$ 46,006 | \$ 61,710 E | \$ 80,349 |
| 1Q March | \$ 10,830 | \$ 17,014 A | \$ 20,054 |
| 2Q June | \$ 10,989 | \$ 16,515 A | \$ 20,795 |
| 3Q September | \$ 13,200 | \$ 13,481 E | \$ 19,375 |
| 4Q December | \$ 10,987 | \$ 14,700 E | \$ 20,125 |
| | F2021A | F2022E | F2023E |
| EBITDA (\$000s) | \$ (11,475) | \$ (11,276)E | \$ (3,090) |
| 1Q March | \$ (2,183) | \$ (2,461)A | \$ (1,084) |
| 2Q June | \$ (2,471) | \$ (3,030)A | \$ (617) |
| 3Q September | \$ (2,876) | \$ (3,173)E | \$ (934) |
| 4Q December | \$ (3,945) | \$ (2,612)E | \$ (455) |
| EV/Sales | 0.5 x | 0.4 x | 0.3 x |
| EV/EBITDA | (2.2) x | (2.2) x | (8.0) x |
| Stock Data | | | |
| 52-Week Range | \$0.78 | - | \$4.25 |
| Shares Outstanding (mil.) | 29.4 | | |
| Market Capitalization (mil.) | \$30 | | |
| Enterprise Value (mil.) | \$25 | | |
| Debt to Capital | 19% | | |
| Cash (mil.) | \$18 | | |
| Cash/Share | \$0.61 | | |
| Average Three Months Trading Volume (K) | 15 | | |
| Insider Ownership | 33.5% | | |
| Institutional Ownership | 32.2% | | |
| Short interest (mil.) | 0.6% | | |
| Dividend / Yield | \$0.00/0.0% | | |



The company entered into an amendment to its credit facility that increases balance sheet flexibility. While the interest rate increases from 285 basis points above the Fed Funds Rate (FFR) to 375 basis points above the FFR, the maturity of the facility has been pushed to October of 2024 (from January of 2024), the amount of restricted cash required declined from \$6.9 million to \$6.3 million and the liquidity covenant (excess availability plus unrestricted cash) has declined from \$13 million to \$8.5 million. The combination of these changes improves the company's financial flexibility to fund its growth over the coming years.

The market has been focusing on cash generation, balance sheet strength and stable revenue streams, and we believe the company is pivoting slightly from the more expensive strategy of adding outlets to a more cost-effective strategy of increasing share at the existing customer outlets. This could result in greater reliance on fewer customers in the near term while the long-term market potential remains as the company can focus on adding outlets when markets become more amenable to paying for more aggressive growth strategies.

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 consumers' balance sheets.

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 opportunities to care for pets.

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.

The company is in the early stages of expansion in the U.S. brick-and-mortar segment, is on track to exceed its \$100 million in aggregate contract minimums through 2025 from international distributors and has completed the integration of its TruDog brand into the Halo product portfolio. The shares have been buffeted by the decline in small-cap stocks and offer substantial value at current levels.

Cash at the end of Q2 was \$17.8 million (including \$7 million in restricted cash required by the company's credit facility), and Q2 cash from operations consumed \$5.3 million of cash. A significant part of the cash use was for inventory, which increased \$2.2 million from Q1. The company has invested in inventory to support the Halo Elevate launch and to anticipate supply chain disruptions. We expect inventory to decline as the Halo Elevate launch matures, but to remain higher than desired until normalcy returns to the supply chain. We believe cash is adequate for the company's growth plans but the margin for unexpected issues or opportunities is less than we prefer.

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 is not likely to achieve these targets until 2024.

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.

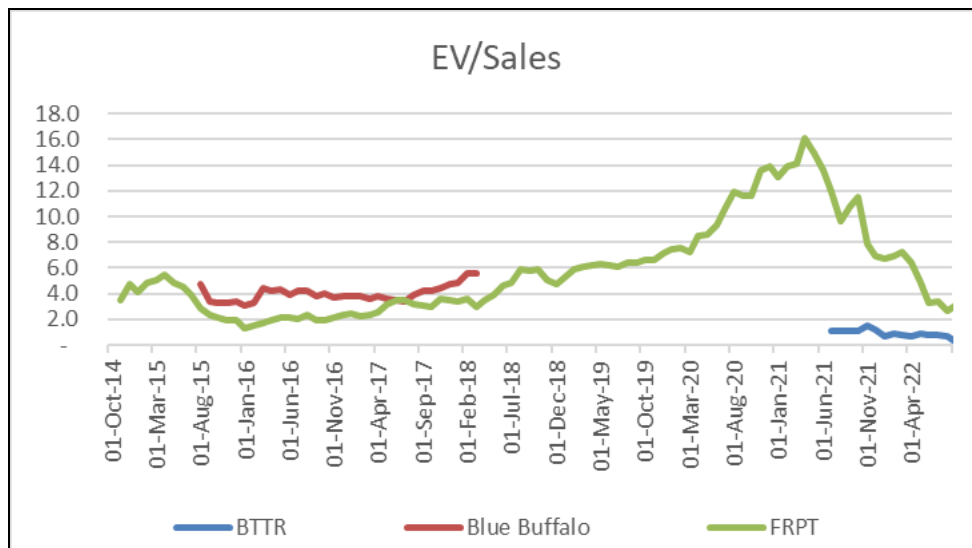
| | | Price | EPS | P/E | TEV (\$ M) | Sales (\$ M) | EV/ Sales | EBITDA (\$ M) | EV/ EBITDA |
|-----------|--|----------|-----------|---------|---------------|-----------------|--------------|------------------|---------------|
| CHWY-US | Chewy, Inc. Class A | \$ 39.79 | \$ 0.01 | 5,515.7 | \$ 16,692.6 | \$ 10,824.3 | 1.54 | \$ 264.6 | 63.1 |
| ELAN-US | Elanco Animal Health, Inc. | 13.31 | 1.19 | 11.2 | 11,866.5 | 4,543.9 | 2.61 | 1,141.3 | 10.4 |
| FRPT-US | Freshpet Inc | 57.68 | (0.28) | (206.5) | 2,513.0 | 718.5 | 3.50 | 72.7 | 34.6 |
| BARK-US | BARK Inc Class A | 1.75 | (0.19) | (9.3) | 263.1 | 633.3 | 0.42 | (13.1) | (20.1) |
| WOOF-US | Petco Health & Wellness Company, Inc | 10.50 | 0.80 | 13.1 | 5,726.6 | 6,279.5 | 0.91 | 611.1 | 9.4 |
| PETQ-US | PetIQ, Inc. Class A | 7.80 | 1.27 | 6.2 | 708.3 | 975.0 | 0.73 | 102.9 | 6.9 |
| PETS-US | PetMed Express, Inc. | 21.73 | 0.99 | 21.9 | 351.2 | 278.3 | 1.26 | 27.2 | 12.9 |
| 300673-CN | Petpal Pet Nutrition Technology Co., Ltd | 18.09 | 0.83 | 21.9 | 4,737.6 | 2,086.2 | 2.27 | 325.8 | 14.5 |
| PET-CA | Pet Valu Holdings Ltd. | 37.12 | 1.64 | 22.7 | 3,166.3 | 992.9 | 3.19 | 222.8 | 14.2 |
| | Median | | | 13.1 | | | 1.54 | | 12.9 |
| | Median-Retail | | | 17.9 | | | 1.23 | | 11.8 |
| | Median-Products | | | 11.2 | | | 2.27 | | 12.9 |
| BTTR-US | Better Choice Company, Inc. | \$ 1.03 | \$ (0.30) | NM | \$ 24.8 | \$ 77.0 | 0.32 | \$ (4.6) | NM |

Source: FactSet and Dawson James Securities estimates

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 10.0x and currently trades at 2.5x FTM sales.

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 A | 30-Jun-22 Q2 22 A | 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 | 17,014 | 16,515 | 13,481 | 14,700 | 61,710 | 80,349 |
| COGS | 9,717 | 26,485 | 30,638 | 12,307 | 11,788 | 8,897 | 9,555 | 42,547 | 51,027 |
| Gross Profit | 5,860 | 16,105 | 15,368 | 4,707 | 4,727 | 4,584 | 5,145 | 19,163 | 29,321 |
| Gross margin | 38% | 38% | 33% | 28% | 29% | 34% | 35% | 31% | 36% |
| SG&A | 34,487 | 34,487 | 28,507 | 7,577 | 8,187 | 8,187 | 8,187 | 32,138 | 34,058 |
| Share-based comp | 10,280 | 8,940 | 4,140 | 1,091 | 801 | 801 | 801 | 3,494 | 2,400 |
| Impairment | 889 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Opex | 45,656 | 43,427 | 32,647 | 8,668 | 8,988 | 8,988 | 8,988 | 35,632 | 36,458 |
| Operating Income | (39,796) | (27,322) | (17,279) | (3,961) | (4,261) | (4,404) | (3,843) | (16,469) | (7,137) |
| Interest Expense | 670 | 9,247 | 3,217 | 76 | 106 | 106 | 106 | 394 | 424 |
| 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 | (4,040) | (4,367) | (4,510) | (3,949) | (16,866) | (7,561) |
| Preferred dividends | 109 | 103 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Net to common | (184,571) | (59,438) | 3,387 | (4,040) | (4,367) | (4,510) | (3,949) | (16,866) | (7,561) |
| Basic Shares | 5,540 | 8,181 | 19,844 | 29,290 | 29,365 | 29,365 | 29,615 | 29,408 | 30,865 |
| Diluted Shares | 5,540 | 8,181 | 22,409 | 29,290 | 29,365 | 29,365 | 29,615 | 29,408 | 30,865 |
| Basic EPS | \$ (33.32) | \$ (7.27) | \$ 0.17 | \$ (0.14) | \$ (0.15) | \$ (0.15) | \$ (0.13) | \$ (0.57) | \$ (0.24) |
| Diluted EPS | \$ (33.32) | \$ (7.27) | \$ 0.15 | \$ (0.14) | \$ (0.15) | \$ (0.15) | \$ (0.13) | \$ (0.57) | \$ (0.24) |
| Depreciation and Amortization | 171 | 1,748 | 1,664 | 409 | 430 | 430 | 430 | 1,699 | 1,647 |
| Stock Comp | 10,280 | 8,940 | 4,140 | 1,091 | 801 | 801 | 801 | 3,494 | 2,400 |
| EBITDA | (29,345) | (16,634) | (11,475) | (2,461) | (3,030) | (3,173) | (2,612) | (11,276) | (3,090) |
| Margin | NM | -39.1% | -24.9% | -14.5% | -18.3% | -23.5% | -17.8% | -18.3% | -3.8% |

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

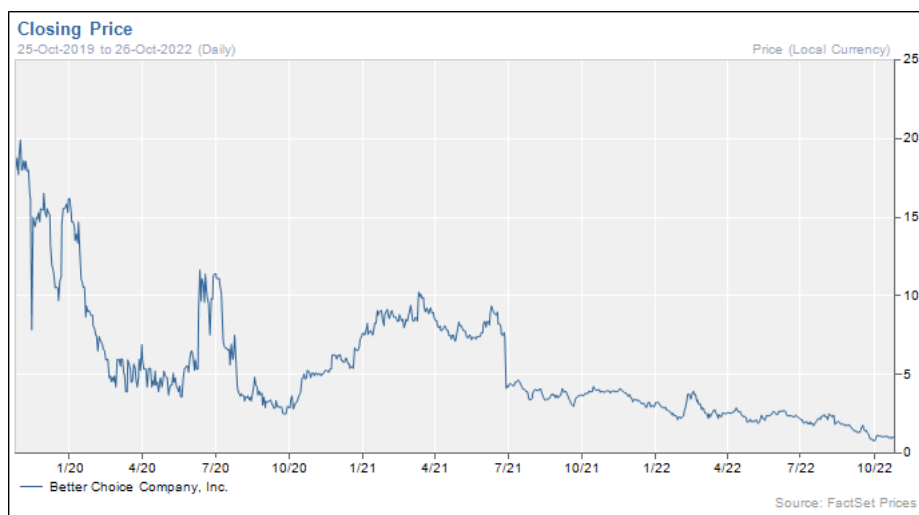
Exhibit 2. Balance Sheet and Cash Flow Statement

| (\$ 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 | \$ 9,379 | \$ 2,815 |
| Restricted Cash | 173 | 63 | 7,213 | 6,963 | 6,963 |
| A/R | 5,824 | 4,631 | 6,792 | 7,843 | 10,738 |
| Inventory | 6,580 | 4,869 | 5,245 | 6,901 | 9,012 |
| Prepaid expenses and other | 2,641 | 4,074 | 2,940 | 2,624 | 3,592 |
| Current Assets | \$ 17,579 | \$ 17,563 | \$ 43,919 | \$ 33,710 | \$ 33,119 |
| PP&E | 417 | 252 | 369 | 480 | 480 |
| Right-of-use assets | 951 | 345 | 56 | 31 | 31 |
| Intangible assets | 14,641 | 13,115 | 11,586 | 10,023 | 8,496 |
| Goodwill | 18,614 | 18,614 | 18,614 | 18,614 | 18,614 |
| Other assets | 1,330 | 1,364 | 116 | 101 | 101 |
| Total Assets | \$ 53,532 | \$ 51,253 | \$ 74,660 | \$ 62,959 | \$ 60,841 |
| Short term loan | \$ 16,061 | \$ 7,826 | \$ 855 | \$ 1,130 | \$ 4,996 |
| Line of credit | 4,819 | 0 | 0 | 0 | 7,368 |
| PPP loans | 0 | 190 | 0 | 0 | 0 |
| Other liabilities | 500 | 47 | 0 | 0 | 0 |
| A/P | 4,049 | 3,137 | 4,553 | 3,564 | 4,879 |
| Accrued liabilities | 4,721 | 3,003 | 1,879 | 1,972 | 2,699 |
| Deferred revenue | 311 | 350 | 0 | 0 | 0 |
| Operating lease | 345 | 173 | 54 | 33 | 33 |
| Warrant derivative liab. | 2,220 | 39,850 | 0 | 0 | 0 |
| Current Liabilities | \$ 33,026 | \$ 54,576 | \$ 7,341 | \$ 6,699 | \$ 19,975 |
| Notes payable | 16,370 | 18,910 | 0 | 0 | 0 |
| Term loans | 0 | 0 | 4,559 | 3,866 | 0 |
| Line of credit | 0 | 5,023 | 4,856 | 7,368 | 0 |
| PPP loans | 0 | 662 | 0 | 0 | 0 |
| Deferred Tax | 0 | 0 | 24 | 24 | 24 |
| Operating lease liab. | 641 | 184 | 5 | 0 | 0 |
| Series E Cv. Preferred | 10,566 | 0 | 0 | 0 | 0 |
| Total Stockholders' Equity | \$ (7,071) | \$ (28,102) | \$ 57,875 | \$ 45,003 | \$ 40,842 |
| Total Liabilities & Equity | \$ 53,532 | \$ 51,253 | \$ 74,660 | \$ 62,959 | \$ 60,841 |
| | | | | | |
| | 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 | (16,866) | (7,561) |
| Depreciation and amort. | 171 | 1,748 | 1,664 | 1,699 | 1,647 |
| Share-based comp. | 10,280 | 8,940 | 4,140 | 3,494 | 2,400 |
| Working Capital and other | 153,151 | 41,245 | (21,049) | (3,246) | (3,931) |
| Operating CF | \$ (20,969) | \$ (7,505) | \$ (11,858) | \$ (14,919) | \$ (7,444) |
| Capex | (110) | (151) | (353) | (249) | (120) |
| Acquisitions | (20,097) | 0 | 0 | 0 | 0 |
| Investing Activities | \$ (20,207) | \$ (151) | \$ (353) | \$ (249) | \$ (120) |
| Equity | 20,333 | 19,101 | 40,181 | 500 | 1,000 |
| Debt | 19,431 | (9,990) | (3,017) | 2,068 | 0 |
| Financing | \$ 39,764 | \$ 9,111 | \$ 37,164 | \$ 2,568 | \$ 1,000 |
| Change in Cash | \$ (1,412) | \$ 1,455 | \$ 24,953 | \$ (12,600) | \$ (6,564) |

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
 Update – Buy – May 13, 2022 – Price Target \$10.00
 Update – Buy – July 20, 2022 – Price Target \$10.00
 Update – Buy – August 12, 2022 – Price Target \$10.00
 Update – Buy – September 14, 2022 – Price Target \$10.00
 Update – Buy – October 26, 2022 – Price Target \$10.00

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Information about valuation methods and risks can be found in the "Valuation" and "Risk Analysis" sections of this report.

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Ratings Definitions:

- 1) **Buy:** the analyst believes the price of the stock will appreciate and produce a total return of at least 20% over the next 12-18 months;
- 2) **Neutral:** the analyst believes the price of the stock is fairly valued for the next 12-18 months;
- 3) **Sell:** the analyst believes the price of the stock will decline by at least 20% over the next 12-18 months and should be sold.

The following chart reflects the range of current research report ratings for all companies, followed by the analysts of the Firm. The chart also reflects the research report ratings relating to those companies for which the Firm has performed investment banking services.

Current as of 19-Oct-22

| | Company Coverage | | Investment Banking | |
|-----------------------------|-------------------------|-------------------|---------------------------|--------------------|
| Ratings Distribution | # of Companies | % of Total | # of Companies | % of Totals |
| Market Outperform (Buy) | 25 | 83% | 3 | 12% |
| Market Perform (Neutral) | 4 | 13% | 1 | 25% |
| Market Underperform (Sell) | 1 | 3% | 0 | 0% |
| Total | 30 | 100% | 4 | 13% |

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