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Toll-Free: 866-928-0928 ♦ www.DawsonJames.com ♦ 101 North Federal Highway - Suite 600 ♦ Boca Raton, FL 33432

Profire Energy, Inc. (NASDAQ: PFIE)

November 4, 2022

Buy: Strong Results and Outlook. Reiterate Buy.

James McIlree, CFA
561-237-2709
jmcilree@dawsonjames.com

Q3 results were better than expected and the outlook remains strong. Although oil prices have declined recently, well completions remain robust and we believe the company can grow revenue and EBITDA to much higher levels, driving substantial stock price appreciation.

Q3 revenue was \$12.8 million, and EBITDA was \$2.6 million, higher than expected. We believe there was some catch-up from Q2, but demand remains strong and we expect growth to continue as oil and gas prices benefit from the current administration's War on Fossil Fuels, OPEC production cuts and the West's policy towards Russian oil.

Valuation is favorable, but there are risks. The equity markets have struggled with the change in Fed policy since March, and more interest rate increases are assumed since the Fed projects a year-end Fed Funds rate of 4.4% versus the current target range of 3% to 3.25%, and a year-end 2023 Fed Funds rate of 4.6%. This could imply a Fed Funds rate exceeding 5% sometime during 2023. All hinges on inflation, which spiked this year, and while the rate could be flattening, the Fed will continue to increase rates until it sees declines in inflation that put the economy back on a path to 2% inflation.

The EIA's reference case estimates tight oil production in the U.S. will increase almost 25% from 2021 to 2025, (assuming wellhead prices of about \$65 per barrel). EIA expects natural gas production from shale gas and tight oil plays to increase 14% from 2021 to 2025. This is based on Henry Hub spot prices declining to \$3.00 per million BTU from \$4.11 in 2021 and far below current prices.

The Biden administration's animus towards oil and gas production and consumption has increased costs to consumers. Whether this is a sustainable policy supported by voters we will discover next week. Also, natural gas accounts for 38% of electricity generation in the U.S., and it will remain above 35% for the next decade even if the massive subsidies to solar and wind remain (a question mark if there is a change in control of Congress and/or the White House, and if budget deficits put these subsidies under closer scrutiny). The move to electric vehicles is still nascent and even optimistic consumer adoption projections will result in increased electricity demand and the necessity of robust natural gas production.

Valuation: Our price target of \$2.00 is based on an EV/Sales multiple of less than 2x the 2022 revenue estimate of \$43.7 million. Our EV/sales target multiple is a discount to the 2.4x EV/sales multiple in 2018 when WTI averaged over \$65 per barrel. We believe the discount is warranted to reflect the risks of reaching our revenue estimate.

Risks: Risks to achieving our price target include changes in oil and gas prices, global economic growth and its impact on demand for oil and gas, regulation that could impact the ability to drill for oil and gas, and regulation that could impede the development of pipelines in the U.S.

Current Price	\$1.04		
Price Target	\$2.00		
Estimates	F2021A	F2022E	F2023E
Revenues (\$000s)	\$ 26,356	\$ 43,699 E	\$ 47,574
1Q March	\$ 5,092	\$ 9,503 A	\$ 11,275
2Q June	\$ 6,034	\$ 9,633 A	\$ 10,993
3Q September	\$ 6,943	\$ 12,829 A	\$ 12,183
4Q December	\$ 8,286	\$ 11,733 E	\$ 13,124
	F2021A	F2022E	F2023E
EBITDA (\$000s)	\$ (192)	\$ 5,879 E	\$ 7,154
1Q March	\$ (386)	\$ 1,109 A	\$ 1,391
2Q June	\$ 3	\$ 647 A	\$ 1,293
3Q September	\$ 113	\$ 2,583 A	\$ 1,984
4Q December	\$ 78	\$ 1,541 E	\$ 2,485
EV/Sales	1.3 x	0.8 x	0.7 x
EV/EBITDA	NM	5.9 x	4.8 x
Stock Data			
52-Week Range	\$0.85	-	\$1.59
Shares Outstanding (mil.)	47.0		
Market Capitalization (mil.)	\$49		
Enterprise Value (mil.)	\$34		
Debt to Capital	0%		
Cash (mil.)	\$14		
Cash/Share	\$0.31		
Average Three Months Trading Volume (K)	159		
Insider Ownership	23.0%		
Institutional Ownership	43.4%		
Short interest (mil.)	0.1%		
Dividend / Yield	\$0.00/0.0%		



Q3 Actual v Estimates

Profile pre-announced Q3 revenues between a range of \$12.5 to \$12.7 million and exceeded the high end of that range. EBITDA was substantially higher than forecast with gross margin a bit higher than our estimate, and operating expenses much lower than expected. There was a one-time expense benefit in the quarter, and we expect operating expenses to remain under control, but at a higher level than Q3.

Q3 22	Actual	Est.	Delta	% Delta
Total Revenues	12,829	12,472	357	3%
Total COGS	6,710	6,545	165	3%
Gross Profit-Total	6,119	5,927	192	3%
G&A	3,413	4,187	(774)	
R&D	435	377	58	
Depreciation	153	160	(7)	
Opex	4,001	4,723	(722)	-15%
Operating income	2,118	1,204	914	76%
Interest and Other	51	217	(166)	
Pretax income	2,169	1,421	748	53%
Taxes	958	369	589	
Net Income	1,211	1,052	159	15%
Basic Shares (000)	47,036	47,033		
Diluted Shares (000)	48,558	47,433		
Basic EPS	\$ 0.03	\$ 0.02	\$ 0.00	
Diluted EPS	\$ 0.02	\$ 0.02	\$ 0.00	
Operating Income	2,118	1,204	914	76%
D&A	272	281		
Stock Comp	193	274		
EBITDA	2,583	1,759	824	47%
EBITDA Margin	20.1%	14.1%		

Source: Company data and Dawson James Securities estimates.

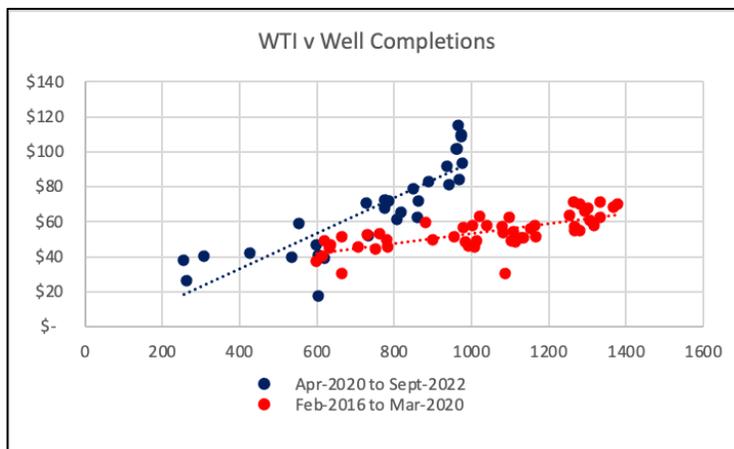
We have modified our estimates for this year and next to reflect the Q3 results. Revenue estimates have increased as well as EBITDA for this year. We have moderated our gross margin estimate for next year, primarily to reflect continued cost pressures on parts and fulfillment.

	2022E		2023E	
	Old	New	Old	New
Revenue (\$M)	\$ 42.5	\$ 43.7	\$ 46.9	\$ 47.6
EPS	\$ 0.06	\$ 0.06	\$ 0.10	\$ 0.08
EBITDA (\$M)	\$ 4.8	\$ 5.9	\$ 8.1	\$ 7.2

Source: Dawson James Securities estimates.

Well Completions

According to the EIA Drilling Productivity Report, well completions since April of 2020 have recovered sharply, to an average of over 956 per month for the first nine months of this year. However, the supply curve has shifted to the left, and elasticity decreased. We attribute this shift to government policies and market pressures to improve producer balance sheets. Well completions were much *higher* when WTI and natural gas prices were much *lower* than it is currently as can be seen on the graph below that compares well completions to WTI for the period before the pandemic and the period after the pandemic started.



Source: [EIA](#) and [EIA Drilling Productivity Report](#).

While oil prices are currently high, a change in the political situation in Russia could change the supply situation in either direction. The increase in interest rates will have an impact on the economy and if inflation remains stubbornly high, we expect the Fed to become even more restrictive. We do not believe consumers/voters will tolerate sustained high gas prices and that they will demand policymakers encourage supply increases domestically. If this occurs simultaneous with an easing of the drilling industry’s labor and equipment shortage, the outlook for Profire could improve considerably.

Outlook

In the smaller and mid-size oilfield applications, demand for burner management systems is driven by the number of well completions, and to a lesser extent, by replacement demand and retrofit of existing wells. According to EIA data, in the U.S., the number of well completions in 2018 was almost 15,000, which fell to under 14,000 in 2019 and to 7,400 in 2020. However, well completions in 2021 increased 32% to 9,793.

We project revenue for Profire in 2022 of \$43.7 million, up from \$26.4 million in 2021. For 2023, we forecast revenue of \$47.6 million, based on stable oil and gas prices and continued improvement in drilling and completion activity. We believe Profire is in a better position than many of its competitors, with a strong balance sheet and positive cash flow. However, it remains at the mercy of oil prices, and its attempts to reduce its dependence on the upstream BMS market have met with limited success.

Profire Energy, Inc. Comparable Group

		Price	TEV (\$M)	FTM Sales (\$M)	EV/Sales	FTM EBITDA (\$M)	EV/EBITDA
CHX	ChampionX Corporation	\$ 29.38	\$ 6,383.3	\$ 4,049.9	1.58	\$ 751.9	8.5
CLB	Core Laboratories NV	20.28	1,167.6	542.4	2.15	80.2	14.5
BOOM	DMC Global Inc.	19.58	746.9	680.1	1.10	97.5	7.7
HTG-GB	Hunting PLC	£ 2.87	£ 414.4	£ 689.7	0.60	£ 66.7	6.2
LBRT	Liberty Energy, Inc. Class A	17.19	3,490.4	5,009.1	0.70	1,144.4	3.0
OIS	Oil States International, Inc.	6.62	572.8	820.7	0.70	90.9	6.3
	Median				1.14		7.7
PFIE	Profire Energy, Inc.	\$ 1.04	\$ 34.5	\$ 47.0	0.73	\$ 7.0	5.0

Source: FactSet and Dawson James Securities estimates.

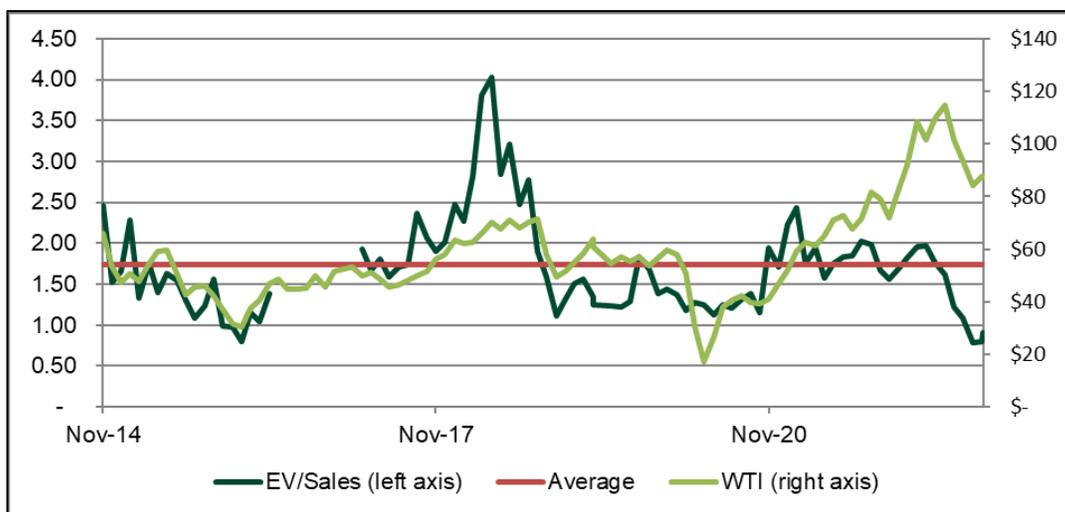
If oil and natural gas prices remain firm, we expect the rig count, drilled wells, and completed wells will continue to increase and the outlook for Profire to improve. WTI is currently far above the average price in 2018 of \$65.23 and the average price in 2019 of \$56.99. The Baker Hughes U.S. rig count, however, at 768, remains about 25% below the average rig counts in 2018 and 2019. Energy Information Administration (EIA) data indicate the number of wells drilled fell 57% in 2020 and the number of completed

wells fell 45%, compared to the 2018-2019 period. There was a 32% increase in completions in 2021 vs. 2020 but there is substantial room for improvement. The number of completed wells in Q3 2022 is almost 30% below its peak level in 2018.



Source: Baker Hughes, EIA

Profire's shares have moved up with the changes in oil prices, but the company's current EV/Sales is lower than levels achieved at much lower oil prices and we think there is further room for improvement.



Source: Dawson James Securities, EIA, Factset

Valuation:

Our price target of \$2.00 is based on an EV/Sales multiple of less than 2x our 2022 revenue estimate of \$43.7 million. Our EV/sales target multiple is a discount to the 2.4x EV/sales multiple in 2018 when WTI averaged over \$65 per barrel. We believe the discount is warranted to reflect the risks of reaching our revenue estimate.

Risk Analysis:

Risks to achieving our price target include changes in oil and gas prices, global economic growth and its impact on demand for oil and gas, regulation that could impact the ability to drill for oil and gas, and regulation that could impede the development of pipelines in the U.S.

Exhibit 1. Income Statement

\$ in 000's except per share data	FY 19	FY 20	FY 21	Mar-22 Q1 22 A	Jun-22 Q2 22 A	Sep-22 Q3 22 A	Dec-22 Q4 22 E	FY 22E	FY 23E
Sales of Goods	36,208	19,396	23,691	8,878	8,861	11,896	10,706	40,341	43,134
Sales of Services	2,773	2,063	2,665	625	772	933	1,027	3,357	4,440
Total Revenues	\$ 38,981	\$ 21,459	\$ 26,356	\$ 9,503	\$ 9,633	\$ 12,829	\$ 11,733	\$ 43,699	\$ 47,574
Cost of Goods	17,588	10,378	12,826	4,383	4,530	5,960	5,353	20,226	21,217
Cost of Services	1,865	1,554	2,129	564	700	750	924	2,938	3,552
Total COGS	19,453	11,932	14,955	4,946	5,230	6,710	6,277	23,164	24,769
Gross Profit-Goods	18,620	9,017	10,865	4,496	4,331	5,936	5,353	20,115	21,917
Gross Profit-Services	908	509	536	61	73	183	103	419	888
Gross Profit-Total	19,528	9,526	11,401	4,557	4,403	6,119	5,456	20,535	22,805
G&A	13,454	10,641	11,533	3,392	3,787	3,413	3,787	14,379	15,046
R&D	1,933	1,299	1,120	308	362	435	450	1,556	1,890
Depreciation	977	666	762	167	160	153	153	632	612
Opex	16,364	12,606	13,416	3,868	4,308	4,001	4,389	16,567	17,548
Operating income	3,164	(3,080)	(2,015)	689	95	2,118	1,066	3,968	5,257
Interest and Other	403	421	334	99	217	51	51	418	205
Pretax income	3,567,561	(2,659)	(1,681)	788	312	2,169	1,117	4,386	5,462
Taxes	1,546	(484)	(629)	160	27	958	291	1,436	1,420
Net Income	\$ 2,021	\$ (2,176)	\$ (1,052)	\$ 627	\$ 285	\$ 1,211	\$ 827	\$ 2,950	\$ 4,042
Basic Shares	47,491	47,778	48,071	47,481	47,092	47,036	47,040	47,958	47,304
Diluted Shares	48,134	47,778	48,071	48,536	48,699	48,558	47,440	48,387	48,176
Basic EPS	\$ 0.04	\$ (0.05)	\$ (0.02)	\$ 0.01	\$ 0.01	\$ 0.03	\$ 0.02	\$ 0.06	\$ 0.09
Diluted EPS	\$ 0.04	\$ (0.05)	\$ (0.02)	\$ 0.01	\$ 0.01	\$ 0.02	\$ 0.02	\$ 0.06	\$ 0.08
Operating Income	3,164	(3,080)	(2,015)	689	95	2,118	1,066	3,968	5,257
D&A	1,467	1,177	1,256	281	278	272	281	1,112	1,124
Stock Comp	391	443	567	139	274	193	193	799	772
EBITDA	\$ 5,022	\$ (1,460)	\$ (192)	\$ 1,109	\$ 647	\$ 2,583	\$ 1,541	\$ 5,879	\$ 7,154
WTI \$/barrel	\$ 56.98	\$ 39.12	\$ 68.09	\$ 95.18	\$ 108.72	\$ 93.06			
	FY 19	FY 20	FY 21	Q1 22 A	Q2 22 A	Q3 22 A	Q4 22 E	FY 22E	FY 23E
Sales of Goods	92.9%	90.4%	89.9%	93.4%	92.0%	92.7%	91.2%	92.3%	90.7%
Sales of Services	7.1%	9.6%	10.1%	6.6%	8.0%	7.3%	8.8%	7.7%	9.3%
Total Revenues	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of goods	48.6%	53.5%	54.1%	49.4%	51.1%	50.1%	50.0%	50.1%	49.2%
Cost of services	67.3%	75.3%	79.9%	90.2%	90.6%	80.4%	90.0%	87.5%	80.0%
Total COGS	49.9%	55.6%	56.7%	52.1%	54.3%	52.3%	53.5%	53.0%	52.1%
Gross Profit-Goods	51.4%	46.5%	45.9%	50.6%	48.9%	49.9%	50.0%	49.9%	50.8%
Gross Profit-Services	32.7%	24.7%	20.1%	9.8%	9.4%	19.6%	10.0%	12.5%	20.0%
Gross Profit-Total	50.1%	44.4%	43.3%	47.9%	45.7%	47.7%	46.5%	47.0%	47.9%
G&A	34.5%	49.6%	43.8%	35.7%	39.3%	26.6%	32.3%	32.9%	31.6%
Payroll Expense	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Depreciation	2.5%	3.1%	2.9%	1.8%	1.7%	1.2%	1.3%	1.4%	1.3%
Opex	42.0%	58.7%	50.9%	40.7%	44.7%	31.2%	37.4%	37.9%	36.9%
Operating income	8.1%	-14.4%	-7.6%	7.3%	1.0%	16.5%	9.1%	9.1%	11.0%
Interest and Other	1.0%	2.0%	1.3%	1.0%	2.3%	0.4%	0.4%	1.0%	0.4%
Pretax income	9.2%	-12.4%	-6.4%	8.3%	3.2%	16.9%	9.5%	10.0%	11.5%
Tax Rate	43.3%	18.2%	37.4%	20.4%	8.7%	44.2%	26.0%	32.8%	26.0%
Net Income	5.2%	-10.1%	-4.0%	6.6%	3.0%	9.4%	7.0%	6.8%	8.5%
EBITDA	12.9%	-6.8%	-0.7%	11.7%	6.7%	20.1%	13.1%	13.5%	15.0%

Source: Profire Energy, Inc. and Dawson James Securities estimates

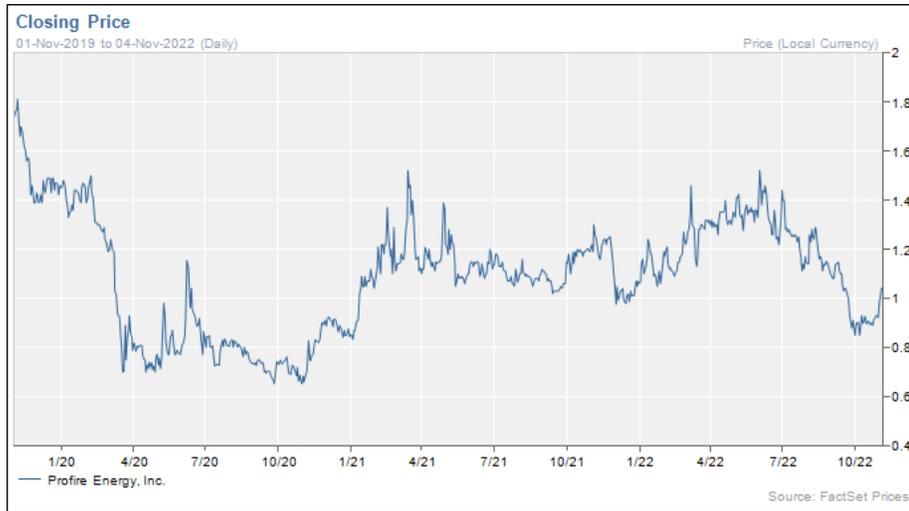
Exhibit 2. Balance Sheet and Cash Flow Statement

\$ in 000's	FY 19	FY 20	FY 21	FY 22E	FY 23E
Cash	7,359	9,148	8,188	7,608	10,547
ST Investments	3,822	2,389	1,014	868	868
A/R	5,598	3,720	6,263	7,822	8,749
Inventories	9,572	8,415	7,185	9,546	10,685
Prepaid Expenses & Other	1,750	2,165	1,586	2,417	2,703
Current Assets	\$ 28,100	\$ 25,836	\$ 24,236	\$ 28,261	\$ 33,552
LT Investments	7,400	6,064	8,260	7,944	7,944
Financing right of use asset	108	50	65	133	133
PP&E	12,071	12,022	11,186	10,218	10,094
Deferred Tax Asset	0	0	163	186	186
Intangible Assets	1,990	1,772	1,549	1,313	1,313
Goodwill	2,579	2,579	2,579	2,579	2,579
Total Assets	\$ 52,248	\$ 48,323	\$ 48,038	\$ 50,633	\$ 55,800
A/P	2,634	1,179	1,823	1,837	2,054
Accrued liabilities	2,089	1,197	1,872	2,124	2,231
Financing lease	59	39	30	53	53
Income tax payable	403	0	0	570	599
Current Liabilities	\$ 5,185	\$ 2,415	\$ 3,725	\$ 4,584	\$ 4,937
Deferred Tax Liability	439	523	136	480	480
Financing Lease Liability	52	13	36	81	81
Equity	46,572	45,372	44,141	45,488	50,302
Total Equity & Liab.	\$ 52,248	\$ 48,323	\$ 48,038	\$ 50,633	\$ 55,800
	FY 19	FY 20	FY 21	FY 22E	FY 23E
Net	2,021	(2,176)	(1,052)	2,950	4,042
D&A	1,467	1,177	1,256	1,112	1,124
Stock issued for services	391	443	567	799	772
Other	201	(123)	(176)	(283)	0
Working Capital	3,633	943	54	(3,682)	(1,999)
Operating Cash Flow	\$ 7,713	\$ 264	\$ 649	\$ 896	\$ 3,939
Other	1,611	3,314	(649)	416	0
Acquisition	(4,384)	0	0	0	0
CapEx	(4,665)	(1,547)	(169)	(496)	(1,000)
Investing Activities	\$ (7,437)	\$ 1,767	\$ (818)	\$ (80)	\$ (1,000)
Equity	(2,977)	(153)	(795)	(1,292)	0
Lease Liability	(74)	(58)	(41)	(28)	0
Financing Activities	\$ (3,050)	\$ (210)	\$ (836)	\$ (1,321)	\$ -
FX	31	(31)	45	(77)	0
Change in Cash	\$ (2,743)	\$ 1,789	\$ (960)	\$ (580)	\$ 2,939

Source: Profire Energy, Inc. and Dawson James Securities estimates

Important Disclosures:

Price Chart:



Price target and ratings changes over the past three years:

- Initiated – Buy – May 12, 2021 – Price Target \$1.65
- Update – Buy – June 21, 2021 – Price Target \$1.65
- Update – Buy – August 6, 2021 – Price Target \$1.65
- Update – Buy – September 28, 2021 – Price Target \$1.65
- Update – Buy – October 18, 2021 – Price Target \$1.65
- Update – Buy – November 5, 2021 – Price Target \$1.65
- Update – Buy – February 18, 2022 – Price Target \$1.65
- Update – Buy – February 18, 2022 – Price Target \$1.65
- Price Target Change – Buy – March 9, 2022 – Price Target changed from \$1.65 to \$2.00
- Update – Buy – May 4, 2022 – Price Target \$2.00
- Update – Buy – July 5, 2022 – Price Target \$2.00
- Update – Buy – August 4, 2022 – Price Target \$2.00
- Update – Buy – August 8, 2022 – Price Target \$2.00
- Update – Buy – September 22, 2022 – Price Target \$2.00
- Update – Buy – October 11, 2022 – Price Target \$2.00
- Update – Buy – November 4, 2022 – Price Target \$2.00

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- 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 28-Oct-22

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	24	80%	3	13%
Market Perform (Neutral)	5	17%	1	20%
Market Underperform (Sell)	1	3%	0	0%
Total	30	100%	4	13%

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