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Profire Energy, Inc. (NASDAQ: PFIE)

August 11, 2023

Buy: EBITDA Higher on Strong Gross Margin.

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Q2 revenue was in line with our estimate and EBITDA far exceeded our forecast on higher gross margin and lower opex relative to our model. For the year our revenue estimate is unchanged, but we have increased our EBITDA estimates for this year and next. We believe the company can grow revenue and EBITDA to much higher levels, driving substantial stock price appreciation.

Q2 revenue of \$14.4 million exceeded our \$14.2 million revenue and was up 50% from the year-ago quarter. The company continues to benefit from increased completion activity and customer focus on efficiency, automation and safety, which are the core value propositions of Profire's burner management system.

EBITDA of \$3.9 million far exceeded our \$2.7 million estimate and consensus of \$2.8 million. The better-than-expected EBITDA was driven primarily by higher than forecast gross margin. Gross margin of 51% was 300 basis points higher than our 48% estimate, although down from Q1's 54%. The company has benefitted from higher volume, mix, price increases and possibly working off some of its lower cost inventory as the company has been increasing inventory levels to shorten delivery times.

Cash at quarter-end was \$10 million and the company holds another \$7 million in long-term investments. Operating cash flow for the quarter was \$1.3 million, after increased A/R of \$1.7 million and increased inventory of \$2.4 million. The company continues to hold a high level of inventory in order to satisfy customer demand in a timely manner. We have modeled inventory and A/R turns to increase in 2024 and sharply higher operating cash flow of \$13.7 million in 2024 compared to \$7.4 million this year.

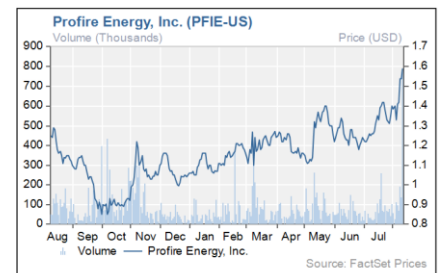
Our revenue estimates for this year and next are unchanged but we have increased our EBITDA estimates based on higher gross margin, although at lower levels than achieved in the first half of this year. For this year we estimate EBITDA margin of 25% and 23% in 2024.

Valuation is favorable, as is the long-term outlook. 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 (see chart on page 2).

Valuation: Our price target of \$2.00 is based on an EV/Sales multiple of less than 1.5x the 2023 revenue estimate of \$61.5 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 the cultural zeitgeist eschewing fossil fuels.

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	\$1.59		
Price Target	\$2.00		
Estimates	F2022A	F2023E	F2024E
Revenues (\$000s)	\$ 45,937	\$ 61,529 E	\$ 64,605
1Q March	\$ 9,503	\$ 14,553 A	\$ 15,281
2Q June	\$ 9,633	\$ 14,444 A	\$ 15,166
3Q September	\$ 12,829	\$ 15,668 E	\$ 16,451
4Q December	\$ 13,971	\$ 16,864 E	\$ 17,707
	F2022A	F2023E	F2024E
EBITDA (\$000s)	\$ 7,110	\$ 15,455 E	\$ 15,017
1Q March	\$ 1,109	\$ 3,791 A	\$ 3,252
2Q June	\$ 647	\$ 3,870 A	\$ 3,571
3Q September	\$ 2,583	\$ 3,698 E	\$ 3,887
4Q December	\$ 2,772	\$ 4,095 E	\$ 4,306
EV/Sales	1.3 x	0.9 x	0.9 x
EV/EBITDA	NM	3.8 x	3.9 x
Stock Data			
52-Week Range	\$0.85	-	\$1.72
Shares Outstanding (mil.)	47.6		
Market Capitalization (mil.)	\$76		
Enterprise Value (mil.)	\$58		
Debt to Capital	0%		
Cash (mil.)	\$17		
Cash/Share	\$0.36		
Average Three Months Trading Volume (K)	105		
Insider Ownership	31.4%		
Institutional Ownership	43.5%		
Short interest (mil.)	0.0%		
Dividend / Yield	\$0.00/0.0%		



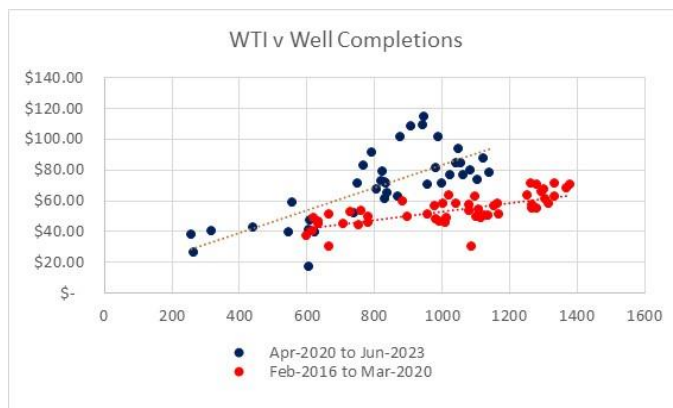
Actual v Estimates

Q2 23	Actual	Est.	Delta	% Delta
Sales of Goods	13,603	13,288	315	2%
Sales of Services	841	902	(61)	-7%
Total Revenues	\$ 14,444	\$ 14,190	254	2%
Cost of Goods	6,270	6,644	(374)	-6%
Cost of Services	759	721	37	5%
Total COGS	7,029	7,365	(336)	-5%
Gross Profit-Goods	7,333	6,644	689	10%
Gross Profit-Services	82	180	(99)	-55%
Gross Profit-Total	7,414	6,824	590	9%
G&A	3,792	3,976	(184)	
R&D	258	380	(122)	
Depreciation	140	143	(3)	
Opex	4,191	4,499	(309)	-7%
Operating income	\$ 3,224	\$ 2,325	899	39%
Interest and Other	267	101	167	
Pretax income	3,491	2,426	1,065	44%
Taxes	634	631	3	
Net Income	2,857	1,795	1,062	59%
Basic Shares	47,394	47,352		
Diluted Shares	49,473	47,752		
Basic EPS	\$ 0.06	\$ 0.04	\$ 0.02	59%
Diluted EPS	\$ 0.06	\$ 0.04	\$ 0.02	54%
Operating Income	3,224	2,325	899	39%
D&A	286	143		
Stock Comp	360	223		
EBITDA	\$ 3,870	\$ 2,691	1,179	44%
EBITDA Margin	26.8%	19.0%		

Source: Profire Energy, Inc. and 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 almost 1,000 per month. 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

Our revenue estimates are unchanged, but a higher gross margin assumption results in higher estimates for EPS and EBITDA.

Estimate Changes

	2023E		2024E	
	Old	New	Old	New
Revenue (\$M)	\$ 61.5	\$ 61.5	\$ 64.6	\$ 64.6
EPS	\$ 0.19	\$ 0.22	\$ 0.19	\$ 0.22
EBITDA (\$M)	\$ 13.8	\$ 15.5	\$ 13.4	\$ 15.0

Source: Dawson James Securities estimates

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 about 7,500 in 2020. However, well completions in 2021 increased 26% and 19% in 2022.

We project revenue for Profire in 2023 of \$61.5 million, up from \$45.9 million in 2022. For 2023, our forecast assumes stable oil and gas prices and current levels of 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.

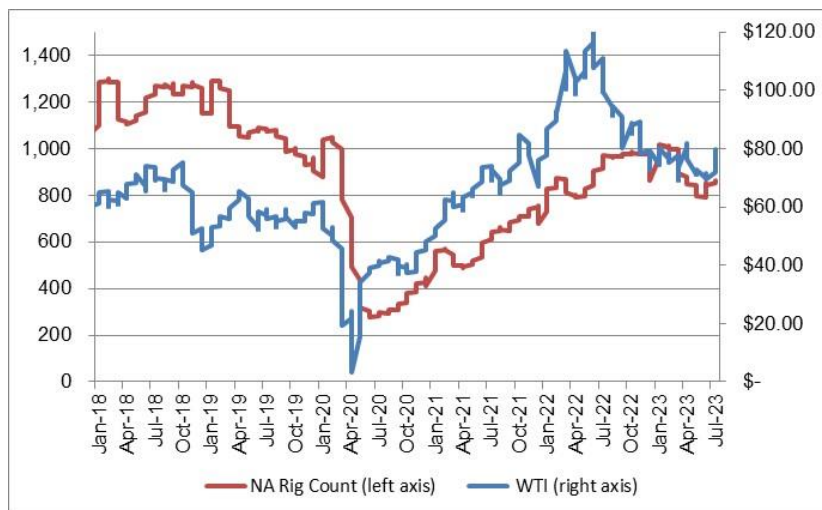
Profire Energy, Inc. Comparable Group

		Price	TEV (\$M)	FTM Sales (\$M)	EV/Sales	FTM EBITDA (\$M)	EV/EBITDA
CHX	ChampionX Corporation	\$ 36.20	\$ 7,515.1	\$ 4,051.9	1.85	\$ 844.3	8.9
CLB	Core Laboratories Inc.	25.76	1,426.3	551.5	2.59	90.0	15.8
BOOM	DMC Global Inc.	21.58	770.0	750.6	1.03	106.1	7.3
HTG-GB	Hunting PLC	£ 2.58	£ 421.3	£ 793.1	0.53	£ 90.6	4.7
LBRT	Liberty Energy, Inc. Class A	16.65	3,234.3	4,512.6	0.72	1,096.1	3.0
OIS	Oil States International, Inc.	7.86	622.4	851.6	0.73	102.1	6.1
	Median				1.24		7.6
PFIE	Profire Energy, Inc.	\$ 1.59	\$ 58.4	\$ 66.5	0.88	\$ 14.7	4.0

Source: FactSet and Dawson James Securities estimates.

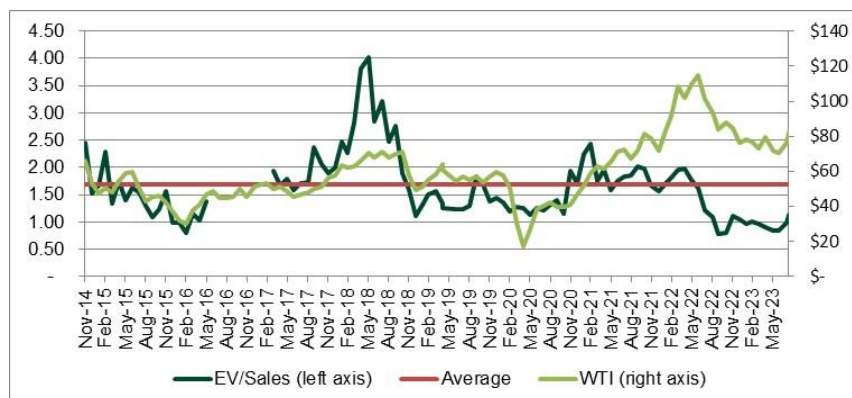
If oil and natural gas prices remain firm, we expect the rig count, drilled wells, and completed wells will remain stable and the outlook for Profire to remain favorable. WTI is currently far above the average price in 2018 of \$65.23 and the average price in

2019 of \$56.99. The Baker Hughes U.S. rig count, however, at 659, remains over 30% 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 26% increase in completions in 2021 vs. 2020 and a 19% increase in 2022, but there is substantial room for improvement. The number of completed wells in the first half of 2023 is 22% 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 1.5x our 2023 revenue estimate of \$61.5 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 20	FY 21	FY 22	Mar-23 Q1 23 A	Jun-23 Q2 23 A	Sep-23 Q3 23 E	Dec-23 Q4 23 E	FY 23E	FY 24E
Sales of Goods	19,396	23,691	42,318	13,629	13,603	14,827	15,939	57,998	60,898
Sales of Services	2,063	2,665	3,618	925	841	841	925	3,531	3,708
Total Revenues	\$ 21,459	\$ 26,356	\$ 45,937	\$ 14,553	\$ 14,444	\$ 15,668	\$ 16,864	\$ 61,529	\$ 64,605
Cost of Goods	10,378	12,826	21,425	5,974	6,270	7,265	7,810	27,320	29,840
Cost of Services	1,554	2,129	2,860	746	759	694	763	2,961	2,966
Total COGS	11,932	14,955	24,285	6,720	7,029	7,959	8,573	30,281	32,806
Gross Profit-Goods	9,017	10,865	20,893	7,654	7,333	7,562	8,129	30,678	31,058
Gross Profit-Services	509	536	758	179	82	147	162	570	742
Gross Profit-Total	9,526	11,401	21,651	7,833	7,414	7,709	8,291	31,247	31,799
G&A	10,641	11,533	14,397	4,048	3,792	3,917	4,216	15,973	16,772
R&D	1,299	1,120	1,432	336	258	457	343	1,394	1,464
Depreciation	666	762	628	143	140	140	140	563	560
Opex	12,606	13,416	16,457	4,527	4,191	4,514	4,699	17,931	18,796
Operating income	(3,080)	(2,015)	5,195	3,306	3,224	3,195	3,592	13,317	13,003
Interest and Other	421	334	492	101	267	267	267	902	1,069
Pretax income	(2,659)	(1,681)	5,686	3,406	3,491	3,462	3,859	14,219	14,072
Taxes	(484)	(629)	1,738	817	634	900	1,003	3,354	3,659
Net Income	\$ (2,176)	\$ (1,052)	\$ 3,948	\$ 2,590	\$ 2,857	\$ 2,562	\$ 2,856	\$ 10,865	\$ 10,414
Basic Shares	47,778	48,071	47,161	47,175	47,394	47,575	47,625	47,107	47,427
Diluted Shares	47,778	48,071	48,447	48,613	49,473	47,975	48,025	48,358	48,333
Basic EPS	\$ (0.05)	\$ (0.02)	\$ 0.08	\$ 0.05	\$ 0.06	\$ 0.05	\$ 0.06	\$ 0.23	\$ 0.22
Diluted EPS	\$ (0.05)	\$ (0.02)	\$ 0.08	\$ 0.05	\$ 0.06	\$ 0.05	\$ 0.06	\$ 0.22	\$ 0.22
Operating Income	(3,080)	(2,015)	5,195	3,306	3,224	3,195	3,592	13,317	13,003
D&A	1,177	1,256	1,101	262	286	143	143	834	572
Stock Comp	443	567	815	223	360	360	360	1,304	1,442
EBITDA	\$ (1,460)	\$ (192)	\$ 7,110	\$ 3,791	\$ 3,870	\$ 3,698	\$ 4,095	\$ 15,455	\$ 15,017
WTI \$/barrel	\$ 39.12	\$ 68.09	\$ 94.90	\$ 75.93	\$ 73.54				
	FY 20	FY 21	FY 22	Q1 23 A	Q2 23 A	Q3 23 E	Q4 23 E	FY 23E	FY 24E
Sales of Goods	90.4%	89.9%	92.1%	93.6%	94.2%	94.6%	94.5%	94.3%	94.3%
Sales of Services	9.6%	10.1%	7.9%	6.4%	5.8%	5.4%	5.5%	5.7%	5.7%
Total Revenues	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of goods	53.5%	54.1%	50.6%	43.8%	46.1%	49.0%	49.0%	47.1%	49.0%
Cost of services	75.3%	79.9%	79.0%	80.7%	90.3%	82.5%	82.5%	83.9%	80.0%
Total COGS	55.6%	56.7%	52.9%	46.2%	48.7%	50.8%	50.8%	49.2%	50.8%
Gross Profit-Goods	46.5%	45.9%	49.4%	56.2%	53.9%	51.0%	51.0%	52.9%	51.0%
Gross Profit-Services	24.7%	20.1%	21.0%	19.3%	9.7%	17.5%	17.5%	16.1%	20.0%
Gross Profit-Total	44.4%	43.3%	47.1%	53.8%	51.3%	49.2%	49.2%	50.8%	49.2%
G&A	49.6%	43.8%	31.3%	27.8%	26.3%	25.0%	25.0%	26.0%	26.0%
Payroll Expense	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Depreciation	3.1%	2.9%	1.4%	1.0%	1.0%	0.9%	0.8%	0.9%	0.9%
Opex	58.7%	50.9%	35.8%	31.1%	29.0%	28.8%	27.9%	29.1%	29.1%
Operating income	-14.4%	-7.6%	11.3%	22.7%	22.3%	20.4%	21.3%	21.6%	20.1%
Interest and Other	2.0%	1.3%	1.1%	0.7%	1.9%	1.7%	1.6%	1.5%	1.7%
Pretax income	-12.4%	-6.4%	12.4%	23.4%	24.2%	22.1%	22.9%	23.1%	21.8%
Tax Rate	18.2%	37.4%	30.6%	24.0%	18.2%	26.0%	26.0%	23.6%	26.0%
Net Income	-10.1%	-4.0%	8.6%	17.8%	19.8%	16.4%	16.9%	17.7%	16.1%
EBITDA	-6.8%	-0.7%	15.5%	26.0%	26.8%	23.6%	24.3%	25.1%	23.2%

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

Exhibit 2. Balance Sheet and Cash Flow Statement

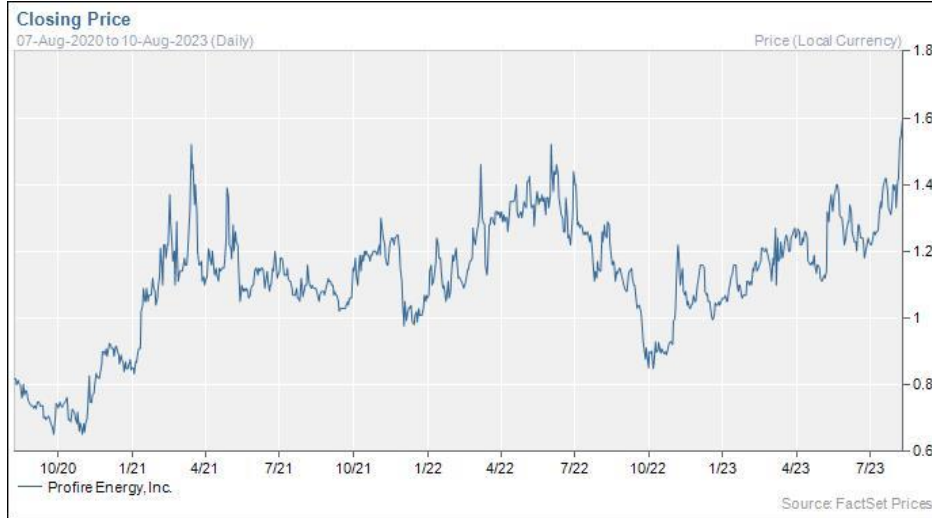
\$ in 000's	FY 20	FY 21	FY 22	FY 23E	FY 24E
Cash	9,148	8,188	7,385	13,390	26,085
ST Investments	2,389	1,014	1,154	1,896	1,896
A/R	3,720	6,263	10,886	12,265	12,878
Inventories	8,415	7,185	10,294	15,875	14,364
Prepaid Expenses & Other	2,165	1,586	2,315	2,802	2,942
Current Assets	\$ 25,836	\$ 24,236	\$ 32,034	\$ 46,228	\$ 58,165
LT Investments	6,064	8,260	7,503	7,213	7,213
Financing right of use asset	50	65	120	157	157
PP&E	12,022	11,186	10,424	10,842	11,270
Deferred Tax Asset	0	163	0	0	0
Intangible Assets	1,772	1,549	1,269	1,183	1,183
Goodwill	2,579	2,579	2,579	2,579	2,579
Total Assets	\$ 48,323	\$ 48,038	\$ 53,930	\$ 68,202	\$ 80,567
A/P	1,179	1,823	2,956	2,476	2,600
Accrued liabilities	1,197	1,872	3,574	4,709	5,030
Financing lease	39	30	54	66	66
Income tax payable	0	0	205	955	1,021
Current Liabilities	\$ 2,415	\$ 3,725	\$ 6,788	\$ 8,206	\$ 8,716
Deferred Tax Liability	523	136	489	694	694
Financing Lease Liability	13	36	68	93	93
Equity	45,372	44,141	46,584	59,209	71,064
Total Equity & Liab.	\$ 48,323	\$ 48,038	\$ 53,930	\$ 68,202	\$ 80,567

	FY 20	FY 21	FY 22	FY 23E	FY 24E
Net	(2,176)	(1,052)	3,948	10,865	10,414
D&A	1,177	1,256	1,101	834	572
Stock issued for services	443	567	815	1,304	1,442
Other	(123)	(176)	(240)	144	0
Working Capital	943	54	(5,107)	(5,721)	1,268
Operating Cash Flow	\$ 264	\$ 649	\$ 516	\$ 7,426	\$ 13,695
Other	3,314	(649)	612	(96)	0
Acquisition	0	0	0	0	0
CapEx	(1,547)	(169)	(601)	(1,107)	(1,000)
Investing Activities	\$ 1,767	\$ (818)	\$ 11	\$ (1,203)	\$ (1,000)
Equity	(153)	(795)	(1,341)	(242)	0
Lease Liability	(58)	(41)	(34)	(14)	0
Financing Activities	\$ (210)	\$ (836)	\$ (1,375)	\$ (256)	\$ -
FX	(31)	45	45	38	0
Change in Cash	\$ 1,789	\$ (960)	\$ (804)	\$ 6,005	\$ 12,695

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
- Update – Buy – December 20, 2022 – Price Target \$2.00
- Update – Buy – May 11, 2023 – Price Target \$2.00
- Update – Buy – August 11, 2023 – Price Target \$2.00

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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 3-Aug-23

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	24	69%	3	8.60%
Market Perform (Neutral)	11	31%	3	8.60%
Market Underperform (Sell)	0	0%	0	0.00%
Total	35	100%	6	17.20%

Analyst Certification:

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