Trickle Research

Every raging river, every great lake, every deep blue sea starts … with a trickle

Price Target & Allocation Upgrades

SOW GOOD

Sow Good Inc.

(OTC: SOWG)

Report Date: 08/17/23

12- 24 month Price Target: *$17.00

Allocation: **5

Closing Stock Price at Initiation (Closing Px: 07/17/23): $3.75

Closing Stock Price at This Allocation & Price Target Increase (Closing Px: 08/16/23): $5.00

Prepared By:
David L. Lavigne
Senior Analyst, Managing Partner
Trickle Research

Disclosure: Portions of this report are excerpted from Sow Good's filings, website(s), presentations or other public collateral. We have attempted to identify those excerpts by *italicizing* them in the text.

Sow Good Inc. (“SGI”) reported results for Q2F23. Those results included Revenues of $1.32 million, Net Income of <$3.32 million> and Basic EPS of <$.68>. The results compare to our estimates of $1.23 million, <$697,000> and <$.14>, respectively. On the face, while the Company bested our revenue estimates, we missed on both Cost of Goods Sold (“COGS”) and on Net Income (“NI”), but there were two extraordinary items that impacted each.

1) COGS were negatively impacted by a *“one-time inventory write down of $1,919,686 as SGI disposed of non-candy freeze dried products”.* To reconcile, subtracting this charge COGS would have been $776,134, which would have compared to our estimate of $733,147. In essence, adjusting out the write-down, normalized COGS for the quarter represented 59% of sales (41% gross margin) which compared to our estimate of 59.6% (gross margin 40.4%). Put another way, after adjusting for the write-down, margins were slightly better (60 basis points) than we projected.

2) Interest Expense for the quarter was $847,509, compared to our estimate of $92,880, for a difference of $754,629. Most of the difference represents the *“amortization of stock warrants issued as a debt discount”*. Recall, in the initiating coverage, we noted that insiders have been funding the Company’s startup phase via debt with attached warrants. This non-cash amortization represents the accounting charge for those warrants. Again, these are non-cash items, and from a practical standpoint, we typically do not attempt to model these types of adjustments. Rather, we generally try to reflect the impact of warrants through fully diluted share count methods. Regardless, in total we modeled a net loss of <$697,048>, which missed the actual loss of <$3.32 million> by <$2,622,952>. In short, the extraordinary items we discussed above sum to <$2,674,315>, thus absent these charges, the loss for the quarter would have been <$646,585> or slightly less than our projection, but largely in-line.

Setting aside the accounting nuances, we thought the quarter was telling. First and foremost, revenues were nearly *440 basis points* higher than the same period last year, and *550 basis points* higher than the sequential (Q1F23) quarter. We recognize that $1.3 million in revenue is a relatively small number and as such, multiple scale improvements need to be kept in perspective. However, we still view the increase as extraordinary. That said, we also recognize that the uninspiring results from prior quarters coupled with the extremely thin float (and associated trading volume) has provided some headwinds for the stock price. That said, as our model reflects, we expect SGI to continue to reflect breakout results for the second half of the current year, and to follow that with continued sequential growth through 2024 as well, and likely beyond our initiating model assumptions. We have made some adjustments to our initiating model, which we will cover below.

As we alluded to above, we have made some adjustments to our initiating model and those adjustments are centered on some of the narrative from the 2QF23 10Q filing. Specifically:

> *“…In the first quarter of 2023, anticipating rising market trends and a significant opportunity with disrupting the candy category, Sow Good launched its freeze-dried candy line. The Company has entered into partnerships with major retailers such as FYE, Big Lots, and Hy-Vee, and has a growing pipeline of other large retailers. With this launch, Sow Good constructed an additional two freeze driers during the second quarter of 2023 to meet the rapidly increasing retail demand. With its continuous growth and consistent sell-out within retailers, Sow Good anticipates freeze dried candy to be a major driver of its growth and has begun the process of constructing an additional fourth and fifth freeze drier to meet anticipated demand…”*

That narrative compares favorably to some of the assessments we laid out in the initiating coverage:

> *“…As we have stated elsewhere in this report, SGI has expanded its distribution space in anticipation of coming growth, and we think that includes an additional (fourth) dryer. Around*

> *that notion, our assumption is that the Company must believe that it can approach full existing capacity if it is planning on adding more? For reference, our model assumes the Company can get to full capacity run rates in 2H fiscal 2024. If that is the case, a fourth dryer could be purchased and deployed in time to provide additional capacity prior to their running out of capacity in the time frame. We recognize that approach may be a bit subjective, but without additional actual operating data, we think it is a reasonable place to start…"*

Obviously, the Company is adding a fourth *and a fifth* freeze dryer, and it appears that they are adding them more quickly than we speculated. That in turn leads us to believe that our model may be understating the trajectory here. Recall, our initiating models were based on our extrapolation of the store counts and associated metrics around the companies SGI identified in its announcements. Given the above narrative from the filing, we think it is fair to say that they have attracted some "*other large retailers"*, beyond those they have specifically identified. To be clear, we alluded to that scenario in the initiating coverage, but we did not model much of that. As a result, we have made some (upside) adjustments to the model, but we also think it is prudent to see another set of numbers to further validate some of our assumptions before we get too far out over our skis.

To summarize, we thought the quarter represented a good first step in the validation of our investment thesis that SGI is positioning for breakout revenue and earnings results, and we believe those results may lead to extraordinary expansions of the valuation of SowGood and the underlying shares. Specifically, as our new model reflects, while for the first half of fiscal 2023 (ended June 30, 2023) the Company reflected revenues of $1.5 million and (adjusted) basic EPS of <$.36>, we are projecting second half revenues of just under $9 million and basic EPS of $.28. Moreover, for fiscal 2024 we are projecting revenues of $29.6 million and basic EPS of $1.65. To highlight the point, that fully diluted EPS would represent a P/E multiple of just over 10X **our new $17.00 price target.**

As a result of what we believe is gathering and marked momentum in SGI's business, we are establishing a new 12-24 month price target of *$17.00 per share and we are raising our allocation from 4 to **5. We will reassess each as new information dictates.

Projected Operating Model

Sow Good Inc.						
Projected Operating Model						
By: Trickle Research						
	(actual)	(actual)	(Estimate)	(Estimate)	(Estimate)	(Estimate)
	3/31/2023	**6/30/2023**	**9/30/2023**	**12/31/2023**	**Fiscal 2023**	**Fiscal 2024**
Revenues	$ 198,930	$ 1,315,347	$ 3,629,019	$ 5,349,085	**$ 10,492,380**	**$ 29,575,886**
Cost of goods sold	$ 76,680	$ 2,695,820	$ 1,919,971	$ 2,594,149	**$ 7,286,620**	**$ 13,257,612**
Gross profit	$ 122,250	$ (1,380,473)	$ 1,709,048	$ 2,754,936	**$ 3,205,760**	**$ 16,318,274**
General and administrative expenses:	$ -	$ -	$ -	$ -	$ -	$ -
Salaries and benefits	$ 544,553	$ 538,916	$ 622,580	$ 656,982	$ 2,363,031	$ 2,791,518
Professional services	$ 46,206	$ 63,329	$ 76,290	$ 93,491	$ 279,316	$ 455,759
Other general and administrative expenses	$ 358,467	$ 483,260	$ 445,161	$ 513,963	$ 1,800,851	$ 2,383,035
Intangible Asset Impairments	$ -	$ -	$ -	$ -	$ -	$ -
Goodwill impairment	$ -	$ -	$ -	$ -	$ -	$ -
Total general and administrative expenses	$ 949,226	$ 1,085,505	$ 1,144,031	$ 1,264,436	**$ 4,443,198**	**$ 5,630,312**
Depreciation and amortization	$ 76,218	$ 7,413	$ 75,000	$ 75,000	$ 233,631	$ 300,000
Total operating expenses	$ 1,025,444	$ 1,092,918	$ 1,219,031	$ 1,339,436	**$ 4,676,829**	**$ 5,930,312**
Net operating loss	$ (903,194)	$ (2,473,391)	$ 490,016	$ 1,415,500	**$ (1,471,069)**	**$ 10,387,962**
Other income (expense):	$ -	$ -	$ -	$ -	$ -	$ -
Interest expense,	$ (498,336)	$ (847,509)	$ (97,880)	$ (197,880)	$ (1,641,605)	$ (731,520)
Other income	$ -	$ -	$ -	$ -	$ -	$ -
Gain on disposal of property and equipment	$ -	$ -	$ -	$ -	$ -	$ -
Gain on early extinguishment of debt	$ -	$ -	$ -	$ -	$ -	$ -
Gain on investment in Allied Esports Entertainment, Inc.	$ -	$ -	$ -	$ -	$ -	$ -
Total other income (expense)	$ (498,336)	$ (847,509)	$ (97,880)	$ (197,880)	**$ (1,641,605)**	**$ (731,520)**
Net Income (Loss)	$ (1,401,530)	$ (3,320,900)	$ 392,136	$ 1,217,620	**$ (3,112,674)**	**$ 9,656,442**
Weighted Average Number of Shares Outstanding, Basic	4,845,851	4,854,208	5,854,208	5,854,208	**5,352,119**	**5,854,208**
Weighted Average Number of Shares Outstanding, Diluted	4,845,851	5,700,610	6,877,218	7,034,903	**6,114,645**	**7,351,145**
Earnings Per Share, Basic	$ (0.29)	$ (0.68)	$ 0.07	$ 0.21	**$ (0.58)**	**$ 1.65**
Earnings Per Share, Diluted	$ (0.29)	$ (0.58)	$ 0.06	$ 0.17	**$ (0.51)**	**$ 1.31**

General Disclaimer:

Trickle Research LLC produces and publishes independent research, due diligence and analysis for the benefit of it investor base. Our publications are for information purposes only. Readers should review all available information on any company mentioned in our reports or updates, including, but not limited to, the company's annual report, quarterly report, press releases, as well as other regulatory filings. Trickle Research is not registered as a securities broker-dealer or an investment advisor either with the U.S. Securities and Exchange Commission or with any state securities regulatory authority. Readers should consult with their own independent tax, business and financial advisors with respect to any reported company. Trickle Research and/or its officers, investors and employees, and/or members of their families may have long/short positions in the securities mentioned in our research and analysis and may make purchases and/or sales for their own account of those securities. David Lavigne owns shares of Sow Good, Inc.

Trickle Research co-sponsors two microcap conferences each year. Trickle Research encourages its coverage companies to present at those conferences and Trickle charges them a fee to do so. Companies are under no obligation to present at these conferences. Sow Good has paid fees to present at past Trickle co-sponsored conferences and we will encourage them to do so in the future.

Portions of this publication excerpted from company filings or other sources are noted in *italics* and referenced throughout the report.

Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "Hold" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.

A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.

A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.