Trickle Research

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

Research Update

Sow Good Inc.

(OTC: SOWG)

Report Date: 01/16/24

12- 24 month Price Target: $23.00

Allocation: 6

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

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

Closing Stock Price at Allocation & Price Target Increase (Closing Px: 11/14/23): $9.00

Closing Stock Price at This Update (Closing Px: 01/16/24): $9.00

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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.

We were not expecting to see the following, but since the Company released preliminary 4QF23 and full Year 2023 results, we will provide some brief color. From the release:

Sow Good Inc.
Tue, January 16, 2024 at 5:30 AM PST

- ***Preliminary Fourth Quarter and Full Year 2023 Financial Highlights***

- *Fourth quarter 2023 revenue is expected to be between $9.54 and $9.57 million, marking a quarterly record and significant increase compared to $0.05 million in the fourth quarter of 2022.*
- *The Company's preliminary fourth quarter 2023 revenue was also an approximate 90% sequential increase over its third quarter 2023 revenue of $5.03M and an approximate 46% increase over the September year-to-date revenue of $6.55M.*
- *Full year 2023 preliminary revenue is expected to be between $16M and $16.12M, a significant increase compared to $0.43M in 2022.*

- ***2023 Operational Highlights***

Sow Good's production and operational capacity has grown extensively and continues to do so with the following advancements:

- *New Freeze Driers — Sow Good's ongoing construction of three additional freeze driers, slated for completion by the end of Q1 2024, is expected to more than double the Company's capacity.*
- *Monterrey, Mexico Corporate Offices — To drive continued expansion and support its growth, Sow Good will be opening a corporate office of approximately 1,500 square feet in Monterrey, Mexico by the end of January 2024. This office will house Sales, Graphics, Accounting, and IT Staff.*
- *Team Growth — Sow Good's corporate team has received powerful new additions, including a Director of Co-Manufacturing and Latin America and our CFO, maintaining Sow Good's lean yet highly efficient and collaborative team. The Company's production team has more than doubled in the last six months and is expected to continue expanding in 2024.*
- *SKU Expansion — For 2024, Sow Good has launched and is continuing to launch new SKUs, comprising diversified flavors, sizes, and textures that the Company anticipates will appeal to a broader customer demographic. Recent expansions include Sour and Sweet Spheres, "jumbo" versions of Sow Good's Bites SKUs, and Jumbo Vanilla and Neapolitan Crunch Cream freeze dried ice cream sandwiches. These expansions reflect Sow Good's highly agile product and partner development.*

"*This exciting growth in the fourth quarter and throughout 2023 is a testament to the dedication, strategic and manufacturing expertise, and passion for innovation ingrained in our team," said Claudia Goldfarb, Sow Good's CEO. "As much as we have grown over the past year, we have continued to support robust customer demand, grow our production capacity, and expand our partner base as we enter 2024. To that effect, we are thrilled to open our doors to new retail and wholesale customers and provide more freeze-dried treats that captivate consumers and revolutionize the candy industry*."

This release contains certain estimated preliminary financial results for the fourth quarter and fiscal year ended December 31, 2023. These estimates are based on the information available to us at this time. Our financial closing procedures for the fourth quarter and full year 2023 are not yet complete and, as a result, our actual results may vary from the estimated preliminary results presented here due to the completion of our financial closing and review procedures, the execution of our internal control over financial reporting, final adjustments, and other developments that may arise between now and the time the financial results for the fourth quarter and fiscal year ended December 31, 2023 are finalized. The estimated preliminary financial results have not been audited or reviewed by our independent registered public accounting firm. These estimates should not be viewed as a substitute for our full interim or annual financial statements. Accordingly, you should not place undue reliance on this preliminary data.

Our Q4F23 estimate was for revenue of $7.2 million providing a preliminary upside of around $2.3+ million to their $9.5 million guidance, or about 32% to the upside. For fiscal 2023, they are looking at preliminary numbers of $16 million versus our estimate of $13.7 million, however, recall, when we initiated the research 6 months ago (July 18,2023), our revenue estimate for F2023 was for $10.2 million. Thus, from that initiation, the upside surprise for F2023 looks like something close to ***+60%.*** In our prior research, we have stepped through our methodology regarding how we arrived at our estimates (based largely on our assessments around customers they had announced publicly), but if we are being honest, when we published those numbers in July we thought (and we think we were right at the time) that the street likely believed our estimates were off the mark. As it turned out, that would have been correct, except, we suspect the sense was that our error was too high versus too low. In short, the Company's candy launch, as manifested in the numbers for 2HF23 has been extraordinary.

Looking ahead here are a few *preliminary* observations of our own.

Our most current estimate is from our 11/14/23 update, and it reflects F2024 revenues of roughly $42 million. Q4F23 looks like $9.5 million (which annualizes to $38 million) and was achieved with 3 dryers. Since (as the release notes and we have discussed in prior updates) they expect to have 6 dryers operational by the end of Q1F24, it sems highly likely that our current estimate for F2024 is likely lite, and perhaps significantly lite.

We have attempted to model corresponding increases in SG&A, versus higher anticipated revenues. For instance, our most recent model assumes a $4.1 million increase in SG&A for F2024 versus F2023. As the release notes, they have added some key personnel to help drive/manage growth, and they have added facilities, including offices in Mexico (which we did not see coming). To translate, we are unsure if our model properly reflects appropriate increases in SG&A relative to corresponding marked increases in revenues. For instance, we think it is likely that Q4F23 and perhaps the first half of F24 could include some extraordinary charges to support the revenue growth, both achieved and planned, that we do not have any particular visibility on - in part because they have not been here before. Further, we would submit from experience, that as serial entrepreneurs, the Goldfarb's are quite proficient at bootstrapping businesses to sustainable success, which includes their willingness to "wear many hats" along the way and to (personally) do whatever needs to be done to make it work. In retrospect, we would further suggest their willingness to support SowGood via personal investments along the way support that view. That being the case, it would not be surprising to us if SG&A settled in at higher levels than we are anticipating as they hand off some of their multiple duties to others. On the other hand, we think it is fair to suggest that their "bootstrapping" frugality is also likely an ingrained part of their entrepreneurial mantra, so we do not expect them to add unneeded expenses either.

To summarize the two prior paragraphs, our model and associated projections clearly need some updating, but we would rather do that from a point of better confirmed visibility (following the filing/release of audited F2023 numbers, or the announcement of further guidance), before we go down that path. In the meantime, we would provide one further anecdotal piece of information that readers can interpret as they will.

As part of our due diligence, we try to support our processes with site visits or other "boots on the ground" analysis when possible. For instance, we visited SowGood management at its office prior to our coverage. Subsequently, we also visited a handful of Five Below, Inc. (Nasdaq: FIVE) retail stores in and around us since we believe that is one of SowGood's largest customers. Anecdotally, the product was difficult to find. Most notably at the store closest to us, it took three visits to finally find some (restocked) on the shelves. The photo above references that visit. Again, that is anecdotal, but it was our experience.

Obviously, we find the above announcement constructive and further supportive of our notion that the Company is in the midst of an extraordinary revenue and earnings expansion. To that end, we expect the Company to operate through much of 2024 with at least double the capacity that it operated through 2023. Specifically, we know they will operate through F2024 with 6 driers, versus 3 dryers *at the end of* F2023. Moreover, as the recent announcement notes, they recently opened offices in Monterrey, Mexico, which to us (speculatively) ultimately looks like the precursor to a manufacturing addition. We will wait for further data points before we wade into that. Again, while it appears that the tea leaves are pointing to higher F2024 revenue results than we are projecting, we will also wait for a few more data points to recast the model. In the meantime, we reiterate our Allocation of 6, and our 12-24 month Price Target of $23.00 per share.

<u>Projected Operating Model</u>

Sow Good Inc.						
Projected Operating Model						
By: Trickle Research						
	(actual)	(actual)	(actual)	(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	$5,034,203	$7,160,815	**$ 13,709,294**	**$41,652,367**
Cost of goods sold	$ 76,680	$ 2,695,820	$2,717,254	$3,638,756	**$ 9,128,510**	**$20,771,976**
Gross profit	$ 122,250	$ (1,380,473)	$2,316,949	$3,522,059	**$ 4,580,785**	**$20,880,390**
General and administrative expenses:	$ -	$ -	$ -	$ 0	$ 0	$ 1
Salaries and benefits	$ 544,553	$ 538,916	$1,262,332	$1,509,298	$ 3,855,099	$ 7,598,284
Professional services	$ 46,206	$ 63,329	$ 294,720	$ 146,608	$ 550,863	$ 716,524
Other general and administrative expenses	$ 358,467	$ 483,260	$ 350,082	$ 407,412	$ 1,599,221	$ 1,824,786
Intangible Asset Impairments	$ -	$ -	$ -	$ -	$ -	$ -
Goodwill impairment	$ -	$ -	$ -	$ -	$ -	$ -
Total general and administrative expenses	$ 949,226	$ 1,085,505	$1,907,134	$2,063,318	**$ 6,005,183**	**$10,139,593**
Depreciation and amortization	$ 76,218	$ 7,413	$ 72,190	$ 75,000	$ 230,821	$ 315,303
Total operating expenses	$ 1,025,444	$ 1,092,918	$1,979,324	$2,138,318	**$ 6,236,004**	**$10,454,896**
Net operating loss	$ (903,194)	$ (2,473,391)	$ 337,625	$1,383,741	**$ (1,655,220)**	**$10,425,494**
Other income (expense):	$ -	$ -	$ -	$ -	$ -	$ -
Interest expense,	$ (498,336)	$ (847,509)	$ (3,641)	$ (171,880)	$ (1,521,366)	$ (627,520)
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)	$ (3,641)	$ (171,880)	**$ (1,521,366)**	**$ (627,520)**
Net Income (Loss)	$(1,401,530)	$ (3,320,900)	$ 333,984	$1,211,861	**$ (3,176,586)**	**$ 9,797,974**
Weighted Average Number of Shares Outstanding, Basic	4,845,851	4,854,208	5,123,735	5,603,083	**5,106,719**	**5,603,083**
Weighted Average Number of Shares Outstanding, Diluted	4,845,851	5,873,295	8,066,577	7,308,910	**6,523,658**	**7,606,400**
Earnings Per Share, Basic	$ (0.29)	$ (0.68)	$ 0.07	$ 0.22	**$ (0.62)**	**$ 1.75**
Earnings Per Share, Diluted	$ (0.29)	$ (0.57)	$ 0.04	$ 0.17	**$ (0.49)**	**$ 1.29**

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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.