Trickle Research

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

Initiating Research Coverage

ALLIANCE ENTERTAINMENT

Alliance Entertainment Holding Corporation

(Nasdaq: AENT)

Report Date: 05/06/24

12- 24 month Price Target: $4.25

Allocation: 4

Closing Stock Price at Initiation (Closing Px: 05/06/24): $2.00

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

Company Overview

Alliance Entertainment Holdings, Inc. ("Alliance") is a leading global wholesaler, direct-to-consumer ("DTC") distributor and e-commerce provider for the entertainment industry. Alliance stocks the world's largest selection of music, movies, video games, gaming hardware, arcades, collectibles, toys and consumer electronics and is a gateway between brands and retailers. Alliance is a trusted omnichannel supplier to Walmart, Amazon, Best Buy, Costco, Target, Kohl's, BJ's, Meyer, Dell, Barnes and Noble, and 2000 additional retailers and wholesalers worldwide, and a trusted distributor for Disney, Paramount, Sony Pictures, Warner Brothers, Universal Pictures, Microsoft, Nintendo, Activision, Electronic Arts, Sega, Mattel, Hasbro, Funko, Arcade1Up, Universal Music, Sony Music, Warner Music Group,and 600 others. Alliance has over 200 customers that sell online worldwide and Alliance ships to more than 35,000 storefronts in 72 countries and has over 325,000 SKU's in stock to sell to the largest retailers and wholesalers in the world.

Alliance consolidates and distributes a vast portfolio of entertainment products, while a proprietary database powers, retailers, online music and gaming offerings, including Vinyl, CDs, DVDs, Blu-ray, gaming products and retro arcades. Alliance has invested in enhancements to our automated handling equipment, which reduced shipping time, streamline order processing, reduce labor costs and also improves overall warehouse management. Just over a year ago, we installed an automated storage retrieval system at our Shepherdsville warehouse. This improved warehouse operations allowing us to achieve increased levels of speed, reliability, capacity and precision that resulted in significant cost savings. This slide highlights our strategically located operations that include seven offices and three distribution centers, including our 873,000 square foot facility in Shepherdsville, Kentucky. In 2023, warehouse shipments totaled over 70 million units through our highly skilled workforce with tech enabled facilities and infrastructure that allows Alliance to achieve industry leading speed and accuracy metrics.

Alliance provides state-of-the art warehousing and distribution technologies, operating systems and services that seamlessly enable entertainment product transactions to better serve customers directly or through our distribution affiliates. These technology-led platforms with access to the Company's in stock inventory of over 325,000 SKU products, consisting of vinyl records, video games, compact discs, DVD, Blu-Rays, toys and collectibles, combined with Alliance's sales and distribution network, create a modern entertainment physical product marketplace that provides the discerning customer with enhanced options on efficient consumer-friendly platforms inventory. Alliance is the retailers' back office for in store and e-commerce solutions. All electronic data interchange ("EDI") and logistics are operational and ready for existing retail channels to add new products.

Alliance is also a leader in vendor managed inventory solutions, providing solutions tailored to our customers to support their inventory needs. These value add services provide a highly technical critical business function for our partners.

Management believes Alliance's existing Service, Selection, and Technology offering has well-positioned the Company to capitalize on shifts towards e-commerce and Omni-Channel strategies, especially with retailers and manufacturers vastly increased reliance on our DTC fulfillment and distribution partners. Alliance's goal has always been to provide all the meta-data of content and images, service, selection, and purchasing to Omni-Channel retailers to expand their selection to compete with the leading on-line retailer. With over 1,200 employees worldwide, Alliance has over 4,000 unique customers and over 35,000 "Ship-To" locations.

Alliance was founded in 1990 (previously named CD Listening Bar, Inc.). Through a series of acquisitions and organic growth, Alliance has expanded and strengthened its global footprint and product breadth, and greatly increased its service capabilities. Since its inception, Alliance has made nine accretive business acquisitions, including Phantom Sound and Vision, MSI Music, Infinity Resources, Alliance, ANConnect, *Mecca Electronics, Distribution Solutions, Mill Creek, and COKeM. Management believes that Alliance's ability to successfully integrate acquisitions is underpinned by its highly efficient operating systems and experienced leadership team.*

On February 10, 2023 Alliance consummated a business combination with a publicly traded Special Purpose Acquisition Company ("SPAC") called Adara acquisition Corp. The original S-4 for this combination was filed with the SEC on July 11, 2022, or approximately 7 months prior to the consummation. Unfortunately, all but 1% of the Adara shareholders exercised their rights under the SPAC agreement to redeem their shares for cash. Given that the SPAC escrow was just under $115 million, we assume Alliance was hoping to get a majority of the Adara shareholders to exchange their Adara shares for those of the new combined company. That did not happen. We suspect some of that had to do with the fact that from the time of the initial announcement of the business combination through its consummation, Alliance's business encountered some challenges around prevailing supply chain issues related to the pandemic. We will address those throughout this report.

As we will also discuss further in this document, Alliance's supply chain problems also created working capital challenges that put them in violation of some of the covenants of their credit facility. Again, we suspect management anticipated remedying those through the Adara combination. Regardless, the Company was forced to replace the credit facility, which they accomplished on December 21, 2023. Our initial introduction to the Company came about two weeks later in January (2024), and at the time our sense was that putting the working capital challenge behind them was likely a catalyst for the stock. In retrospect, the stock doubled from that point, so that particular sense was apparently prescient.

Since our introduction to management, we have spent considerable time trying to understand Alliance's business, and that includes the minutia of their navigation through the pandemic, as well as the business combination addressed above. Our general thesis, which we lay out in this report, is that Alliance is a market leader in a very challenging environment. That notion on the face includes both positive and negative context. Further, we think there has been a considerable amount of "noise" around the story, which we believe has made identifying the opportunity going forward difficult. However, as we will attempt to illustrate, we think the business is beginning to normalize again, which we believe should provide better visibility including identifiable/defensible paths to higher valuations from current levels.

Industry Overview

Alliance operates across a handful of industries or verticals therein, but collectively we refer to their core competency as physical entertainment fulfillment and distribution. That said, we have attempted to provide some color regarding these relevant industries and how Alliance operates around, through and in conjunction with each. That requires some basic understanding of the workings of these industries so we will try to provide some of that.

For the sake of (our) definition, "physical entertainment" includes physical form factors that store/deliver music, movies, video games and other associated forms of entertainment. More specifically, these include CDs, DVDs, vinyl record albums, video game cartridges and other similar items. In order to frame the posture of these types of entertainment delivery in today's digital world a brief overview of these industries as well as a history of the "digital transformation" in each might be helpful.

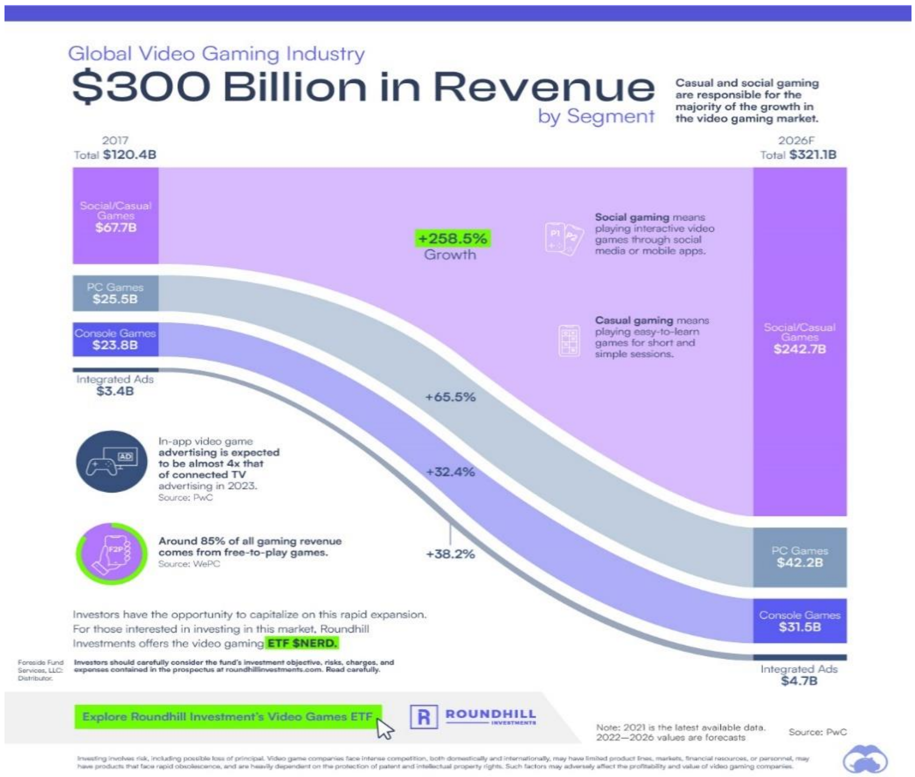
According to data released by the Entertainment Software Association and Circana, U.S. Consumer Video Game Spending Totaled $57.2 Billion in 2023 (prnewswire.com) :

> *"Overall consumer spending on video games in the United States totaled $57.2 billion in 2023. This figure reflects profits from all video game content categories (physical and digital full-game,*

downloadable content/microtransactions (DLC/MTX) and subscription spending across console, cloud, mobile, portable, PC and virtual reality (VR) platforms), video game hardware and video game accessories".

"These figures reinforce the position of the video game industry as a growth engine for the United States economy," said ESA President and CEO Stanley Pierre-Louis. "When combined with the fact that nearly two-thirds of Americans play video games regularly, cutting across all demographics and backgrounds, these results confirm the video game industry's impact as an economic and creative powerhouse with far-reaching cultural influence."

Table 1.



Visualized: $300B of Video Gaming Revenue, by Source (visualcapitalist.com)

According to the International Federation of the Phonographic Industry ("IFPI") IFPI Global Music Report: Global Recorded Music Revenues Grew 10.2% In 2023 - IFPI :

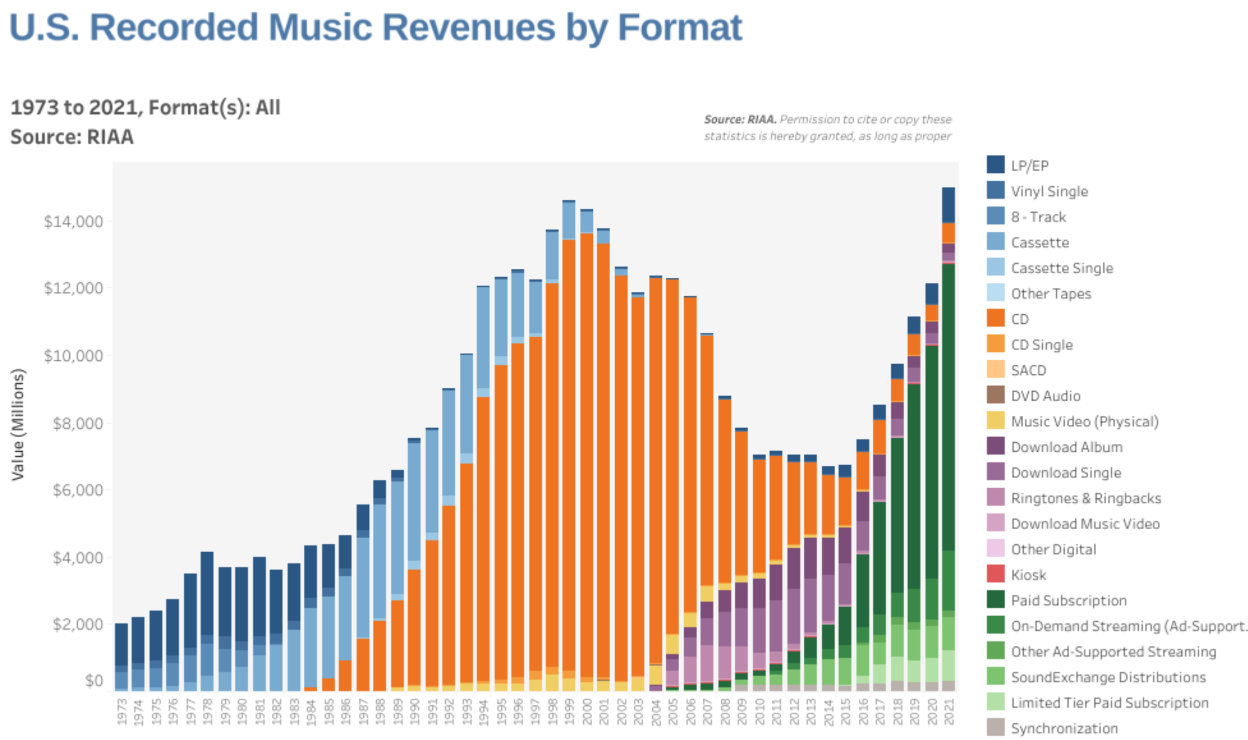
Global recorded music revenues increased by 10.2% in 2023, driven largely by growth in paid streaming subscribers, according to IFPI, the organization that represents the recording industry worldwide. Figures released today in IFPI's Global Music Report show that total trade revenues reached US$28.6 billion in 2023, the ninth consecutive year of growth.

Streaming revenues accounted for the majority of revenue growth and total share of the market. Subscription streaming revenues alone grew by 11.2% and made up almost half (48.9%) of the global market. In 2023 the number of paid subscriptions to music streaming services passed 500 million for the first time and there are now more than 667 million users of paid subscription accounts, with household penetration varying greatly by country.

There was strong growth in other formats too with a double-digit percentage increase in physical revenues (up by 13.4%) *and gains in income from performance rights (up by 9.5%). This is the third consecutive year in which both digital and physical revenues have increased simultaneously.*

According to Statista Music industry revenue in the U.S. 2023 | Statista *"In the United States, recorded music industry revenue amounted to 11 billion U.S. dollars in 2023, which is more than twice as much compared to 2009".*

Table 2.



2021 RIAA Music Industry Data Confirms that Physical Media is Still Very Relevant - ecoustics.com

According to the Digital Entertainment Group f1_Year-end-2023-Digital-Entertainment-cover-note-with-grid.pdf (degonline.org) :

*"Overall U.S. consumer spending across digital and physical home entertainment formats in 2023 was **$43 billion**, a 16.8 percent increase from the almost $37 billion consumers spent in 2022, driven by the continued growth of Subscription Video on Demand ("SVOD"), as well as theatrical new releases offered for digital purchase in premium and traditional windows. Consumers spent $**41.4** billion on digital entertainment purchases (EST2), rentals (VOD2) and subscriptions for the full year, a jump of 19.3 percent over full year 2022. Spending on subscription streaming rose 21.5 percent for full year 2023, topping $37 billion.*

Doing a bit of math, the remainder of the above noted sales ($43 billion minus $41.4 billion or about $1.6 billion) is related to DVD and Blu-ray sales, rentals of the same.

Table 3.

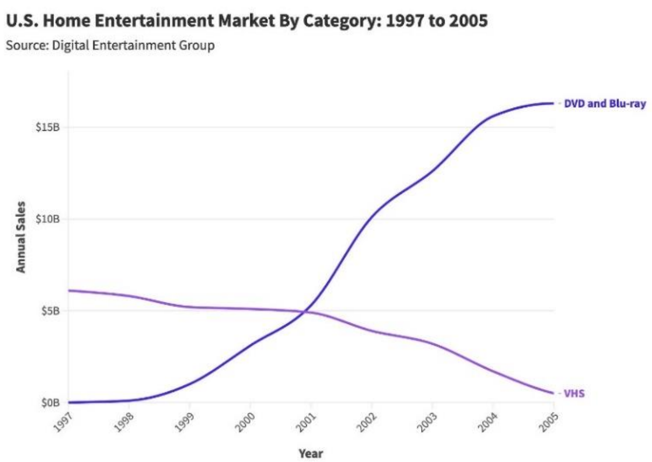
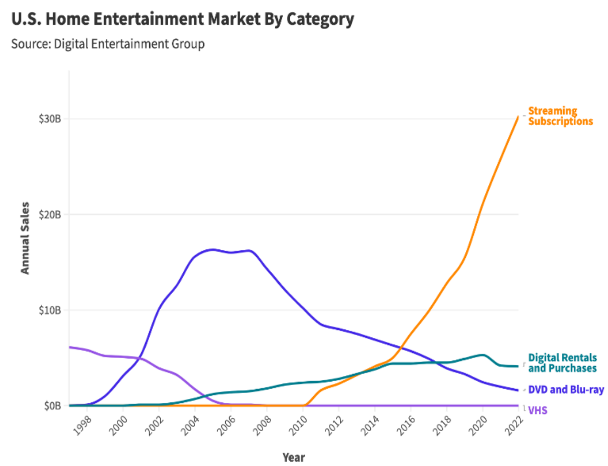


Table 4.



The Rise, Fall, and (Slight) Rise of DVDs. A Statistical Analysis (statsignificant.com)

Stepping back for a moment, the above narrative and associated graphics provide a handful of cogent, but likely not surprising notions:

- Annual collective domestic recorded audio/video and gaming revenue is considerable. If we add up the numbers provided above, they represent domestic 2023 revenues of approximately $111 billion.

- The transition from physical media to streaming and digital download formats has been rapid and definitive. Granted, that transition has been more dramatic for some physical mediums than for others. For instance, physical mediums in the gaming space have performed much better than DVDs/Blu-rays in the movie/video space. In addition, within the music business, vinyl LPs have increasingly outperformed CDs over the past few years.

- Over time, and as the illustrations above suggest, changes in technology have ultimately driven the rise and fall of different formats. In video, while the introduction of the cassette started the displacement of the vinyl LP, both were ultimately overrun by CDs. In video, DVDs replaced VHS, to ultimately be replaced by digital download and streaming.

- Technology advances have not only displaced legacy technologies, but in most instances, those technology advances have provided entirely new growth legs to these industries. In the recorded music business, the introduction of digital download and streaming formats ostensibly rescued the industry from declines it experienced from its peak in or around 2000. (There was a notable catalyst to that, which we will address later). Further, the advent of downloadable and/or streaming movies has provided marked growth for the movie industry both in terms of overall sales as well as (and perhaps in part as a result of) the marked expansion of content. Granted, some of that "growth" may be zero sum since it has come at the expense of movie theaters, but we think it is fair to say that things like advanced codec technologies as well as the continued improvement and reach of high-speed internet and mobile networks have propelled the industry to new and growing heights. However, as we will attempt to illustrate further below, while these technologies have provided clear net advantages over the legacy formats they have displaced, *they are not perfect substitutes for all of these*. We believe that distinction provides opportunities for Alliance.

To expand on our "not perfect substitutes" notion above, we would submit the following regarding particular physical recorded entertainment formats.

- Download and/or streaming options clearly provide advantages in terms of accessibility, mobility and ease of use. Further, in our view, they also address some of the disadvantages that LP/CD buyers lamented prior to the availability of these options, namely the ability to purchase a single track rather than having to purchase an entire album/cd that may include songs that the purchaser does not care to hear. To that end, prior to streaming options, many consumers created cassette and later cd mixes of their favorite songs that equate to today's "playlists". Moreover, while this observation may not be true in all instances, or even over time, we suspect for many consumers streaming options are less expensive in the aggregate, than purchasing physical formats.

- Some music consumers prefer the sound of an LP to that of CD's, downloads or streaming. Technically, that is the "analog vs. digital" argument that has been raging since the dawn of the CD. Succinctly, there is considerable debate about which formats provide the most precise recording of the original, and that includes science around what the human ear is even capable of hearing and a host of other observations. Further, that debate inevitably leads into other variables that impact the perception, and those include a variety of things like the quality of the devices transmitting the music. In short, it is not a stretch to believe music played through a high-end stereo system will sound better than the same music delivered through a cell phone. From that perspective alone, one could envision why *some* consumers may be willing to listen to music over their phone and through a set of headphones while they are at the gym, but if they are listening from their home theater systems, they may prefer a "better" format. The point is, on some level, and perhaps to varying degrees in terms of the delivery music or video, some consumers prefer the perceived sound/quality of physical formats to those of streamed alternatives, and as long as those preferences persist in some meaningful number, we suspect companies like Alliance will remain in the business of providing them.

- It is *not* all about the music. According to entertainment industry data and insights company Luminate (New Report: 50% of Vinyl Record Purchasers in U.S. Don't Have a Record Player americansongwriter.com) "only 50% of the people who bought a record in the past year own a record player. (And only 15% of music listeners overall own one)". We found that insight particularly telling for those in the business of selling vinyl records. As we noted above, some consumers buy LPs/vinyl records because they prefer the sound, but apparently for a considerable number of other consumers, the sound has nothing to do with it. We think vinyl records have managed to work their way onto the "collectible" line of consumer products, and it is not difficult to understand how/why that has happened. In retrospect, even in the "heyday" of vinyl through the 1970's, the visuals of the album cover were an integral part of the marketing of and attraction to an album, which by itself, had little to do with the actual music. We submit, the Beatle's White Album, which is one of the highest selling albums of all time, stands in contrast to our cover art notion, but generally we believe vinyl has carved out a piece of the music merchandise market, alongside tee-shirts, ball caps, posters etc. We would add, as we understand it, Alliance ships **over 40%** of all vinyl records sold in the U.S. today.

- Purchasing physical media is the only way to actually "own" it. Consumers who utilize download and/or streaming services may or may not be aware that "purchasing" content from one of these providers does not afford the purchaser access to the content for an indefinite amount of time. For any number of reasons, providers may lose access to certain titles/libraries, and in that case, they can no longer allow their customers to access the content on demand, *even if they think they paid to do so*. That reality challenges the providers' use of the word "purchase", but we are confident it is in the fine print of these providers' Terms and Conditions.

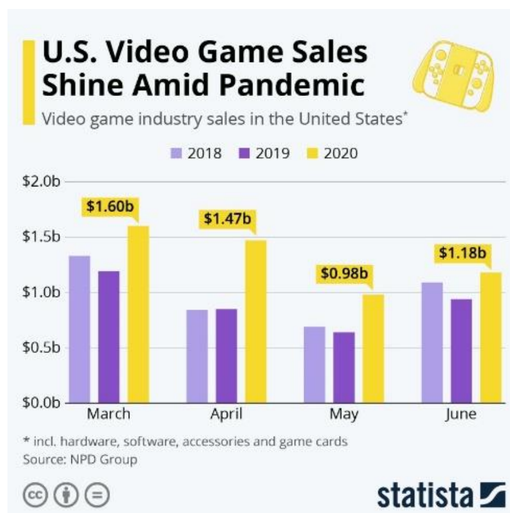
- If consumers have been lucky enough to avoid the "purchase that's not really a purchase", scenario above, they may have encountered another problem associated with downloads/streaming vis-à-vis physical purchases. Streaming services actively manage access to the content they provide their customers. In short, if a consumer wants to watch Home Alone in the middle of July, they may very well be able to stream it for free, however, if they want to do the same in the middle of December, they may need to rent it. Those who own the dvd, and (still) have a dvd player, can watch it whenever they would like and at no additional charge.

- In addition to the above, there is content that is simply not available from *any streaming service* and that list includes movies that many would likely recognize. There are a handful of reasons for that situation, but the fact remains, they are not available…anywhere. Again, the only true guaranteed, perpetual on demand access a consumer has to a movie, is the physical dvd in their possession. To reiterate, *purchasing physical media is the only way to actually "own" it* and we believe there are consumers who are keenly aware of that, and others who are becoming more aware of it, which we think provides continued opportunity for Alliance.

While much of what we have provided above addresses some of the industry's transition away from physical media, there are some other industry level nuances that we think are worth noting, as we think they are topical to understanding Alliance's challenges and opportunities.

While the pandemic proved cataclysmic for many industries and the businesses within them, the home entertainment industry was one of the clear exceptions and **Table 5** provides an example of just one segment of that. Alliance was part of that phenomenon for example, for Fiscal 2021 and Fiscal 2022 (ended June 30, 2021 and June 30, 2022) Alliance reported revenue of $1.33 billion and $1.4 billion and net income of $34 million and $28.6 million respectively. Those numbers compare to fiscal 2023 results of $1.2 billion and <$35.4 million> respectively. We will revisit that relative performance further in this document, but suffice it to say, like others in the industry, the Company was able to capitalize on the shelter-at-home dynamics of the pandemic. We believe that success set some pieces in motion that are topical to the story today which includes providing some challenges in terms of modeling the business against that comparative backdrop.

Table 5.



As we alluded to above, Alliance participates in a variety of markets that we refer to as physical entertainment fulfillment and distribution, which includes the music industry, the movie/video industry, the gaming industry, toys and collectibles and others. The industry has been described as "labyrinthine", a description we concur with, and it may be an understatement. Frankly, the complexities across these industries are far beyond the scope of this report, but we will try to touch on some things that we think are particularly important, especially as they pertain to Alliance.

Collectively, the industries in which Alliance operates have experienced a fair amount of volatility over the past several years. We think much of that volatility can be traced to the impact of new/disruptive technologies that effectively reshuffled the deck(s) in terms of how content was controlled, distributed, priced and consumed. Again, the impact has been profound. For instance, MP3 is a data compression technology developed in Germany in the late 1980's and early 1990's that allows users to copy a high-quality audio file. The value of MP3 was (is) that it yields a high-quality copy using low bitrates, which allows the copy to be done inexpensively and quickly. While the developers were trying to figure out a business model that could monetize their creation, MP3 found its way into the public domain. From The MP3: A History Of Innovation And Betrayal : The Record : NPR :

> *In 1997 as MPEG's encoding system got out into the world, it began to spark the imagination of users who definitely weren't thinking of Fraunhofer's* (the developer of MP3) *bottom line. Before its second birthday, the MP3 was setting fires that its creators couldn't put out. The story of how the technology was hijacked and adapted for widespread consumers contains not only the roots of the war that the music industry would later wage over the tiny, compressed, user-friendly files, but also echoes of some of the very ideas that war was fought over: intellectual property, copyright, technology, theft, control and the free distribution of ideas and products that had taken years to realize.*
>
> *"There were more and more people using this technology to store music on their hard discs. The idea was [originally] that encoders would be much more expensive. ... In, I think it was '97, some Australian student bought professional grade — from our point of view — encoding software for MP3 from a small company in Germany. He paid with a stolen credit card number from Taiwan. He looked at the software, found that we had used some Microsoft internal application programming interface ... racked everything up into an archive and wired some Swedish side, [and] put that to a U.S. university FTP site together with a read-me file saying, 'This is freeware thanks to Fraunhofer.'*

The narrative above set the stage for the proliferation of peer-to-peer file sharing platforms, perhaps most notably Napster. The music industry frantically attempted to repel the proliferation of file sharing via moral suasion, technology patches, litigation etc., some of which ultimately worked to shut down major portions of the file sharing apparatus, however, they could not put the "genie back in the bottle". Napster launched in mid-1999, and as a result of unsuccessful litigation, ceased operations in the first half of 2001. While short lived, at its peak in late 2000 and early 2001, the platform had attracted over 60 million users across the globe, *freely* sharing millions of music files. The catastrophic financial impact of file sharing can be seen in **Table 2** above. It is no coincidence that recorded music sales peaked in 1999, the same year Napster launched, and took *over 20 years* to fully regain those sales thresholds. Despite the industry's best efforts, the digital transfer of music was here to stay, paving the way in our view, for the digital transfer of video and gaming as well.

In our view, what was/is particularly telling about the Napster/file sharing phenomenon, was that it exposed some of the leaks in the moat the music industry had forged over many years. That moat included in part, a small number of large and powerful record labels that controlled the content (artists), the marketing (radio, print, media etc.), the distribution (retail) and by extension, the price of recorded music from start to finish. In short, the fast, inexpensive digital distribution of music ultimately undermined each of those advantages. Further, we think it is fair to say that the digital technologies that enabled that disruption did not emerge under the radar of the industry's biggest players, but rather, they emerged despite those players' best efforts to ignore, dismiss and suppress them. To reiterate, the digital disruption that started in music also created the same disruption in the recorded movie industry, and in the gaming industry largely for similar reasons. That said, despite the transformation, remnants of these industries' legacy footprints remain today, and provide some of the complexities we referenced above. We will edify, but first we have one additional observation regarding the impact that file sharing has had on the music industry specifically.

As we alluded to above, the pre-Napster music industry could reasonably be described as an oligopoly. That is, it was dominated by a small handful of record labels that controlled not only the content (artists), but also the marketing and distribution of the recorded music landscape. That made for a very challenging environment for independent ("indie") artists. At that time, we suspect the term "indie" was more practically related to the lack of backing from one of those few major labels than it was to any sort of artistic freedom. (Maybe Chris Kristofferson/Janis Joplin had that right?). That said, in our view the digital "new-world order" provided marked openings for artists who could not, or perhaps did not wish to sign with major labels. To that point, we believe that indie labels in the aggregate currently control just under 1/3rd of market share. Further, we believe that portion relative to the large (remaining 3) labels has increased considerably post-Napster, although the large labels continue to acquire smaller emerging indie players so the "organic" change in market share is difficult to measure. All things considered, we think it is fair to say that the current environment is more favorable for indie artists because they can gain access to millions of listeners and be paid from streaming services without the representation of a large label. By extension, we believe access to and perhaps the number of indie artists (as well as the genres they represent) has likely grown dramatically in the post Napster era. Improvements aside, we also know that the environment remains challenging for most artists, which brings us to our point.

Despite access to more fans via social media and revenue sharing from streaming services, indie artists still generate the bulk of their revenue from live performance and the sale of merchandise, including physical CDs and LPs. To that end, consider the following math from atVenu How Much Money Artists Make in Streaming Royalties vs. Merchandise Sales (atvenu.com) :

> ***…If you are being streamed millions of times then it is still a good source of revenue right?***
>
> *Sure, but how much revenue? Using the royalty conversion of $0.004 per stream, if you are streaming one million times you would make $4,000. To make $1M in streaming royalties you would need to be streamed 250 million times. In comparison, to make $4,000 from merchandise you would need to sell 115 shirts. To make $1M? 28.5K shirts.*
>
> *1M Stream = $4,000 = 115 T-shirts sold*
>
> ***In 2023, the average artist made $10K per show in Gross Merchandise Sales. Based on 2022 Spotify data, 61% of artists on Spotify made less than that from a year's worth of royalties.***

As we will delineate further in the **Products/Services Overview** below, Alliance's AMPED division has experienced marked success serving independent artists and labels, as well as new and emerging genres worldwide by providing them the opportunity to generate revenue from their recorded music. We are comfortable suggesting that opportunity is available to many more indie artists today than in the pre-Napster period, and we think Alliance is a meaningful and growing contributor to that dynamic.

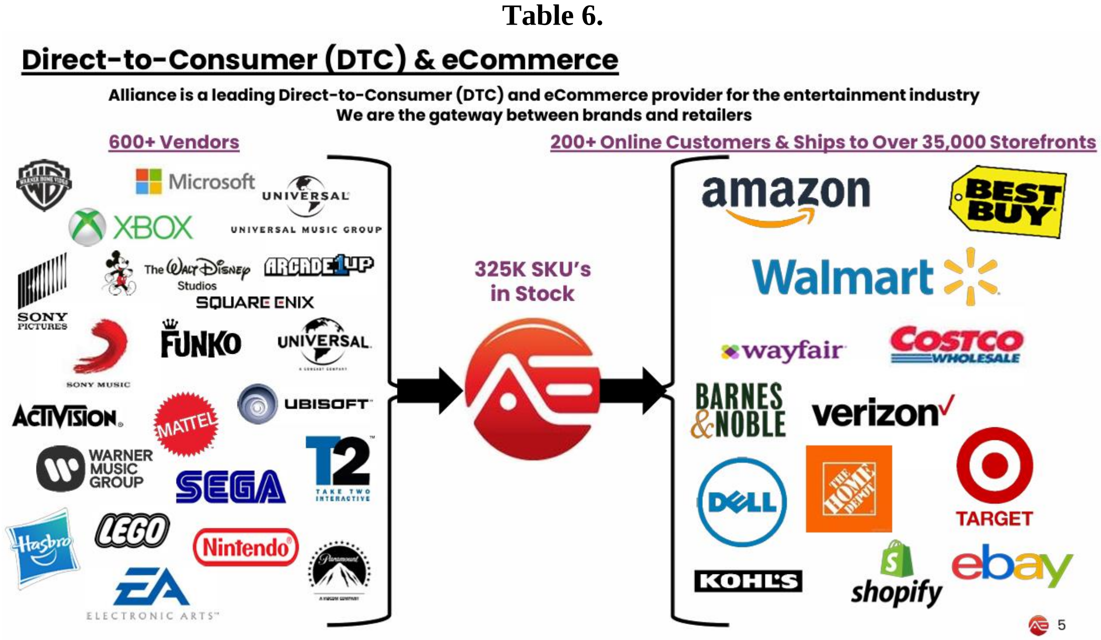
The industries Alliance operates within include a web of relationships along the entirety of the supply chain and those relationships include some combinations that in our view are unintuitive. For example, Alliance has suppliers and/or customers that are also their competitors in certain instances. They have studios for which they fulfill and/or distribute only certain pieces of that studio's content. They have relationships with retailers they sell only certain content to but not all of their content, and in some instances the studios or labels they distribute for may dictate who they can and cannot sell some or all of their content to. Further, while the Company primarily sells physical content, **it is also able to capture overrides on the digital sale of some of the content it represents**. Frankly, the combinations across the supply chain in terms of relationships and other nuances are voluminous, which is much of the basis for our "complexity" notion, which in turn makes evaluating and modeling the business challenging. As we will illuminate further in this document, there are a lot of moving parts here. That said, our point is that we believe success across the physical entertainment fulfillment and distribution business, both horizontally and vertically, is certainly driven by traditional economic factors: price, flexibility, scale etc. but we also think there is a fair amount that is driven by established relationships. With that in mind, Alliance has clearly established the necessary infrastructure to efficiently fulfill and deliver physical media content at scale, however, much of our enthusiasm for Alliance stems from what we see as management's long history within, and tribal knowledge of the business, that provides them some of the relationships we just noted, but also the ability to understand and negotiate the complexities around the industry, which includes (among many other things) adapting to change, quickly and optimally. We recognize that may be subjective, but we think it is quite topical to their opportunity.

Products/Services Overview

Alliance is the conduit for leading brands to reach Alliance's current customer base, while helping Omnichannel Retailers expand their product selection and fulfillment goals. Alliance is the retailers' back office for in-store and eCommerce solutions. All Electronic Data Interchange (EDI) and logistics are operational and ready for existing retail channels to add new products. Alliance's goal has always been to provide all the meta-data of content & images, service, selection, and purchasing to Omni-Channel retailers to expand their selection to compete with the leading on-line Retailer.

Before we cover some of the specific products/services, **Tabel 6** below from the Company's presentation provides a compelling graphic of the major brands the Company sells for and sells to:

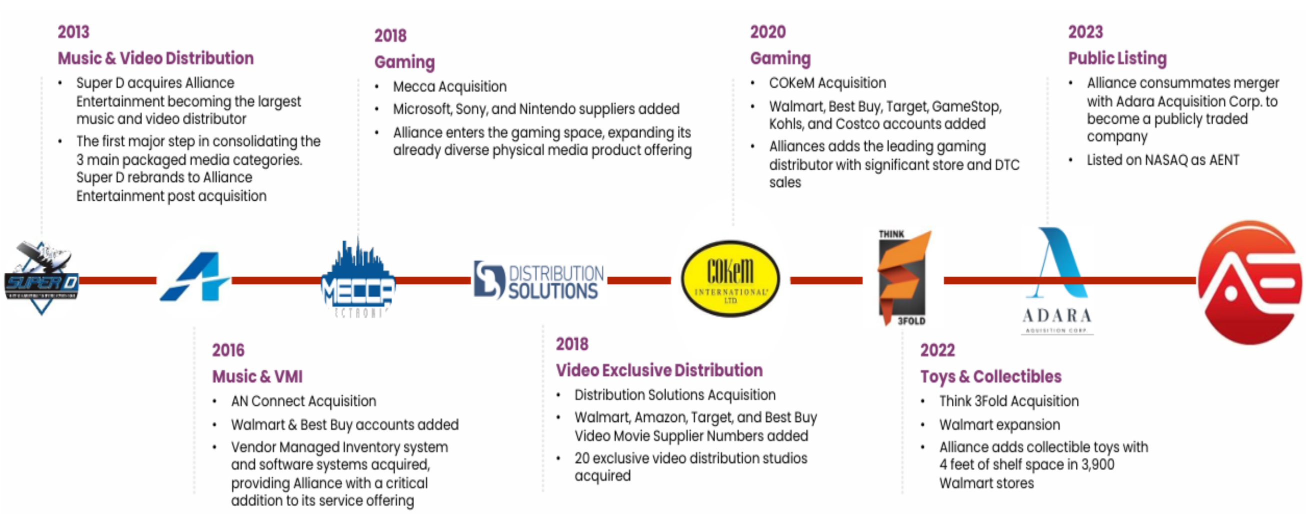
Table 6.



Alliance provides several products and services to/for a large contingency of customers across the physical entertainment fulfillment and distribution landscape. The backbone of the enterprise is the Company's 873,000 square foot warehouse and fulfillment center located just south of Louisville, Kentucky. The facility includes *state-of-the-art material automation and handling equipment advanced warehouse management software (WMS) systems which include wave picking by RF hand-held scanners and barcode-scanned item progress, and more recently, the AutoStore™ cube-based warehouse automated storage and retrieval system and Sure Sort® X, a cost savings sortation technology system that complements five existing CD/DVD and vinyl record sorters at the facility*. *The facility supports order fulfillment of 52 million units shipped across more than 325,000 SKUs*.

We believe the Louisville facility, in conjunction with Alliance's commitment to these fulfillment technologies, may provide them with some comparative advantages. From our perspective, their fulfillment and distribution capabilities are the foundation for their strategy, which is to provide end-to-end omnichannel solutions for the provisioning of physical recorded entertainment products. Recognize, those omni-channel capabilities include the turnkey execution of Direct-to-Consumer ("DTC") eCommerce transactions for very small to very large online providers that (through Alliance) do not need to inventory, or even touch the product they sell and deliver to their online customers. As **Table 7** below illustrates and we will attempt to expand upon, that foundation has allowed them to acquire synergistic pieces that have broadened the Company's reach both horizontally and vertically. Further, these acquisitions have allowed them to add and integrate valuable relationships with upstream enterprises (studios, labels etc.) as well as other important downstream customers (big box and online retailers). In our view, the platform they have built (and perhaps in conjunction with their new publicly traded profile) should position Alliance to continue to make highly additive acquisitions that can optimally leverage the platform. Succinctly, that potential encompasses a meaningful portion of our thesis here.

Table 7.



Alliance provides products and services through several brands/divisions, depending on the function and the service or product type they are delivering. Recognize, below is some of the Company's narrative regarding its primary divisions including some of our own color regarding each.

Distribution Solutions ("DS") *is a division of Alliance that has over 62 significant video studios that by exclusive contract rely on Distribution Solutions to manufacture, supply, and market video products. DS has direct sales accounts with Amazon, Walmart, Target, Best Buy, and many other significant customers. Smaller non-direct accounts are sold through Alliance Entertainment. All product is held on consignment in the Alliance warehouse. By having all the product in stock, it maximizes the "in stock" buy buttons on all retailers' websites as well. DS, through Alliance, has significantly larger distribution channels of retailers and CDF for websites than any major studio can offer. DS was acquired from Sony Picture in 2018.* Distribution Solutions is the Company's flagship video distribution brand.

***AMPED** is a division of Alliance that has **more than 90 labels** representing hundreds of artists, that by exclusive contract rely on AMPED to supply and market music (Vinyl and CD). AMPED is a top tier independent distributor committed to establishing and developing independent artists and labels worldwide. Being part of Alliance Entertainment, AMPED™ gives the indie community access to a global distribution system with a seasoned and skilled staff that provides a suite of services and data second to none. AMPED's customer base is the largest in the industry, directly servicing brick and click retailers large and small along with (DTC) direct consumers. AMPED sells and markets music through Amazon, Walmart, Target, Best Buy and over 1000 independent music stores in the U.S. Because Alliance can offer direct to store and state of the art ecommerce fulfillment AMPED has become the go to Independent distributor to maximize a labels physical sales.*

AMPED™ is the future model for physical distribution of Vinyl LP's, CDs, Cassettes, DVDs and Blu-ray and offers state of the art digital music distribution. This unique distribution model combines global reach, world-wide sales force, label marketing & advertising and state-of-the-art distribution in a package suited to Vendors, Labels & Artists of all sizes. AMPED™ is directly available to thousands of independent stores, all major chains retailers and mass merchants, online retailers, specialty retailers, global marketplaces and other wholesalers.

AMPED was organically grown over the last 10 years and in FY '23 exceeded $75M in net sales.

Top ranking in the music industry, Alliance Entertainment consistently excels with suppliers, which include all major and independent labels. In fact, in 2015 we represented a full 48% market share of the total 11.9 million vinyl records sold.

To reiterate, Alliance's AMPED division is focused on the music distribution portion of the business and as such has experienced marked success serving independent artists and labels, as well as new and emerging genres worldwide by providing them the opportunity to generate revenue from their recorded music. We are comfortable suggesting that opportunity is available to many more indie artists today than in the pre-Napster period, and we think Alliance is a meaningful and growing contributor to that dynamic.

***Mill Creek** is a division of Alliance that exclusively licenses video content from studios to create, manufacture, market and sell video DVD's. Video content licensed from Disney, Sony, Universal, Lionsgate, CBS and significant independent studios. Mill Creek's product is then sold through Distribution Solutions direct to major retailers. Mill Creek Entertainment is the home entertainment industry's leading independent studio for Blu-ray, DVD, and digital distribution. With direct sales pipelines to all primary retail and online partners, Mill Creek Entertainment licenses, produces, markets and distributes a dynamic array of film and television content to over 30,000 retail stores and thousands of websites reaching millions of customers across North America.*

Mill Creek Entertainment's expansive library includes Oscar®-winning theatrical feature films, Emmy®-winning classic and contemporary TV series, original documentary productions and pop-culture favorites that enlighten, educate and entertain.

Mill Creek is a studio, which means that it owns a library of films, which is at least in part why Alliance acquired them in 2019. In that regard, Mill Creek's purpose is to acquire or license other exclusive content from other studios that they can then fulfill and distribute through Distribution Solutions/Alliance's retail pipelines. As one example, in January 2023 Mill Creek signed a home entertainment licensing agreement with The Walt Disney Company whereby Mill Creek (through DS/Alliance) effectively became the exclusive vendor ("Vendor of Record") for "*select physical live-action film and television properties from* *the ABC Signature, 20th Television, Hollywood Pictures, Touchstone Pictures, and 20th Century Studios content libraries".*

For 40 years Mecca has specialized in the distribution of video games, interactive hardware and accessories to hundreds video games stores in the U.S. including regional and national chain stores We are direct with all three of the first party companies (SONY, MICROSOFT & NINTENDO) and is an authorized distributor for all major 3rd party game publishers and many of the top 3rd party accessory makers. Alliance acquired Mecca in 2018.

***COKeM International** is a wholesale distributor of video games, video game accessories, home arcades, collectibles and consumer electronics. COKeM is not only for every type of gamer, it's for every type of business. COKeM removes the middleman and offers tailored solutions, collaborating directly with the customer. COKeM provides full-service distribution, fulfillment and 3PL services. If your consumers want it, we'll ship it. Anytime, anywhere, with around-the-clock care. COKeM also offers end-to-end e-commerce solutions, helping customers develop a user-friendly website and sales channel, complete with sales support and an in-house marketing team. Alliance acquired* COKeM in 2020.

The acquisitions of Mecca and COKeM represented Alliance's entree into the gaming space, and the third leg of their distribution stool. Collectively, Mecca and COKeM have many agreements with the largest suppliers of physical software, consoles and accessories and customers that are among the largest retailers in the world.

Alliance acquired Think 3Fold in July 2022. The acquisition of Think 3Fold brought significant additional licensed toy and collectible products and sales channels. Think 3Fold has strong established relationships with vendors including McFarlane, Bandai, Little Buddy, The Loyal Subjects, Mego Toys and Figures, WETA, Great Eastern and many others. Think 3Fold was the brainchild of 3 executives who founded the company with the mission to find gaps in the toy and collectible marketplace and bring solutions to suppliers and retailers.

Think 3Fold represents the fourth and newest leg of Alliance's product line, which they refer to as "Toys, Collectibles and Consumer Products".

While the above are all entities under the Alliance umbrella, there are others as well, for instance direct-to-consumer websites like www.deepdiscount.com and www.importcds.com, www.popmarket.com as well as others.

Lastly, as we attempted to illustrate above, Alliance has expanded the business organically on the strength of its broad fulfillment and delivery capabilities. At the same time, they have also leveraged that capability by adding and successfully integrating strategic acquisitions along the way that brought them additional/new relationships (both content providers and content retailers) as well as entirely new product lines. In that regard, we believe part of Management's calculus for taking the company public via the Adara transaction was to provide them with financing flexibility around additional potential acquisitions. While we have not attempted to model additional acquisitions, we think they are more likely than not.

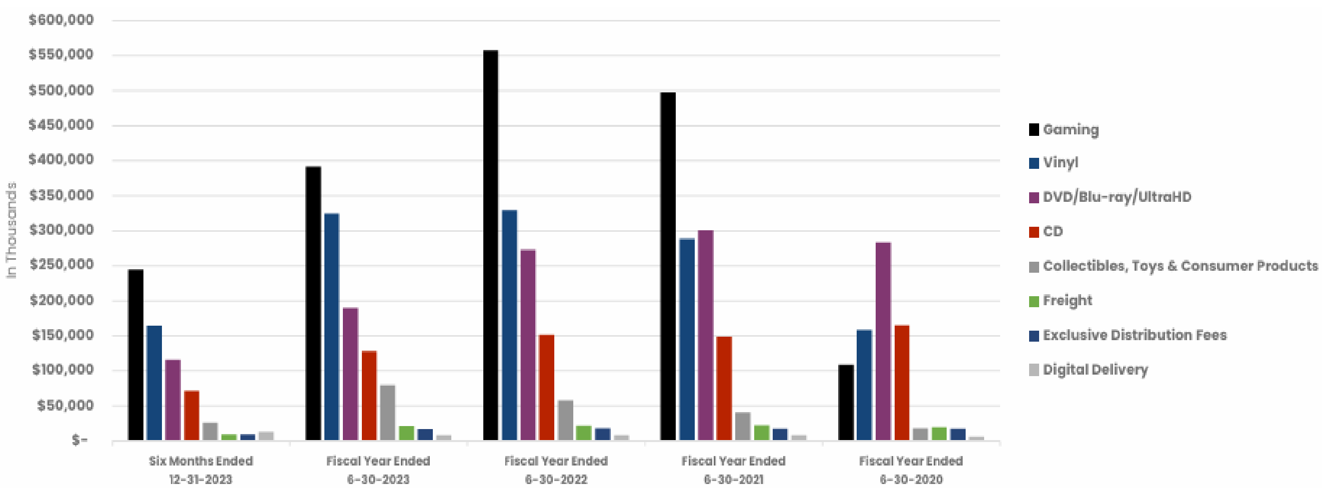
To summarize, Alliance has built a robust end-to-end beachhead in the physical recorded entertainment space. In all four categories they operate in, Music, video, gaming and toys/collectibles, they have established relationships with both the sellers and the buyers of those products. Those relationships include small indie labels and small video studios as well as the largest labels and the largest studios in the world. They also include small independently owned record and/or video stores as well as the largest retailers in the U.S. Further, they provide these services on an omnichannel basis, which means for instance, that they ship large volumes of orders to big box retailers, and a single album direct to a consumer from that same big box retailer's eCommerce site. We would add, while we did not cover this above, the Company also offers its customers (both buyers and sellers) a host of other services to manage and enhance their sale efforts. A list and associate narrative regarding some of those services are available on Alliance site: Service - Alliance Entertainment - Premier Wholesale Distributor (aent.com) . Here again, we think these additional services further support our "turnkey" description of their services.

Operating Overview

The past several quarters of Alliance's results have included a fair amount of noise that in our view makes it challenging to ascertain the "normalized" view of the company. We will briefly cover some of those issues to better frame the operating posture going forward as we see it.

First, as we touched on above, industries that included any sort of stay-at-home entertainment generally saw a lift from the pandemic. Given that people were sequestered at home, we do not think that requires much color, and to that end Alliance was not an exception. To illustrate the point, **Table 8** reflects the Company's segment reporting, which shows the marked inflection in their business through the pandemic relative to the pre-pandemic reporting period (fiscal 2020) which ended June 30, 2020, just as the pandemic was gathering momentum. We will refer to this Table later in the report as well, but the favorable impact of the event on their numbers is clear.

Table 8.



While the pandemic certainly provided a boost to the Company, it also came with an unfortunate "flip-side" that may not be quite as obvious. Recall, one of the more dire elements of the pandemic (beyond the health concerns) was its impact on global supply chains. In short, the pandemic exposed the risks associated with globalization, "just-in-time" inventory approaches, and a host of other associated paradigms. To be clear, we are not suggesting those things were bad, but every benefit comes with costs, and covid exposed several of those. In the case of Alliance, that cost turned out to be acute.

Coming out of calendar 2020 and into fiscal 2021 (June 30, 2021), the Company recognized the tailwind that the pandemic created for stay-at-home entertainment products, so they attempted to build inventory to meet demand. In particular, the Company placed orders for approximately $130 million worth of personal arcade games in response to corresponding orders from customers. (To edify, these games are smaller versions of their larger commercial counter parts, and they typically retail in the $300 to $500 range). Unfortunately, the sell through of those arcades was upended by the supply chain disruptions, which in this case manifested in the form of cargo containers stranded in U.S ports, that started in late calendar 2020, but reached their peak of stagnation in mid-4Q calendar 2021 (we denoted this peak with the red arrow in **Table 9** below). The result for Alliance was that its arcades were stranded on boats that could not be unloaded, and they were unable to deliver them to customers when promised, and in time for the 2021 holiday season. That circumstance led to a cascade of other problems that collectively had a negative impact on the Company's financial performance, including its liquidity/working capital posture. The following narrative regarding the issue is from the Company's S-1 filing:

The residual effects of the Covid-19 pandemic will continue to directly or indirectly impact our business and the results of operations and financial impact, including expenses and employee-related costs, but are highly dependent on future developments that are uncertain at this time. While we maintained uninterrupted operations during the pandemic, macroeconomic conditions and supply chain disruptions resulted in downstream shocks. The most pronounced consequences were the exorbitant international shipping costs for arcades, and the incremental Marketing Development Funds in the form of customer rebates recorded during year ended June 30, 2023. The disruptions in the transportation industry resulted in higher landed costs and a $8.2 million write down was recorded for units sold and a $7.1 million write down for gaming arcade units on-hand. In addition, customer rebates of approximately $12.2 million were incurred to spur demand for arcades. Finally, approximately $4.6 million of incremental storage costs was recognized to warehouse excess arcade inventory.

Table 9.

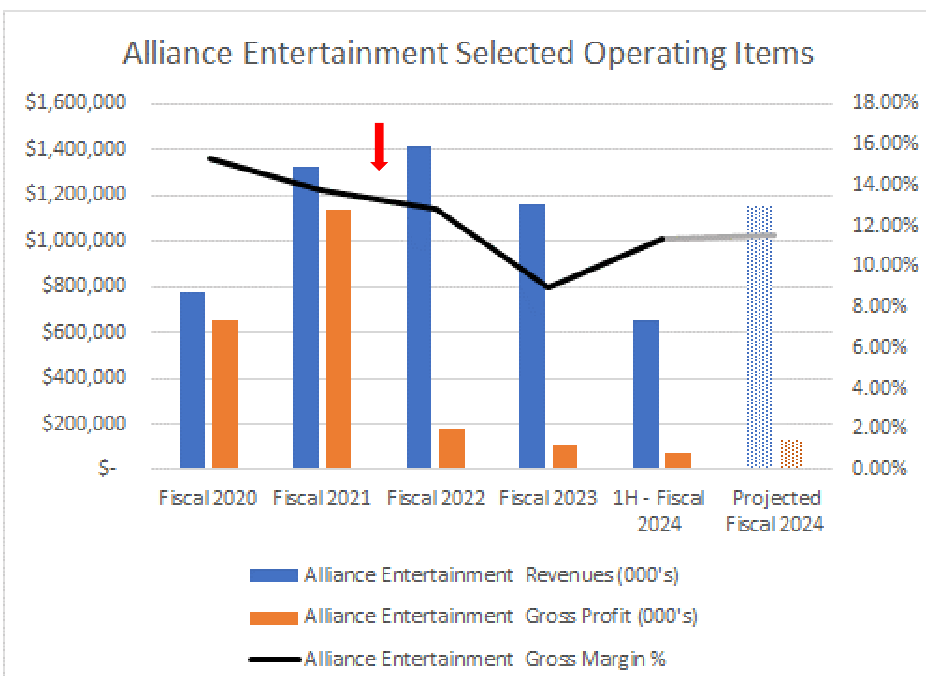
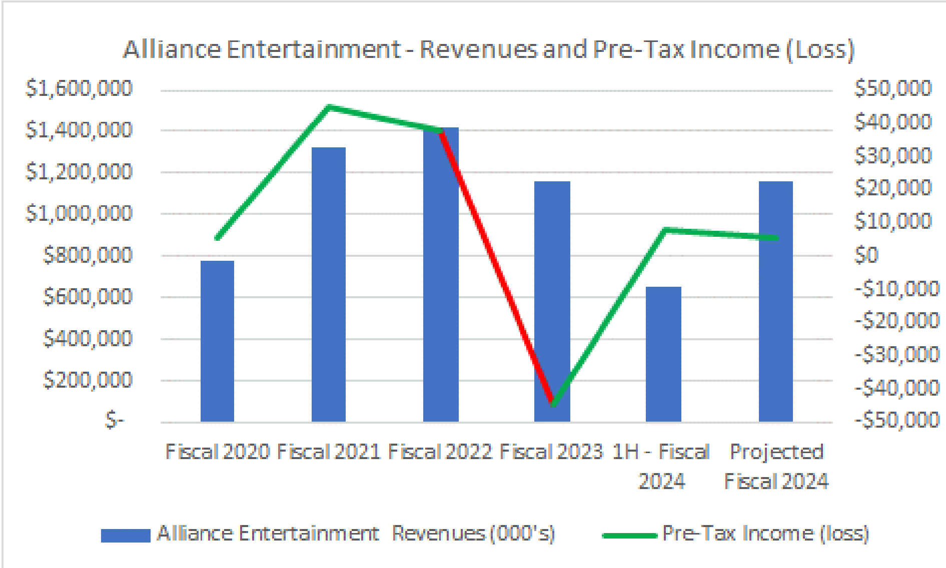


Table 10.



We have provided **Tables 9 & 10** as visual representations of the Company's narrative above, but the takeaway is this. While the compression in revenue from Fiscal 2022 to Fiscal 2023 is easy enough to understand (the pandemic contracted and people left their homes returning the industry to more normalized results), the more topical data points is the concurrent compression in margins, and by extension, the marked (negative) impact that margin compression had on earnings. To be clear, our thesis here is that the Company's business has largely "normalized", which we view as a return to more historic gross margins of around ± 12%, and annual revenue growth in the *low* single digits (assuming no additional acquisitions). That said, here is a bit more granular color on those assumptions.

The Company provides segment data as illustrated in **Table 11** below. We have attempted to model Alliances revenues around that same format. More specifically, we have modeled very modest YoY growth rates, which include negative growth for some of these segments. In addition, as we noted in the Risks and Caveats section above, we think slower economic activity will likely be negative for Alliance, and we have modeled that scenario through the second half of calendar 2024 and through fiscal 2025. To reiterate, while we have suggested that we believe additional acquisitions are a likely outcome, we have not modeled that scenario.

Table 11.

(In Thousands)

Sales by Configuration	Six Months Ended 12-31-2023		Fiscal Year Ended 06-30-2023		Fiscal Year Ended 06-30-2022		Fiscal Year Ended 06-30-2021		Fiscal Year Ended 06-30-2020	
Gaming	$244,160	37.4%	$391,308	33.8%	$557,658	39.3%	$497,817	37.6%	$108,735	14.0%
Vinyl	$164,005	25.1%	$324,141	28.0%	$329,202	23.2%	$288,326	21.8%	$158,633	20.5%
DVD/Blu-ray/UltraHD	$115,319	17.7%	$189,997	16.4%	$272,921	19.3%	$300,522	22.7%	$283,371	36.5%
CD	$71,377	10.9%	$127,999	11.0%	$151,583	10.7%	$148,263	11.2%	$164,728	21.2%
Collectibles, Toys & Consumer Products	$26,383	4.0%	$79,524	6.9%	$57,980	4.1%	$40,729	3.1%	$17,591	2.3%
Freight	$9,094	1.4%	$21,091	1.8%	$21,682	1.5%	$22,260	1.7%	$19,138	2.5%
Exclusive Distribution Fees	$8,953	1.4%	$16,269	1.4%	$17,874	1.3%	$17,460	1.3%	$17,430	2.2%
Digital Delivery	$13,051	2.0%	$8,393	0.7%	$8,476	0.6%	$8,191	0.6%	$5,967	0.8%
Grand Total	$652,342	100.0%	$1,158,722	100.0%	$1,417,377	100.0%	$1,323,567	100.0%	$775,596	100.0%

While trying to grow (and in some cases just maintain) revenue levels across each segment is the major challenge, maintaining margins is also paramount. To put the margin piece into perspective, we think Alliance has some operating leverage in the sense that incremental increases in revenues should not require similar incremental increases in operating expenses. To that end, we are projecting SG&A for fiscal 2024 of $59.4 million and we expect only modest increases in that going forward. Again, we are projecting gross margins in the 11.5% to 12% range and gross margin *after Fulfillment and Distribution* of between 7.5% and 8%. Doing some simple math, on $1 billion of revenues, each 1% of gross margin after Fulfillment and Distribution should generate $10 million of operating contribution. Clearly, margins matter *acutely* here. Doing the math, covering $60 million of SG&A requires 6% of gross margin after Fulfillment and Distribution. From another perspective, assuming gross margin after Fulfillment and Distribution of 7.5%, each incremental $100 million of revenue should generate an additional $7.5 million to $ million of *operating income* (before depreciation and amortization), which is about 14¢ per share. Clearly, revenues matter acutely here as well. Again, we believe the business has normalized, which translates to less volatility from revenues and margins going forward. We submit, our model and resulting targets depend significantly on that notion. To be clear, we suggested that there are elements of the business that could cause some lumpiness in sequential results, however, again, we expect annual results to be less volatile than those periods that were impacted by the pandemic.

To reiterate, the above analysis concerns operating results so it does not include interest expense. As we covered, the Company's supply chain issues compromised the covenants of their credit facility, which forced them to seek an alternative. Succinctly, their success replacing the facility was an important milestone given the supply chain challenges. That said, the current facility is more expensive than the previous facility. The terms (roughly) are as follows. The facility carries *a maturity date of December 21, 2026. The new credit facility includes a $120 million asset based revolving credit facility (the "Revolving Credit Facility"). Borrowings under the new Revolving Credit Facility bear interest at the 30-day SOFR rate, subject to a floor rate of 2.00% plus a margin of 4.50% to 4.75%, depending on the level of the Company's utilization of the facility and consolidated fixed charge coverage ratio.* We believe the rate as of this report date is approximately 10%.

Management Overview

Bruce Ogilvie. *Bruce Ogilvie has been Alliance's Executive Chairman since 2023 and has been Executive Chairman of Legacy Alliance since 2013. Prior to assuming his current role, in 1996 Bruce was selected by a bank group to turn around the 600-store chain, Wherehouse Records. Under Bruce's leadership Wherehouse emerged from bankruptcy within nine months and was sold to Cerberus Capital. Following his success with Wherehouse Records, Bruce bought a one-third interest in Super D in 2001 and assumed the role as CEO, joining with founders Jeff Walker and David Hurwitz. Bruce became the Chairman in 2013 after the merger of Super D and Alliance. Mr. Ogilvie has spent his entire career in the entertainment distribution industry starting with the founding of Abbey Road Distributors in 1980. Over the next 14 years, Bruce led Abbey Road's growth to over $94 million in sales and successfully sold the business in 1994. In 1995, Bruce was awarded E&Y's Distribution Entrepreneur of the Year Award for his work with Abbey Road.*

Jeffrey Walker. *Jeffrey Walker has been Alliance's Chief Executive Officer since February 2023 and was Legacy Alliance's Chief Executive Officer since 2013. Mr. Walker has also been a director of Alliance since February 2023 and a director of Legacy Alliance since 2013. In 1990, Jeff co-founded the CD Listening Bar, Inc., a retail music store. A few years later, Jeff started wholesaling CDs from the back of the store, beginning the journey to create Super D, a music wholesaler founded in 1995. In 2001, Jeff and co-founder David Hurwitz sold a third of Super D to Bruce Ogilvie. Over the next decade, Bruce and Jeff continued to grow Super D's presence in the music wholesaling space, with the acquisition of Alliance in 2013. In 2015,* *Jeff was awarded E&Y's Distribution Entrepreneur of the Year award in Orange County. Mr. Walker received a bachelor's degree in economics from University of California — Irvine.*

Risks and Caveats

We think the most obvious risk in the Alliance story is that they sell physical recorded entertainment, including DVDs/Blu-ray, CDs, LPs, video games and others. As we covered above, and as we think most investors probably intuitively ascertain, these are products that have been markedly displaced by platforms that provide the digital download and/or streaming of audio, video and gaming content. That begs the question, "why invest in a company that sells products that have been/are being displaced by technology driven alternatives"? That is a fair question, and while we have attempted to argue the answer to that question, we submit, it is perhaps, the "elephant in the room".

One of the challenges modeling Alliance is that it is difficult to ascertain the ongoing degree to which physical products are being displaced by digital counterparts, and part of that answer requires breaking down the individual mediums they focus on. For instance, Best Buy stopped selling CDs in their stores in 2018 and just recently stopped selling DVDs as well. It appears that other larger retailers have, or are preparing, to do the same. With harbingers of that nature, it is no surprise that physical CD and DVD sales continue to struggle. On the other hand, after nearly fading away completely in the early 2000's, LPs have enjoyed robust and sustained growth since the latter part of that decade. Further, physical video games continue to achieve YoY growth as well. That said, the visibility around where these segments are headed is not good and as such, we think that poses risks to the accuracy of our model assessments, and by extension, the future success of Alliance.

Aside for the above, there are other elements to the Alliance story that also compromise visibility. For instance, as we covered prior, in retrospect while the supply chain problems the Company encountered may fit into the "long tail risk" category, they nonetheless came to pass. When long tail risks come to fruition, it leaves analysts like us asking whether or not the tail was actually as long as we assumed. The point is, there may be risks of that nature out there that we are not able to identify but may still have the potential to be considerably detrimental or even catastrophic for Alliance.

The Company's business includes some seasonality that readers should be aware of. In general, seasonality tends to favor Fiscal Q2 (ended December 31) as retailers gear up for holiday sales. However, aside from that anticipated/recurring seasonality, the Company's business has experienced and will likely continue to experience additional lumpiness around things like the timing of new releases of particular content, the introduction of applicable hardware upgrades/additions, "record store day" (one Saturday each April) and a host of others. We have no idea how to reflect or otherwise handicap those events, or for that matter, ascertain the impact they may have. We are comfortable suggesting that if, for example, a high-profile artist releases a new album (for instance Usher's **Coming Home**, or Taylor Swift's **The Tortured Poets Department**), that event may create some outsized contributions to Alliance depending on Alliance's relationship with the associated label etc. It is important to keep the non-recurring nature of those "bumps" in mind.

While the Company's most recently reported quarter (Q2F24-Ended Decembre 31, 2023) reflected highly positive earnings, the prior 5 quarters all included losses. Again, as we covered in the Operating Overview, certainly much of those losses were related to the Company's exposure to supply chain issues caused by the pandemic, as well as perhaps to a lesser degree, their transition to a public company, the past 18 months have been challenging from earnings as well as cash flow perspectives. In that regard, our model assumes improving comparative financial results, however, our assessments could prove inaccurate. In that case, if the Company predominantly continues to experience losses it could impair their liquidity, and perhaps (again) compromise loan covenants and other working capital arrangements they rely on that would negatively impact the business. We would add, while our model continues to assume losses in some future quarters, it projects positive *annual* results. Again, if our assessments therein prove aggressive, our target assessments will likely prove aggressive as well, which could in turn compromise the Company's viability.

As **Table 6** above reflects, The Company's business depends on relationships with several large and well-established enterprises. If they lose some of these relationships for one reason or another, or if some of these businesses face their own difficulties, it will likely have a negative impact on Alliance.

The Company inventories, fulfills and distributes nearly all its products from its single facility near Louisville, Kentucky. If anything should happen to impair the facility it would likely prove considerably detrimental to the business.

The Company does not manufacture the products it distributes. As a result, it is reliant on others to provide their products. Given the waning status of physical recorded media in general, manufacturers may find it increasingly difficult to maintain their businesses and by extension the products Alliance sells. In our view, that scenario carries clear risks for Alliance.

Currently, the Company relies heavily on its founders to operate the business. That posture carries obvious risks with respect to the performance and continued participation of those individuals. For reference, this is a risk we note in most of our coverage, but in the case of Alliance, this risk may be particularly acute. Moreover, as we noted above, these individuals collectively control a very large portion of the Company's equity, so they have considerable control over its direction.

The Company sells discretionary products which will almost certainly be negatively impacted if the current economic climate deteriorates. Frankly, *in our view*, looking out over the next 18 months or so, this particular risk may be the most topical.

The Company's stock is *very thinly traded*, which generally leads to volatile share prices and illiquidity. That may remain the case into the foreseeable future especially since many of the outstanding shares are held by insiders and as such the float is comparatively small.

These are just some of the more obvious risks we see in the Company. There are likely others we have overlooked as well as others that may arise in the future.

Valuation and Conclusion

As microcap generalists, we do not often initiate coverage of companies with $1 billion+ annual revenue run rates. Moreover, we do not typically initiate coverage of companies with market caps in excess of $100+ million either (or 200 million+ enterprise values for that matter). From that perspective, Alliance may be a bit unique for our coverage universe. On the other hand, we are often asked what our coverage criteria is, and our typical answer to that is, we are looking for under covered stories, which generally goes hand in hand with illiquid and thinly traded, that for some reason or set of reasons, we believe will perform better over the next 12, 24 or 36 months, than they did the last 12, 24 or 36 months. We think Alliance may check that box.

To be clear, our 12, 24 or 36 months ideas do not always start from the same place. That is, sometimes that setup is the result of circumstances or challenges that diminished a Company's past performance, but we think they have overcome (and the street has not figured out), but other times they are the result of something new the Company has developed or perhaps the environment becoming more favorable toward something they developed some time ago. As we attempted to illustrate throughout this report, we think

Alliance's situation is more of the first, but we also think, like many of the small stories we follow, the Company's business, including its established beachhead within the industry and for that matter the industry itself is not well understood, or broadly understood, or both. For instance, we think many people would be shocked to know that there are *still* over 40 million vinyl records (over $1.2 billion) sold in the U.S. each year. On the other hand, they might be more shocked that 50% of those records are sold to people that *do not even own a turntable*.

Another notion we like to focus our research on is management. We submit, judging management is generally a bit more subjective than we might like, and we certainly do not always get that right. That is, some of the managers we thought would be very good turned out be very awful. Regardless, we think it is fair to say that management with a successful background in whatever industry they are operating in is a good place to start. Alliances management collectively has *nearly 80 years* of entertainment industry experience, and that includes *relationships* that we believe are highly important to the success of their business. From another perspective, Alliance management also has considerable skin in the game. Management collectively owns over 90% of the outstanding shares of the Company as well as carrying $10 million of related party debt. Clearly, they are committed to the success of the business.

As we see it, Alliance has built a considerable business as a market leader around two primary attributes; management's tribal knowledge of the space, and management's ability to identify and then successfully integrate additive acquisitions. While we have not attempted to model as much, our expectation is that they will continue to try to identify and add synergistic enterprises to the business that will allow them to further leverage the infrastructure and the distribution footprint it has established. As we attempted to address in the Operating Overview, we think the business is particularly conducive to that sort of leverage so again, we would expect acquired piece to be quite additive.

We recognize that Alliance's success will depend on consumers maintaining some level of continued appetite for physical recorded entertainment. To that end, there is no shortage of "experts" who believe that physical recorded media is on the way out… all the way out. That may be true, and in that scenario assuming the Company makes no additional pivots, they will likely fail. *However,* consumers do not, and will not, all have the same preferences, and as we have attempted to illustrate, there are viable markets for companies that serve the niches created by consumers with preferences that are "off the beaten path" (or perhaps in this case, *still on* the beaten path). Our view is that Alliance is positioned to prosper in a normalized environment where some number of consumers uphold their preferences for physical recorded entertainment. As a result, we are initiating coverage of Alliance Entertainment with our typical allocation of 4 and a 12-24 month price target of $4.25. We will revisit each as relevant data points emerge.

Projected Operating Model

Alliance Entertainment Holdings Corp.						
Projected Operating Model						
By: Trickle Research						
	(Actual)	(Actual)	(Estimate)	(Estimate)	(Estimate)	(Estimate)
	09/30/23	12/31/23	03/31/24	06/30/24	Fiscal 2024	Fiscal 2025
Net Revenues	$ 226,755	$ 425,586	$ 237,629	$ 266,734	$ 1,156,704	$ 1,159,949
Cost of Revenues (excluding depreciation and amortization)	200,501	377,883	$ 210,837	$ 235,059	$ 1,024,280	$ 1,021,156
Operating Expenses:						
Distribution and Fulfillment Expense	11,714	15,144	$ 11,253	$ 11,835	$ 49,945	$ 49,199
Selling, General and Administrative Expense	14,439	15,116	$ 15,575	$ 14,933	$ 60,064	$ 59,920
Depreciation and Amortization	1,641	1,412	$ 1,500	$ 1,500	$ 6,053	$ 6,000
Transaction Costs			$ -	$ -	$ -	$ -
IC DISC Commissions			$ -	$ -	$ -	$ -
Restructuring Cost			$ -	$ -	$ -	$ -
Loss on Disposal of Fixed Assets	47		$ -	$ -	$ 47	$ -
Total Operating Expenses	27,841	31,672	$ 28,328	$ 28,268	$ 116,109	$ 115,119
Operating (Loss) Income	(1,587)	16,031	$ (1,536)	$ 3,407	$ 16,315	$ 23,674
Other Expenses:					$ -	$ -
Interest Expense, Net	3,140	3,328	$ 3,081	$ 2,775	$ 12,324	$ 11,513
Change in Fair Value of Warrants			$ -	$ -	$ -	$ -
Total Other Expenses	3,140	3,328	$ 3,081	$ 2,775	$ 12,324	$ 11,513
(Loss) Income Before Income Tax (Benefit) Expense	(4,727)	12,703	$ (4,617)	$ 632	$ 3,991	$ 12,162
Income Tax (Benefit) Expense	(1,265)	3,789	$ (1,201)	$ 164	$ 1,488	$ 3,162
Net (Loss) Income	(3,462)	$ 8,914	$ (3,417)	$ 468	$ 2,503	$ 9,000
Other Comprehensive Income:						
Foreign Currency Translation			$ -	$ -	$ -	$ -
Total Comprehensive (Loss) Income	$ (3,462)	$ 8,914	$ (3,417)	$ 468	$ 2,503	$ 9,000
Net (Loss) Income per Share - Basic	$ (0.07)	$ 0.18	$ (0.07)	$ 0.01	$ 0.05	$ 0.18
Net (Loss) Income per Share - Diluted	$ (0.07)	$ 0.18	$ (0.07)	$ 0.01	$ 0.05	$ 0.18
Shares Used in Computing Net Income per Share, Basic	50,502,170	50,930,770	50,930,770	50,930,770	50,823,620	50,930,770
Shares Used in Computing Net Income per Share, Diluted	50,502,170	50,930,770	50,930,770	50,930,770	50,823,620	50,930,770

General Disclaimer:

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Trickle Research holds 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. As of the date of this report, Alliance Entertainment Holding Corporation has not paid fees to present at Trickle co-sponsored conferences, but 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.