Trickle Research

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

Q1F25 Earnings Update

ALLIANCE ENTERTAINMENT

Alliance Entertainment Holding Corporation

(Nasdaq: AENT)

Report Date: 11/20/24

12- 24 month Price Target: *$6.00

Allocation: 4

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

Closing Stock Price at This Target Update (Closing Px: 11/19/24): $3.95

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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.

For Q1F25 (ended 09/30/24) Alliance reported revenues of $229 million, Net Income of $397,000 and fully diluted EPS of $.01. Those results compare to our estimates for revenues of $222.4 million, Net Income of <$895,000>, million and fully diluted EPS of <$.02>. Perhaps more notably, pre-tax net income was <$760,000>, versus our estimate of <$1,210,000>. In short, the Company bested our estimates again, in what is historically one of their two seasonally weaker quarters. As an aside, not surprisingly, the current quarter (ended December 31) is the strongest seasonal quarter generally representing 60%+ of all revenues. As we have addressed in prior updates, the Company has emerged from some pandemic-related challenges and with those behind them have been able to focus on advancing the business. That has included particular emphasis on profitability. In that regard, given the importance of the current quarter to the business, we think the coming 2QF25 results (ended 12/31/24), could be telling in terms of that assessment.

Briefly digging into the numbers, gross margin for the quarter was 11.15%, which was about 21 basis points lower than the sequential quarter comp. In terms of our estimates, when we adjusted our revenues (up) to meet the actual results, we overestimated gross margins by about 16 basis points. However, the positive revenue surprise of roughly $6.5 million was largely spread across the 4 major legacy product lines Gaming, Vinyl, DVD/Blu-Ray/Ultra HD and CDs. More specifically, DVDs and CDs performed marginally better than all of the other categories, and those two segments typically carry lower margins than the rest, which led to the modest margin compression. We continue to be surprised by the resilience of the DVD and CD sales. On the other hand, we overstated revenues in Collectibles, as well as in Digital Delivery. We have to admit, we are having trouble understanding the contribution/trajectory of the latter. Regardless, overstating the highest margin line item (Digital Delivery) also contributed to the margin compression. All things considered, again, the quarter was a top line success versus our relative estimates.

On the expense side, the Company realized Operating Expenses of $23.5 million. That compared favorably to our estimate of $26.6 million. $1.8 million of that positive difference came from Distribution and Fulfillment. Given our site visit where we saw the benefits of many of their distribution and fulfillment upgrades, it is not surprising to us that they continue to wring efficiencies out of the process. We will consider that as we model things going forward. Much of the balance of the savings came from SG&A, which again they continue to control. In short, collectively, operating expenses provided an additional positive surprise. To reiterate a notion, we have raised in prior updates, we think Alliance's veteran management team remains dialed in and continues to drive improving performance.

Looking ahead, as we noted above, we think the current quarter (2QF25 ended 12/31/24) may be a telling gauge with respect to our assessment that management has put the Company back on a path to sustainable profit growth. That said, we continue to believe that will include further emphasis on profitability. For instance, as our model below reflects, we are estimating that fiscal 2025 revenues to be largely flat vs. fiscal 2024, but we are looking for eps to advance over 400% from $.09 to $.39. Moreover, we are looking for about 3% revenue growth for fiscal 2026 vs. fiscal 2025, with a 16% increase in eps ($.39 to $.45).

On another note, our model does not reflect any acquisitions by Alliance, but as we have noted in prior coverage, management has built the business by identifying, purchasing and integrating strategic pieces. We suspect that will continue to be an integral part of their plan. Further, intuitively the strengthening of the platform including the underly financial foundation, should expand the breadth and the quality of the potential acquisition opportunities. To translate, while we are modeling benign organic revenue growth, we think growth via additional acquisition in the coming quarters remains likely. In the meantime, we think the addition of new industry collaborations like those they have announced over the past weeks could also provide upside surprises to our revenue estimates.

Lastly, Alliance Founder and Executive Chairman Bruce Ogilvie recently presented at our November 11, 2024, Trickle Microcap Conference -Fall 2024 event, at Ball Arena in Denver, Colorado. We believe the content of his presentation further supports our general views of the opportunity here. A copy of that presentation is available under the "CONFERENCES" tab on our site. In addition, although our conferences are always in-person we also provided a live stream of this particular event. The livestream of Bruce's presentation can be accessed at the following link:

Alliance Entertainment Holding Corp (AENT) - Fall 2024 Investor Presentation

In our opinion, the results of Q1F25 continue to validate our notion that Alliance shares remain undervalued at current levels and to reiterate our view from the prior earnings update, we think the continued derisking of the balance sheet along with the expansion of operating margins further supports that view. We would however also reiterate, our one concern here remains the macro environment and by extension the health of the consumer and their continued ability to spend on discretionary items. All things considered, we are establishing a new 12-24 month price target for Alliance shares of *$6.00 and we reiterate our allocation of 4. We will reassess all of our conclusions here as new information emerges.

Projected Operating Model

Alliance Entertainment Holdings Corp.						
Projected Operating Model ('000's)						
By: Trickle Research						
	(Actual)	(Estimate)	(Estimate)	(Estimate)	(Estimate)	(Estimate)
	09/30/24	12/31/24	03/31/25	06/30/25	Fiscal 2025	Fiscal 2026
Net Revenues	$ 228,990	$ 421,315	$ 209,898	$ 241,122	$ 1,101,325	$ 1,132,774
Cost of Revenues (excluding depreciation and amortization)	$ 203,455	$ 363,735	$ 183,090	$ 210,270	$ 960,551	$ 984,128
Operating Expenses:						
Distribution and Fulfillment Expense	$ 9,018	$ 14,744	$ 9,352	$ 10,149	$ 43,263	$ 44,886
Selling, General and Administrative Expense	$ 13,145	$ 14,132	$ 13,815	$ 13,862	$ 54,954	$ 55,699
Depreciation and Amortization	$ 1,258	$ 1,380	$ 1,380	$ 1,380	$ 5,398	$ 5,520
Transaction Costs	$ -	$ -	$ -	$ -	$ -	$ -
IC DISC Commissions	$ -	$ -	$ -	$ -	$ -	$ -
Restructuring Cost	$ 50	$ -	$ -	$ -	$ 50	$ -
Loss on Disposal of Fixed Assets	$ (15)	$ -	$ -	$ -	$ (15)	$ -
Total Operating Expenses	$ 23,456	$ 30,256	$ 24,547	$ 25,390	$ 103,650	$ 106,105
Operating (Loss) Income	$ 2,078	$ 27,324	$ 2,261	$ 5,461	$ 37,124	$ 42,540
Other Expenses:					$ -	$ -
Interest Expense, Net	$ 2,839	$ 3,344	$ 2,622	$ 2,725	$ 11,530	$ 11,313
Change in Fair Value of Warrants	$ -	$ -	$ -	$ -	$ -	$ -
Total Other Expenses	$ 2,839	$ 3,344	$ 2,622	$ 2,725	$ 11,530	$ 11,313
(Loss) Income Before Income Tax (Benefit) Expense	$ (761)	$ 23,980	$ (361)	$ 2,736	$ 25,594	$ 31,228
Income Tax (Benefit) Expense	$ (1,157)	$ 6,235	$ (94)	$ 711	$ 5,695	$ 8,119
Net (Loss) Income	$ 396	$ 17,746	$ (267)	$ 2,025	$ 19,899	$ 23,109
Other Comprehensive Income:						
Foreign Currency Translation	$ -	$ -	$ -	$ -	$ -	$ -
Total Comprehensive (Loss) Income	$ 396	$ 17,746	$ (267)	$ 2,025	$ 19,899	$ 23,109
Net (Loss) Income per Share - Basic	$ 0.01	$ 0.35	$ (0.01)	$ 0.04	$ 0.39	$ 0.45
Net (Loss) Income per Share - Diluted	$ 0.01	$ 0.35	$ (0.01)	$ 0.04	$ 0.39	$ 0.45
Shares Used in Computing Net Income per Share, Basic	50,957,370	50,977,976	50,998,788	51,019,808	50,988,486	51,073,418
Shares Used in Computing Net Income per Share, Diluted	50,965,970	50,986,576	51,007,388	51,028,408	50,997,086	51,082,018

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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. Alliance Entertainment Holding Corporation has paid fees to present at 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.