

January 21, 2021

## BETTER CHOICE COMPANY INC. (BTTR: OTCQX)

### BUSINESS DESCRIPTION

Better Choice is a rapidly growing animal health and wellness company that sells premium alternatives to traditional pet food. We believe that Better Choice is well positioned to capitalize on the global trends of growing pet humanization, expanding consumer focus on health and wellness, and the recession-proof nature of consumer spending on pets. Better Choice has an experienced management team, with a multi-decade track record in the packaged goods space, including animal health. It also has strong e-commerce capabilities that allow pet owners to easily learn about and order its products.

Better Choice sells primarily through retail-partner channels, which include Amazon, Chewy, Petco, and PetSmart, as well as its own direct-to-consumer online web platform. According to market-research firm Packaged Facts, online purchases of pet food continue to take market share from brick-and-mortar retailers, expanding from 7% of U.S. pet product sales in 2015 to 22% in 2019. We expect Better Choice to take advantage of this trend by focusing on new product innovation to attract consumers who already purchase frequently online, rather than by investing resources to convert traditional brick-and-mortar consumers to online shopping.

Better Choice's primary brands are Halo and TruDog. Halo, with a current revenue run rate of approximately \$35 million, is a premium, natural pet-nutrition brand with a full line of dry kibble, canned wet food, treats, and supplements for dogs and cats. TruDog, with a current revenue run rate near \$15 million, is an ultra-premium, boutique, direct-to-consumer brand that offers raw freeze-dried dog food, toppers, treats, and supplements. Both Halo and TruDog have a commitment to product quality, and their sustainably sourced kibble, canned wet, freeze-dried and dehydrated raw foods are derived only from whole meat and minimally processed raw-diet ingredients. In total, Better Choice offers more than 100 product SKU's across its portfolio.

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### KEY STATISTICS

#### Key Stock Statistics

Recent price (1/20/21)	\$1.45
52 week high/low	\$2.20-\$0.24
Common Shares Outstanding (M)	51.6
Preferred Shares Outstanding (M)	43.6
Total Shares Outstanding	95.2
Market cap (M)	\$138.0
Dividend	Nil
Yield	Nil

#### Sector Overview

Sector	Consumer Staples
Sector % of S&P 500	6.5%

#### Financials (\$M)

Cash & Mkt Securities	4.1
Debt	31.1
Working Capital (\$M)	-17.0
Current Ratio	0.5
Total Debt/Equity (%)	NM
Payout ratio	NM
Revenue (M) TTM	37.3
Net Income (M) TTM	NM
Net Margin	NM

#### Risk

Beta	NA
Inst. ownership	12%

#### Valuation

P/E forward EPS	NA
Price/Sales (TTM)	1.9
Price/Book (TTM)	NA

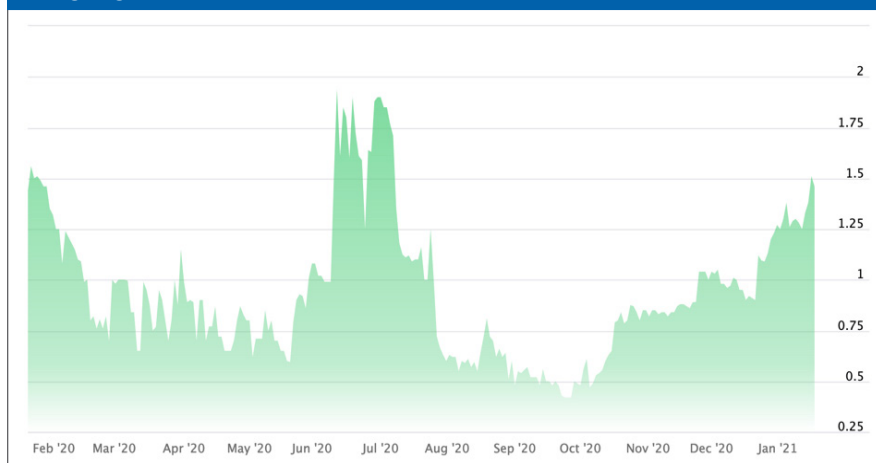
#### Top Holders

NA  
NA  
NA

#### Management

Chief Executive Officer	Mr. Scott Lerner
Chief Financial Officer	Ms. Sharla Cook
EVP of Sales	Mr. Donald Young
Company website	<a href="http://betterchoicecompany.com">http://betterchoicecompany.com</a>

### PRICE CHART



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Halo, founded in 1986, is an ultra-premium, natural pet-food brand that was acquired by Better Choice in December 2019. Halo's dog and cat products are sold in the United States and Canada, as well as in Japan, South Korea, China, Taiwan, Australia, and the Philippines. E-commerce is the largest and fastest-growing distribution channel for Halo, though the brand also appears at brick-and-mortar stores such as Petco and PetSmart. Unlike many other kibble and canned products, Halo uses whole meat (with no rendered meat meal) from animals raised on sustainable farms, and non-GMO fruits and vegetables. Foods sold under the TruDog and Halo product lines meet The Association of American Feed Control Officials ("AAFCO") guidelines. TruDog was founded in 2013, and was acquired by Better Choice in May 2019. Its products use natural ingredients and are oven-baked and preserved through freeze drying or gentle air dehydration to eliminate the need for artificial preservatives and chemicals. Currently, TruDog products are sold exclusively online.

The integration of Halo and TruDog are driving increased economies of scale, which we expect to help drive margin expansion and position Better Choice for continued growth and, ultimately, profitability. These acquisitions have enabled Better Choice to enter new, fast-growing international markets, particularly in Asia. The international segment accounted for 27% of net sales in 3Q20 (and 20% for the nine-month period). We expect the percentage of international sales to continue to increase, with China the company's largest growth market in the near term. Despite the impact of tariffs and the trade dispute with the U.S., sales in China continue to provide solid contribution margins to Better Choice and its distribution partners, and could benefit further from the January 2021 change of administration in Washington, D.C.

Better Choice should also benefit from strong growth in pet ownership and spending on pet supplies, irrespective of macroeconomic trends. The American Pet Products Association estimates that the U.S. has nearly 85 million pet-owning families (67% of all households), representing a \$75 billion annual market for spending on pets. Similarly, a recent report published by Frost & Sullivan noted that China had approximately 100 million pet owners in 2018, which represented approximately 22% of households in China. According to trade organization Pet Fair Asia, spending on pets in China totaled approximately \$25 billion in 2019.

Pet ownership has also expanded during the pandemic, as people spend more time at home. In a September 2020 survey by the American Pet Products Association (APPA), 9% of respondents that said they had adopted a pet during the pandemic, up from 6% in June 2020. In addition, only 2% of respondents said that they had to give up a pet due to economic challenges created by the pandemic. Nearly three-quarters

of respondents said that their pet's diet was important, and that they did not plan to make any changes in pet food for economic reasons.

We also believe that Better Choice is well positioned for further growth despite trade tensions between the U.S. and China and the impact of the pandemic. Management noted that normal purchasing patterns had resumed by June, helped by the company's focus on e-commerce and direct-to-consumer sales.

## COMPETITIVE ADVANTAGE

The pet health and wellness industry is highly competitive, as more companies focus on enhancing product quality while also working to build brand awareness and customer loyalty. We view Better Choice as a leader in the fastest-growing segments of the industry, as evidenced by its strong online business. We also note that recurring subscription revenue accounts for about 50% of the company's online sales.

Better Choice generates approximately 60% of revenue in the e-commerce and DTC channels, above the industry average of 25%-30%. These segments are also growing at 15%-20% annually. The company's DTC strategy leverages one-on-one customer relationships and uses consumer behavior data to guide its marketing efforts and lower customer acquisition costs (relative to traditional marketing efforts such as product discounting). Better Choice also tailors its marketing to reach specific demographic groups, including women, millennials, and middle-class consumers in emerging economies. Management believes that these groups are more likely to become pet owners and purchase pet products through online shopping sites.

In our view, the acquisition of Halo and the sales expansion through the retail channel represent key, underappreciated areas of distinction for Better Choice. The retail channel has become the primary contributor of company sales and growth. Better Choice is now able to leverage the customer data and behavior information it gathers from its DTC efforts and apply these lessons to the retail offerings, most notably the pet specialty channel. In addition, Halo's established sales channels position Better Choice to sell other current and future product lines more effectively through the retail channels. Lastly, Halo's established commercial foothold in high growth markets, including China, should enable Better Choice to expand its product reach more broadly.

Better Choice is working to educate consumers and build awareness about its portfolio. These efforts include the use of social influence marketing, which can better reach its tech-focused target customers, in addition to other technology-focused and social media campaigns.

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## PEER COMPARISON

Company	Ticker	Recent Price (\$)	52-Week High (\$)	52-Week Low (\$)	Mkt. Cap (\$MIL)	1-yr Price Change (%)	1-yr Rev Growth (%)	1 YR EPS Growth (%)	P/E Ratio	Beta	Yield (%)
BETTER CHOICE COMPANY INC.	BTTR	1.45	2.20	0.24	138	16	NA	NA	NA	NA	NA
FRESHPET INC.	FRPT	146.53	149.60	40.79	5955	119	27	140	NM	0.84	NA
TDH HOLDINGS INC.	PETZ	2.02	3.76	0.52	93	41	-47	NA	NA	1.19	NA
PETMED EXPRESS INC	PETS	29.77	42.9	21.2	604	25	4	1	20.0	0.70	3.2
CENTRAL GARDEN AND PET CO	CENTA	38.46	41.10	21.66	2115	24	8	52	17.5	0.64	NA

The company has built a portfolio of brands that can address changing consumer trends, such as an extension of the Halo brand that includes vegan alternatives. In our view, this platform, through which Better Choice plans to expand with new innovative products, is supported by a supply-and-distribution infrastructure that typically can develop, manufacture and commercialize new products within 90 days.

Better Choice shares trade on the OTCQX, under ticker BTTR. The company plans to uplist to the NASDAQ or NYSE in mid-2021, which should expand its investor base and access to capital.

The pet wellness industry has experienced significant consolidation, and has recently seen a flurry of acquisitions, which we believe underscore its attractive dynamics. One industry leader, WellPet, itself the product of a series of acquisitions, was acquired by private equity investor Clearlake Equity Group in November 2020. The same month, another peer (Solid Gold Pet) was acquired by Hong Kong-based H&H Group for \$163 million. The acquisition added a pet care portfolio that complemented the company's existing products for adults, children and infants.

As a result of this industry consolidation, Better Choice now has few publicly traded peers, making performance and valuation comparisons more difficult. The company has one true public peer, Fresh Pet (FRPT), which currently trades at a much higher fundamental valuation than BTTR. During the fourth quarter of 2020, Fresh Pet traded at more than 20-times its 2019 revenues, while Better Choice traded at only 2-to-3 times its pro-forma 2019 revenues.

Over time, we expect Better Choice's valuation to benefit from the strong market outlook for premium pet food, and believe that the discount to FRPT will narrow as the company executes on its business model, integrates its recent acquisitions, and uplists to a major exchange.

## ANALYST COMMENTARY: EARNINGS

For the nine months ended September 30, 2020, Better Choice reported revenue of \$33.3 million, up 187% from the same period in 2019, reflecting contributions from the TruDog and Halo acquisitions. In recent years, gross margin has consistently been in the 35%-40% range, which we believe underscores the favorable market dynamics for its premium products. Year-to-date, the company has reported an adjusted EBITDA loss of \$1.1 million, excluding non-cash charges related to acquisitions and financing-related expenses.

In October 2020, Better Choice consolidated its warehouse and fulfillment operations at one location near Nashville, Tennessee. The consolidation will lower annualized expenses by approximately \$600,000.

As of September 30, 2020, Better Choice had roughly \$2.1 million in cash/restricted cash on its balance sheet, \$14.8 million in current assets and current liabilities of \$31.8 million. A primary component of the latter was \$13.3 million in term debt, all of which was refinanced in January 2021, with longer-term maturities and attractive terms that Better Choice expects will reduce annual interest expense to \$300,000 in 2021, down more than \$2 million from 2020. Also subsequent to the September quarter-end, in October 2020, the company executed on a Series F private placement, raising \$21.7 million in gross cash proceeds, approximately \$11.5 million of which was invested by company officers and directors. We expect these transactions to reduce balance sheet leverage significantly.

## MANAGEMENT

Scott Lerner has served as the company's CEO since January 2021. He has over 20 years of brand management experience in the consumer-packaged goods industry, including with brands focused on health and wellness. Mr. Lerner was most recently CEO of food brand Farmhouse Culture, and has previously served in leadership roles with renowned global brands including PepsiCo, ConAgra Foods, Kimberly-Clark and Parkay Margarine. Mr. Lerner has also led two companies, including one as founder, to significant value and creation and successful exits, via acquisition.

## RECENT DEVELOPMENTS

Over the past two years, Better Choice has become a leader in the premium pet-food industry, acquiring its flagship Halo and TruDog brands. In 2020, the company focused on integrating these acquisitions and generating synergies across its commercial footprint. In 2021, we expect the company to transition from consolidation and integration to implementing a plan for product innovation and continued robust sales growth. We believe that efficiencies from the recent consolidation of its warehouse and fulfillment operations and sales expansion, particularly internationally, position the company to reach adjusted, non-GAAP profitability by the end of 2021.

In January 2021, Better Choice appointed two new executives with established histories growing commercial operations and leading organizations to successful liquidity events to its leadership team. Better Choice first appointed Scott Lerner, as Chief Executive Officer. Mr. Lerner, a consumer products veteran and brand-management leader with over 20 years of experience in the consumer-packaged goods industry, replaced Werner von Pein, who helped lead the integration of the Halo Brand into the Better Choice portfolio.

To drive Better Choice's sales growth across the Pet Specialty channel, the company also appointed Donald Young to a newly created position as Executive Vice President of Sales. Mr. Young has nearly 30 years of sales leadership experience of several prominent pet specialty pet food brands including The Nutro Company and Merrick Pet Care. At Merrick, Mr. Young was directly responsible for transforming the company from a niche brand to the #3 pure play company in the pet specialty retail channel. Under Mr. Young's leadership, sales quadrupled over a 10-year period, which led to its sale to Nestle Purina PetCare in 2015. Mr. Young has earned numerous peer-awarded accolades, including being recognized among Pet Age Magazine's 2019 ICON Winners.

Lastly, in January 2021, Better Choice took key steps to solidify its balance sheet, securing a new \$12 million long-term credit facility, which refinanced its previous \$13.3 million debt. The transaction is expected to reduce annual cash interest payments to approximately \$300,000, down more than \$2 million compared with 2020, and a more than 5% reduction in the blended term rates.

Like most companies, Better Choice was heavily impacted by the COVID-19 pandemic in the first half of 2020. However, sales had largely returned to normal levels by June, helped by the company's strong e-commerce presence and DTC channels. As noted above, the company has also strengthened its balance sheet, raising \$21.7 million in gross proceeds through its Series F financing in 4Q20.

Steve Silver

**INCOME STATEMENT**

<b>Growth Analysis (\$MIL)</b>	<b>2018</b>	<b>2019</b>	<b>1Q 2020</b>	<b>2Q 2020</b>	<b>3Q2020</b>
Revenue	14.8	15.6	12.2	9.9	11.1
Gross Profit	7.3	5.9	4.2	4.1	4.4
SG&A	11.0	29.9	10.0	13.4	6.0
Stock Compensation Expense	0.4	10.3	2.5	3.0	1.5
Operating Income	-5.2	-36.3	-8.5	-12.5	-3.3
Interest Expense	0.9	0.7	2.3	2.4	2.5
Pretax Income	NA	NA	-8.1	-14.9	-5.9
Tax Rate (%)	NA	NA	NA	NA	NA
Net income	-6.0	-37.1	-8.1	-14.9	-5.9
Diluted Shares	11.5	33.2	48.5	48.7	48.8
EPS	-0.52	-1.12	-0.17	-0.31	-0.12
Dividend	NA	NA	NA	NA	NA
<b>Growth Rates (%)</b>					
Revenue	NA	5%	244%	143%	183%
Operating Income	NA	NA	NA	NA	NA
Net Income	NA	NA	NA	NA	NA
EPS	NA	NA	NA	NA	NA
<b>Valuation Analysis</b>					
Price (\$): High	NA	NA	NA	NA	NA
Price (\$):Low	NA	NA	NA	NA	NA
PE: High	NA	NA	NA	NA	NA
PE: Low	NA	NA	NA	NA	NA
PS: High	NA	NA	NA	NA	NA
PS: Low	NA	NA	NA	NA	NA
Yield: High	NA	NA	NA	NA	NA
Yield: Low	NA	NA	NA	NA	NA
<b>Financial &amp; Risk Analysis (\$MIL)</b>					
Cash	3.9	2.6	1.8	3.5	0.6
Working Capital	-3.1	-15.4	-17.1	-21.7	-17.0
Current Ratio	0.7	0.5	0.5	0.4	0.5
LTDebt/Equity (%)	NA	NA	NA	NA	NA
Total Debt/Equity (%)	NA	NA	NA	NA	NA
<b>Ratio Analysis</b>					
Gross Profit Margin	49%	38%	34%	41%	40%
Operating Margin	NA	NA	NA	NA	NA
Net Margin	NA	NA	NA	NA	NA
Return on Assets (%)	NA	NA	NA	NA	NA
Return on Equity (%)	NA	NA	NA	NA	NA
Op Inc/Int Exp	NA	NA	NA	NA	NA
Div Payout	NA	NA	NA	NA	NA

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