

Reed's, Inc.

NYSE: REED



Production problems greatly impacted Reed's 3Q15, but expanded production is on track to allow for a strong 2016. Reiterate Strong Buy

Reed's engages in the development, manufacture, and marketing, sale of natural non-alcoholic carbonated soft drinks, kombucha, candies, and ice creams primarily in the US.

3Q15 Takeaways

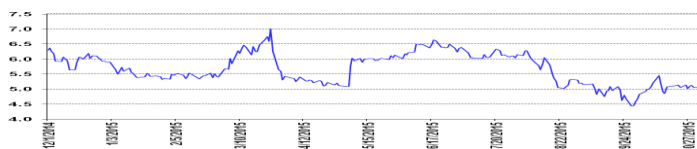
Reed's reported 3Q15 revenue of \$10.7M (-13% YoY) due to production shortfalls that limited supply well below demand. Specifically, reorganizing the supply chain, disposal of inferior quality product from the new plant, and reduction in obsolete material were all factors negatively impacting results. **Excluding production problems, Reed's management claims the company might have generated revenues above \$15M in the quarter.**

Reed's continues to make adjustments that will greatly increase production capacity and efficiency, including adding 3-4 co-packing facilities. They are revamping their Los Angeles plant.

The two new plants (East & West Coast) may save the company at least \$2M a year in labor and freight charges. The majority of the Los Angeles equipment is at the plant ready to go and management says that it should be up and running in the next few months. The savings from the West Coast plant will be from a reduction in idle plant capacity and labor costs.

Kombucha shortfall of \$1.3M was largely operational with some competitive headwinds. Reed's was unable to supply orders of Kombucha to large natural food chains. Aside from production difficulties, management stated competition from regional brands is hurting Reed's Kombucha in certain markets. Specifically, the difficulty of penetrating certain regions remains a minor hurdle. In addition, Management stated that regional brands backed by large promotional budgets are trying to go main stream (increasing competition).

Reed's roll out of all-natural fountain soda products in fast casual restaurants could provide major future growth for the company. Reed's is in discussion with a large fast casual chain (2,000+ units) to test Reed's Ginger Brew and Virgil's in a number of restaurants. If all the tests go well, the fast casual chain might want to order as much as \$40M+ of product from late 2016 through 2017.



Rating	Strong Buy
Risk Rating	Speculative
Current Price (12/3/2015)	\$5.10
2015 Price Target	\$9.28
Implied dividend yield	0.0%
Projected total return	+82%

Shares outstanding (M)	13.1
Market capitalization (M)	\$66.8
Long term debt (MRQ)	\$11.3
Cash (MRQ)	\$1.2
Enterprise value	\$76.9
EV/2016 Rev estimate	2.1x

Average daily volume (3 m)	190,000
Float as % of shares out.	75.5%
Short interest as % of Float	1%
Insider ownership	25%
Institutional ownership	6%

Tangible book value p/s	\$0.35
Cash/share	\$0.13

Revenue (M)				
	2013	2014A	2015E	2016E
Q1	\$8.1	\$9.0	\$10.7a	\$13.6
Q2	\$9.5	\$11.2	\$12.2a	\$14.4
Q3	\$10.1	\$12.4	\$10.7a	\$15.2
Q4	\$9.5	\$11.0	\$14.0	\$15.3
FY	\$37.3	\$44.9	\$47.6	\$58.5
EBITDA (M) Mgmt.				
	2013	2014A	2015E	2016E
Q1	\$0.0	\$0.2	\$0.4	\$1.0
Q2	\$0.3	\$1.1	\$0.1	\$0.9
Q3	\$0.4	\$0.5	(\$1.8)	\$0.9
Q4	(\$0.4)	(\$0.4)	\$1.0	\$1.0
FY	\$0.3	\$1.4	(\$0.3)	\$3.8

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Appendix A: Income Statement

INCOME STATEMENT	1Q12A	2Q12A	3Q12A	4Q12A	1Q13A	2Q13A	3Q13A	4Q13A	1Q14A	2Q14A	3Q14A	4Q14A	1Q15A	2Q15A	3Q15A	4Q15E	1Q16E	2Q16E	3Q16E	4Q16E	2010	2011	2012	2013	2014	2015E	2016E
	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Dec-10	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15	Dec-16
Revenues	6.5	7.8	7.9	7.7	8.1	9.5	10.1	9.5	9.0	11.2	12.3	11.0	10.7	12.2	10.7	14.0	13.6	14.4	15.2	15.3	20.4	25.0	30.0	37.3	43.4	47.6	58.5
COGS (Tangible Goods)	4.2	4.8	4.8	5.2	4.9	6.6	6.4	5.8	5.6	7.0	8.0	7.8	6.7	7.9	8.8	8.9	8.5	9.1	9.6	9.7	13.1	15.8	18.9	23.3	28.6	32.2	36.9
COGS (Idle Capacity)	0.4	0.4	0.6	0.6	0.7	0.4	0.5	1.2	0.5	0.5	0.4	0.4	0.7	0.7	0.4	0.1	0.1	0.1	0.2	0.2	1.2	1.8	1.9	2.8	1.8	1.9	0.6
Gross Profit	2.0	2.7	2.5	2.0	2.5	2.5	3.2	2.6	2.9	3.7	3.9	2.7	3.3	3.6	1.6	5.0	4.9	5.2	5.4	5.5	6.1	7.4	9.1	11.2	13.0	13.4	21.0
Gross Margin	30.4%	34.4%	31.1%	25.9%	31.2%	25.8%	31.7%	27.1%	32.4%	33.2%	31.5%	25.0%	30.7%	29.9%	14.6%	35.5%	36.2%	35.8%	35.8%	35.7%	29.8%	29.6%	30.5%	30.0%	30.0%	28.3%	35.9%
Delivery and Handling	0.5	0.6	0.8	0.8	0.9	1.0	1.0	1.2	0.9	0.9	1.3	1.1	1.2	1.4	1.4	1.2	1.2	1.3	1.3	1.3	1.7	2.3	2.6	4.0	4.5	5.2	5.1
General and Administrative	0.7	0.8	0.7	1.0	1.0	0.9	0.8	0.8	1.1	1.0	0.8	1.1	1.0	1.4	1.1	1.4	1.4	1.4	1.5	1.5	2.7	2.9	3.2	3.5	3.6	4.8	5.8
Selling and Marketing	0.7	0.7	0.8	0.9	0.9	1.0	1.2	1.1	1.0	0.9	1.5	1.6	1.2	1.3	1.2	1.7	1.6	1.9	2.0	1.8	2.3	2.5	3.1	4.2	4.8	5.5	7.3
EBITDA	0.2	0.8	0.4	(0.5)	(0.1)	(0.2)	0.3	(0.5)	0.1	1.0	0.4	(0.5)	0.2	(0.3)	(1.9)	0.9	0.9	0.8	0.8	0.9	(0.1)	0.4	0.9	(0.0)	0.8	(1.1)	3.5
EBITDA margin	3.5%	10.2%	4.7%	(6.7%)	(1.1%)	(1.8%)	3.3%	(5.4%)	1.7%	9.2%	3.2%	(4.3%)	1.5%	(2.1%)	(17.8%)	6.1%	6.9%	5.4%	5.3%	6.2%	(0.5%)	1.6%	2.9%	(0.1%)	1.9%	(2.4%)	5.9%
EBITDA Modified (Mgmt.)	0.3	0.8	0.4	(0.2)	0.0	0.3	0.4	(0.4)	0.2	1.1	0.5	(0.4)	0.3	(0.2)	(1.8)	1.0	1.0	0.9	0.9	1.0	0.5	0.8	1.3	0.3	1.5	(0.8)	3.9
EBITDA Adj. (Ours)	0.2	0.8	0.4	(0.2)	(0.1)	0.2	0.3	(0.5)	0.1	1.0	0.4	(0.5)	0.2	(0.3)	(1.9)	0.9	0.9	0.8	0.8	0.9	(0.1)	0.7	0.9	0.1	0.8	(1.1)	3.5
EBITDA margin	3.5%	10.2%	4.7%	(2.5%)	(1.1%)	2.6%	3.3%	(5.4%)	1.7%	9.2%	3.2%	(4.3%)	1.5%	(2.1%)	(17.8%)	6.1%	6.9%	5.4%	5.3%	6.2%	(0.5%)	2.9%	2.9%	0.2%	1.9%	(2.4%)	5.9%
Depreciation	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.0	0.2	0.2	0.1	0.5	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.6	0.7	0.7	0.4	0.8	0.9	0.8
Amortization of intangibles	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	0.0	0.6	0.2	(0.7)	(0.2)	(0.4)	0.2	(0.5)	(0.0)	0.8	0.2	(1.0)	(0.1)	(0.5)	(2.1)	0.7	0.7	0.6	0.6	0.7	(0.7)	(0.2)	0.1	(0.5)	0.1	(2.0)	2.7
EBIT margin	0.7%	7.8%	2.3%	(9.0%)	(2.9%)	(3.9%)	2.4%	(5.5%)	(0.4%)	7.4%	2.0%	(9.2%)	(0.5%)	(4.0%)	(20.0%)	4.7%	5.4%	4.0%	4.0%	4.9%	(3.6%)	(1.0%)	0.5%	(1.3%)	0.1%	(4.3%)	4.6%
Non-oper expenses	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gain (loss) on asset sales	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest Income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest expense	0.2	0.2	0.2	0.2	0.2	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3	0.3	0.1	0.1	0.1	0.1	0.1	0.6	0.7	0.7	0.7	0.8	0.8	0.4
EBT	(0.1)	0.4	0.0	(0.9)	(0.4)	(0.5)	0.1	(0.7)	(0.2)	0.7	0.1	(1.2)	(0.3)	(0.7)	(2.5)	0.6	0.6	0.5	0.5	0.6	(1.3)	(0.9)	(0.5)	(1.1)	(0.7)	(2.8)	2.3
EBT margin	(1.9%)	5.7%	0.3%	(11.2%)	(5.0%)	(5.2%)	0.7%	(7.4%)	(2.6%)	5.8%	0.4%	(10.9%)	(2.4%)	(5.6%)	(23.0%)	4.0%	4.7%	3.3%	3.3%	4.2%	(6.4%)	(3.8%)	(1.7%)	(3.0%)	(1.7%)	(6.0%)	3.9%
Provision for taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.0
Equity earnings in affiliate	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Minority interest in earnings	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Income	(0.1)	0.4	0.0	(0.9)	(0.4)	(0.5)	0.1	(0.7)	(0.2)	0.7	0.0	(1.2)	(0.3)	(0.7)	(2.5)	0.6	0.6	0.5	0.5	0.6	(1.3)	(0.9)	(0.5)	(1.1)	(0.7)	(2.9)	2.3
Net Margin	(1.9%)	5.7%	0.3%	(11.2%)	(5.0%)	(5.2%)	0.7%	(7.4%)	(2.6%)	5.8%	0.2%	(11.2%)	(2.7%)	(5.9%)	(23.3%)	4.0%	4.7%	3.3%	3.3%	4.2%	(6.4%)	(3.8%)	(1.7%)	(3.0%)	(1.7%)	(6.2%)	3.9%
Net Income Adj.	(0.1)	0.4	0.0	(0.5)	(0.4)	(0.1)	0.1	(0.7)	(0.2)	0.7	0.0	(1.2)	(0.3)	(0.7)	(2.5)	0.6	0.6	0.5	0.5	0.6	(1.3)	(0.6)	(0.5)	(1.1)	(0.7)	(2.9)	2.3
Net Margin	(1.9%)	5.7%	0.3%	(7.0%)	(5.0%)	(0.9%)	0.7%	(7.4%)	(2.6%)	5.8%	0.2%	(11.2%)	(2.7%)	(5.9%)	(23.3%)	4.0%	4.7%	3.3%	3.3%	4.2%	(6.4%)	(2.5%)	(1.7%)	(3.0%)	(1.7%)	(6.2%)	3.9%
WACSO	10.9	11.0	11.5	11.4	12.3	12.5	12.8	12.5	13.0	13.0	13.1	13.1	13.1	13.1	13.1	13.5	13.8	13.8	13.8	13.8	10.1	10.8	11.4	12.5	13.0	13.2	13.8
Diluted	10.9	11.0	11.5	11.4	12.3	12.5	12.8	12.5	13.0	13.3	13.1	13.1	13.1	13.1	13.1	13.5	13.8	13.8	13.8	13.8	10.1	10.8	11.4	12.5	13.0	13.2	13.8
WACSO (Adj.)	10.9	11.0	11.5	11.4	12.3	12.5	12.8	12.5	13.0	13.0	13.1	13.1	13.1	13.1	13.1	13.5	13.8	13.8	13.8	13.8	10.1	10.8	11.4	12.5	13.0	13.2	13.8
EPS Basic	(\$0.01)	\$0.04	\$0.00	(\$0.08)	(\$0.03)	(\$0.04)	\$0.01	(\$0.06)	(\$0.02)	\$0.05	\$0.00	(\$0.09)	(\$0.02)	(\$0.05)	(\$0.19)	\$0.04	\$0.05	\$0.03	\$0.04	\$0.05	(\$0.13)	(\$0.09)	(\$0.05)	(\$0.12)	(\$0.06)	(\$0.22)	\$0.16
EPS Diluted	(\$0.01)	\$0.04	\$0.00	(\$0.08)	(\$0.03)	(\$0.04)	\$0.01	(\$0.06)	(\$0.02)	\$0.05	\$0.00	(\$0.09)	(\$0.02)	(\$0.05)	(\$0.19)	\$0.04	\$0.05	\$0.03	\$0.04	\$0.05	(\$0.13)	(\$0.09)	(\$0.05)	(\$0.12)	(\$0.06)	(\$0.22)	\$0.16
EPS Adj	(\$0.01)	\$0.04	\$0.00	(\$0.05)	(\$0.03)	(\$0.01)	\$0.01	(\$0.06)	(\$0.02)	\$0.05	\$0.00	(\$0.09)	(\$0.02)	(\$0.05)	(\$0.19)	\$0.04	\$0.05	\$0.03	\$0.04	\$0.05	(\$0.13)	(\$0.06)	(\$0.05)	(\$0.09)	(\$0.06)	(\$0.22)	\$0.16

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