

INTERNAL REPORT

Simply Good Foods Co.

June 5, 2018
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(SMPL - NASDAQ)
Initial Report

Current Price	\$13.18
52-week High	\$14.52
52-week Low	\$11.14
Price Target	\$17.00

Rating	Buy
Shares Out	70.6M
Market Cap	930.3M
Avg. Daily Vol	339.7K

FY18 EPS	\$0.53
EPS Growth Rate	25%
FY18 PE	24.8
FY18 PEG	1.8

Book Value/Share	\$9.23
Cash/Share	-\$0.09
Insider Ownership	29%
Institution Ownership	87%

Business Description

Simply Good Foods, based in Denver, Colorado, is a leading developer, marketer, and seller of branded nutritional foods and snacking products. The company's product line consists of nutrition bars, ready-to-drink shakes, snacks, and confectionary products marketed under the *Atkins*, *SimplyProtien*, *Atkins Harvest Trail*, and *Atkins Endulge* brands. Atkins is a roughly **\$600 million** brand at retail, consisting of **\$461 million** in the U.S. snacking category, over **\$100 million** in frozen foods, and over **\$40 million** international sales. In 2017, Simply Good Foods generated **\$396.2 million** in revenues with adjusted EBITDA of **\$72.5 million (18.3% margin)**. Simply Good Foods was formed in July 2017 via the merger of privately-held **Atkins Nutritional** with publicly-traded **Conyers Park Acquisition Corp.**, a special purpose acquisition corporation (SPAC), which was sponsored by *Conyers Park*, an affiliate of private equity firm *Centerview Capital*.

Competitive Advantages

- **Nutritional Snacking Leader** – Atkins ranks as the leading Nutritional Snacking company by IRI with a market share of **11.7%**, outpacing **CLIF Bar** at **10.9%**, **KIND** at **9.2%**, **Premier Protein** at **6.8%**, **Muscle Milk** at **4.8%**, and **Special K** at **3.5%**. Atkins averages **62 servings per buyer** per year, which is well ahead of peers such as **CLIF Bar** at **46**, **QuestNutrition** at **38**, and **KIND** at **23**. Atkins also has an impressive **85%** aided brand awareness level with consumers, according to a company-sponsored survey completed in 2016. Atkins is the only brand in the Nutritional Snacking space to spend a meaningful amount on advertising, devoting 9%-10% of revenues to sales and marketing.
- **Asset-Lite Business Model** – Simply Goods Foods operates as an asset-lite business, as it combines the company's core expertise in the areas of sales and marketing, brand management, customer relationships, product development, and supply-chain expertise with a diversified pool of contract manufacturers and distributors to execute manufacturing and distribution. This has enabled the business to grow relatively quickly and profitably with sales growth, adjusted EBITDA growth, and profit margins among the leaders in the packaged foods industry, despite the company's relatively small size.

Assessment of Management

Simply Good Foods combines highly experienced executive management with the expert tutelage, strategic insight, and merger and acquisition capabilities of a highly skilled Board of Directors stemming from the company's relationship with Conyers Park. The company is led by CEO **Joseph Scalzo**, who served as the CEO of Atkins Nutritional since 2013. Prior to joining Atkins, Mr. Scalzo previously served as the President & COO of *Dean Foods* where he lead the creation and transformation of *WhiteWave Foods*, where he also served as President and CEO. Prior to joining Dean Foods, Mr. Scalzo served in various executive roles at *Proctor & Gamble* and The *Coca Cola Company*. The company's CFO is **Todd Cunfer**, who prior to joining Simply Good Foods served in various finance executive roles with *The Hershey Company* over a 20-year period, including VP, Finance-International, VP, Global Supply Chain Finance, and VP – North America Finance. The company recently added another veteran of The Hershey Company with its VP, Investor Relations and Business Development **Mark Pogharian**, who previously led the Investor Relations team at The Hershey Company.

From a Board level, the company is overseen by Chairman **Jim Kilts**. Mr. Kilts is a consumer packaged goods industry icon, having founded Centerview Capital in 2006 and previously served as Vice Chairman of Proctor & Gamble, Chairman, CEO and President of *The Gillette Company*, CEO and President of *Nabisco*, and Head of the Worldwide Food Group for *Phillip Morris (including Kraft Foods and General Foods)*. Mr. Kilts is relatively active in overseeing Simply Good Foods and mentoring CEO Scalzo. Simply Good Food's Vice Chairman is **David West**, who is a partner of Centerview Capital and previously served as CEO of *Big Heart Pet Brands* (f/k/a Del

Monte Corporation), CEO of The Hershey Company, and held various senior management roles at Nabisco and Kraft Foods. Mr. West devotes the majority of his time to Simply Good Foods and is highly involved with the company’s merger and acquisitions strategy. Simply Good Foods has one of the most impressive management teams and Board of Directors of any small cap Consumer Staples company and it uniquely positions the company to execute on its strategies to drive organic growth for the core business and build a platform to consolidate the highly fragmented nutritional snacking and broader snacking industries. In addition, the Board includes several members with extensive experience in and around the consumer packaged goods industry whose insight may prove invaluable as the company executes its growth strategy, including *Arvin Kash*, who previously served as Vice Chairperson of *Nielsen Holdings*; *Robert Montgomery*, who served in various executive positions with *Birds Eye Foods*, *HJ Heinz Company*, *ConAgra*, and *Sara Lee*; *James Healy*, who previously served as CFO of *Nabisco*; and *Clayton Dayle, Jr.*, who previously served as CFO of *Procter & Gamble*.

Simply Good Foods has adequate corporate governance practices. The Board is largely independent with nine independent members out of a ten person Board of Directors. Management compensation levels appear reasonable and include meaningful incentives based on the achievement of revenue and adjusted EBITDA based targets. The interests of insiders appear to be well aligned with shareholders, as they hold nearly **29%** of the company’s total outstanding shares.

Growth Drivers

- **Growth in Nutritional Snacking** – Atkins has an impressive track record of growth with a **nine-year (2008-2017)** compounded annual growth rate of U.S. snacking industry retail sales of **14%**, reaching **\$461 million** in sales in 2017. Fiscal year-to-date U.S. snacking industry **POS sales** are **up 5.1%**. Management expects **long-term growth** of **4%-6%**. Atkins has benefitted from its alignment with consumer mega trends associated with low carb, low sugar, and protein-rich nutrition. POS data available on Simply Good Foods shows that its two largest segments of **Snack Bars/Granola Bars** at **~50%** of sales and **Shakes** at **~28%**, are continuing to perform well. For the trailing 4-, 12-, 24-, and 52-week periods, the Bar business has **generated double-digit retail revenue growth** and has been accelerating over the past two months. The shake business has been improving sequentially y/y, as well. Even as we remain optimistic for future additions to Simply Good Food’s product line, the strength of the core business continues to be a positive driver.

SMPL	% of Sales	y/y % change			
		52 W	24 W	12 W	4 W
Total Store	100%	2.3%	3.5%	5.6%	6.5%
Snack Bars/Granola Bars	50%	10.2%	10.5%	12.6%	12.1%
Weight Control	28%	0.6%	2.7%	4.4%	4.4%
Dinners/Entrees - Fz	11%	-16.2%	-18.1%	-17.3%	-15.1%
Chocolate Candy	6%	2.2%	4.6%	9.2%	17.2%
Breakfast Food - Fz	2%	0.3%	7.0%	9.5%	12.7%
Pizza - Fz	1%	-16.8%	12.6%	-9.1%	-5.4%
Other Snacks	1%	-29.7%	-13.2%	-10.9%	-9.6%

- **Large Customer Base** - Historically, Atkins core market has consisted of individuals participating in self-directed or branded weight management programs. The company is working to expand the reach of the brand to the larger healthy lifestyle market, which management estimates is **4x** the size of the company’s core market. Simply Good Food’s advertising campaign has shifted focus towards healthy snacking and healthy lifestyles, away from a “*before and after*” weight loss message with the introduction of actor **Rob Lowe** as Atkins’ spokesperson in January 2018. Simply Good Foods has not made a weight loss claim in over three years. Company research indicates that the Atkins consumer is a relatively sticky consumer with a long tail in buying trends. Atkins has a well-defined brand and its consumers do not exhibit a high degree of switching among brands.
- **Market Expansion Opportunities** – Simply Good Foods derives over **80%** of its revenues from the **Mass Merchant (46%)** and **Grocery (37%)** channels. **Management believes the convenience store, club, and e-commerce channels are relatively underpenetrated.** The company has achieved notable success in recent

periods with **Amazon** in the e-commerce channel. Atkins currently ranks as one of the highest performing brands for subscription re-orders with Amazon. Management attributes this to the strength of the brand and the company's core manufacturing and packaging focus on multi-item packages. In club, the company has significant traction with both **Sam's Club** (#2 overall customer) and **BJ's**, but not with **Costco**. The issues with Costco stem from the earlier bankruptcy of the Atkins brand, which resulted in significant write-offs for Costco. Management is actively working to rebuild this relationship. Management sees the convenience store channel as a potential opportunity, but views the lack of penetration as an internal resource issue. The channel is more conducive to single-bar offerings, which is not an area where Atkins currently plays, but is willing to expand into in the future.

- **M&A Opportunities** – Mergers and acquisitions are expected to be a meaningful part of Simply Good Food's long-term growth strategy as the company seeks to consolidate the highly fragmented nutritional snacking market and expand into adjacent markets. Management is likely to focus on opportunities within the **nutritional snacking market**, as it would provide Simply Good Foods the most leverage in terms of sales force productivity, relationships with third-party manufacturers, and customer relationships. Simply Good Food's management team has extensive experience in brand building, merchandising, and product development that will be instrumental in elevating acquired brands. The company is also looking to **adjacent markets**, such as **better-for-you eating**, and the **overall snacking and convenience markets**, although these markets appear to represent longer term opportunities. **Simply Good Foods is well positioned to aggressively pursue merger and acquisition opportunities with the depth and breadth of its management team and relationship with Conyers Park and its relatively strong balance sheet.** In addition, management believes that Simply Good Foods represents an attractive Reverse Morris Trust partner for large companies looking to monetize portions of their portfolio in a tax-efficient manner.

Issues / Risks

Issues and risks related to the shares of Simply Good Foods include the following:

- **Atkins Nutritional operates in the highly competitive nutritional snacking industry, which has relatively low barriers to entry and tends to be highly promotional.** Atkins has successfully established a market leadership position through the strength of its brand, quality of its products, and success of its marketing campaigns. The company strategically focuses its retail distribution on the Health and Beauty Aids section of retail outlets with performance and nutrition driven offerings in a multi-pack format, rather than **“center of the store”** nutritional snacking section of the store that is more heavily dominated by highly promotional single-serving products. Any adverse changes in the competitive environment or strategic focus of the distribution strategy could impact the company's ability to meet its financial targets.
- **While Simply Good Foods appears to have an adequate information technology infrastructure for its current size and scale, the company will likely need to invest in the infrastructure to facilitate the future growth of the business.** This will likely come from internal investment or the acquisition of a business with a more robust IT infrastructure that can be rolled out on a company-wide basis. We expect that a “buy vs build” decision will be made during the next twelve months.
- While Simply Good Foods has not completed an acquisition since the SPAC merger transaction, mergers and acquisition are likely to be an important element of the company's growth strategy going forward. **The ability of the company to successfully identify, acquire, and integrate attractive brands and business, while maintaining a strong balance sheet, will be critical to the company achieving its growth potential.**
- **Simply Good Foods has roughly 20 million warrants outstanding with an exercise price of \$11.50 per share as a result of the SPAC merger.** Approximately 2/3 of the warrants are held by Conyers Park and have no expiration date. The remaining expire in 2022. The company has the ability to call the warrants for redemption if the stock price exceeds **\$18.00 per share** for any 20 trading days within a 30-day period. The full exercise of the warrants could increase the company's total shares outstanding by as much as **28%**. As such, we believe the potential warrant exercise could represent an overhang for the share price until they are redeemed or retired.

Summary and Recommendation

Simply Good Foods represents an intriguing growth opportunity in the Consumer Staples Sector. The company is well positioned with the leading brand in the Nutritional Snacking industry that should continue to yield

above industry average revenue growth with attractive profit margins. In addition, the company is well positioned in the long term as a leading consolidator of the highly fragmented Nutritional Snacking industry and adjacent markets, given the expertise and experience of Simply Good Food's management team, access to Conyers Park's management experience and merger & acquisition capabilities, and the company's relatively strong balance sheet.

We believe the strength of the business and the magnitude of the growth opportunity is not fully reflected in the company's share price. Simply Good Food's shares are currently trading at **15x** our 2018 adjusted EBITDA estimate of **\$70 million** and **14x** our 2019 adjusted EBITDA estimate of **\$80 million**. This compares with (the relatively growth-starved) consumer packaged goods peer group that trades at multiples between **14x** and **17x** current year estimated adjusted EBITDA. We believe Simply Good Foods should trade at or above the upper end of the peer group given the company's superior growth profile and attractive business model. **As a result, our 12-month price target is \$17 per share, or roughly 16x our 2019 adjusted EBITDA estimate, representing upside potential of over 23%. We rate Simply Good Food's shares as a BUY.**

Financial Summary

SMPL	Annual Results	FY17A	FY18E	FY19E
	Revenue	396.2M	418.9M	439.3M
	EPS	-0.03	0.53	0.58
	Y-Y Rev Growth	#N/A	5.7%	4.9%
	Y-Y EPS Growth	44.0%	-	9.6%

Comments

Estimates reflect sell-side consensus

FY0a	12-16	@NA	5-17	8-17
Revenue	0.0M	#N/AM	#N/AM	96.5M
EPS	-0.01	#N/A	#N/A	0.06

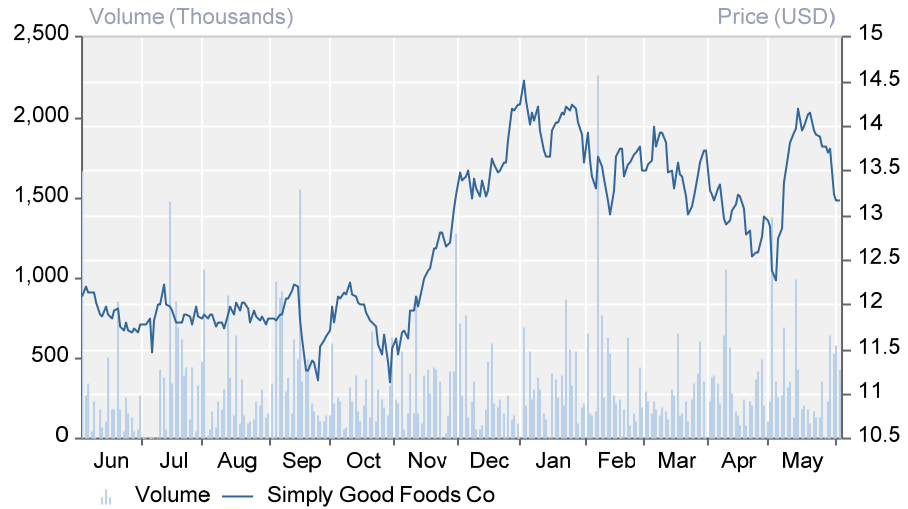
FY1e	11-17	2-18	5-18	8-18
Revenue	106.6M	109.3M	101.2M	101.6M
EPS	0.14	0.56	0.10	0.12
Y-Y Rev Growth	#N/A	#N/A	4.9%	4.1%
Y-Y EPS Growth	#N/A	#N/A	56.2%	12.9%

Additional Data

Current Price	13.18
12-month High	14.52
12-month Low	11.14
FY End	08/2017
Dividend	0
Shares Outstanding	70.6M
Shares Short	3.0M
Avg Daily Vol	339.7K
Cash and ST Invest	#N/AM
ST & LT Debt	#N/AM

Updated: 6/5/2018

Simply Good Foods Co (SMPL-US)



Growth Oriented Packaged Food Cos.	FY	Share	52-wk	52-wk	Market	EV	FY2018	FY2019	LT Growth	FY2018*	FY2019*	FY2018*	FY2019*	FY2018	FY2019	FY2018*	FY2019*	FY2018	FY2019	Sales	EPS	EBITDA	
	End	Price	High	Low	Cap. (\$M)	(\$M)	EPS	EPS	Rate (%)	P/E	P/E	Rev(\$M)	Rev(\$M)	P/S	P/S	EBITDA	EBITDA	EV/EBITDA	EV/EBITDA	Growth	Growth	Growth	
Pinnacle Foods, Inc.	PF	Dec	\$63.47	\$64.42	\$52.85	\$7,563.8	\$10,245.9	\$2.90	\$3.18	10.62	21.9x	19.9x	\$3,148.9	\$3,209.6	3.25x	3.19x	\$699.42	\$743.99	14.6x	13.8x	1.93%	9.63%	6.37%
Lancaster Colony Corporation	LANC	Jun	\$129.01	\$134.42	\$115.02	\$3,544.9	\$3,357.6	\$4.59	\$5.26	10.00	28.1x	24.5x	\$1,209.6	\$1,242.3	2.78x	2.70x	\$198.00	\$219.30	17.0x	15.3x	2.71%	14.52%	10.76%
Hain Celestial Group, Inc.	HAIN	Jun	\$27.14	\$45.00	\$25.52	\$2,941.5	\$3,573.5	\$1.24	\$1.42	6.57	21.9x	19.2x	\$2,556.3	\$2,602.2	1.40x	1.37x	\$265.80	\$288.11	13.4x	12.4x	1.79%	14.32%	8.39%
J & J Snack Foods Corp.	JJSF	Sep	\$146.16	\$153.80	\$124.78	\$2,733.5	\$2,609.0	\$4.77	\$5.28	#N/A	30.6x	27.7x	\$1,150.5	\$1,190.4	2.27x	2.19x	\$167.29	\$179.44	15.6x	14.5x	3.46%	10.63%	7.26%
Hostess Brands, Inc. Class A	TWPK	Dec	\$13.19	\$16.73	\$11.27	\$1,317.9	\$2,557.3	\$0.69	\$0.84	11.23	19.3x	15.7x	\$865.8	\$903.7	2.95x	2.83x	\$222.59	\$252.23	11.5x	10.1x	4.38%	22.79%	13.31%
Simply Good Foods Co	SMPL	Aug	\$13.45	\$14.52	\$11.14	\$949.3	\$1,089.9	\$0.53	\$0.58	13.46	25.6x	23.3x	\$418.9	\$439.3	2.60x	2.48x	\$74.30	\$78.27	14.7x	13.9x	4.85%	9.62%	5.34%
Freshpet Inc	FRPT	Dec	\$23.65	\$23.65	\$14.50	\$832.4	\$835.3	(\$0.02)	\$0.30	#N/A	-1330.3x	79.2x	\$186.6	\$227.4	4.48x	3.67x	\$20.24	\$30.99	41.3x	27.0x	21.89%	-1780.47%	53.13%
					\$2,840.5	\$3,466.9			10.4%	-169.0x	29.9x			2.8x	2.6x	\$235.4	\$256.0	\$18.3	\$15.3				