Trickle Research

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

Do Not Distribute

Initiating Research Coverage

Generation Next Franchise Brands, Inc.

(OTC: VEND)

http://www.gennextbrands.com

Report Date: 07/23/19

12- 24 month Price Target: $1.10

Allocation: 3

Closing Stock Price at Initiation (Closing Px: 07/23/19): $.59

Prepared By:
David L. Lavigne
Senior Analyst, Managing Partner
Trickle Research

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

Company Overview

Generation Next Franchise Brands Inc. primarily develops and operates franchise concepts as well as related technology. To date, the Company's franchise brands have focused on vending franchises. The Company develops unique combinations of products and vending form factors that set them apart from traditional vending machine offerings. In that regard, their current endeavors are centered around the development and expansion of a vending platform that they sometimes refer to as "vending frozen yogurt robots". As we will illustrate in this report, "unattended retail" of which vending machines are a part, is a burgeoning portion of the retail industry.

Previous to their current focus of vending frozen yogurt ("froyo") robots, the Company was a franchisor of vending machines and operator of Company-owned vending machines and micro markets that made healthy eating more convenient through access to high quality healthy foods at high foot traffic vending destinations. That particular offering proved less robust than the Company had anticipated, which eventually lead to them terminating the business. On the other hand, in 1H-2016 the Company launched a new concept called Reis & Irvy's ("R&I"), which included the frozen vending technology they use today.

Following the launch of R&I in December 2016, VEND entered into an Asset Purchase Agreement with Robofusion, Inc. ("RFI"), the developer of the frozen robotic-kiosk vending technology. The transaction included the Company's acquisition of the intellectual property assets of RFI, as well as the Reis & Irvy's trademark. As a result of the acquisition, the Company's primary business is focused on developing the franchising and licensing business of R&I, expanding Company owned opportunities of the brand and furthering the development of its robot based unattended retail technologies to perhaps develop and deliver additional brands in the future.

Having acquired R&I at the tail end of 2016, the Company spent 2017 preparing for the launch of the R&I brand and franchise. That entailed creating a host of processes including design, manufacturing, robot delivery and deployment, servicing, franchising, finance and the other part that support those functions and tie them all together. Those endeavors lead to several topical agreements with vendors and other partners to provide a turnkey delivery solution for the brand. For instance, through 2017 they were able to ink arrangements with Dannon, which provides the Company's frozen YoCream® product, as well as the Canteen Vending Division of Compass Group USA, Inc., which provides location procurement services for the placement of Generation Next's vending robots. We think it is fair to say that each of those arrangements has proven to be highly positive for VEND.

In September 2017, the Company also announced an agreement with Flex, Ltd., to be its exclusive manufacturing partner for the Company's frozen yogurt robots. As the press release of that agreement noted: *"Flex, Ltd. ("Flex"), is the Sketch-to-Scale™ solutions provider that designs and builds Intelligent Products for a Connected World™. With approximately $24 billion in annual revenue and 200,000 professionals across 30 countries, Flex, Ltd. provides innovative design, engineering, manufacturing, real-time supply chain insight and logistics services to companies of all sizes in various industries and end-markets. Throughout the world, Flex has provided manufacturing services for clients that include Redbox, Kodak, Microsoft, Amazon, Google, Nike, and Bose to name just a few".* When first announced, this arrangement looked to be a milestone of sorts for the Company given the profile of Flex and it anticipated *"the production and rollout of approximately 760 pre-sold vending robots before June 30, 2018."* Unfortunately, that did not happen and certainly through 2018, the agreement has proven to be a bit of an albatross for Generation Next. As a result of design, production and quality control shortfalls, VEND effectively spent 2018 managing the fallout of their inability to deliver pre-sold units, as well as trying to mitigate the failures of the few units that they did deliver. As a result, whereas 2018 *should have* been a year of initial launch, growth and improving financial performance, it was instead marked by a myriad of problems including franchisees waiting on deliveries of robots, and ultimately a deterioration in their financial

Do Not Distribute

condition as a result of their inability monetize their sales efforts. Ironically, their successful sales efforts in anticipation of mid-2018 deliveries probably exacerbated the problem.

As a result of these issues, the Company has spent much of the past year addressing their challenges. To that end, we would add that in early January (2019), the Company hired current CFO/COO Ryan Polk as a consultant, and we believe Mr. Polk has been quite instrumental in helping the Company rectify several of the prevailing problems. The Company added Mr. Polk to the C-Suite in early April (2019). We believe his addition has proven to be highly positive, as illustrated by improvements on a variety of fronts including a new supply chain and manufacturing arrangements. We will discuss those improvements in greater detail below.

To summarize, despite some of the challenges, some of which have been acute, we don't view the trajectory here as particularly atypical when it comes to small emerging enterprises (read: microcap stocks). Anyone who has done this for as long as we have is conditioned to the possibility that companies in this phase are prone to the notion that nothing ever happens when/how we expect it to. That is certainly not an excuse for things that could have likely been done differently, but again, we don't find the "issues" atypical for the space, especially with respect to a small company being compromised by an agreement with a large company.

That said, we think they have a viable concept. As we will address, "unattended retail" is an emerging concept that is being driven by a variety of relevant economic factors (climbing commercial rents, tighter labor markets, increasing minimum wages etc.), and in some instances, technological factors like AI, voice recognition, and others. Further, we suspect that some of the design/QC problems they have encountered stem from the fact that getting a vending machine to dispense various iterations of a frozen product flawlessly, consistently and safely is complex. If it weren't, we suspect they would have other competitors in the marketplace, which as far as we can tell they do not. We think there are potentially *thousands* of places where these machines might provide favorable returns.

Lastly, the Company has recently announced a string of positive items that we think point to momentum in the business and if that path continues, could go a long way towards improving valuations for the Company. Recognize, as a result of the manufacturing and delivery delays, they also have some near and intermediate term financing requirements that will be paramount to their continued success and represent clear risks in the deal.

As the chart below illustrates, the stock price has deteriorated significantly since the onslaught of some of the challenges. Obviously, that is not a good thing for legacy shareholders, but if the thesis we have delineated in this report proves reasonably accurate, the compressed valuations could prove opportunistic for those looking at the stock for the first time.

Do Not Distribute

Do Not Distribute

Product/Services Overview

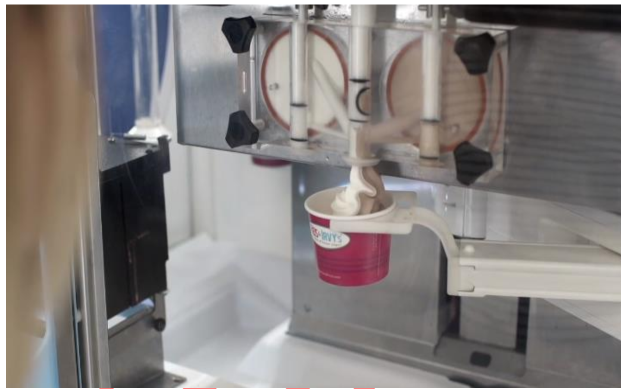
Before we address the Company's current vending product, we think it is germane to address their manufacturing situation since that has been a flashpoint for the Company over the past several quarters. As we alluded to above, the Company's arrangement with Flex has been problematic on a variety of fronts, although it looks as if they may have most of those problems resolved, as we know they have resumed production/delivery of Flex manufactured products into the field. However, our understanding is that at least some of the required additional development fixes of the machines were done by Keil, Wisconsin based Stoelting. Importantly, Stoelting is an industry leader in the design and manufacturing of a variety of commercial grade soft serve machines. For instance, in 1939 Stoelting engineers developed the first commercial soft serve dispenser for Home-Made Ice Cream Company, which today we know as Dairy Queen. Obviously, their industry expertise is broad and deep. Prior to VEND's recruitment of Stoelting to help rectify some of its design problems, we believe that Stoelting was/is a provider of some of the components used in the Flex manufactured machines, so Stoelting involvement in the fixes/upgrades has some history to it. We would add, in early February (2019) VEND announced an agreement with Stoelting wherein the later will provide *"manufacturing and engineering services"* for VEND's robots. That agreement anticipates that Stoelting will begin delivering robots by Q3 (2019). We believe the addition of Stoelting, among other things, should provide adequate capacity for VEND's future delivery requirements, as well as perhaps helping VEND catch up on the delays in deliveries they encountered through 2018. In short, it looks to us like the expanded role of Stoelting has been critically fortuitous on a variety of levels. As an adjunct to that notion, as we understand it, Stoelting had a competing (conveyor based) machine they were marketing prior to this arrangement, which they agreed to stop selling as a result of the deal. We think that is telling and suggests to us that perhaps Stoelting sees opportunity in VEND's approach to the market.

VEND's froyo robot is a patented (4) fully automated self-contained vending machine, and as such, it requires no plumbing or drain. The robot operates on a dedicated 220 volt/30-amp circuit and takes up just 15 square feet of space (roughly 5 feet by 3 feet). Outside of that, there are few other site requirements needed to install and maintain the machines. Aside from their dispensing capabilities, the machines were designed to be easy to maintain as well. For instance, VEND is adding the Hydra Rinse cleaning/sanitizing system to units produced by Stoelting, which they note "*decreases water consumption by 50%, is environmentally friendly, and significantly reduces cleaning time"*.

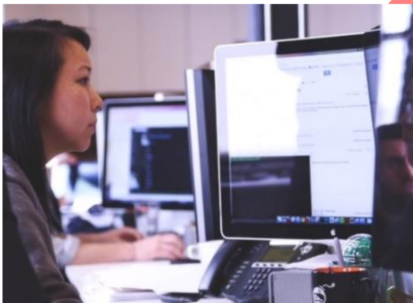
Aside from the technical specifications, VEND's robots are designed to deliver up to 6 flavors as well as 6 different toppings, which can be mixed and matched as the consumer chooses. We would note, the machines in the field currently offer just two flavors, but the Company plans to roll out the six-flavor functionality in early calendar 2020, and the machines in the field are configured to accommodate the retrofit.

As we noted, the Company has an arrangement with Dannon for the supply of Dannon's frozen products, which we believe include not just frozen yogurt, but also ice cream, gelato and sorbet. Franchisees are free to choose whatever products they wish to serve in the machines. The robots provide 2 serving sizes (5 oz. and 7oz.) and it takes the robot approximately 60 seconds to deliver a serving. Each machine can inventory 12 gallons of frozen product, which equates to approximately 200 servings.

In addition to providing frozen treats, the machines are designed to provide an entertaining buying experience. For instance, consumers can watch as the robotic arm retrieves and fills the serving cup and delivers it to the customer. In addition, the television screen provides entertaining animation of the Company's Res & Irvy robots, which attracts consumers to the kiosk and facilitates sales. We think that screen could provide additional marketing opportunities as well.



Each machine is equipped with internet access capabilities, which enable a variety of payment processing options. As such, consumers utilize a simple touch screen interface to make purchases with cash, credit cards, Apple Pay, Google Pay and even Bitcoin. The Company has also provided *"industrial-internet-of-things"* functionality that allows for real-time collection of sales data as well as monitoring the ongoing operation of the machines. For example, VEND employs operators who monitor machine feedback for maintenance issues like temperature changes that might impact food safety as well as inventory levels that may indicate a need to replenish the machine. Company filings also note that the machines are manufactured to meet a handful of relevant industry standards, specifically, their machines are *UL ("Underwriters Laboratories") (approval in process), NSF ("National Sanitation Foundation") recognized (approved in August 2018), and National Automated Merchandising Association ("NAMA") certified (approved in September 2018), which we believe are among the highest standards in the industry"*. As we will reinforce later in this report, "intelligent vending machines" like these developed by VEND, are the "wave of the future" in vending, and we think they will ultimately supplant legacy "static" form factors.



As we alluded to above, the Company has to this point largely focused its sales efforts around a franchise model. Currently, that model provides for franchisees to pay a handful of fees associated with their franchise rights. (We will provide some additional color on these numbers in the Operating Overview below). Here are the basic elements of the franchise commitment. (Recognize this represent today's approximate pricing, as prior deals were done at lower levels and fees may vary by unit commitment as well).

One-time fees paid by franchisees:

Purchase of Robot Vending Machine	$50,000.00
Franchise Fee	$ 5,000.00
Location Fee	$ 2,500.00
Total	**$57,500.00**

Franchisees are typically required to purchase a minimum of two machines, and machines are apportioned to franchisees on a typical territory basis.

Generally, the Company collects a portion of each of these fees up front as a deposit, and collects the balance when machines are delivered. In some cases, depending on applicable state law, the Company is required to escrow those deposits until units are delivered. The Company recognizes revenues from these line items upon delivery.

As with most franchises, the Company also collects a royalty payment based on the gross sales of each unit, which in this case is equal to 12% of sales. The Company has also negotiated a rebate from food and disposables vendors (Dannon for instance) that is based on a small percentage of those sales to franchisees.

Obviously, the attractiveness of the investment is a significant driver in the adoption of any franchise opportunity. To that end, we have provided a few examples of costs and returns a typical Reis & Irvy's franchisee might encounter. As a preface, again, we will address some of the following tables in the Operating Overview, but there are a few items worth pointing out about the comparative tables below.

Table 1.

Group	March	January & February
Top 25	29.6 Transactions Per Day $5.77 Average Transaction	21.6 Transactions Per Day $5.13 Average Transaction
Top 50	23.2 Transactions Per Day $5.25 Average Transaction	18.0 Transactions Per Day $4.93 Average Transaction

Table 1.1

Group	May 19 - June 16	March
Top 25	35.0 Transactions Per Day $5.67 Per Transaction	29.6 Transactions Per Day $5.77 Per Transaction
Top 50	26.6 Transactions Per Day $5.47 Per Transaction	23.2 Transactions Per Day $5.25 Per Transaction

Table 2.

Assumptions:		
Days		365
Assumed Down Days (Holidays, Weekends, maintenance etc.)		10
Operating Days		355
Cups Per Day		18
Average Px. Per Cup	$	4.75
Est. Cost of Consumables per Serving		$0.86
Estimated Local Sales Tax %		7.00%
Estimated Machine Servicing Per Month		$720.00
Location Rent/Override		15%
Generation Next Royalty		12%
Insurance (Annual)	$	600
Permits & Licensing (annual)	$	100
Storage Rental	$	400
Profit/Loss Analysis:		
Revenue	$	30,353
Cost of Sales	$	5,650
Sales Tax	$	2,125
Gross Profit	$	22,578
Machine Service	$	8,640
Locataion Commissions	$	4,553
Royalties to Generation Next	$	3,642
Insurance	$	600
Fees, licenses, & permits	$	100
Storage rent	$	400
Annual Operating Income	$	4,642
Investment Analysis:		
Robot Purchase Cost	$	50,000
Fracnshise Fee to Generation Next	$	5,000
Location Fee	$	2,500
Cleaning Cart	$	333
220 Electrical Upgrade	$	500
Misc. Site Prep.	$	250
Total Investment	$	58,583
Payback Period (In months)		151.43
Payback Period (In years)		12.62
Annual ROI		7.9%
Internal Rate of Return (15 year)		3%

Do Not Distribute

Table 3.

Assumptions:		
Days		365
Assumed Down Days (Holidays, Weekends, maintenance etc.)		10
Operating Days		355
Cups Per Day		23.2
Average Px. Per Cup	$	4.75
Est. Cost of Consumables per Serving		$0.86
Estimated Local Sales Tax %		7.00%
Estimated Machine Servicing Per Month		$720.00
Location Rent/Override		15%
Generation Next Royalty		12%
Insurance (Annual)	$	600
Permits & Licensing (annual)	$	100
Storage Rental	$	400
Profit/Loss Analysis:		
Revenue	$	39,121
Cost of Sales	$	7,282
Sales Tax	$	2,738
Gross Profit	$	29,100
Machine Service	$	8,640
Locataion Commissions	$	5,868
Royalties to Generation Next	$	4,695
Insurance	$	600
Fees, licenses, & permits	$	100
Storage rent	$	400
Annual Operating Income	$	8,797
Investment Analysis:		
Robot Purchase Cost	$	50,000
Fracnshise Fee to Generation Next	$	5,000
Location Fee	$	2,500
Cleaning Cart	$	333
220 Electrical Upgrade	$	500
Misc. Site Prep.	$	250
Total Investment	$	58,583
Payback Period (In months)		79.91
Payback Period (In years)		6.66
Annual ROI		15.0%
Internal Rate of Return (15 year)		15%

Table 4.

Assumptions:		
Days		365
Assumed Down Days (Holidays, Weekends, maintenance etc.)		10
Operating Days		355
Cups Per Day		29.6
Average Px. Per Cup	$	4.75
Est. Cost of Consumables per Serving		$0.86
Estimated Local Sales Tax %		7.00%
Estimated Machine Servicing Per Month		$720.00
Location Rent/Override		15%
Generation Next Royalty		12%
Insurance (Annual)	$	600
Permits & Licensing (annual)	$	100
Storage Rental	$	400
Profit/Loss Analysis:		
Revenue	$	49,913
Cost of Sales	$	9,291
Sales Tax	$	3,494
Gross Profit	$	37,128
Machine Service	$	8,640
Locataion Commissions	$	7,487
Royalties to Generation Next	$	5,990
Insurance	$	600
Fees, licenses, & permits	$	100
Storage rent	$	400
Annual Operating Income	$	13,911
Investment Analysis:		
Robot Purchase Cost	$	50,000
Fracnshise Fee to Generation Next	$	5,000
Location Fee	$	2,500
Cleaning Cart	$	333
220 Electrical Upgrade	$	500
Misc. Site Prep.	$	250
Total Investment	$	58,583
Payback Period (In months)		50.54
Payback Period (In years)		4.21
Annual ROI		23.7%
Internal Rate of Return (15 year)		30%

To segue for a moment, as we mentioned prior, the Company had trouble getting machines manufactured and deployed, but those problems also included issues with the machines that were deployed working properly and consistently. As a result, because many of the deployed machines experienced intermittent downtime, our view is that associated data in terms of sell through (cups sold per day) was not particularly good/reliable data since the machines were not working consistently. We think that is a reasonable assumption. As a result, the data associated with machines *recently deployed* (which as we understand are performing far more consistently) while relatively new and as such limited in sample size, is really the best information we have in terms of ascertaining how the machines are selling through. **Recognize, assumptions regarding the number of cups sold per day by these machines is one of the single most important variables in determining the success of the R&I franchisees, and by extension Generation Next**. This is a classic "razor/razor blade" story, and VEND's success will largely boil down to the sell through of these machines. Succinctly, not only will their franchise royalty be determined by the number of cups per day, but, that same metric will determine the economics of owning these machines. That is, the cups per day metric has a major impact on the franchisee investment decision, thus, the better the economics, the better the prospects of franchisees placing more machines. Obviously, placing more machines is

the ultimately goal for VEND because they get paid from the sale of each machine, as well as for (a portion of) the sale of each cup of product in the field.

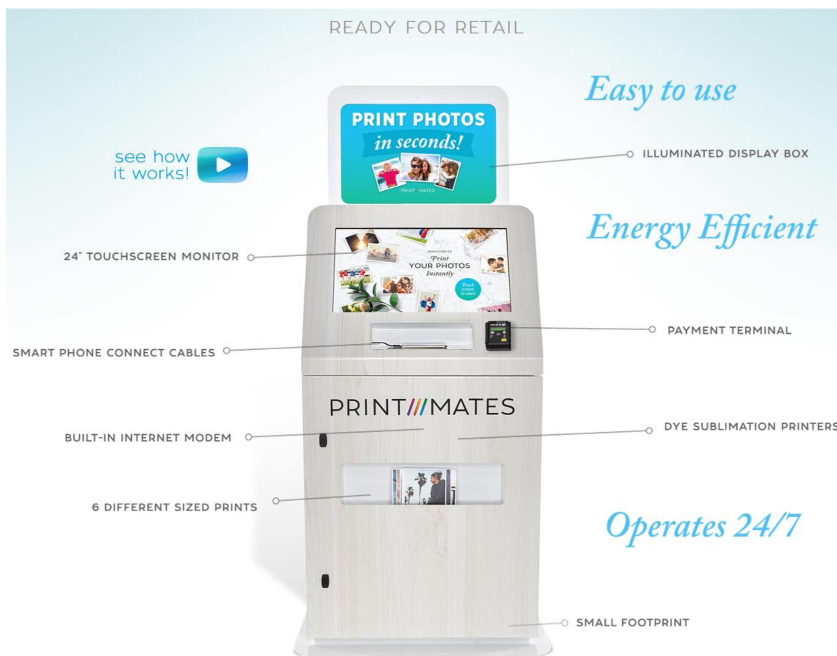
Tables 1. and 1.1 above were excerpted from a Company news release from April 11, 2019, which referenced some of the results that R&I machines were achieving in the field. Again, most of these results involve relatively new machines. Notice, we used some of these results as "cups-per-day" inputs for the other tables (Tables 2 thru 4), which demonstrate the financial performance franchisees might achieves from owning a machine. While we suggested that cups-per-day, are certainly a major driver in the analysis, we submit there are several other moving parts. For instance, we made some assumptions about "down days" which in the tables above we assumed to be a handful of holidays as well as a few days where the machine might need some maintenance or some other factors that might impact a particular day of operations. Recognize, locations may vary as to the number of operating days. For instance, if the machine is in a workplace, there may be no one there on Saturday and Sunday. That noted, we built the above tables with some Company guidance regarding operating costs and we think these are reasonable assessments of "average" costs. We don't think the tables need much color beyond that, but we would point out a few more items below.

First, notice the difference between the results in Table 2 versus Table 4. These represent the differences between the lowest average results from the Company's samples (Table 1) and the highest results from the same. We think the takeaway is that seemingly small differences in cup sales make a big difference in performance. That speaks to the importance of good locations for machine placement, which is why the Company utilizes Compass and other national food service management companies to help with that determination. To that point, notice the "Location Commissions" line item. This is the gross proceeds a landlord would receive from each different table iteration. While the landlord would have some costs associated with this (electricity for example), we think those represent a compelling return for the "rental" of 15 square feet of real estate (regardless of which iteration we are looking at). We *think* that should help franchisees procure higher traffic and potentially higher volume locations. Additionally, Table 1.1 was not available when we first began writing this report. We added it above because we believe it demonstrates further progress in terms of sell through success by deployed robots.

Second, the portion of the franchise costs apportioned to Generation Next is significant. It doesn't take a great deal of complicated math to determine that if they can (hypothetically) place 5,000 franchise machines in service, that sell roughly 30 cups of product each per day, Generation Next would generate annual revenues of nearly $30 million which would include 90%+ margins. Product sell-through is the real "ax" in this story.

Third, this report addresses almost exclusively VEND's expansion of the R&I franchise since that is the current primary focus of the enterprise. However, recognize, VEND has also developed some additional products that could provide the basis for future growth and they appear to be developing some initial traction in these pursuits as well. For instance, on April 9, (2019), VEND announced the acquisition of Print Mates™, a maker of photo printing kiosks which provide consumers a fast and inexpensive way to get their photos *"out of their phone into their hand, while creating a low-to-no maintenance, extremely high margin business opportunity in unattended retail for entrepreneurs and retailers"*. Since the acquisition, VEND has announced some pilot programs with different brick-and-mortar retail brands to test the Print Mates kiosks. We have not modeled the impact of Print Mates on Generation Next, although we are prepared to do that when further data points are available. In addition to Print Mates, we also believe the Company is developing a smaller version of the R&I robot (likely a 2020 launch), as well as working on some additional potential unattended retail vending concepts. Again, we will provide additional assessments of these developments as information unfolds. Below are some graphics of both the Print Mates and the smaller R&I kiosks:

DO Not Distribute



Do Not Dist

Industry Overview

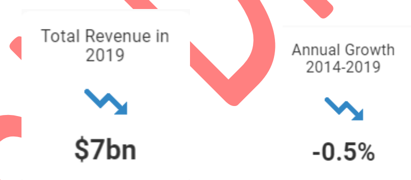
The vending machine business has been around for many years. Historians suggest that the very first vending machine may have been developed in 215 B.C. by a Greek mathematician and inventor by the name of Tesibius. He apparently developed a machine that dispensed Holy Water for a few drachma. That same research from http://business.highbeam.com/industry-reports/equipment/automatic-vending-machines further notes that English pubs featured tobacco/snuff machines early in the 1600's, while in the 1820's an English bookseller by the name of Richard Carlile in an attempt to avoid prosecution, developed a vending machine designed to distribute copies of books that had been banned (Thomas Paine's The Age of Reason as the story goes). Apparently, the machine worked but he ended up in jail regardless.

The above reference continues: *"The first known patent for a vending machine was issued in 1857 to Simeon Denham for a penny postage stamp device. Over the next couple of decades, inventors began showing up at patent offices all over the world with coin-operated machines that sold candy, cigarettes, handkerchiefs, and other small items. In 1884, the first U.S. vending machine patent was issued to W.H. Fruen. However, the American vending machine industry was truly born in 1888, when Thomas Adams of the Adams Gum Company began selling his Tutti-Frutti gum out of machines on the platforms of New York's elevated rail system".* Further, *"by the 1920s, the vending industry had been divided into manufacturers and operators. The Doehler Die Casting Company, for example, developed machines for vending a diverse range of products that included Life Savers, lighter fluid, and sanitary napkins. Another industry revolution took place in 1925, when three new machines were developed, all of which sold cigarettes. Candy machines offering customers a choice of products began to spread in the 1930s. Nathaniel Leverone, the founder of the Canteen Company, was a pioneer in the development of this type of machine".* That last part might sound familiar since as we noted above, Canteen (now a division of food service

giant Compass Group) is one of VEND's national location partners, assisting them with finding optimal locations for their machines. While not necessarily telling, we think it is at least interesting that two of VEND's current partners, Stoelting and Canteen are both pioneers in VEND's relevant market, with Canteen being the developer of one of the first multi-choice vending machines and Stoelting being the developer of the first soft serve machine.

Obviously, given its long history of operations, the vending industry is probably best described as mature, which may beg the question, "how do we expect a small emerging company to develop a high growth offering in a mature business?", but frankly, we have encountered that issue with many past research subjects and we are quite comfortable suggesting that they would certainly not be the first to do that. That said, as with most sizeable, mature and recognized industries there is considerable industry research on the vending business and like most industry research, it varies in terms of estimates of both the current market size as well as the future market size, and that same variance applies to projections regarding domestic and international markets. To translate, we don't know what the best proxy is for determining the size of the vending machine market(s) but here are a few bullet points to help frame the opportunity in that regard. Keep in mind, as the Operating Overview below will address, we are projecting that VEND will install between 5,000 and 6,000 machines over the next 4 years, which is a rounding error in terms of the assumed size (units) of the domestic and international vending markets.

The *National Automated Merchandising Association ("NAMA") estimates that 100 million Americans will use one of seven million vending machines each day.* To edify, according to their website, NAMA is *"the universally recognized and influential advocate of the convenience services industry"*, of which the vending industry is a major part. (We would also note, according to those metrics, on average U.S. consumers access each vending machine about 14.3 times per day. That number is topical to our Operating Overview below). IBISWorld, one of the more recognized industry researcher providers (and one we are partial to) suggests that the U.S. vending industry will generate $7 billion in revenues for 2019, which will reflect a negative (five year) annual growth rate of -.5%. The graphics below are theirs:



The IBISWorld numbers correspond with other similar conclusions regarding machine numbers: http://www.firstresearch.com/Industry-Research/Vending-Machine-Operators.html. Further, on an international basis, Berg Insights estimates there are approximately 16 million vending machines worldwide and notes that Japan is a particularly robust vending market. We suspect that will be a market that VEND will address in the future.

In spite of what looks like a shrinking industry, the above statistics do not reflect some positive attributes of the industry that we think are directly topical to VEND. Specifically, like most industries, vending has experienced some changes around a handful of issues, but perhaps most notably changing consumer preferences and technology. On the consumer preference side, the obvious observation is that it seems as though consumers are becoming more conscious of the food they consume and in general are opting for healthier choices. Given that certainly a considerable portion of the a fore mentioned 7 million vending machines in the U.S. dispense high fructose soft drinks, high fat chips, and candy, it's not hard to understand how vending machine sales might be taking it on the chin. In addition, while on some levels they may be one-and-the-same, we believe the preferences for better nutritional choices are also augmented by preferences for fresher choices. On the face, that second preference has provided a layer of complexity to the business, because clearly the processes and requirements to deliver fresh alternatives through vending platforms is far more complex than delivering ready-to-consume food products with long shelf lives and minimal required quality control (temperature for instance). In addition, beyond food choices, other changing consumer preferences are also impacting the industry. For instance, payment processing options are influencing purchasing decisions. Whereas the legacy vending machine platforms

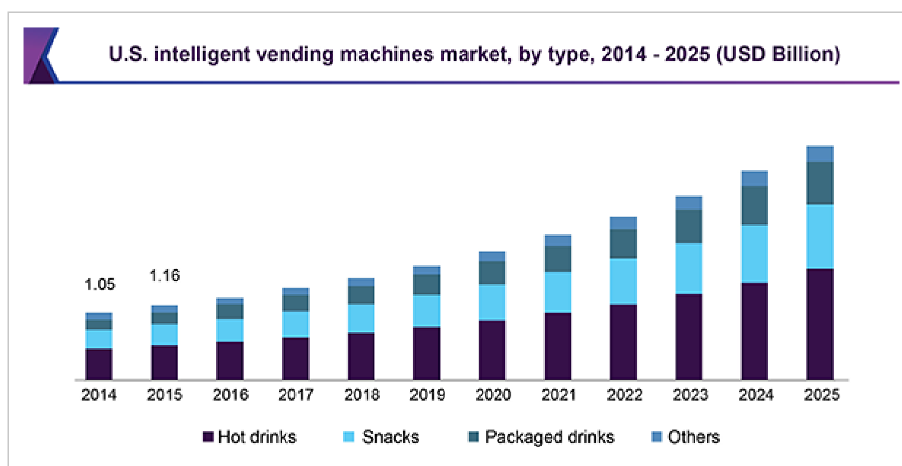
Do Not Distribute

required/require cash payments (and even limited forms of that), cash is rapidly becoming a decreasingly utilized form of payment, supplanted by a multitude of other largely technology based options. Although there is likely no definitive proof of our claim, we think payment limitations have likely contributed to the shrinking of legacy vending platforms, and perhaps even to a greater extent than food choice. While we submit, millennials may in fact be more food conscious than their predecessors, we think their reluctance to buy a candy bar from a vending machine is probably driven more by the fact that they don't carry cash than it is that they don't like Snickers bars…but that's just us.

Given the above, again like most other industries, the vending industry has responded to some of the challenges addressed above by including technology solutions to their dispensing platforms. These technology solutions include things like internet/cloud connectivity that enable various electronic payment forms, but also allow for "Internet-of-Things" ("IoT") applications like remote monitoring of machine function, inventory, sales figures and others. Of course, they also include new functionality that allows for the dispensing of more fresh alternatives, which again includes added complexity to the machines capable of executing those new requirements. This transition towards technology in the vending business is not subtle and in fact has its own label often referred to as "intelligent vending".

As we illustrated, whereas data suggest that the overall vending industry has experienced decline over the past few years, growth in intelligent vending platforms has been quite robust, and is expected to continue to mark impressive growth in the coming years. According to recent research from Global Industry Analysts, Inc. ("GIA") (https://www.strategyr.com/MarketResearch/market-report-infographic-vending-machines-forecasts-global-industry-analysts-inc.asp) *"The global installed base of Vending machines is expected to reach 31.6 million units by 2025, driven by favorable trends in food consumption, growth in food retailing infrastructure, a transformation in vending payment options* ***and growing penetration of intelligent, smart and connected vending machines.*** Analysis from Grandview Research pegs intelligent vending growth as follows:

Distribute



https://www.grandviewresearch.com/industry-analysis/intelligent-vending-machines-industry

According to PYMNTS.com, (https://www.pymnts.com/unattended-retail/2019/worldnet-kiosk-vending/) "*the intelligent vending machine market, measured globally, could be worth as much as $15 billion by 2025*". Correspondingly, ResearchAndMarkets.com suggests that unattended cashless retail is *"a thriving segment of the economy that is forecasted to grow to $34 billion by 2023"*. Unlike legacy vending platforms, intelligent vending is a rapidly growing industry.

To reinforce the point, Global Industry Analysts, Inc. continues, *"In the current on-demand economy where customer tolerance for "waiting lines" are close to zero, it is mission critical for businesses to upgrade to 24/7 self-service solutions….Poised to gain in this regard are smart vending machines that maximize the upsell potential with zero human intervention".*

GIA provides the following illustration regarding what they view as primary intelligent vending attributes. Notice, most of these are characteristics found in VEND's technology.

© Global Industry Analysts, Inc., USA. All Rights Reserved.

Just to summarize the above a bit, it is not difficult to understand how the legacy vending industry may be experiencing some challenges, considering changing demographics and changing technologies that fly in the face of those platforms/offering. On the other hand, it also not difficult to see how those deploying vending solutions that address these challenges should capture increasingly larger portions of a growing market. (To add a salient point, the one attribute above that seemingly may not apply to VEND is the "healthy food" category. However, it is important to note that the Company also provides access to a fruit based product that complies with nutritional guidelines for schools. We think this is a highly topical attribute that could provide entre into thousands of potential locations (schools) that would not be available without this option. In our view, this attribute could prove quite topical going forward).

In addition to the above, we think there are some other attributes of the vending industry that speak to advantages that should bode well for players like VEND. As we noted above, vending solutions are part of the "unattended retail" sector. Unattended retail is a growing segment of the retail space and is even beginning to see deployments outside of the traditional food and beverage offerings of the original vending machines. The push towards unattended retail is a function of a handful of variables that include consumer preferences such as fast and convenient service, 24/7 availability, multiple payment options and a variety of others. However, from a business standpoint, unattended retail is also getting a boost from other sources. For instance, one of the attractive attributes of unattended retail is its lack of human inputs. That is, it requires no employees, which avoids a handful of "costs" not the least of which are wages and associated taxes. Whether it is VEND and its ROI pitch to potential franchisees, or really any other vending related financial analysis, the cost of labor in *attended* retail enterprises relative to *unattended* alternatives in significant. Succinctly, each push towards higher minimum wage laws in various jurisdictions around the country effectively increases the relative ROI of unattended retail alternatives. In our view, minimum wage legislation, which appears to be gathering further momentum, is a boon to the investment rationale for unattended retail.

Operating Overview

Given the above backdrops, there are a few high-level overriding themes to VEND's operating model. In case it is not clear, the development/manufacturing delays created a cascade of complications that significantly hampered the Company's progress and created a handful of problems on their own. For instance, we don't think the business plan was ever meant to be driven by anticipated profits generated from the sale of kiosks. Specifically, the "sale" of a kiosk involves three pieces of revenue to VEND; the sale of the robot, a franchise fee and a location fee. In that context, we estimate that VEND's current cost of manufacturing and delivering a kiosk is somewhere around $40,000, which includes VEND's cost of robots (currently about $32,000), commissions paid for the franchise sale as well as for site location and delivery. Given those parameters, while today we believe the blended gross margin on these combined line items is approaching the 30% range, we also think some of the original franchise sales were closer to just 10% to 15%. Doing some quick math, even at today's improved margins, a single sale *might* generate $18,000 of non-recurring profit, which means that the Company would need to deliver around 200 machines per quarter to achieve cash flow breakeven. Clearly, the long-term success of this model is largely built on the (recurring) sale of frozen product.

To reiterate, even without the manufacturing delays, the plan required capital because while machines were to be assembled and finished by Flex, the supply chain included a number of vendors along the way (Stoelting for example), which generally meant paying for parts/inventories ahead of assembly and delivery (collection). In addition, while franchisees were required to put down deposits (in part to bridge the gap between payables and receivables), in many instances, those deposits were restricted by franchise laws in certain states that prohibited the Company from using them to procure inventories. However, as a means of managing the working capital requirements (as well as launching the rollout), during fiscal 2018 (ended June 30, 2018) the Company raised nearly $17 million of equity capital. Over that same period, we believe they spent approximately $8 million of that capital on R&D and marketing, obviously preparing for the launch. The remaining $8+ million provided working capital to build inventory as well as finance the operations to positive cash flow. To quickly put this issue into perspective, if we assume an "all-in" cost to deliver a machine to be $40,000, then $8 million would provide the capital to build and deliver 200 machines. That does not address the overhead requirements to support the business. Obviously, the capital required to build the next 200 machines would need to come from the sale and collection of the first 200. In short, because of the manufacturing delays, the cash flow model broke down, since they could not monetize what they could not deliver. As a result, generally speaking, much of the $8 million needed to build machines was used to finance overhead to keep the business intact (although they worked to reduce the relative burn) through 2H-calendar 2018. Moreover, we are assuming much of the R&D spend during the period was dedicated to fixing design and manufacturing problems, while much of the marketing resources were spent preparing for a launch that effectively couldn't happen. In a nutshell, the manufacturing delays created the perfect storm.

The Company has spent the better part of the past year trying to "right the ship" from the impact of that storm. Frankly, all things considered it appears they have done an admirable job doing so, and that view is based on a handful of milestones including new manufacturing arrangements and what looks like a renewed ability to deliver robots that perform as advertised, the acceleration of deliveries as well as new orders and a host of other positive data points. However, from a capital standpoint, we think they are back where they started in 2H/F17-1H/F18, in terms of requiring capital to (re)launch the R&I brand. Unfortunately, that probably includes a requirement for a similar $15-$20 million of fresh capital. We will address that further in this report, but we would note, they have already raised some portion of that required amount, but that remains a very topical element to the story.

Setting aside the capital requirements, here are some of the key operating metrics as we see them. Just to reiterate, we have largely focused our operating model around the Company's exploitation of the R&I brand until such time as we get more clarity on potential contributions from Print Mates. That is not meant to minimize the asset, we just don't know enough about it to analyze it at this point. (We will likely be revisiting it before too long).

As noted, we believe the Company is current selling a franchise package for something around $57,500 per machine. That cost includes $5,000 for franchise fees and $2,500 for location fees, with the balance ($50,000) representing the robot sale. We believe the Company generally seeks to sell franchisees a minimum of three machines. The Company pairs internal location acquisition specialists with external partners managing a national footprint, (Canteen for example) to identify what they believe to be high foot traffic, high value locations, although franchisees are free to find their own locations as well (which we believe saves them some fees). As with most franchise arrangements, the Company uses a territory approach to protect franchisees from competing for the same customers. We believe VEND's cost of good for robots is currently approximately $32,000, and they anticipate they may be able to reduce that unit cost with some scale. Given those numbers, once normalized we think franchise sales will provide a revenue contribution of about $57,500 per unit (up considerably from what we think was closer to $45,000 per unit during the initial/original rollout) and we think associated blended margins are about 30% after robot costs, franchise and placement commissions and delivery fees.

Franchisees are required to deposit a portion of each of these three line items upon signing of the agreement. These amounts vary from state to state typically in accordance with applicable franchisee laws, but we believe the "blended" required down payments to be about 40% for franchise and location fees and 20% for robot sales. Any remaining balances beyond those required up front, are due upon delivery of the machines. Again, while the Company generally collects some portion of the fees and costs up-front, some states require that they escrow those funds until delivery is made. Of course, these items ultimately encompass the working capital/collections issue we alluded to above. While there are several moving parts like some we identified here, there are others we really don't know specifically. For instance, we don't know the payments terms from component providers (which we suspect may have gotten more onerous after the rollout delay). That said, for our cash flow analysis we have applied a blended upfront collection (taking onto account the variables we noted) and we have applied a typical accounts receivable "days outstanding" approach to the balance. Currently, we are modeling the time from order to delivery ("DSO's" in or analogy) at about 120 days. Our sense is that this will improve as Stoelting ramps production and the Company is able to fill the backlog that backed up as a result of the manufacturing delays. (Actually, some recent narrative from the Company suggests a shorter DSO period than we are assuming).

For the near term, as we also discussed, beyond franchise fees and machine sales the other major revenue component is the franchise fees from unit sales of each machine. This number amounts to 12% of gross sales from each (domestic) machine. We would again refer to the three tables provided/referenced above. Our model assumes similar variables to the tables (in terms of sale price, costs per unit etc.) but we have assumed sales per day of 20 units for machines delivered in prior quarters and 50% of that number for units delivered in the current quarter (in order to smooth differences in delivery timing throughout the quarter, as well as lower sales in the initial start-up phase). Notice the 20 cups per day represents a discount from the initial results the Company has collected to this point (Tables 1 & 1.1.) We have also assumed that the Company will fill its outstanding "commitments" (reported as 2666 units at March 31, 2019) through September of 2021. That assumption will require that they install an average of approximately 275 (net) units per quarter between now and then. We are also modeling them to moderately exceed that pace over approximately the next two-three years and then declining considerably hereafter. Clearly, that is a major data point we will be monitoring closely.

Frankly, we don't think our model will be accurate at 20 cups per day. As Table 2. reflects, we don't view the return on investment metrics of 7.9% from 18 cups per day as overly compelling. Put another way, we tend to think that if ongoing data from larger samples of kiosks delineate 18 cup averages and corresponding 7.9% ROI's the Company may have trouble selling the 300+ units per quarter we are assuming. While 20 cups is a better number than 18, we think it may represent a sort of minimum ROI required to sell machines. This is also another major data point we will be watching. (We would add, our model also reflects fewer operating days per month than the above tables, so it is a bit more "conservative" in that regard). As a point of reference, we estimate the franchise ROI to be between 10% and 11% at 20 servings per day. To further illustrate the sensitivity of the data point, we think each addition assumed serving per day (for instance 21 versus 20) impacts our DCF price target analysis by about $.05 per share. So then assuming 30 cups per day versus 20 would raise our price target from

the current $1.10 per share to something closer to $1.60 per share. Obviously lesser assumptions would lead to equivalently lower price targets.

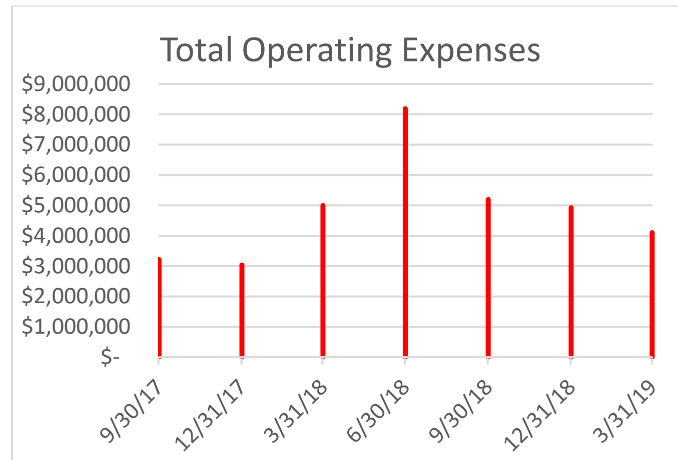
There are two additional angles to the revenue line items that require some color.

First, from the Company's most recent 10-Q (March 31, 2019): "*In January 2019, the Company announced the launch of 19 Degrees Corporate Service, LLC as a corporate operated Robot Investment Fund ("the Fund"). This advantages kiosk owners through the switch from active to passive income; more even distribution of revenue; faster installation of kiosks; a "no hassle" maintenance program provided by CSA Server Solutions; a nationwide on-site flavor promotion plan managed by Dannon, access to a newly designed back-office portal that will allow members of the fund to remotely access each kiosk's sales performance in "real time" as well as a plethora of software features used to guide the fund's performance".* To edify, 19 Degrees was established as a way for investors to invest in the R&I franchise concept without owning specific machines in specific locations. In short, hypothetically, if the fund includes 100 machines, each investor owns a pro-rata share of each of those machines. Further, they avoid the work involved in managing their own machines. In effect, it allows the investors to participate in the R&I concept, but with a passive (geographic) diversification twist. We think it's innovative in that not only does it provide investors with some benefits they don't get being a more traditional franchisee, but it also provides the Company another avenue to sell more machines and place them in service. In addition, ultimately, we think VEND is interested in owing some number of their own locations. That approach requires capital they currently do not have, but at least conceptually, we believe that is something they would prefer to do. Obviously that sort of approach would change our model considerably. In that regard, we think 19 Degree's may be the precursor to that strategy. That is, at some point they could use 19-Degrees to purchase and/or hold Company owned machines eventually becoming the largest participant in the fund, and perhaps even ultimately consolidate the entity. That is just our speculation regarding the endgame of 19 Degrees. That may or may not happen, but the point is, we feel comfortable suggesting that Company owned kiosks are likely in the cards if capital permits, although we have not modeled that scenario given the current capital constraints. We believe 19 Degrees currently owns approximately 20 machines.

Second, we also believe the Company has its sight firmly set on international markets. We believe there are nearly 50 machines installed in Canada and Australia collectively, with agreements for considerably more. As we understand it, they are also in the process of adding machines in Israel and expect to be shipping to Mexico shortly as well. Again, we think the Company views the opportunity as a major growth driver in coming quarters/years. Recognize, the Company's participation in international markets is currently different than the current domestic franchise model. In short, the Company's current international efforts essentially involve the sale of master franchises for particular countries/regions. Those master franchisors agree to minimum purchases and in exchange to essentially act as the franchisor (much like VEND domestically) and as such are responsible for all aspects of the business in that particular territory/jurisdiction. The Company views it as a sort of "wholesale" approach to proliferating the brand around the globe. The downside of the approach is that instead of the 12% royalty, they collect a $100 monthly "software" fee per machine. That is likely considerably less than the typical 12% fee generated from most domestic machines. However, again, outside of selling the master franchisor machines, VEND is not required to provide considerable resources to the ongoing operations. Further, in jurisdictions where the typical vendors are still utilized (Dannon in Canada for instance) VEND continues to collect a consumables rebates associated with kiosk sales. Our sense is that the Company may not necessarily utilize this approach in all places around the globe. For instance, as we alluded to above, research suggests that Japan is a particularly large vending machine market. It is conceivable to us that the Company might keep the master franchise for an area like that and (hypothetically) set up a Japanese subsidiary to franchise Japan. On the other hand, we could also envision situations where, as the brand gathers strength, perhaps master franchises could involve significant up-front fees or other revenue streams that currently do not exist under the legacy international agreements. To summarize, we think international opportunities are a considerable part of the plan here, but we also think future agreement may be different than they are today.

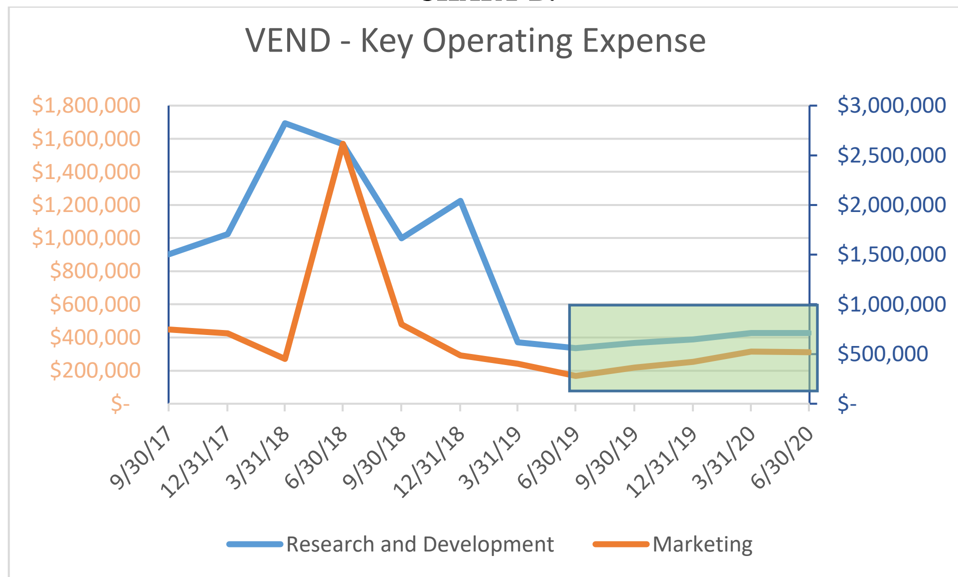
Moving to operating expenses, in line with the franchise launch from 2H17 thru 1H18 operating expenses ramped accordingly.

CHART A.



More specifically, while not entirely, much of the acceleration of operating expenses over the period were related to marked expansion in Research and Development as well as Marketing. Here again, we would view those increases as consistent with the build and launch of the R&I franchise business, however, we also think that certainly some of the R&D expansion was related to attempts to fix design problems that contributed to manufacturing delays as well as machine failures in the field.

CHART B.



At any rate, as both charts A. & B. reflect, operating expense ramped into the anticipated launch, but "normalized" thereafter. Moreover, we anticipate lower levels of operating expenses into the foreseeable future (relative to the past several quarters, March 31, 2019 notwithstanding). Granted, we suspect some of this compression was/is

related to capital constraints, so assuming they can solve some of those issues, we could see higher levels of these numbers going forward than we currently anticipate. That may be especially true if they continue to gain traction in the Print Mates business, or even in R&I if that accelerates more than we anticipate. However, absent something unanticipated, we expect Operating Expense to be in the range of $3.5 million to $4 million per quarter. (Our estimates are represented by the light blue box above).

Before we leave the issue, there are a few other operating lines worth addressing.

The Company has experienced considerable "Professional Fees". This line has averaged just under $450,000 per quarter over the trailing 12 months. As we understand it, there were a handful of issues that led to these fees, some of which were related to the issues at Flex and the associated fallout. While we expect them to continue to incur professional fees (audits, legal matters etc.), we suspect this line item should decrease in coming quarters relative to prior periods.

Lastly, they have realized considerable charges for stock based compensation. Again, as we understand it, most of those charges are related to employee options, many of which are predicated on particular sales levels and other such metrics. Our model projects that they will reach these sales goals and as such we anticipate further sizeable non-cash stock compensation charges to continue into the foreseeable future.

To reiterate, we expect the model to be quite fluid as the Company accelerates into full commercialization, which includes the rollout of Print Mates. While we think the model reflects reasonable assumptions regarding operating expenses, we could see material differences since we have no true (post commercialization) operating numbers to build projections around or otherwise back test against. We will make appropriate changes to the model as relevant data points become available.

Do Not Di

Risks and Caveats

As discussed, the Flex manufacturing problems resulted in a cascade of problems that likely would have been avoided had things rolled out as planned. Some of those issues remain problematic today (we will discuss those) but perhaps the most of those is the substantial capital that was raised to execute the commercialization that in part instead ended up supporting general working capital burn as they were trying to get things back on track. To be clear, as we noted above, much of that capital was spent preparing for a launch that didn't happen and on R&D *redeveloping* the technology, but in any event, that capital was spent and not available once they got to the point of being able to relaunch, which has essentially turned out to be the past few months. Succinctly, we believe the Company has demonstrated marked momentum since getting the robot design right, but their marked capital requirements remain topical. That is especially true given the cash flow lag between the time they need to pay for at least portions of machine manufacturing before they collect payments for sales (upon delivery). They have a working capital problem and, in spite of the favorable momentum, it is the "elephant in the room". In our view, their ability to access sufficient capital, which our model estimates to be between $15 million and $20 million through Q1 Calendar 2020, is the single most topical risk in the story. What is particularly interesting about that is the Company, even in its filings, seems quite confident in their ability to access that capital, which makes us think that maybe they have some insights in that regard that we clearly do not have. Granted, with orders in hand, and a demonstrated ability to deliver functional robots, they likely have more financing opportunities than they would (or had) without those attributes. Nonetheless, *this is an acute risk in the story* with potentially catastrophic outcomes if they are unable to raise necessary capital. On the flip-side of that issue, we would view clarity on the financing front as perhaps a markedly favorable milestone for the Company.

As the Company's history demonstrates, while "intelligent vending machines" are clearly the future of the industry, they come with a fair amount of complexities, which ultimately translates to more things that can go wrong. While we believe *the Company* believes they have largely solved the technical issues, more hours in the field may challenge that assessment. Here again, we would view another technical setback as considerably detrimental to the Company.

The delays in getting robots to franchisees have created a handful of problems, which include some ill-will amongst some franchisees and ultimately some rescissions/refunds. We have modeled some provisions for that in line with Company filing guidance on the issue, but we don't know the full extent of that. We also do not know the extend if any of the negative narrative that might exist in the franchise world or what impact that might have in terms of them signing franchises going forward.

The Company's filings indicate that it has been dealing with some ongoing issues regarding the sale of some VEND shares by Company employees. Here is the filing narrative regarding that issue: *"During fiscal year 2018, the Company began a voluntary internal review into payments made with respect to primary stock sales. The Company has engaged outside counsel, has ceased selling the stocks, and will not make further payments with regard to stock sales, will take remedial measures (including oversight and education), and, as deemed appropriate, will take steps to recapture the value of those payments previously made. The Audit Committee is overseeing the internal review and remediation efforts*". This is a potentially negative unknown in the story that again, we do not know the extent of. Obviously, the Company is currently engaged in attempting to rectify this issue.

As with many small companies, VEND is operated by a small handful of people with varying roles and the loss of any one of them could have a measurably negative impact on the enterprise.

As we noted above, the Company has a number of relationships with larger companies to execute various aspects of the business. Some of those relationships are likely more important than others, but their inability to maintain these relationships could impair the ongoing operations of the business. Further, the Company may have little control over decisions that impact these ongoing arrangements. We think this is particularly true of their new manufacturing relationship with Stoelting, which we view as potentially critical to the success of the Company.

The vending industry has a handful of large players that compete in various portions of the industry. In some cases, the Company may compete directly with some of these players in terms of important elements of the business, for instance site choices, but certainly others as well. In those cases, we would submit the VEND will clearly encounter considerable disadvantages vis-à-vis these larger players.

As an extension of the prior paragraph, while unattended platforms are changing some aspects of retail, one rule probably remains the same: location, location, location. In case we did not make it clear above, the success of the R&I brand depends on the sell through of frozen products. Specifically, while the Company does realize margin from machine sales, this is a razor/razor blade story. That means that VEND's success will ultimately be driven by the sell through of frozen products by individual machines in the field. As our tables above illustrate, the machines need to sell a number of cups per day to generate returns necessary to attract franchisees. We suspect that number is likely in the 20-25 cups per day realm. The Company has already demonstrated an ability to place machines that generate those types of numbers. However, those are relatively new placements so we really don't know what the longer term performance of these machines might be. We suspect the answer to that will depend on location. We have no doubt they will have machines that will likely far exceed that 25 cup threshold, the question is, can they identify and place machines in hundreds, and ultimately thousands of locations that have access to the foot traffic necessary to consistently generate those types of sales? In the end, the answer to that question may well involve competitive (placement) elements with respect to other vending alternatives.

Do Not Distribute

Historically, VEND shares have experienced marked volatility. Recognize, our approach to valuation is purely fundamental, so our research is void of technical analysis of any kind. We do not try to ascertain who owns the stock or where they own it, and when/if those shares my find their way to the market. As such, we don't typically pay measurable attention to short positions or other similar data points. Further, as a microcap, VEND is likely to spend measurable amounts of time being generally underfollowed and largely illiquid. We have no insights as to when that posture might change.

In addition to requiring marked amounts of additional capital that will likely require the issuance of more equity, the Company also has a number of equity derivatives outstanding that could result in further dilution. As a result of these items, and as our model indicates, we anticipate far larger share counts (dilution) as we move forward. Inasmuch as we have modeled what we think are reasonable estimates in that regard, it is certainly conceivable that they could have to issue even great numbers of shares than we are projecting.

These are just some of the more apparent risks we see in VEND at this time. There may be others we have missed or yet others that are not foreseeable at this time or may evolve as we move forward.

Do Not Distribute

Valuation, Summary and Conclusion

*As a personal preface to our conclusion, I was introduced to VEND by the late Marc Robins. Marc was an enduring and well-respected member of the microcap community, and more importantly, a good friend. Marc was working with/helping Generation Next with a handful of items when he passed. As I recall, the last conversation I had with him included a discussion about the Company as he had encouraged me to look into the story because he believed they were at the front end of a marked inflection in the business if they could close a few loops. Like all of us who have spent any measurable time in the microcap space (especially when that time is measured in decades), Marc had his share of stories that didn't work out as planned, however, he also identified more than his share of companies that became extraordinary investments. His recently completed book **"Confessions of A Ten-Bagger Junkie"** is a compilation of some of those discoveries. As I have said many times to many people, I considered Marc one of my mentors, and as a result, when he told me I should look at something, I generally complied, because I tend to embrace the notion that if you want to be successful at something, following around others with demonstrated success in the discipline to "see what they eat" is a good place to start.*

The above noted, in case it was not clear from the above Risks and Caveats section of this report, VEND is in a precarious spot, which stems from the manufacturing delays of last year. Investors should be keenly aware of the risks associated with their inability to raise adequate amounts of capital. Their ability to raise capital and/or the degree to which they can accomplish that will be a paramount piece of their success or failure. Again, people need to be keenly apprised of that risk. To that end, our model reflects substantial addition dilution and our assessments in that regard could prove markedly inaccurate.

With the risks in mind, the other side of that coin is that with the manufacturing issues largely addressed, the Company is demonstrating marked traction in placing machines in service, as well as in adding franchisees that should provide a robust pipeline of future installs as well. While again, the pace of installs could be negatively impacted by the timing and magnitude of theirs access to capital required to build deliverables, we think their recent (and presumably continued) momentum should provided a much better basis for solving the capital problem. We don't think it is a stretch to suggests that raising capital should be less difficult when the business is demonstrating success versus not.

As we also addressed, the Company should begin to experience better margins on robot sales as they move forward, largely because they have established higher price points on new sales. Some of that will take some time to work its way through the system since the manufacturing delays mean that they are just now delivering machines that were sold at lower price points. Obviously as they deliver higher priced machines margins should expand accordingly. Further, the Company expects to experience some manufacturing scale, which should also have a positive impact on future margins as unit production costs decline.

While expanding margins on robot sales is a positive element, keep in mind, this is a "razor-razor blade" story. That is, the end game is to get as many machines in service in as many high traffic locations as possible and collect ongoing (nearly pure margin) royalties. To that point, the average cups sold per day (per machine) will be a critical data point going forward. As we addressed in some of the tables above, the initial sell through data over the past few months has been impressive and in fact beyond what we are modeling. We are not ready to suggests that those initial results constitute a definitive trend, but we are certainly encouraged by the initial results. Just to reiterate the math, hypothetically, if VEND were to place 5,000 machines selling 25 cups per day (assuming an average of 5.8 selling days per week), the system would sell roughly 9.3 million cups per quarter. At an average price of $5 per cup (here again, initial results are reflecting better), the system would generate $46.6 million in sales per quarter, which would result in quarterly franchise fees of $5.6 million per quarter of what is largely gross profit to VEND.

On the international front, the "razor blade" math is not quite as compelling since to this point, they have essentially granted *franchisor* rights to international partners. In that case, VEND really has no obligations or responsibilities other than delivering contracted machines. That said, again hypothetically, 5,000 international machines would generate $6 million of annual gross margin with very little administrative input. By the way, we believe there are likely considerably more than 10,000 potential high traffic domestic and international locations. Additionally, while the granting of the international franchise rights has historically included minimum delivery numbers that we think support our notion regarding potential locations, we also think that future international deals could perhaps include cash payments. We have not modeled that iteration.

As we suggested, we tend to believe the Company's end game is to own (as opposed to franchising) as many locations as possible. Again, that iteration will require capital, but in that instance, the model would obviously change considerably (for the better if cup sell through is robust). We have not modeled this scenario either at this point.

The Company appears to be making progress with its Print Mate kiosks. Here again, we have not modeled any contribution from Print Mates, in part because of our views of the capital constraints (although cost of goods is a small fraction of those for the R&I kiosks). However, as they have noted in recent releases, they have been able to establish a handful of pilot programs with a number of high profile retail brands, so we will likely have to address this piece in future model updates. Moreover, it looks like that may be something we will need to address a bit sooner than we anticipated.

The Company recently announced results from Fiscal 2019 (ended June 30, 2019) and those results were in line with our model. Since we did not publish the model prior, readers will have to take our word on that. Those numbers, (although not yet filed under 10K), reflected sales of $17.1 million versus less than $1 million in fiscal 2018. That release also noted that they ended the year with 407 units in the field, of which 74 were delivered in the month of June alone. Clearly, the Company is transitioning into commercialization, and that process appears robust. The Company also guided to revenues of $40 million for fiscal 2020, provided they can attract the capital to support that growth. We think that rationale is defensible in the context of our modeling approach.

Lastly, from the macro view, we believe unattended retail is likely to become more prevalent rather than less, and we think intelligent vending machines will be a measurable part of that growth. In our view, unattended retail will be driven by a handful of economic and social variables/changes that will augment its success. However, we also

Do Not Distribute

think winning in the space will take more than just showing up. It will also require technology platforms and functions capable of not only replacing human inputs but also providing other critical attributes like real time reporting and monitoring, multiple payment options and others. Like many industries, the successful players in the space will need to adopt and implement technologies and/or platforms that are accessible and appealing to consumers both in terms of function and content. We think Generation Next has developed a kiosk that does those things, with an eye towards adding others as well. As we have addressed, the Company has some major obstacles it still needs to address, but its persistence in terms of emerging from the manufacturing delays has been impressive, and we think with some financing help, they could continue to extend what looks like the front end of an operating/financial inflection. We also think there are elements to the story that could provide additional valuation legs beyond our initial assumptions here.

We re initiating coverage of Generation Next with an allocation of 3 and a 12-24 month price target of $1.10. As some will recognize, this is a tick below our typical initiating allocation of 4, reflecting what we view as relatively acute risks associated with the financing requirements we have discussed, (which by the way we believe have negatively impacted the stock price as of late). We will revisit our allocations (and associated discount rates) if/when financing is attained and articulated to the markets as we would view a financing as *highly positive* (assuming reasonably appropriate pricing).

DO Not Distribute

Projected Operating Model

Generation Next Franchise Brands Inc.										
Projected Operating Model										
Prepared By: Trickle Research										
	(Actual)	(Actual)	(Actual)	(Estimate)	(Estimate)	(Estimate)	(Estimate)	(Estimate)	(Estimate)	(Estimate)
	9/30/2018	12/31/2018	3/31/19	6/30/19	Fiscal 2019	9/30/19	12/31/19	3/31/20	6/30/20	Fiscal 2020
Revenues:										
Vending machine sales, net		$ 4,407,121	$ 1,996,696	$ 7,600,106	$ 14,003,923	$ 7,968,863	$ 7,600,000	$ 8,000,000	$ 9,200,250	$ 32,769,113
Franchise fees		$ 10,927	$ 16,496	$ 287,655	$ 315,078	$ 1,062,500	$ 1,000,000	$ 1,000,000	$ 1,057,500	$ 4,120,000
Company owned machines		$ 13,354	$ 1,988	$ -	$ 15,342	$ -	$ -	$ -	$ -	$ -
Royalties		$ 50,500	$ 88,940	$ 218,499	$ 357,939	$ 378,151	$ 540,039	$ 695,217	$ 856,772	$ 2,470,179
Agency sales (net)			$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Other		$ 32,559	$ 3,001	$ 9,104	$ 44,664	$ 15,756	$ 22,502	$ 28,967	$ 35,699	$ 102,924
Total revenues	**$ 1,757,993**	**$ 4,514,461**	**$ 2,107,121**	**$ 8,115,365**	**$ 16,494,940**	**$ 9,425,270**	**$ 9,162,541**	**$ 9,724,184**	**$ 11,150,221**	**$ 39,462,215**
Cost of revenues	$ 1,661,623	$ 4,211,809	$ 3,651,827	$ 7,825,000	$ 17,350,259	$ 8,314,063	$ 7,825,000	$ 7,825,000	$ 8,207,813	$ 32,171,875
Gross margin	**$ 96,370**	**$ 302,652**	$ (1,544,706)	$ 290,365	$ (855,319)	$ 1,111,207	$ 1,337,541	$ 1,899,184	$ 2,942,408	$ 7,290,340
Operating expenses:					$ -					$ -
Personnel	$ 1,335,407	$ 1,003,717	$ 1,285,157	$ 1,346,002	$ 4,970,283	$ 1,351,533	$ 1,346,000	$ 1,352,000	$ 1,370,004	$ 5,419,537
Marketing	$ 798,045	$ 487,830	$ 401,214	$ 579,950	$ 2,267,039	$ 364,002	$ 369,533	$ 364,000	$ 370,000	$ 1,467,535
Professional fees	$ 426,106	$ 700,040	$ 370,258	$ 600,000	$ 2,096,404	$ 400,000	$ 400,000	$ 400,000	$ 300,000	$ 1,500,000
Insurance	$ 81,945	$ 88,283	$ 158,136	$ 88,900	$ 417,264	$ 93,463	$ 95,338	$ 97,213	$ 101,775	$ 387,788
Rent	$ 54,193	$ 70,681	$ 101,284	$ 101,284	$ 327,442	$ 101,284	$ 101,284	$ 101,284	$ 101,284	$ 405,136
Depreciation and amortization	$ 111,399	$ 110,701	$ 102,467	$ 102,467	$ 427,034	$ 110,000	$ 110,000	$ 110,000	$ 110,000	$ 440,000
Stock compensation	$ 762,534	$ 711,195	$ 685,875	$ 600,000	$ 2,759,604	$ 500,000	$ 400,000	$ 200,000	$ 100,000	$ 1,200,000
Research and Development	$ 999,005	$ 1,224,701	$ 371,799	$ 335,536	$ 2,931,041	$ 365,577	$ 372,126	$ 370,813	$ 373,621	$ 1,482,137
Provision for Legal Settlement	$ 83,474	$ 49,218	$ 92,448	$ 100,000	$ 325,140	$ 75,000	$ 75,000	$ 50,000	$ 50,000	$ 250,000
Other	$ 545,239	$ 477,902	$ 537,798	$ 50,000	$ 1,610,939	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 200,000
Total operating expenses	**$ 5,197,347**	**$ 4,924,268**	**$ 4,106,436**	**$ 3,904,139**	**$ 18,132,190**	**$ 3,410,858**	**$ 3,319,281**	**$ 3,095,309**	**$ 2,926,684**	**$ 12,752,132**
Loss from operations	**$ (5,100,977)**	**$ (4,621,616)**	**$ (5,651,142)**	**$ (3,613,774)**	**$ (18,987,509)**	**$ (2,299,651)**	**$ (1,981,740)**	**$ (1,196,125)**	**$ 15,724**	**$ (5,461,791)**
Other expenses:			$ -		$ -					$ -
Interest expense	$ (35,592)	$ (46,109)	$ (54,186)	$ (60,000)	$ (195,887)	$ (60,000)	$ (60,000)	$ (60,000)	$ (60,000)	$ (240,000)
Accretion of discount on notes payable	$ (12,429)	$ (12,429)	$ (12,429)	$ -	$ (37,287)	$ -	$ -	$ -	$ -	$ -
Loss on conversion of franchisee debt to stock			$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Derivative liability			$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Total other expenses		$ (67,718)	$ (62,063)	$ (60,000)	$ (189,781)	$ (60,000)	$ (60,000)	$ (60,000)	$ (60,000)	$ (240,000)
Loss before provision for income taxes	**$ (5,148,998)**	$ (4,747,872)	$ (5,713,205)	$ (3,553,774)	$ (19,163,849)	$ (2,239,651)	$ (1,921,740)	$ (1,136,125)	$ 75,724	$ (5,221,791)
Provision for income tax	**$ -**		$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Loss from continuing operations	**$ (5,148,998)**	**$ (4,747,872)**	$ (5,713,205)	$ (3,553,774)	$ (19,163,849)	$ (2,239,651)	$ (1,921,740)	$ (1,136,125)	$ 75,724	$ (5,221,791)
Gain (loss) from discontinued operations	**$ 141,502**		$ -	$ -	$ 141,502	$ -	$ -	$ -	$ -	$ -
Net loss	**$ (5,007,496)**	**$ (4,747,872)**	$ (5,713,205)	$ (3,553,774)	$ (19,022,347)	$ (2,239,651)	$ (1,921,740)	$ (1,136,125)	$ 75,724	$ (5,221,791)
Net loss per share - basic and diluted (in dollars per share)	**$ (0.07)**	**$ (0.07)**	$ (0.08)	$ (0.05)	$ (0.27)	$ (0.02)	$ (0.02)	$ (0.01)	$ 0.00	$ (0.05)
Weighted average shares used in computing net loss per share - basic and diluted (in shares)	**69,611,593**	**70,069,253**	71,860,591	73,961,944	71,375,845	90,152,420	99,645,995	102,444,109	102,855,461	98,774,496

DO Not

General Disclaimer:

Trickle Research LLC produces and publishes independent research, due diligence and analysis for the benefit of it investor base. Our publications are for information purposes only. Readers should review all available information on any company mentioned in our reports or updates, including, but not limited to, the company's annual report, quarterly report, press releases, as well as other regulatory filings. Trickle Research is not registered as a securities broker-dealer or an investment advisor either with the U.S. Securities and Exchange Commission or with any state securities regulatory authority. Readers should consult with their own independent tax, business and financial advisors with respect to any reported company. Trickle Research and/or its officers, investors and employees, and/or members of their families may have long/short positions in the securities mentioned in our research and analysis and may make purchases and/or sales for their own account of those securities. David Lavigne does not hold a position in Generation Next.

Trickle Research has not been compensated directly by Generation Next for the publication of this report nor has Generation Next compensated Trickle Research for any other services associated with this research report.

Trickle Research has an exclusive content distribution agreement with SMM.Global whereby SMM.Global pays Trickle Research a fee for any Trickle labeled content displayed, hosted or distributed on its site: www.SMM.Global. Per that agreement, SMM.Global charges issuers to host and distribute licensed research. Issuers may choose to pay SMM.Global for the hosting and distribution of Trickle Research. They are under no obligation to do so.

Generation Next has paid fees to present at investor conferences co-sponsored by Trickle Research.

Reproduction of any portion of Trickle Research's reports, updates or other publications without **written** permission of Trickle Research is prohibited.

All rights reserved.

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 "Speculative Buy" 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.