Trickle Research

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

Allocation Upgrade and Price Target Downgrade

SIGMA LABS

Sigma Labs, Inc.

(NasdaqGS: **SGLB)**

(http://www.sigmalabsinc.com)

Report Date: 07/29/21

12- 24 month Price Target (Adjusted): **$9.50

Allocation: *6

(Adjusted) Closing Stock Price at Initiation (Closing Px: 10/29/19): $5.10

Closing Stock Price at Allocation Increase (Closing Px: 10/07/20): $2.58

Stock Price at This Allocation Increase and Price Target Decrease (Closing Px: 07/29/21): $3.76

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

Sigma Labs reported their 2Q-F21 quarter and the results were below our expectations and judging from the comments on the call, they were below the expectations of most who follow the stock including the Company. However, as management noted on the call, we are not sure that the quarter is indicative of the opportunity, and we think that is a point worth covering.

We started covering Sigma in October 2019, and frankly, we were well ahead of the "revenue" events then, and we continue to be now. That is, the revenue ramp has taken longer than we modeled then, and that continues to be the case, but we are not sure it is the overriding point to our enthusiasm for the Company. Obviously, that requires some color.

To be clear, we have attracted several new readers over the past few months, so we will take a moment to reiterate our approach at Trickle. First, we are generalist microcap analysts. Further, we view our mission as one of finding companies that we think are in front of what we see as a marked developing catalyst, but we do not pretend to know when or if for that matter, that catalyst might unfold and ultimately benefit the particular company(s) we initiate. In short, we are looking for companies that we think have extraordinary potential that could lead to results that drive the stock to fundamentally based valuations that are multiples of where we initiate them. It can be a lonely pursuit because as most of us who have spent much time in the space can generally attest, things rarely happen as quickly as we anticipate or hope. In that regard, our research is probably not of much value to traders and it clearly requires some patience as the fundamentals unfold and ostensibly, progress. We recognize that approach is not for everyone, and we also recognize that it is not without inherent risks and setbacks.

That said, specifically, while Sigma has yet to see the market for its technology/products develop to the point of better revenue visibility, we continue to believe in our original thesis and here are a few of bullet points to consider:

1) Obviously, Sigma's success depends on the adoption/proliferation of additive manufacturing/3D metal printing. To be clear, the industry has had its own difficulties gaining traction and momentum and there are a number of reasons for that. We believe one of the *major* reasons is a lack of quality assurance standards across the industry, and specifically from one printer manufacturer to the next. We think that impediment remains relevant, so in turn we think the opportunity for Sigma to mitigate it remains as well. However, while we believe the acceleration of the industry could be enabled by the adoption of PrintRite3D®, conversely the adoption of PrintRite3D® will likely be driven by the acceleration of the industry. We submit there is some "chicken or the egg" quandary to the story.

2) In our view while some of Sigma's lack of revenue traction is related to the macro "quandary" noted above, we also take responsibility for our research being a bit ahead of itself in terms of Sigma's ability (at the time) to provide a largely ubiquitous solution *at the time of that initiation*. To translate, in retrospect, Sigma was still dealing with more technical challenges than we understood at the time of our initiation. More specifically, they had managed to integrate the system into the protocols of some of the printers, but not all of them, and they still had some added bugs therein. Obviously, Sigma's goal is to become a ubiquitous provider of the additive QA solution, which requires that it work across a preponderant portion of the metal 3D landscape. Succinctly, they were not there at the time. In the context of our "chicken and the egg" notion above their inability to deliver a broad solution may have contributed to their slower than anticipated adoption. From another perspective, the industry's muted advance may have allowed Sigma time to catch up. Regardless, we believe the Company is in a far better position today to address a far greater portion of the market and we think it is fair to suggest that management said as much on the call.

3) We will not belabor this because everyone is aware of it, but the pandemic has clearly had a negative impact on the advance of the additive industry and Sigma by extension. We think that is particularly true

with some of their collaborations in Europe, which as we see it involves some of their more robust relationships. We think it is fair to say that inasmuch as Covid has wreaked havoc in U.S., its overall impact has perhaps been even more acute through much of the E.U. The Company alluded to that on the call as well.

4) Managing a small undercapitalized public technology company is challenging. We would argue that is far more challenging than many of the microcap critics (along with many shareholders) fully understand. Given that view, we do not typically make a habit of criticizing management, but we also recognize that some is much better than others. Without belaboring the point, in our view CEO Mark Ruport has provided the Company with a path that we are not sure they would be on without him. That is less a critique of past management as much as it is an opinion about his (excuse the pun) additive contribution. In the context of some of the past technical challenges, pandemic problems etc. we think that notion is constructive to our view that the stars may be aligning despite the challenges to this point. That includes by the way, the building of a new sales force that from their comments on the call sounds like it is beginning to hit its stride.

5) We have covered this in prior research, but one of Sigma's challenges is to drive acceptance of their platform by more printer manufacturers (as opposed to by printer users who are manufacturing 3D metal parts). As evidenced in part by their recent collaborations with 3D printer manufacture DMG MORI, we believe they are making headway on that front. In addition, they continue to make headway with printer users as well. Recall, it was their announcement in March (2021) regarding a system sale to Lockheed Martin that sent the stock to a high trade of $9.75.

6) At the time of our initiation the Company actually had negative working capital. That had some obvious risks associated with it and it also mitigated their ability to proactively market and otherwise grow the business. Subsequently, the Company has been able to raise some capital, including approximately $15 million through the first half of F21. We submit, dilution is a double-edged sword, but from our perspective, the capital certainly provides them flexibility to execute and ostensibly accelerate the Company's growth. Obviously, the dilution impacts some of our per share valuation conclusions.

7) On the earnings call the Company alluded to another item that we found interesting and in line with an issue we have discussed in the past. From the call: *There's also a growing consensus that a standards-based third-party quality monitoring system like PrintRite3D is required to ensure consistent quality and accelerate the adoption of 3D metal printed parts. This consensus is being reinforced by regulatory bodies, driving standards within specific vertical industries.* As we have discussed in several pieces of research over the years history suggests that emerging industries often evolve faster when they adopt standards that help customers compare, evaluate and integrate competing products and services. We think it is fair to say that additive manufacturing lacks such standards and in fact that is the basis for Sigma's opportunity; to develop a QA standard that can be applied across the preponderance of available additive printers. However, recognize that the statement above suggests something a bit more overriding than an internally developed industry standards. The statement above suggests that there may be growing pressure from industries *served by* additive manufacturing. That is, these industries, are requiring standardized and reliable QA processes from the manufacturers of 3D metal parts. We think that is especially true in industries where those parts are used in mission critical applications (a jet engine for instance) wherein failure might be catastrophic. Again, we do not know when the push for standards will finally drive opportunity for Sigma, and we have certainly not gotten that right to this point, however we remain quite constructive on the notion that the push for standardization across the industry will prove to be a major driver for PrintRite3D adoption.

To summarize, obviously by now, 20+ months into the coverage, we would have liked to see more progress out of Sigma on the revenue front. To be fair, the pandemic has encompassed the lion's share of that coverage period, so while we will not suggest that it is the only reason for the revenue shortfall, it has clearly been a measurable contributor. We would add, recall that from the time of our initiation through the end of 2019 and into January 2020, Sigma spent much of that period trading at levels 2X +- our initiation price. Clearly, the Pandemic played *some* role in the retracing of the stock. Moreover, they reversed the stock 10:1 in late February (2020) so that probably did not help either. Regardless, given what we view as progress on multiple business fronts, a much needed (albeit expensive) round of meaningful capital and presumably the waning of the pandemic, we are comfortable suggesting that from current levels and all things considered (and the benefit of hindsight), Sigma shares are probably more attractive today than at any time since our initiation. As a result, we are increasing our allocation of Sigma shares from 5 to *6 . However, we have also recast our model to include the added dilution as well as reducing the pace of the revenue ramp relative to our prior models. In conjunction with the model adjustments, we are also establishing a new (lower) 12-24 month price target of **$9.50. Clearly, visibility remains a challenge, so we will reassess all of these conclusions as data points emerge and visibility improves.

Projected Operating Model

Projected Operating Model						
Sigma Labs, Inc.						
Prepared By: Dave Lavigne, Trickle Research						
	(Actual)	(Actual)	(Estimate)	(Estimate)	(Estimate)	(Estimate)
	3/31/2021	6/30/2021	9/30/2021	12/31/2021	Fiscal 2021	Fiscal 2022
REVENUES	$ 458,140	$ 144,148	$ 843,580	$ 1,503,203	$ 2,949,071	$ 8,440,346
COST OF REVENUE	$ 128,331	$ 116,397	$ 380,439	$ 689,191	$ 1,314,358	$ 3,703,153
GROSS PROFIT	$ 329,809	$ 27,751	$ 463,140	$ 814,012	$ 1,634,712	$ 4,737,193
EXPENSES:					$ -	$ -
Salaries & Benefits	$ 847,171	$ 985,348	$ 993,559	$ 1,008,070	$ 3,834,148	$ 4,085,688
Stock-Based Compensation	$ 117,477	$ 116,441	$ 150,000	$ 150,000	$ 533,918	$ 600,000
Operating R&D Costs	$ 196,340	$ 280,700	$ 108,649	$ 150,615	$ 736,304	$ 841,207
Investor & Public Relations	$ 108,341	$ 114,762	$ 180,000	$ 180,000	$ 583,103	$ 720,000
Organizational Costs	$ 77,616	$ 158,529	$ 75,000	$ 75,375	$ 386,520	$ 305,288
Legal & Professional Service Fees	$ 176,847	$ 244,019	$ 206,872	$ 220,064	$ 847,802	$ 928,807
Office Expenses	$ 148,225	$ 151,871	$ 125,307	$ 145,096	$ 570,499	$ 653,210
Depreciation & Amortization	$ 23,031	$ 25,783	$ 25,912	$ 26,041	$ 100,767	$ 105,474
Other Operating Expenses	$ 86,356	$ 91,198	$ 88,000	$ 88,440	$ 353,994	$ 358,204
Total Operating Expenses	$ 1,781,404	$ 2,168,651	$ 1,953,299	$ 2,043,702	$ 7,947,055	$ 8,597,878
LOSS FROM OPERATIONS	$ (1,451,595)	$ (2,140,900)	$ (1,490,158)	$ (1,229,690)	$ (6,312,343)	$ (3,860,685)
OTHER INCOME (EXPENSE)					$ -	$ -
Interest Income	$ 55	$ 7,018	$ 37,850	$ 34,654	$ 79,576	$ 115,145
State Incentives	$ -	$ -	$ -	$ -	$ -	$ -
Change in fair value of derivative liabilities	$ 802,285	$ -	$ -	$ -	$ 802,285	$ -
Exchange Rate Gain (Loss)	$ (51)	$ 208	$ -	$ -	$ 157	$ -
Interest Expense	$ (1,353)	$ (2,029)	$ (2,039)	$ (2,049)	$ (7,470)	$ (8,300)
Loss on Disposal of Assets	$ -	$ -	$ -	$ -	$ -	$ -
Debt discount amortization	$ -	$ -	$ -	$ -	$ -	$ -
Total Other Income (Expense)	$ 800,936	$ 295,353	$ 35,811	$ 32,604	$ 1,164,704	$ 106,845
LOSS BEFORE PROVISION FOR INCOME TAXES	$ (650,659)	$ (1,845,547)	$ (1,454,348)	$ (1,197,085)	$ (5,147,639)	$ (3,753,840)
Provision for Income Taxes	$ -	$ -	$ -	$ -	$ -	$ -
Net Loss	$ (650,659)	$ (1,845,547)	$ (1,454,348)	$ (1,197,085)	$ (5,147,639)	$ (3,753,840)
Preferred Dividends	$ 60,908	$ -	$ -	$ -	$ 60,908	$ -
Net Loss applicable to Common Stockholders	$ (711,567)	$ (1,845,547)	$ (1,454,348)	$ (1,197,085)	$ (5,208,547)	$ (3,753,840)
Net Loss per Common Share - Basic and Diluted	$ (0.09)	$ (0.18)	$ (0.14)	$ (0.11)	$ (0.53)	$ (0.35)
Net Loss per Common Share - Diluted	$ (0.09)	$ (0.18)	$ (0.14)	$ (0.11)	$ (0.53)	$ (0.35)
Weighted Average Number of Shares Outstanding - Basic	7,790,121	10,493,598	10,555,418	10,579,087	9,854,556	10,628,207
Weighted Average Number of Shares Outstanding - Diluted	7,790,121	10,493,598	10,555,418	10,579,087	9,854,556	10,644,361

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Sigma Labs has paid fees to present at investor conferences co-sponsored by Trickle Research.

Portions of this publication excerpted from company filings or other sources are noted in *italics* and referenced throughout the report.

Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "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.