

Trickle Research

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



Q2-F21 Earnings Update



COMSovereign Holding Corp.

(NasdaqGS: COMS)

Report Date: 08/20/21

12- 24 month Price Target: \$9.00

Allocation: 4

Closing Stock Price at Initiation (Closing Px: 07/16/21): \$1.92

Closing Stock Price at This Update (Closing Px: 08/20/21): \$1.81

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

We just initiated our coverage of COMS about 1 month ago, and frankly it probably would have made some sense to wait for the release of these numbers. However, our coverage encompasses a long term view of the Company and as such is not predicated on the outcome of this particular quarter (or even the balance of fiscal 2021 for that matter).

The above said, we were pleased with the results in the context of our projections, so we will cover that minutia briefly.

For 2Q-F21 COMS reported revenues of \$3.61 million versus our estimate of \$4.17 million. Actual revenues were nearly 75% higher than the prior quarter, so the bump was notable. The Company reported an operating loss of \$10.38 million versus our estimate of \$9.43 million, so operating expenses were a bit higher than we anticipated, but, given where we believe revenues are headed, getting the levels of relative associated expenses right is going to be a fluid process. That said, we have some aggressive projections for the coming quarters, and our interpretation of the earnings call suggests to us that the Company is comfortable with our revenue projections for the second half of F-21, *which amounts to about \$50 million versus the first half actual numbers of approximately \$5.7 million.* To be clear, we understand why some may be skeptical about that extraordinary level of growth, but at least for now, the Company appears to believe the pipeline supports the view.

More specifically, as we noted in the initial coverage, we think the Company's drone business is robust, which we think is primarily (but not completely) driven by demand from government agencies, which makes sense to us given the state of affairs at our borders and in other places around the world. However, in addition, the Company also addressed demand for its Fastback radios and that discussion dovetailed with an announcement the Company made on 8.16.21 regarding the same. That announcement noted:

"...increased production capacity at its U.S.-based contract manufacturing partner, it is resuming volume shipments of its Fastback Networks radio products under its multi-year Master Vendor Agreement (MVA) with a Tier 1 U.S. Mobile Network Operator.

Fastback has begun fulfillment of open orders valued at more than \$8.7 million under the multi-year MVA after resolving initial delays caused by global component shortages, post-production testing capacity, as well as the lingering impact of COVID-19 on operations and supply chains. With its current component inventory and production capacity, COMSovereign believes that it will fulfill these initial orders throughout the third and fourth quarters of 2021. Based upon rapidly increasing production capacity, and the availability of necessary components, the Company expects the ability to meet Fastback radio order volumes of approximately \$40 million from customers over the next 8 to 10 months..."

Succinctly, if they deliver against this order around the time frame they are suggesting here, and the drone business performs close to where we think it can, the Company will likely meet or exceed our expectations. One would think that sort of business trajectory would be constructive for the stock price, but regardless of how the stock reacts, we would view that sort of trajectory as a highly positive fundamental achievement, and one that fits with our thesis that COMS may have a meaningful opportunity in the continued 4G and emerging 5G space(s).

The above noted, there are still some challenges here that may "keep us up at night" and at least two of those issues were appropriately raised on the call. The first of those is the continued tightness in supply chains across the globe (which could most certainly impact the Company's ability to fulfill orders) and the second is the Company's requirements for additional capital to fund the ramp of the business through positive cash flow. Obviously, one of those is a more macro risk that many companies are experiencing, while the other is a bit more micro in nature. In either case, we submit, these are clear risks in the deal that we think they will be able to overcome but will remain topical until they are addressed.

To summarize, the 2Q results and associated discussions were in line with our expectation, so our investment thesis and enthusiasm for the Company remains intact. In addition, the Company alluded to a recent “IP audit” they conducted, which verified 176 patents (142, granted, 32 pending and 2 provisional). To be clear, certainly part of our positive view of COMS is built on the notion that the proliferation of 5G will require considerably more new and innovative technology to reach anything close to its potential. We believe, for a variety of reasons we laid out in the initial coverage, that domestic companies that can provide that innovation will possess some comparative advantages in terms of providing it. Our view is that COMS fits that mold, and while certainly not definitive, we think their considerable IP position may speak to that comparative advantage.

We reiterate our 12-24 month price target of \$9.00 as well as our initial allocation of 4, and we will look to emerging data points (and presumably improving results) to support that view. That noted, if it is not clear, we view the stock under \$2.00 as particularly attractive.

Projected Operating Model

COM Sovereign Holding Corp.						
Projected Operating Overview						
By: Trickle Research						
	Actual	Actual	Estimate	Estimate	Estimate	Estimate
	3/31/2021	6/30/2021	9/30/2021	12/31/2021	Fiscal 2021	Fiscal 2022
Revenue	\$ 2,086,452	\$ 3,611,000	\$ 16,691,616	\$ 33,383,232	\$ 55,772,300	\$ 154,919,061
Cost of Goods Sold	\$ 1,073,990	\$ 1,813,000	\$ 7,845,060	\$ 13,499,889	\$ 24,231,938	\$ 77,227,152
Gross Profit	\$ 1,012,462	\$ 1,798,000	\$ 8,846,556	\$ 19,883,343	\$ 31,540,362	\$ 77,691,909
Operating Expenses					\$ -	\$ -
Research and development	\$ 547,556	\$ 1,199,000	\$ 1,200,000	\$ 1,300,000	\$ 4,246,556	\$ 11,884,606
Sales and marketing	\$ 48,123	\$ 109,000	\$ 200,000	\$ 600,000	\$ 957,123	\$ 8,278,626
General and administrative	\$ 7,135,126	\$ 6,976,000	\$ 7,300,000	\$ 7,500,000	\$ 28,911,126	\$ 33,022,167
Depreciation and amortization	\$ 3,660,811	\$ 3,617,000	\$ 3,500,000	\$ 3,525,000	\$ 14,302,811	\$ 14,085,663
Gain on the sale of assets	\$ (83,000)	\$ -	\$ -	\$ -	\$ (83,000)	\$ -
Gain on the sale of assets	\$ -	\$ 281,000	\$ -	\$ -	\$ 281,000	\$ -
Total Operating Expenses	\$ 11,308,616	\$ 12,182,000	\$ 12,200,000	\$ 12,925,000	\$ 48,615,616	\$ 67,271,063
Net Operating Loss	\$ (10,296,154)	\$ (10,384,000)	\$ (3,353,444)	\$ 6,958,343	\$ (17,075,254)	\$ 10,420,846
Other Income (Expense)					\$ -	\$ -
Interest expense	\$ (468,534)	\$ (547,000)	\$ (763,325)	\$ (763,325)	\$ (2,542,184)	\$ (3,053,300)
Other income (expense)	\$ (13,042)	\$ 13,000	\$ -	\$ -	\$ (42)	\$ -
Loss on extinguishment of debt	\$ (5,348,469)	\$ 323,000	\$ -	\$ -	\$ (5,025,469)	\$ -
Loss on conversion of debt	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Foreign currency transaction gain (loss)	\$ (80,234)	\$ 18,000	\$ -	\$ -	\$ (62,234)	\$ -
Interest income	\$ 4	\$ -	\$ -	\$ -	\$ 4	\$ -
Gain on the sale of assets	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Impairment Expense	\$ (5,910,275)	\$ -	\$ -	\$ -	\$ -	\$ -
Total Other Expenses	\$ (5,910,275)	\$ (193,000)	\$ (763,325)	\$ (763,325)	\$ (7,629,925)	\$ (3,053,300)
Net Loss Before Income Taxes	\$ (16,206,429)	\$ (10,577,000)	\$ (4,116,769)	\$ 6,195,018	\$ (24,705,179)	\$ 7,367,546
Deferred Tax Benefit	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Net Income (Loss)	\$ (16,206,429)	\$ (10,577,000)	\$ (4,116,769)	\$ 6,195,018	\$ (24,705,179)	\$ 7,367,546
Loss per common share:						
Basic	\$ (0.25)	\$ (0.15)	\$ (0.05)	\$ 0.08	\$ (0.37)	\$ 0.10
Diluted	\$ (0.25)	\$ (0.15)	\$ (0.05)	\$ 0.08	\$ (0.37)	\$ 0.09
Weighted-average shares outstanding:						
Basic	65,941,513	68,770,644	77,363,292	77,363,292	72,359,685	77,363,292
Diluted	65,941,513	68,770,644	78,832,544	79,214,730	73,189,858	82,347,663

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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.