

XELB / Nasdaq

**SPECULATIVE  
BUY**

Initial

**\$4.80**

Target

**CAPITALIZATION**

Shares Outstanding (8/12/22)	19.62 M
Recent Price (8/23/22)	\$1.14

Market Capitalization	\$22.37 M
+ Debt	-0- M
- Cash	10.87 M
Enterprise Value	\$11.50 M

Book Value	\$80.73 M
Working Capital	\$14.86 M
Dividend	Nil

Balance sheet figures as of 6/30/22

**MARKET DATA**

Bid-Ask Spread, % Price	3.5%
52 Week High/Low	\$2.25 - \$0.95

Shares Outstanding	19.62 M
Inside Ownership	56.1%
Institutional Ownership	20.0%
Estimated Flotation	5.20 M

Average Daily Volume	103 K
Short Interest, % of Float	0.32%
Beta	1.51

Source: Bloomberg LP

**INVESTMENT RETURNS**

	XELB	Sector
Return on Equity	neg	16.85%
Return on Assets	neg	5.05%
Return on Capital	neg	9.77%

Source: Crystal Equity Research, CSI Markets

**FINANCIAL PROFILE**

	FY20	FY21
Sales	\$29.45 M	\$37.93 M
(L)EBITDA	2.20	(4.35)
(L)EPS	(\$0.68)	(\$0.63)

Source: Company Reports

**HIGHLIGHTS**

- **Strengthened Balance Sheet.** Following the sale of a majority interest in the *Mizrahi* brand asset for \$45.4 million in net cash and the paydown of debt by \$29.0 million, Xcel reported \$10.9 million in cash and zero debt at the end of June 2022.
- **Gain on Asset Sale.** Xcel recorded a \$20.6 million gain on the *Mizrahi* asset sale, demonstrating the team's success in using its media platform to promote and grow one of its portfolio brands.
- **Growth Plans.** With a newly strengthened balance sheet, Xcel leadership is aggressively moving ahead with growth plans. Projects include a new line of *Mizrahi* brand women's clothing, new points of distribution for its *C-Wonder* and *Halston* brands and strategic acquisitions of new brands.
- **Undervaluation.** We estimate the intrinsic value of XELB is \$4.80 and set our target price accordingly. The current price is a compelling entry point for patient investors.
- **Catalysts.** In the coming months, expect Xcel news regarding new distribution arrangements for its *Halston* and *C-Wonder* brands. The Company could also surprise with a brand acquisition.

**Debra Fiakas, CFA**  
Security Analyst  
212-400-7519  
dfiakas@crystalequityresearch.com

PLEASE READ THE IMPORTANT DISCLOSURES AND DISCLAIMERS AT THE END OF THIS REPORT.

INDUSTRY: Consumer Cyclical, Apparel

XELB: NASDAQ

## RECENT DEVELOPMENTS

Shareholders of Xcel Brands were treated to an 'as expected' report for the quarter ending June 2022, following the previously disclosed sale of a majority share in one of the Company's principal consumer brands. The deal to sell a 70% interest in the *Mizrahi* brand closed at the end of May 2022, and could be observed first in the Company's balance sheet. A portion of the \$45.4 million in net cash proceeds was used to paydown all debt, leaving the balance sheet with excess cash in the bank and a debt-to-equity ratio of 0.00. The Company also reported a \$20.6 million gain on the sale of the *Mizrahi* asset, demonstrating the success the Xcel team achieved with the asset.

Financial strength should give the Xcel team the fire-power to move opportunistically for growth. During the earnings conference call management cited projects to boost organic sales, including changes to its supply chain to exploit duty-free importation rules and new distribution points for existing brands. The Xcel team is hungry and ready to acquire another brand to manage and grow, much like Mizrahi home run.

## RECOMMENDATION

We continue to look favorably at XELB. In our view, the stock is deeply undervalued. Based on the recent sale of the *Mizrahi* asset, the retained portion was valued at \$19.8 million at the end of June 2022. This compares to a current market capitalization of \$22.4 million and an enterprise value of \$11.5 million for the entire Company. Based on the deal terms, we estimate the intrinsic value of XELB is \$4.80 per share, which informs our price target. Our valuation exercise does not include the value that we expect to accrue from growth investments the Xcel team has already initiated.

Accordingly, we believe XELB is priced at a compelling level for long-term investors who can look past the unflattering top-line comparisons in the recently reported quarter. The full picture includes the lubricating potential of the Company's investment cash kitty and the experience the team has in finding and growing strong brands. The Company's innovative media platform remains a key differentiator for brand growth by effectively converting viewers to customers.

VALUATION		OPERATING PROJECTIONS				
		US\$	2020A	2021A	2022E	2023E
Price/Sales	0.32 X	Sales	\$29.45 M	\$37.93 M	\$ 29.81 M	\$ 30.50 M
Price/Cash Flow	neg	Operating (Loss)	(16.46)	(12.56)	(11.63)	(6.09)
Price/EPS	neg	CFO (U)	3.19	( 6.56)	(3.64)	0.61
Price/Book Value	0.28 X	EPS (LPS)	(\$0.68)	(\$0.63)	\$0.21	\$(0.17)
Consensus EPS 2022	na	<i>Dollars in millions except per share earnings</i>				
Forward PE	na					

*Per share figures estimated 6/30/22*

*Company Reports and Crystal Equity Research Estimates*

**QUARTER REPORT HIGHLIGHTS - changes at the top-line**

Xcel Brands reported \$8.5 million in total sales in the three months ending June 2022, representing 21.3% year-over-year decrease and 3.2% sequential decrease. The comparison was not unexpected following the Company's sale of a majority interest in the *Mizrahi* consumer brand. The deal closed in late May 2022, impacting the top-line in the final month of the quarter.

License fees of \$5.2 million contributed 61% of total sales compared to 68.1% of the mix in the previous quarter. It is license fees that were impacted by the sale of the *Mizrahi* brand, which did not contribute to sales in the final month of the quarter.

Product sales totaled \$3.3 million or 39% of total sales, increasing sequentially but declining by 28% year-over-year. During the conference call to discuss the quarter results with shareholders and analysts, management suggested the decline in apparel sales was largely due to and inflationary economic environment that chilled consumer demand for discretionary goods. Indeed, certain of the Company's wholesale orders were cancelled as retailers anticipated lower sales activity.

Gross profit margin on product sales shrank to 22% of segment revenue. This compares to 32.5% margin in the prior-year quarter and 39.7% margin in the previous quarter. The Company had to write-down inventory values following the cancellation of certain orders, increasing product costs. Additionally, management acknowledged actions to sell off seasonal apparel inventory.

Henceforth, contributions to results from the 30% ownership retained in the *Mizrahi* brand will appear in Other Income with costs netted against revenue. Management indicated that in the one month in the quarter that the new ownership position was in place, the net result was a wash. Other income in future quarters may include a figure for the contribution by the retained share in the *Mizrahi* brand.



Notable in the quarter was a gain of \$20.6 million on the sale of the *Mizrahi* brand, which was included in other income. Monetization of the Company's achievements with the brand is already leading to significant change in Xcel's financial profile.

**BALANCE SHEET - no debt and new assets**

Following the sale of a majority share in the Mizrahi brand for \$45.4 million in net cash proceeds, management speedily used \$29.0 million to pay off debt and outstanding interest. Another \$1.5 million was used for fees and prepayment penalties. The Company now has a debt-to-equity ratio of 0.00 and a left-over cash kitty of \$10.9 million. Working capital at the end of June 2022, was \$14.9 million, well more than the quarter sales level.

As expected, Xcel's Non-current Assets also reflected significant change. Following the sale of the *Mizrahi* brand asset, Trademarks and Other Intangible assets, net of amortization was reduced to \$50.7 million. This compares to \$98.3 million at the end of the last fiscal year ending December 2021. Xcel's balance sheet now includes a new asset representing the Company's retained 30% share in the *Mizrahi* brand. In the June 2022 balance sheet, it was reflected in Non-current Assets as Equity Method Investment valued at \$19.8 million.

## UPDATED PROJECTIONS

Our earnings model has been updated to reflect the reported results in the June 2022 quarter. We made additional adjustments to our estimates based on cues in spending patterns in the June quarter.

- The combination of these additions and adjustments results in slightly higher sales projection of \$29.8 million for the full year 2022 (compared to previous \$26.8 million). The increase is largely due to better-than-expected Product Sales, at least better than our conservative approach to the segment.
- Our projected operating loss for the full year 2022 is now \$11.6 million (compared to previous \$8.53 million). The deeper loss is largely the result of the inventory write-off reported in the June quarter as well as higher than anticipated Salaries, Benefits & Taxes that included bonuses.

Our model still reflects a \$800,000 contribution from the minority interest in Mizrahi in Other Income. Admittedly, this line could be more a placeholder than a studied estimate. We anticipate more clarity on the income potential in the retained portion of the *Mizrahi* asset when the Company reports financial results from the third quarter ending September 2022.

**Table I: Summary Historical and Projected Sales and Earnings**

	2020 Actual	2021 Actual	2022 Estimate	2023 Estimate
Sales	\$29.45 M	\$37.93 M	\$26.75 M	\$ 30.50 M
Gross profit	23.99	27.27	22.41	22.88
Gross Margin %	81.5%	71.9%	83.8%	75.0%
Operating income (Loss)	(16.46)	(12.56)	(11.63)	(6.09)
Earnings (Loss) per share	(\$0.68)	(\$0.63)	\$0.21	(\$0.17)
Cash flow from operations	\$ 3.19 M	(\$ 6.56) M	(\$ 3.64) M	\$ 0.61 M

Source: Company Reports and Crystal Equity Research Estimates

In coming quarters, shareholders must be prepared for a more noticeable decline in sales compared to year ago periods. For example, our estimate of \$2.8 million in Net Licensing Fees in the September 2022 quarter, represents a 59.9% year-over-year decrease in that segment. The decrease is largely the result of the Mizrahi brand asset sale, but also reflects a concern that demand conditions could deteriorate even further.

### Upside

That said, we note that Xcel's brand portfolio could withstand the unfavorable economic conditions better than most apparel companies, given its lead in using the media to reach consumers. Some apparel names are only just now beginning to use live media events as they grapple with store closings, inventory write-downs and personnel lay-offs. For example, Japan's casual and professional clothing brand Uniqlo is just now streaming its first live fashion event. We believe Uniqlo is just one of many retailers that is turning to media to save their market share. By contrast, Xcel is in a significantly better position with a well-developed body of knowledge in how to use media to convert prospects to buyers.

More importantly, Xcel has several product development and distribution plans in the works that put the Company in an advantageous position to deliver stronger sales and better profit margins. During the earnings conference call, management provided an update.

- A new warehouse in Mexico will be operational by the end of the 2022. The facility is expected to be eligible for reduced tariffs under the 'Section 321A' trade rule that should deliver 17% to 36% in duty savings that Xcel can use to boost margins or entice wholesalers and consumers with competitive pricing. We believe this will put Xcel in a significantly better position relative to rivals.
- Future quarters should reflect the benefits of a new third-party logistics (3PL) provider for the *Longaberger* brand located in Ohio. The move could deliver savings all along the supply chain, from inventory management to fulfillment and returns. The move should help reduce margin pressure at a time when supply chain costs are rising.
- New distribution projects for the *Halston* and *C-Wonder* brands in the United Kingdom are already underway. The opportunities involve a channel composed of 300 independent boutiques in the UK. Both projects are expected to begin before the end of 2022.
- New women's apparel designs under the *Mizrahi* brand are expected in the coming months. This is pursuant to a new license arranged by Xcel as part of the deal to sell the Mizrahi majority position to WHP Group. Understandably, Xcel leadership is a bit tightlipped on these designs and the exact timing may of an announcement, likely for competitive reasons.

We expect plenty of opportunity to fine-tune our assumptions and to increase both sales estimates and profit margins.

## TARGET PRICE

Our price target is unchanged at \$4.80 and, in our view, still represents a conservative objective.

In our original valuation of XELB, we relied on multiples found in precedent transactions in the sector. This is a common approach that begins with the price buyers have recently paid for companies in the sector. Of course, such multiples require adjustments the premium buyers pay for control of a company. Additionally, precedent transactions may be starkly different in make-up that the company under scrutiny. We solved both problems by using one particular precedent transaction: the sale of majority interest in the *Mizrahi* brand to privately-held WHP Group. Who better to rely on than an industry leader that has just completed extensive due diligence to support a material strategic transaction?

WHP's purchase price for 70% of the *Mizrahi* asset - \$46.2 million and a possible \$2.0 million earnout payment if revenue and cash earnings goals are met - implied a multiple of 4.68 times trailing sales for the brand. We adjusted the multiple downward to 4.0 for control and liquidity factors inherent in private transactions. After also adjusting Xcel's trailing revenue for the *Mizrahi* asset sale, the implied intrinsic value was \$4.80 per share for XCEL. The calculation is largely unchanged today and, if our target is achieved, still represents a potential return over 400%

## OUTLOOK

Admittedly, progress toward our price target may take time. Investors are conditioned to watch for growth in sales with each passing quarter report. Xcel Brands may disappoint in the next couple of quarters as economic headwinds cut into sales right as the Company shifts the focus of its brand portfolio. Sales may not demonstrate positive comparisons with prior-year. Assets may look underutilized as the proceeds of its success with the *Mizrahi* brand still sit in cash on the balance sheet.

The appearance of sluggish conditions is not expected to continue. The Company is now well capitalized for growth, both organic and acquired. The lubricating effects of monetizing Xcel's investment in the *Mizrahi* brand will become apparent in reported financial results as the Company is able to execute on its strategic growth plan, including a new line of *Mizrahi* brand women's clothing, new points of distribution for its *C-Wonder* and *Halston* brands, and possibly the addition of newly acquired brands.

We do expect near-term price catalysts. In the next few weeks, we are expecting an announcement related to a new distribution opportunity in the United Kingdom for the *C-Wonder* brand. Such an announcement could have a reinforcing impact on investor sentiment as it could demonstrate the dynamic nature of Xcel's brand portfolio. Management could also treat shareholders to an announcement related to the Company's new facility in Mexico when it becomes fully operational later this year.

Table II: Historic and Projected Quarterly Sales and Earnings

Dollars in Thousands	2021				2021	2022				2022
	1Q	2Q	3Q	4Q	Year	1Q	2Q	3Q	4Q	Year
Net licensing revenue	4,307	6,224	6,854	4,491	21,876	5,961	5,175	2,750	3,000	16,886
Net product sales	3,502	4,540	4,407	3,607	16,056	2,786	3,292	3,350	3,500	12,928
Total revenue	7,809	10,764	11,261	8,098	37,932	8,747	8,467	6,100	6,500	19,814
Cost of product sales	1,835	3,063	2,865	2,904	10,667	1,680	2,570	1,525	1,625	7,400
Gross profit	5,974	7,701	8,396	5,194	27,265	7,067	5,897	4,575	4,875	22,414
Operating expenses:										
Salaries, benefits & taxes	4,052	4,049	4,185	4,249	16,535	4,853	5,236	3,050	2,925	16,064
Selling, general & administrative expenses	3,038	3,090	3,463	4,773	14,364	3,392	3,803	2,318	2,470	11,983
Depreciation and amortization	1,210	1,848	1,891	1,881	6,830	1,820	1,812	925	925	5,482
Other operating expenses	160	431	163	(34)	720	32	485	-	-	517
Asset impairment charges	-	-	-	1,372	1,372	-	-	-	-	-
Total operating expenses	8,460	9,418	9,702	12,241	39,821	10,097	6,293	6,293	6,320	34,046
Operating income (loss)	(2,486)	(1,717)	(1,306)	(7,047)	(12,556)	(3,030)	(1,445)	(1,718)	(1,445)	(11,632)
Other income (expense)										
Equity in earnings of unconsolidated affiliates					-	-	-	400	400	800
Interest expense	(280)	(522)	(565)	(549)	(1,916)	(708)	(1,187)	-	-	(1,187)
Loss on extinguishment of debt	-	(821)	-	(695)	(1,516)	-	(2,324)	-	-	(2,324)
Other, net	-	(100)	(23)	(24)	(147)	(1)	20,608	-	-	20,608
Total other income (expense)	(280)	(1,443)	(588)	(1,268)	(3,579)	(709)	17,897	400	400	17,897
Income (loss) before income taxes	(2,766)	(3,160)	(1,894)	(8,315)	(16,135)	(3,739)	6,265	(1,318)	(1,045)	6,265
Provision for income taxes (benefit from)	138	(1,346)	(535)	(1,087)	(3,106)	-	3,178	-	-	3,178
Minority interest in profits (losses)	(81)	(256)	(223)	(285)	(845)	(252)	(301)	(250)	(250)	(1,053)
Net income (loss)	(2,547)	(1,558)	(1,136)	(6,943)	(12,184)	(3,487)	9,490	(1,068)	(795)	4,140
Net earnings (loss) per share	\$(0.13)	\$(0.08)	\$(0.06)	\$(0.35)	\$(0.63)	\$(0.18)	\$0.48	\$(0.05)	\$(0.04)	\$0.21
Weighted shares outstanding, diluted	19,261	19,449	19,542	19,570	19,456	19,571	19,677	19,600	19,600	19,612



## CRYSTAL EQUITY RESEARCH, LLC

Crystal Equity Research, LLC is an objective research resource, providing coverage of small capitalization companies in selected industries. The firm provides research reports by subscription to institutional investors, supplies research consulting services to financial professionals and offers an issuer sponsored research program for qualifying companies. Additional information is available at the firm's web site at [www.crystalequityresearch.com](http://www.crystalequityresearch.com).

## ANALYST

Debra Fiakas, CFA is a seasoned, credentialed investment professional with a diversified and successful track record as a research analyst and as an investment banker. Her decade-plus career includes solid experience in all aspects of the equity capital markets with particular emphasis on emerging growth companies operating in the technology sectors. Ms. Fiakas is also the principal member of Crystal Equity Research, LLC.

## ANALYST CERTIFICATION

The analyst who is primarily responsible for this research and whose name is listed first on this front cover certifies that: 1) all of the views expressed in this research accurately reflect his or her professional views about any and all of the subject securities or issuers, and 2) no part of any of the analyst's compensation was, is or will be directly or indirectly related to the specific rating expressed by analyst in this research.

## RATING SYSTEM

Buy	Price appreciation expected 10% or more over a 12-month period.
Hold	Price appreciation/depreciation expected between 10% and –10% over 12 months.
Sell	Price depreciation expected 10% or more over a 12-month period.

## CRYSTAL RESEARCH UNIVERSE

Buys	80%
Holds	5%
Sells	<u>15%</u>
Total	100%

## HISTORICAL RECOMMENDATIONS AND TARGET PRICE: XELB: Nasdaq

<u>Report</u>	<u>Date</u>	<u>Price</u>	<u>Rating</u>	<u>Target Price</u>
Initial	7/27/2022	\$1.10	Speculative Buy	\$4.80
Update	8/24/2022	\$1.14	Speculative Buy	\$4.80



**DISCLOSURES**

<u>Name</u>	<u>Symbol: Exchange</u>	<u>Disclosures</u>
Xcel Brand, Inc.	XELB: Nasdaq	D

**Disclosure Key**

- A A member or employee of Crystal Equity Research, LLC serves on the board of directors of the company.
- B A controlling member of Crystal Equity Research, LLC has a beneficial interest in the common stock of the company.
- C A person or persons preparing this report or an immediate family member of the preparer has a beneficial interest in the common stock of the company.
- D Crystal Equity Research, LLC received compensation for research coverage from the company or one of its agents. The fees are paid in advance in cash.
- E The company has a convertible issue outstanding.
- F The securities covered in this report can be optioned.
- G The securities covered in this report can be margined.

**ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST**

---

The information and opinions in this report were prepared by Crystal Equity Research, LLC. The information herein is believed to be reliable and has been obtained from public sources believed to be reliable. We make no representation as to the accuracy or completeness of such information. Opinions, estimates and projections in this report constitute the current judgment of the author as of the date of the report and are subject to change without notice. We have no obligation to update, modify or amend this report or to otherwise notify a reader thereof in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate, or if research on the subject company is withdrawn.

This report is provided for informational purposes only. It is not to be construed as an offer to buy or sell or a solicitation of an offer to buy or sell any financial instruments or to participate in any particular trading strategy in any jurisdiction. Opinions and recommendations in our reports do not take into account individual investor circumstances, objectives, or needs and are not intended as recommendations of particular securities or strategies to particular investors. The recipients of our reports must make their own independent decisions regarding any securities mentioned in our reports.

Crystal Equity Research, LLC may receive compensation from the company or companies mentioned in this report or agents acting on their behalf. Please review the important disclosures in this report.

This report may not be reproduced, distributed or published by any person for any purpose without the prior written consent of Crystal Equity Research. Please cite source when quoting.

Copyright © 2003-2022 Crystal Equity Research, LLC.