

KONARED CORPORATION ANALYST REPORT

SURF'S UP WITH BOTTLED SUPERFRUIT

RATING: OVERWEIGHT/BUY

PRICE TARGET: \$1.20

KonaRed Corporation
P.O. Box 701
Kalaheo, HI 96741
Tel: 808-212-1553

RESEARCH REPORT:

I. OVERVIEW:

- KonaRed Corporation (OTCQB: KRED) is in the business of bringing the health and wellness attributes of Hawaiian Coffee fruit to the masses. KonaRed Corporation has developed an innovative, state-of-the-art, proprietary process that produces antioxidant-packed extracts and powders from Hawaiian Coffee Fruit, which are used in its Antioxidant Juices, Organic Green Teas, and On-the-Go Packs, as well as ingredients which can be added to food, beverages, and nutritional products. The company was founded in 2008 and is headquartered in Kalaheo, Hawaii with a 10,000 sq. ft. warehousing and shipping facility in San Clemente, CA. It launched its first products in 2011 and became a public company in 2013.
- The Company's main product is the KonaRed Antioxidant Juice, a Coffee Fruit wellness drink high in nutrients offered to retail consumers. KonaRed has 30+ distributors in the US including UNFI and Nature's Best and its products are sold in select Kroger, Vitamin Shoppe, Whole Foods, Safeway, Walmart, 7-Eleven, Ralphs, Fred Meyer and many other retail locations throughout the US and Canada. KonaRed offers its products through wholesale and direct online retail channels and its products will be in approximately 7,500 store locations by the end of 2014.

II. BUSINESS TRENDS:

- Nutraceuticals World Magazine estimates the functional beverage market sales total around \$23.4 billion and growing. Trends show that sales for high sugary sodas and diet sodas are on a steady decline and consumers are demanding healthy drinks and alternatives. Many want a brand that reflects and enhances their active lifestyle and identity. The New York Times stated, "Cold, bubbly sweet soda, long the American champagne, is not welcomed in many places these days."
- Found in the Kona region of Hawaii, CoffeeBerry® is the fruit, high in antioxidant value that surrounds and protects the world famous Kona coffee bean. KonaRed uses the fruit and dries it and processes it to create its all-natural CoffeeBerry® beverages and mixable powders. The outer part of the coffee bean had been frequently discarded, but recent studies show that the Coffee Fruit is actually an antioxidant powerhouse.
- KonaRed products have an extraordinary level of nutrients and antioxidants that get absorbed by the body at the cellular level. They offer wellness qualities including healthy energy, immune support, focus, clarity and cognitive brain health. Antioxidants are known to help prevent diseases, delay the body's aging process and provide a long-lasting, natural mood boost. KonaRed is an emerging leader in the functional Coffee Fruit category with new cutting edge products and a highly appealing marketing story to the health conscious consumer.
- KonaRed has been provided a license by VDF FutureCeuticals Inc. a Nutraceuticals powerhouse that provides patent protection, human clinical science, ongoing research and license of the CoffeeBerry®. VDF FutureCeuticals is a leader in the bio-research, development, and manufacture of high-quality fruit,

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vegetable, and grain-based nutraceutical and functional food ingredients. FutureCeuticals is committed to discovery-based research that leads to the expansion of human health, and is the trusted partner-of-choice for companies in search of creative, ethical solutions for the health and wellness needs of today's consumer. Its sister company, Van Drunen Farms, was founded over one hundred years ago, and has grown into one of the largest dried food ingredient manufacturers and suppliers in the world.

- KonaRed's ability to secure exclusive Kona-based and other Hawaiian Coffee Fruit allows the company to operate without constraints in the supply chain far out into the future. KonaRed has a 5-year exclusive supply relationship with Greenwell farms. Greenwell Farms was founded in 1850 and is known for planting some of the first coffee trees in Kona. Greenwell Farms offers a substantial yearly supply of coffee fruit of more than 4 million pounds, translating to an approximate capacity of \$100 million in potential KonaRed consumer products revenue.
- To expand its distribution throughout the US, KonaRed teamed up with Splash Beverages Group, Inc. (SBG). The distribution agreement includes increases in sales and placement in key retail stores nationwide.

III. REVENUE SUMMARY:

	Nine Months Ended September 30,			
	2014	2013	Change	
Revenues	\$1,260,856	\$864,233	\$396,623	46%
Cost of Sales	\$238,095	\$322,825	\$(84,730)	-26%
Operating Expenses	\$3,190,622	\$947,839	\$2,242,783	237%

- Net sales for the nine months period ended September 30, 2014 is \$1,260,856 compared to \$864,233 for the nine months ended September 30, 2013. This represents an increase of 39% in comparative nine months product sales. The increase in sales can be attributed to key initiatives undertaken in fiscal 2014, including the strategic alliance with Splash Beverage Inc. which has expanded the distribution network.
- During the nine month period ended September 30, 2014 COGS were 81% of the sales, compared with 63% of the sales for the nine month period ended September 30, 2013. This corresponds to gross margin percentage of 19% percentage versus 47% for the comparative nine months periods. Higher COGS can be attributed to rush processing fees which were required to meet high demand from new major clients. As the order flow becomes steadier, COGS will decrease due to the economies of scale from larger production runs.
- A significant contribution factor in the relative period over period decrease in gross margin is that during fiscal 2014, the company has been phasing out its wholesale ingredients business. This phase-out was a component of patent settlement agreement with VDF that began in early 2014.

IV. FINANCIAL CONDITION:

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	September 30, 2014	December 31, 2013	December 31, 2012	2014 vs 2013	2013 vs 2012
Assets	\$1,382,102	\$640,705	\$180,754	\$741,397	\$459,951
Liabilities	\$95,298	\$276,957	\$844,685	\$(181,659)	\$(567,728)
Total Equity	\$1,286,804	\$363,748	\$(663,931)	\$923,056	\$1,027,679

- Net working capital increased from a balance of \$363,748 at December 31, 2013 to a balance of \$1,273,135 at September 30, 2014. This significant increase in working capital was supposed by January 2014 \$1,000,000 unit private placement, and \$1,700,000 raised from company's Equity Line.

V. COMPETITION:

- The beverage industry is extremely competitive. The principal areas of competition include pricing, packaging, development of new products and flavors, and marketing campaigns. KonaRed's product is competing directly with a wide range of drinks produced by a relatively large number of manufacturers. Most of these brands have enjoyed broad, well-established national recognition for years, through well-funded ad and other marketing campaigns. In addition, companies manufacturing these products generally have far greater financial, marketing, and distribution resources than KonaRed does.
- Important factors that will affect KonaRed's ability to compete successfully include taste and flavor of its products, trade and consumer promotions, the development of new, unique and cutting edge products, attractive and unique packaging, branded product advertising, pricing, and the success of the distribution network.
- Although KonaRed has the rights to use the necessary processing and manufacturing intellectual property relating to processing and manufacturing the Coffee Fruit, it does not own the manufacturing process for making the finished beverages. The company intends to aggressively assert its right under trade secret, unfair competition, trademark and copyright laws to protect its intellectual property. These rights are protected through the acquisition of partners and trademark registrations, the maintenance of trade secrets, the development of trade dress, and where appropriate, litigation against infringing these rights.
- The key element of KonaRed business advantage is the License it has been provided by VDF FutureCeuticals Inc. The license agreement has effectively formed a strategic alliance between KonaRed and VDF and eliminates competition and patent defense costs between the parties for rights to valuable proprietary R&D. The license agreement provides KonaRed with access to use of VDF's patent, as existing and/or modified in the future, along with the process, products, methods, compositions and know-how developed by VDF related to the patented Coffee Cherry-related inventions, trade secrets and know-how.
- A key to KonaRed growth is a sales and marketing agreement that executed with Splash Beverage Group (SGB). Since then KonaRed sales strategy is on extremely effective way by using SGB distribution lines within the United States. SGB providing an effective method for the expansion of KonaRed distribution in the near term and that distribution expansion is on track.

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VI. RECENT STOCK PERFORMANCE:



Source: Yahoo Finance

- Let's start with the fact that KRED became publicly traded in October, 2013. The company offered real products and has been generating revenues for years. It was the first of its kind, the product was unique, focusing on the health benefits of the coffee fruit, and strongly positioned to be the popular new drink at the right time. The volumes started to pick up the ticker and the price inched its way up. The movement wasn't explosive, but it seemed consistent which could suggest that investors are starting to pay attention to KRED.
- During April and May 2014, the stock was one of the most active stocks in the OTCBB market. The company, through its partnership with Splash Beverage Group and its Nevada distributor, Southern Wine & Spirits; announced that more than 20 Speedee Marts throughout Nevada have begun carrying 10.5oz KonaRed Original and KonaRed Green Tea. Speedee Mart is one of the leading convenient stores in the country.

VII. RECOMMENDATION & VALUATION

- KonaRed Corporation has a rating score of *Overweight/Buy*. The primary factors that have impacted this rating are the company's strengths that can be seen in multiple areas, such as its relative strength in developing new products, R&D as a percentage of sales and long term debt/equity ratios. It is worth stating that KonaRed is not a concept company, instead it is a value play. People at KonaRed are building the base for substantial returns over a period of years.

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- In assigning a price target to KonaRed we can consider the impressive 39% growth in revenue for the 9 month period over the prior 9 month period as well as a noticeable improvement in the Company's working capital position, both of which serve to improve KonaRed's financial strength and flexibility going forward. In consideration of improvements already realized and future expected improvements we are assigning a short term price target of \$0.60 per share and a long term (18-24 months) price target of \$1.20 per share. We also give consideration to the technical performance and likely oversold condition.

Sources:

1. KRED Form 10-Q, 04 November 2014.
2. KRED Form 10-K, 20 March 2014.
3. <http://www.konared.com/investor-relations>
4. <http://seekingalpha.com/symbol/KRED>
5. <http://www.bloomberg.com/quote/KRED:US>

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We rate enrolled companies based on the appreciation potential we believe their shares represent, and the "riskiness" we perceive in our ratings. The business results of those companies "NOT RATED" are often highly dependent on some future event, such as FDA drug approval or the option of a new key technology.

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EQUAL WEIGHT/HOLD	Equal-weight (E or Equal) - The stock's total return is expected to be in line with the total return of the relevant country Index or the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis over the next 12-18 months.
NOT RATED	Not-Rated (NR) - Currently the analyst does not have adequate conviction about the stock's total return relative to the relevant country Index or the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
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