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Workhorse Group, INC--*The Small Cincinnati Company* ***“Delivering” in the Electric Vehicle Race***

It is rare to find a company at the intersection of two major trends; it’s even more unusual that it is in your hometown. However, that is the case with the aptly named Workhorse Group, Inc. (ticker: WKHS) headquartered in Loveland, OH. Formidable Asset Management (“FAM”) recently established a position; following are the key pieces of our investment thesis:

- Established technology and infrastructure
- Marquee customers
- Undervalued investments

Overview

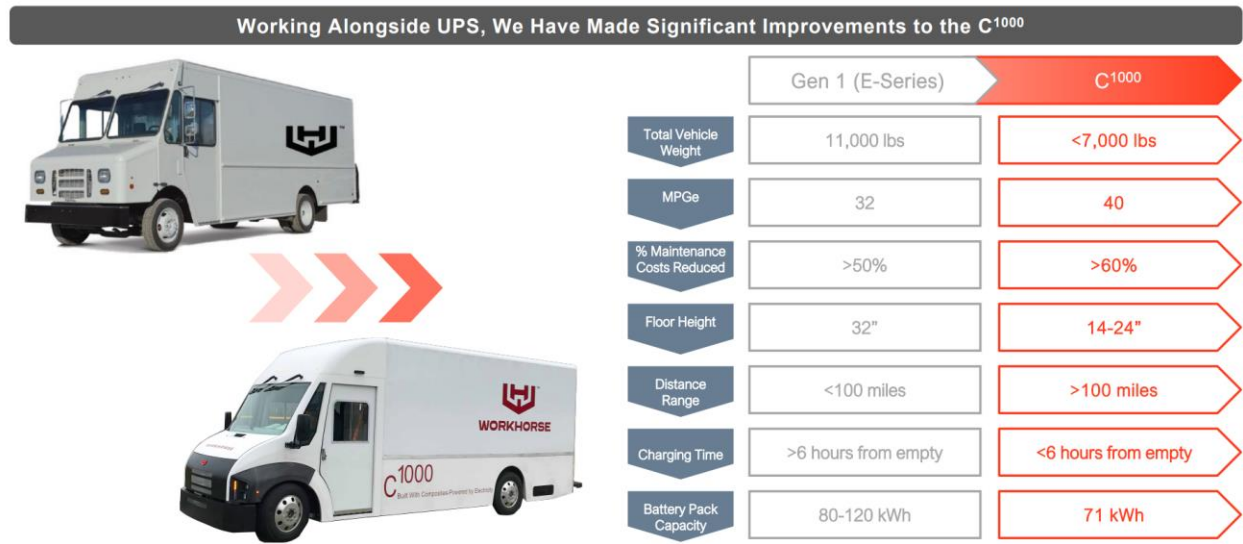
Workhorse manufactures electric vehicles (both land-based and aerial), predominantly for use in deliveries (think Amazon, UPS, or the U.S. Postal Service). Despite its presence in this attractive niche, valuable intellectual property, and potentially transformative strategic partnerships, the company trades at a significant discount to our estimate of its intrinsic value.

Established technology and infrastructure

The company builds more than electric vehicles; it has developed an integrated platform to offer clients a holistic delivery solution that includes cost efficient ground vehicles, telematics to optimize deliveries, and unmanned aerial systems (UASs) for last mile delivery. In the company’s opinion, it is a first mover with a two-to-three year head start over its competitors, which is critically important. Once established, it is very difficult to displace an incumbent within the context of a vehicle fleet, especially one that is integrated.

The company has seven (7) granted and four (4) pending patents. As we'll see later, some of Workhorse's core electric vehicle intellectual property is currently being licensed. Its Metron telematics are potentially valuable on a licensing basis as well.

The company is expected to deliver between 300 and 400 vehicles this year for its C-Series, which is the next generation of its core delivery vehicle. These vehicles are built at its Union City, Indiana assembly plant. The company collaborated with UPS on a redesign of the C-Series; UPS is invested in the success of the endeavor and has been a partner since 2012.



One facet of the companies many investors are underestimating is the value of having a sizable installed base, which requires service and maintenance. Think of the auto dealership model, where revenues go beyond the initial sale and become a perpetuity through the useful life of the vehicle; Workhorse has the potential for consistent revenue from this part of its business.

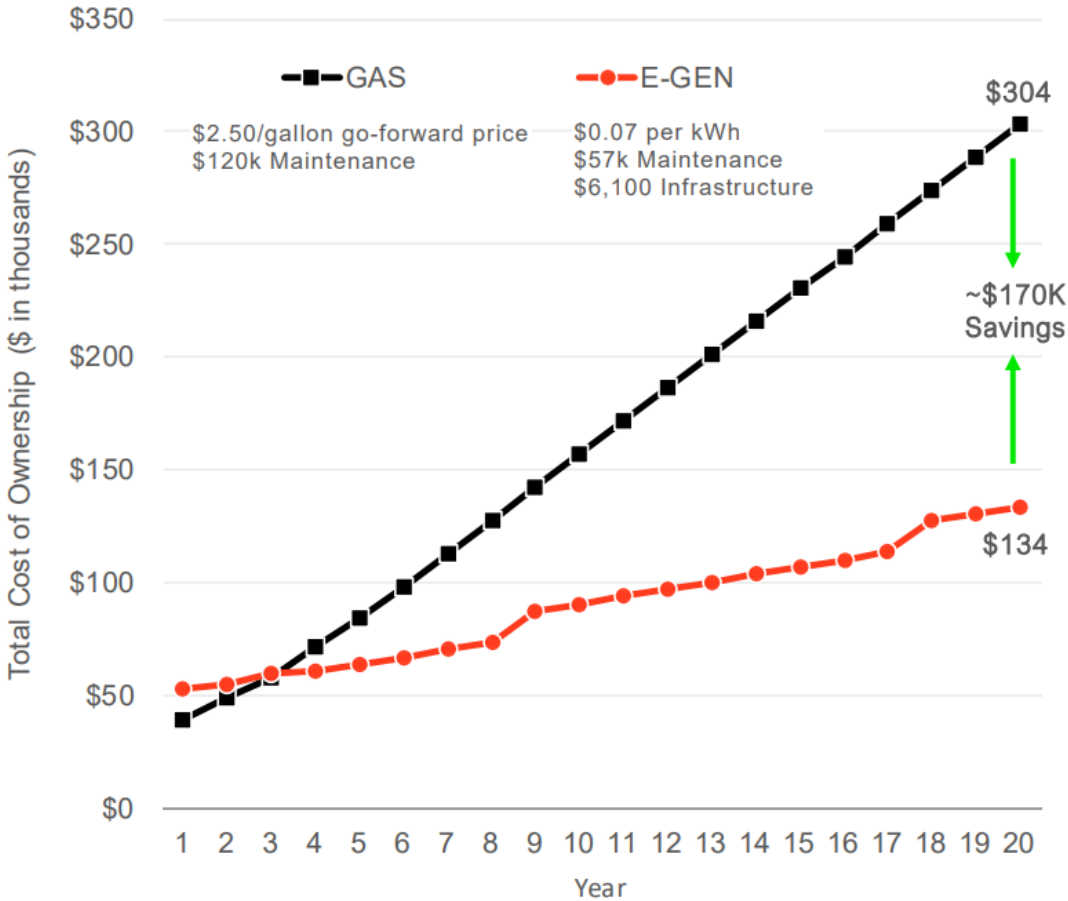
Marquee Customers

A key stamp of approval for the company is its client roster. Given the critical importance of last-mile delivery, companies like UPS, DHL, FedEx, and Ryder would not trust just anyone. With over 350,000 delivery vehicles purchased annually, the total addressable market (TAM) for Workhorse is exponentially larger than its current production levels. From the buyer's perspective, the payback period associated with the slightly higher initial cost of a Workhorse vehicle is short.

3 Technology validation from blue chip customers and partners

Positive Customer ROI in Three Years

Total Cost of Ownership Analysis



The next generation of products for the company is straight out of a science fiction novel from the 1950s, with unmanned drones, which it calls the HorseFly, that work with its land-based vehicles. This UAS is FAA compliant and the value proposition for clients is immense, with the cost per mile for the HorseFly around \$0.04 per mile versus around \$1.00 for traditional vehicles. Each UAS can carry up to 30 lbs at a speed of up to 50 mph.

The company is currently vying for a \$6 billion contract with the USPS, which would provide revenue visibility for five-plus years. While this would require \$200 million in capital (in the event the company won the entire contract), it would be transformative. Bids are due in July, with a decision expected in mid-October.


Undervalued Investments

The kicker for the company is its investment in Lordstown Motors Corp. (LMC). It is carried at a value of around \$12M on the company’s balance sheet, a pittance compared to WKHS’s market cap of over \$250M.



At one point, Workhorse was developing (and taking orders for) its own electric pickup truck. Management made a strategic decision to focus on its core delivery solution and instead licensed its intellectual property to LMC so the latter could begin development and production of an electric pickup truck, the Endurance. In exchange, the company received a 10% ownership stake in LMC as well as the opportunity for variable revenue consisting of commissions and royalties based on LMC’s productions, which are slated to begin this year, with delivery in 2021. Per LMC CEO Steve Burns, in a Detroit Free press article, “I think we’ll have well, well north of the 20,000 well spoken for. The demand side is super strong, I am starting to worry we won’t be able to make them fast enough.”

Lordstown Motors will License and Manufacture Electric Pickup Trucks Utilizing the W-15 Technology

State of the Art Safety & Driver Experience:



Workhorse W-15 Electric Pickup Truck

Lordstown Endurance Electric Pickup Truck

Lordstown Motors Partnership

Workhorse granted Lordstown Motors a license to the technology and design of the Workhorse W-15 pickup truck

Lordstown will be the sole manufacturer of the vehicles

The 6.2M sq-foot facility was purchased from GM and can produce up to 250,000 vehicles per year

Workhorse Highlights

- ✓ Workhorse will retain a two year, non-dilutable 10% equity stake in Lordstown Motors in exchange for the license of the technology
- ✓ Workhorse will receive a royalty fee for each electric pickup truck delivered by Lordstown
- ✓ Workhorse will no longer manufacture the W-15, allowing its manufacturing facility to focus solely on last-mile delivery vehicles

Work Ahead.

For those who think this is not a big deal, we would point to the recent IPO of Nikola Corp. (ticker: NKLA), which (as of 6/10/2020) traded at a market cap of \$23 billion on a pre-revenue basis, i.e., it, too, is taking orders for an electric pickup truck, which won’t be delivered until 2022, after the anticipated release of the LMC pickup. Electric vehicle manufacture Tesla Motors (ticker: TSLA) has a market cap of over \$190 billion on revenues of only \$25 billion for 2019.

In other words, this is a hot area for institutional investors, and even if LMC came to the market a valuation of \$3 billion, Workhorse’s stake in LMC would roughly equal the company’s current market cap, i.e., you would be getting the delivery solution business for free.

Conclusion

Ultimately, we believe the market has a tremendous appetite for electric vehicles, especially given investors’ increasing consideration of ESG (environmental, social, and governance) factors, not to mention the proliferation of investment products that focus on ESG companies. Both WKHS and LMC would certainly fit this bill. Even if LMC was seen as only half as valuable as NKLA in the eyes of the market, the company’s stake in LMC alone would be worth over \$1 billion.

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