CER Report

Nasdaq: REED

Update **August 19, 2009**

Reed's, Inc.

Consumer; Specialty Beverages

Rating:	**Speculative Buy** (Unchanged)
Recent Price:	**$2.16** (5/18/09)
Price Target:	**$5.25** (Unchanged)

MARKET DATA

52-Week High/Low	$3.29 - $0.75
Ave. Daily Volume (6-mos.)	8 K
Shares Outstanding	9.2 M
Inside Ownership	35%
Institutional Ownership	<1%
Float	6.0 M
Short Interest (% of float)	<1%

FINANCIAL DATA

Market Capitalization	$19.9 M
- Cash & Equivalents	$ 0.4 M
+ Preferred Stock	$ 0.5 M
+ Long-term Debt	$ 3.0 M
Enterprise Value	$23.0 M
Book Value	$3.8 M
Working Capital	$1.8 M
Dividend Yield	nil

Balance sheet figures pro forma as of 6/30/09

	SALES	NET LOSS	CFO	EPS
2007A	$13.1	($5.6)	($5.8)	($0.70)
2008A	$15.3	($3.8)	($2.5)	($0.43)
1Q09A	$ 3.4	($0.5)	($0.0)	($0.06)
2Q09A	$ 4.2	($0.9)	($0.7)	($0.10)
TTM	$14.8	($2.7)	($0.8)	($0.30)

Dollars in millions, except EPS; Fiscal year ends Dec.

VALUATION

Price/Sales	1.3 X
Price/CFO	Neg
Price/Trailing 12-mo. Earnings	Neg
Price/Book Value	5.2 X
Consensus EPS Estimate 2009	NA
Forward PE	NA
Consensus EPS Estimate 2010	NA
Forward PE	NA

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Reed's is an emerging producer of distinguishing non-alcoholic beverages and specialty candies and ice creams. It is the only commercial beverage producer in the U.S. to produce and market "brewed" ginger, root beer and cola products. The Reed's brand can be found on the shelves of specialty gourmet and natural food stores, such as Whole Foods, Wild Oats and Trader Joes as well as supermarket chains such as Ralph's.

HIGHLIGHTS

- **Quarter Results.** Reed's reported $4.2 million in total sales in the June quarter, resulting in a net loss of $800,000 or $0.10 per share. This compares to $4.6 million in sales in the prior year quarter, representing a year-over-year decrease of 9.7%.

- **One-time Charge.** Operating income was reduced by a one-time charge of $641,000 for impaired assets related to the sale and leaseback of the Company's buildings and brewery equipment in June 2009. Excluding this charge, we estimate the operating loss was $119,000 versus the reported operating loss of $759,000.

- **Strategic Growth Plans.** Reed's has several strategic plans underway that could impact sales and profit margins in the coming quarters. Reed's announced its intention to acquire the assets of Sonoma Cider Mill for approximately $250,000. The Company also plans to engage in private label beverage production, which could increase utilization of fixed plant.

- **Target Price and Valuation.** We reiterate our price target of $5.25. Our target implies a multiple of 3.2 times sales in the twelve months ending June 2009. In our view, this represents fair value for REED shares since it compares to the average metric of 3.5 times sales for the greater soft-drink beverage sector.

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OUTLOOK

Reed's management continues to block and tackle the natural beverage market during a particularly challenging economic period. June quarter sales were higher sequentially on seasonal factors, but failed to reach record levels set in the year-ago quarter when the Company was running a promotion of certain products. The net loss was deepened by a one-time, non-cash asset impairment charge related to the sale and leaseback of the Company's building and brewery equipment. While that transaction negatively impacted the bottom line in the quarter, in our view the Company's balance sheet was rendered substantially stronger. Despite a nominal increase in the debt-to-equity ratio, cash resources and working capital both doubled in the last six months.

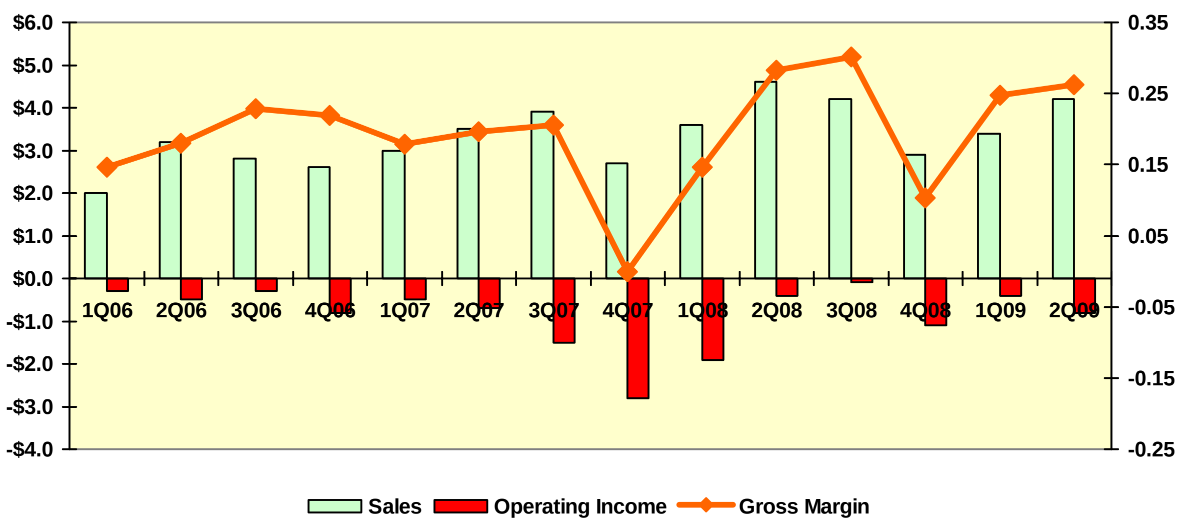
We reiterate our Speculative Buy rating on REED. Mixed news in the June quarter could require time for investors to fully digest. Consequently we expect a possible period of directionless trading for REED shares. If we are correct, the coming weeks could present an opportunity for investors with long-term investment horizons to accumulate REED shares at attractive price levels.

SECOND QUARTER 2009 RESULTS

Reed's reported $4.2 million in total sales in the June quarter, resulting in a net loss of $800,000 or $0.10 per share. This compares to $4.6 million in sales in the prior year quarter, representing a year-over-year decrease of 9.7%. Year-over-year comparisons are limited in valued given that the June 2009 quarter results were impacted by a one-time promotional event that increased sales volume for root beer "party kegs." However, the most recently reported quarter included 20% higher volume of 12-oz. products. This increased volume was offset by lower selling prices under promotional discounts.

Gross margin in the quarter was 26.1% compared to 24.8% in the March 2009 quarter and 27.8% in the year-ago quarter. Per unit costs declined in the quarter compared to the prior year following renegotiation of the Company's co-packing arrangements. Lower commodity prices also contributed to cost savings. Nonetheless, the gross margin was lower than the year-ago quarter in part due to a shift in the sales mix.

Chart I: Quarter Results Comparison



Source: Company Reports

Operating expenses totaled $1.2 million compared to $1.2 million in the March 2009 quarter and $1.7 million in the prior-year quarter. The 29.4% year-over-year decline in operating expenses resulted from changes in strategic direction for sales and marketing and a reduction in personnel. Operating income was reduced by a one-time charge of $641,000 for impaired assets related to the sale and leaseback of the Company's buildings and brewery equipment in June 2009. Excluding this charge, we estimate the operating loss was $119,000 versus the reported operating loss of $759,000.

Balance Sheet and Cash Flows

Operations used $657,000 in cash during the first half of 2009, compared to $2.4 million in the same period a year ago. The reduction in net cash usage was due primarily to cost and expense controls in production, sales and marketing, and administrative functions.

Cash at the end of the quarter increased to $421,000, as the Company restructured its balance sheet through the sale and leaseback of its California-based brewery building and equipment. Since the terms of the deal include an option to repurchase the assets at the end of the lease, it is being treated for accounting purposes as long-term financing rather than an outright sale. The $3.1 million obligation is included in long-term liabilities and is payable in nominal principal repayments over the next five years followed by a balloon payment in year six of $2.7 million. The interest rate is 9.9% payable monthly. As noted above the Company took a write down for impaired assets in conjunction with the sale and leaseback transaction. The agreed upon value was less than the carrying value at the time of the transaction. A total of $641,000 was charged to equity.

In tandem with this transaction, the Company also revised the terms of its revolving line of credit. At the end of June 2009, $563,000 remained available under a bank line of credit.

The debt-to-equity ratio increased to 0.80 from 0.40 at the end of December 2008. However, cash resources nearly doubled and working capital increased to $1.8 million at the end of June 2009. Inventory increased to $3.4 million from $2.8 million at the end of December 2008 largely in anticipation of the summer peak selling season. We expect to observe further improvements in working capital as seasonal increases in accounts receivable are reversed in the coming months. Accounts receivable increased to $1.4 million from $897,000 six month earlier. Inventory increased to $3.4 million from $2.8 million at the end of December 2008 largely in anticipation of the summer peak selling season. Accounts payable increased to $2.4 million from $1.9 million six months earlier.

STRATEGIC PLANS AND FUTURE RESULTS

Reed's has several strategic plans underway that could impact sales and profit margins in the coming quarters.

- Mid-June, Reed's announced its intention to **acquire the assets of Sonoma Cider Mill** located in Healdsburg, California for approximately $250,000. The deal could provide Reed's with new production capacity.
- The Company plans to engage in **private label beverage production**, which could increase utilization of fixed plant and ultimately improved profit margins. According to Market Research, by 2010, 27.4% of all soft drinks sold will be under private labels. Private label soft drink manufacturers remain a threat to branded soft drinks manufacturers and will continue to do so in the coming years. We see Reed's plans to enter the private label market as a net plus for future growth. We believe it would allow the Company to participate in the fastest growth segment of the business while continuing to capture its own market share for its unique beverage brands that may be less susceptible to encroachment by private label brands.
- Reed's sales and marketing strategy has been further refined to **focus on improving product placement** among the 10,500 mainstream supermarkets and natural food grocers that now carry the Company's brands. The net effect should be higher same store sales at a lower per unit marketing cost.

- **Raw materials supply negotiations** could result in additional cost savings. The Company expects material savings in the coming quarters from new glass bottle supply arrangements.
- The Company plans to **continue promoting its *Elixer* natural energy drink**. According to Market Research, sports and energy drinks saw an increase of 47% in product launches between 2004 and 2007. This is a result of the trend for health and wellness drinks that provide sustainable energy. We do not observe a reversal in this trend and expect the Company's *Elixer* product to contribute more meaningfully to the top-line in the coming quarters.

Reed's strategic plans are expected to unfold during a period in which consumers appear to be more receptive than ever to natural drink options. In our field work we recently learned that demand for a sustained natural energy boost is driving a shift in soft drinks from stimulants (i.e. Red Bull) to a more sustainable energy enhancement. Consumers are becoming more experimental and as such are demanding new and exciting flavors in their soft drinks. We believe Reed's entire product line could be a beneficiary of these trends.

We note that interest expense increased to $114,000 in the June quarter compared to $50,000 in the same period a year ago. We expect interest expense near $100,000 per quarter going forward as the Company pays interest on its leaseback obligation.

VALUATION

We reiterate our price target of $5.25. Our target implies a multiple of 3.2 times sales in the twelve months ending June 2009. In our view, this represents fair value for REED shares since it compares to the average of 3.5 times sales metric for the greater soft-drink beverage sector.

The Company has made progress in building up internal controls and reporting practices. The accomplishment should have a positive impact on valuation going forward as the discount for uncertainty is no longer required.

A review of historic trading patterns in REED shares suggests a level of support/resistance has developed at the $1.75 and $2.25 price levels. REED shares briefly pierced the $2.25 price level two times since the sell-off in U.S. equity markets beginning in Fall 2008, and traded down to but did not fall through the $1.75 price level during the trading sessions leading up to the June quarter results announcement. Thus we believe there is support in historic trading to limit downside risk from the current stock price to 15% at the $1.75 level as well as precedent for rising above the resistance level at $2.25.

Exhibit I: Stock Price Chart

Source: Stockcharts.com

Table I: Historic Sales and Earnings (dollars in thousands except per share earnings)

Dollars in Thousands Except EPS	2006	2007	2008	1Q08	2Q08	1Q09	2Q09	TTM
Sales	10,484	13,059	15,277	3,564	4,571	3,417	4,214	14,773
Cost of sales	8,427	11,040	11,891	3,044	3,301	2,570	3,114	11,230
Gross profit	2,057	2,019	3,386	520	1,270	847	1,100	3,713
Selling expense	1,352	4,587	3,817	1,124	1,051	659	548	2,849
General & admin. Expense	2,187	2,621	3,140	1,330	660	603	670	2,423
Other expense	325	300	-	-	-	-	641	641
Income from operations	(1,807)	(5,489)	(3,571)	(1,934)	(441)	(415)	(759)	(2,052)
Net interest income (expense)	(407)	(62)	(243)	(56)	(50)	(83)	(114)	(334)
Income before taxes	(2,214)	(5,551)	(3,814)	(1,990)	(491)	(498)	(873)	(2,322)
Provision for taxes	-	-	-	-	-	-	-	-
Net income	(2,214)	(5,551)	(3,814)	(1,990)	(491)	(498)	(873)	(2,322)
Preferred dividend	(29)	(28)	(24)	-	(24)	-	(23)	(23)
Net income for shareholders	(2,243)	(5,579)	(3,838)	(1,990)	(515)	(498)	(896)	(2,346)
Diluted earnings per share	($0.41)	($0.70)	$0.43	($0.23)	($0.06)	($0.06)	($0.10)	($0.26)
Wtd shares outstanding	5,523	8,009	8,884	8,765	8,911	9,041	9,119	9,045
SELECTED MEASURES:								
Sales growth, yr/yr	10.7%	24.6%	17.0%					
Net income growth, yr/yr	168.0%	150.7%	-31.3%					
EPS growth, yr/yr	127.8%	70.7%	-161.4%					
Gross margin	19.6%	15.5%	22.2%	14.6%	27.8%	24.8%	26.1%	25.1%
Operating margin	-17.2%	-42.0%	-23.4%	-54.3%	-9.6%	-12.1%	-18.0%	-13.9%
Net margin	-21.1%	-42.5%	-25.0%	-55.8%	-10.7%	-14.6%	-20.7%	-15.7%
Direct costs as a % of sales	80.4%	84.5%	77.8%	85.4%	72.2%	75.2%	73.9%	76.0%
SG&A as a % of sales	33.8%	55.2%	45.5%	68.9%	37.4%	36.9%	28.9%	35.7%

Source: Company reports and Crystal Equity Research measures

Table II: Historic Balances (dollars in thousands)

	12/31/2005	12/31/2006	12/31/2007	12/31/2008	6/30/2009
Current assets					
Cash and equivalents	27	3,220	743	229	421
Accounts receivable	535	1,184	1,161	897	1,356
Inventory	1,208	1,511	3,028	2,837	3,375
Prepaid expenses	74	164	77	68	178
Other current assets	11	25	16	-	-
Total current assets	1,855	6,104	5,025	4,031	5,330
PP&E	1,886	1,795	4,249	4,133	3,431
Other long-term assets	1,171	814	814	939	1,612
Total assets	4,912	8,713	10,088	9,103	10,373
Current liabilities					
Accounts payable	1,645	1,695	1,997	1,929	2,372
Lines of credit	1,446	1,356	-	1,354	974
Current portion of long-term debt/financing	169	72	27	16	19
Accrued liabilities	190	146	58	96	141
Total current liabilities	3,450	3,269	2,082	3,395	3,506
Long-term debt, less current portion	1,313	821	766	1,747	3,022
Stockholders' equity					
Preferred stock	589	589	481	471	466
Common stock	1	1	1	1	1
Common stock in reserve	29	-	-	-	-
Paid-in-capital	2,789	9,535	17,838	18,408	19,691
Retained earnings (deficit)	(3,259)	(5,502)	(11,081)	(14,919)	(16,313)
Stockholders' equity	149	4,623	7,239	3,961	3,845
Total liabilities and equity	4,912	8,713	10,087	9,103	10,373
SELECTED MEASURES					
Working capital	(1,595)	2,835	2,943	636	1,824
Debt to equity	9.90	0.20	0.10	0.40	0.80
Productivity measures					
Growth in sales	5.5%	10.7%	24.6%	0.0%	0.0%
Growth in inventory		25.1%	100.4%	-6.3%	19.0%
Growth in accounts receivable		121.3%	-1.9%	-22.7%	51.2%

Source: Company reports and Crystal Equity Research measures

Table III: Historic Cash Flows (dollars in thousands)

	2004	2005	2006	2007	2008	1H09
Cash flows from operations						
Net income	(479)	(826)	(2,214)	(5,551)	(3,814)	(1,371)
Depreciation & amortization	97	119	156	205	355	239
Provision for amounts due from director	153	124	3	-	-	-
Stock compensation expense	-	-	6	425	536	352
Write-off of note receivable	-	-	-	300	-	-
Loss on disposal of equipment	-	-	-	-	5	-
Impairment loss on assets						641
Working capital changes	53	540	(954)	(1,185)	450	(518)
Net cash provided by operations	(176)	(43)	(3,003)	(5,806)	(2,468)	(657)
Cash flows from investing activities						
Capital expenditures	(204)	(182)	(65)	(2,650)	(191)	(1)
Other investments	(44)	(33)	-	(300)	-	
Net cash used by investing activities	(248)	(215)	(65)	(2,950)	(191)	(1)
Cash flows from financing activities						
Proceeds (payments) on debt, net	673	400	(403)	(100)	970	1,278
Proceeds (payments) on line of credit			1,081	(1,356)	1,354	(380)
Proceeds from issuance of equity	-	197	7,005	7,626	-	150
Proceeds from issuance of warrants	-	-	-	165	-	
Decrease (increase) in restricted stock	-	-	(2,752)	1,580	-	
Offering costs	(220)	(333)	(252)	(55)	(179)	(100)
Other	-	(21)		-	-	
Net cash from financing activities	453	243	4,679	7,860	2,145	948
Cash and equivalents, beginning of the year	13	42	27	1,638	743	229
Cash and equivalents, end of the year	42	27	1,638	742	229	421
Selected Measures:						
Free cash flow	(380)	(225)	(3,068)	(8,456)	(2,659)	(658)
Conversion ratio (CFO to sales)	-2.0%	-0.5%	-28.6%	-44.5%	-16.2%	-4.4%

Source: Company reports and Crystal Equity Research measures

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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 under Analysts above 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.

CER REPORT RESEARCH UNIVERSE*

Speculative Buy	2	50%	Unproved business model; catalysts exist to generate higher returns
Accumulate	1	25%	Long-term return potential above 10%; near-term catalysts may not exist
Hold	0	0%	Total return potential below 10%; an acceptable long-term holding
Sell	0	0%	Potential return greater than negative 10%; take profits or stem losses
Not Rated	1	25%	No rating
Total	5	100%	

**Research universe categorized by rating only; Crystal Equity Research provides no investment banking services.*

HISTORICAL RECOMMENDATIONS AND TARGET PRICE: Reed's, Inc. / REED

Report	Date	Price	Rating	Target Price
Initial	4/24/08	$2.85	Speculative Buy	$5.25
Update	5/22/08	$2.40	Speculative Buy	$5.25
Update	8/21/08	$2.95	Speculative Buy	$5.25
Update	11/14/08	$1.59	Speculative Buy	$5.25
Update	4/1/09	$0.99	Speculative Buy	$5.25
Update	5/14/09	$2.12	Speculative Buy	$5.25
Update	8/19/09	$2.16	Speculative Buy	$5.25

DISCLOSURES

Name	Symbol: Exchange	Disclosures
Reed's, Inc.	REED: 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. Subscription fees for CER Research Coverage 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.

**An agent of Reed's, Inc. has sponsored research coverage of REED. The agent provided investment banking and advisory services to Reed's, Inc. in the past and may again provide such services to Reed's, Inc. in the future.*

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST. Inquiries may be made by telephone at **212-400-7519**, by electronic message to **info@crystalequityresearch.com** or by mail to **1040 Avenue of the Americas, Floor 24, New York, NY 10018**. Additional information about Crystal Equity Research is available at the firm's web site at **www.crystalequityresearch.com.**
