EASTSIDE DISTILLING, INC.
(NASDAQ: EAST)

EASTSIDE DISTILLING

First Quarter Fiscal Year 2019 Financial Results Conference Call

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CORPORATE PARTICIPANTS

Grover Wickersham – Executive Chairman, Eastside Distilling, Inc.
Steve Shum – Chief Financial Officer, Eastside Distilling, Inc.
Robert Mandfredonia – President, Eastside Distilling, Inc.
Robert Blum – Managing Partner, Lytham Partners

PRESENTATION

Operator
Good morning, and welcome to the Eastside Distilling reports First Quarter Fiscal Year 2019 Financial Results Conference Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question you may press star, then one on your telephone keypad. To withdraw your question please press star, then two. Please note this event is being recorded.

I would now like to turn the conference over to Robert Blum with Lytham Partners. Please go ahead.

Robert Blum
Thank you, Andrea. And good morning, everyone, and thank you for joining us today to discuss Eastside Distilling's financial results for the quarter ended March 31, 2019, as well as management transition. I am Robert Blum with Lytham Partners. I will be your moderator for today's call. Earlier, Eastside issued their first quarter 2019 results in a press release, as well as issued their 10-Q. Joining us on the call today to discuss these results are Grover Wickersham, Robert Manfredonia, and Steve Shum. Following their remarks, we'll open the call to your questions.

Before we begin with prepared remarks, we submit for the record the following statement. Certain matters discussed on this conference call by the management of Eastside Distilling may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and such forward-looking statements are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements describe future expectations, plans, results, or strategies, and are generally preceded by words such as: may, future, plan or planned, will or should, expected, anticipates, draft, eventually, or projected. Listeners are cautioned that such statements are subject to a multitude of risks and uncertainties that could cause future circumstances, events, or results to differ materially from those projected in the forward-looking statements.

Such matters involve risk and uncertainty that may cause actual results to differ materially, include, but are not limited to, the company's acceptance and the company's products in the market, success in obtaining new customers, success in product development, ability to execute its business model and strategic plans, success in integrating acquired entities and assets, ability to obtain capital, ability to continue as a growing concern, and all the risks and related information described from time to time in the company's filings with the Securities and Exchange Commission, including the financial statements and related information pertaining to the company's annual report on Form 10-K for the year ended December 31, 2018 filed with the Securities and Exchange Commission on March 28, 2019. Now, I'd like to turn the call over to Grover Wickersham, Executive Chairman of Eastside Distilling. Grover, please proceed.

Grover Wickersham
Thank you very much, and good morning, Robert, and good morning to all of you. I'd just do a shout out to the Eastside employees that are on the call, most of whom are also shareholders, and I know we've got a lot of them on the call today, too. So, let me just launch into our financial recap.

We completed the acquisition of Craft Canning + Bottling during a historically slow quarter for that business, and obtained results that surpassed our internal projections and contributed more than $1.4 million in revenue during the quarter. Craft has taken over a lead role in increasing production efficiencies across the board with all of our products, and is surpassing expectations for an integration of the two businesses. As we'll talk about later we're getting some very, very good efficiencies in our production, which are going to be flowing through the cost of goods sold in Q2 and Q3.

Also, we accelerated authorizations of Redneck Riviera Whiskey in some of the country's largest retailers, including Kroger, Fred Meyer, QFC, Albertsons, VONS, Pavilions, Safeway, Walmart, Winn-Dixie, Jewel-Osco, Binny's, Meijers, WinCo, and many others.

Overall this quarter, we shipped 6,000 cases of Redneck Riviera, and very few of those cases include the above-mentioned authorization. In Oregon, we maintained, this quarter, 50% year-over-year organic growth in case sales. We also launched a major advertising program to invest in our Burnside brand. And I'm very, very happy about the momentum that we have going in Oregon.

I just mentioned that last month we did a largest ever month of our flagship Portland Potato Vodka, and it seems like it's gathering momentum every month, and our whiskeys are growing 5% to 10% sequentially every month this year. So I really feel this momentum is building, and will continue to build.

We expanded our operations into some new high-growth categories, including RTD cocktails, which we canned on our own equipment, and that was with our launch of the new Portland Mule, and our initial introduction into the CBD beverage market is also on the brink right now.

Overall, on a comparable basis, our sales grew by 161%, to $3.7 million, and again, this is during a historically slower quarter for our business and for Craft. This surpassed our original Q1 expectations, and I believe it's safe to say that surpassed those on the street. I could not be more proud of the team's execution during the first quarter of 2019.

I'd like to talk a little bit myself personally, and we can spend a couple minutes on that. But as many of you are aware, I recently became involved in Eastside, originally as an investor, and this was back in 2016. In those days I was captivated by — with Mel and Steve, and the other great people on the team had in terms of a product base, and I saw a lot of potential in it.

In the end of 2016 when I became CEO, I put forth, as a company policy and with the board, a three-point strategy to, first of all, create the scalable platform that will allow the company to benefit from a so-called brand factory approach to development of new products in partnership with the leading branding firm, Sandstrom, also based in Portland.

Secondly, I wanted to maintain, build a cash generating business in Oregon with the large number of product offerings that we have across the board, and the solid co-packing business to take advantage of other things, very solid wine canning growth in the Pacific Northwest. And then finally, make use of our public company status to make accretive acquisitions.

One of the first moves we made as a company at that point was to bring on Sandstrom Partners to create high-level branding that reflected, on the outside of the bottle, the tremendous product I believe we have on the inside. We also looked to expand our production capabilities to meet the growth demands that we believed we could create, and we also made strategic acquisitions, including Motherlode in 2017, which got us into our current Milwaukee location, Milwaukee, Oregon, and now recently the Craft Canning + Bottling acquisition to greatly expand our co-packing capabilities, as well as I alluded to, increase our own manufacturing efficiencies with our core products.

We also expanded the product portfolio, including the acquisition of Big Bottom Distilling. We reached an agreement with country music star John Rich to develop Redneck Riviera Whiskey, and that's gone on to become one of the most successful first year product launches for a craft spirits brand.

More recently, we leveraged these integrated capabilities of product development, branding production, and distribution so that we can enter the high-growth RTD and CBD markets. I just mentioned regarding RTD and the CBD markets, we're relying very heavily, as you can imagine, on our relationship with Sandstrom, and they've created the product we refer to as Outlandish.

Importantly, I think we have a very strong and deep management team. We have Tom Wood, who's done a great job in production. We have the Craft distilling crew with Owen Lingley heading that up as Chairman of Craft Canning. We have Mel Heim, Travis Schoney, two of the best distillers in the industry. On the sales side, obviously, Robert Manfredonia is leading on the sales side, but we have a good team underneath him. And then we have Steve Shum, who has really been my right-hand guy during this whole process, and will continue to be.

So anyway, I believe that we have a great team in place. We can execute and drive operating efficiencies and performance, and help take Eastside to the next stage of its evolution. We're conducting a search to identify a CEO with a solid industry background, and we already have candidates in that department. And me staying in my role as Executive Chairman, I'll remain focused on the key strategic opportunities, including the rollout of our CDB initiative.

Just a couple more words on the CBD initiative, because I think that consistent with our philosophy on CBD, we've been very conservative about not getting ahead of our skis and announcing things as future developments, so I'll just say where we are right now. We've been sampling product in Oregon. Our initial feedback is excellent. We hope to have the production details dialed in very, very quickly, and I hope to have more news coming in that area. Our goal on that product, just for those of you that are coming in late to the discussion of Outlandish, this is a CBD product in the 187 can. That's kind of a wine glass size can, and it's designed to go through our existing channels of distribution nationally and locally. Our initial strategy is to take advantage of the laws in Oregon. Oregon legalized CBD in 2014, and because of current FDA regulations, we're not planning to go outside of Oregon at this time. But our plan is to gear up so that when the expected flood gates open for having products with CBD available throughout the country, our goal is to create a product that would be appealing to our existing distributor, and other distributors that sell to on premise alcohol establishments, and also liquor in convenience stores. So it's designed to be a mixer-type product that would be served with alcohol, or it could be standalone, and we have three initial iterations of that, that all three of which I expect us to be shipping this for.

So, with that, I'm going to turn to Robert, and Robert Manfredonia will drive further into the progress we're achieving with Redneck, and also touch on our other Oregon-based brands. Robert?

Robert Manfredonia
Thanks, Grover, and good morning, everyone. As Grover stated, I'll be adding some additional details off of Grover's remarks, because I think it's important to provide additional detail, and let's get right to it.

Quarter one, Redneck Riviera, our internal plan for quarter one was 6,250 cases, we finished slightly above plan at 6,320 cases. General market update, and we have not communicated on previous calls our focus in progress in this all-important area, but as we move forward we will be providing an update.

So the latest information in this channel, we have now secured distribution in most of the larger retailers across the country, including Hi-Time's Liquor in Southern California, Yankee Spirits in Boston, Kenwood in Chicago, Argonaut in Denver, just to name a few.

Quarter one, on premise account buys were 91% above buying accounts in the fourth quarter of 2018. New distribution in regional and state chains include Twin Peaks, in 80 stores in 25 states; Coyote Ugly and Ford's Garage in all Florida locations. Also, Redneck has created a light and refreshing signature cocktail called the Saddle Up. You'll find the Saddle Up in selected menus across the country, and there'll be more to come. All of this is due to a concerted effort by the national sales team that continue to improve brand awareness and promote sampling.

Last call we announced regarding national corporate off-premise accounts that we will be adding 2,150 new points of distribution by the end of May. We will slightly exceed that by 303 points of distribution. Redneck Riviera is now confirmed in 2,453 corporate accounts, just for the first trimester of the year. We announced on 5/9 that Redneck Riviera is mandated in 856 Walmart stores in 17 states. The exciting news is that this new distribution was achieved in large part due to the current distribution of 350 stores exceeding the Walmart internal rate of sale performance expectation. So, existing distribution validates future decisions, and in part because we exceeded their plan, they provided us an additional 856 incremental points of distribution. We will be shipping, initially, two full cases to all 856 stores by June the 2nd.

On our previous call, we announced the release of Redneck Riviera 175 for April 1st. To confirm, we released the last week of March. The early market response has exceeded our 2019 expectation. In fact, we will be announcing a very large account authorization in the near term by the end of the month, in fact. The opportunity in the market continues to grow for the 175 size. This, in part, is driven by an increasing size by our consumers.

Pivoting to non-Redneck related brands, Grover mentioned the Oregon performance. Quarter one finished 51% over quarter one of 2018, and we're on track to exceed our 2019 volume objective. Burnside Whiskey and Bourbon entering into California was announced on Friday, May 10th. This is our first non-Redneck-related brand on to the national platform. This is consistent with our platform strategy to gateway other brands off of the accelerated development and performance of Redneck on to the national and regional markets. Burnside will continue to expand to other key markets in the coming months. There'll be other brands to follow originating from our existing portfolio, or new product development, or through M&A.

In closing, we will be announcing other substantial new distribution confirmations later this month, or in the early part of June.

And I'll turn that over to Steve.

Steve Shum
Thanks, Robert. Before running through the numbers, I'd like to thank Grover in helping bring the organization to its current state, and working to put the foundational pieces in place that position the company with a solid platform for future success. With Grover's desire to evolve his role in the company, I agreed to assume the CEO title on an interim basis, and look forward to working with and supporting the board's efforts to identify a permanent, long-term industry expert to fill the role.

I would also like to take a quick moment to make mention of Richard Wolf. Richard is an industry veteran, and has been actively consulting and working with the company over the past few months. Richard was formerly the Vice President, General Manager at Sazerac Buffalo Trace Distillery, maker of Pappy Van Winkle, where he helped lead a massive growth effort during his tenure. Richard is working closely with us as a senior consultant in all areas of the business, and we may consider him for a more permanent role in the future, but we recognize the fact that he has other obligations and logistics to contend with first. Either way, we are thrilled to have Richard's involvement, advice, consultation, and active participation in our operations.

With that, I'll review the numbers. For the first quarter 2019, gross sales totaled approximately $3.7 million, compared to $1.4 million in 2018. Net sales, which exclude the excise taxes and customer incentives, increased 187%, to $3.5 million, versus $1.2 million in the prior year. For the period, we sold 270,447 cases overall. This consisted of 12,091 cases of our branded products, and 258,356 cases of co-packaged product. The case volume reflects an increase of 76% over the prior year in our branded products. The dramatic increase in co-packing in the quarter, compared to just under 1,500 cases last year, was enhanced by the recent acquisition of Craft, which added a substantial operation to this side of the business in the period. As we had anticipated, the addition of Craft also contributed to an increase in volumes within our motherload of co-packing operations.

From a revenue standpoint, wholesale revenues grew by approximately 94% in the period over the last year. That success was driven by was Redneck Riviera Whiskey, as well as continued strong increases in wholesale traction within the Pacific Northwest, especially with our Vodka and Burnside lines.

Revenues derived from our retail and special events operations were approximately $225,000, which represented a 26% decrease from a year ago. As we have mentioned on a number of occasions, we've made decisions to reduce certain unprofitable event activities, along with targeting a more focused retail approach.

Overall, the average case sale price for the branded products, inclusive of wholesale and retail for the period, was approximately $140 in the quarter. Revenues from co-packing jumped to nearly $2 million, representing a 467% increase. The addition of Craft this quarter contributed just over $1.4 million of that dollar increase. Gross profit for the period totaled approximately $1.18 million, compared to $592,000 in the prior year. Gross Margin relative to net sales was 34%, versus 49% last year. While the mix of business was much different this year than last year, the margin in the first quarter of this year was also lower than we expected to be in the upcoming quarters, as we anticipate higher volumes and improved efficiencies in our now larger production facilities.

Advertising, promotional, and selling expenses for the period increased to $1.33 million, up approximately 107% over last year. As we had noted throughout 2018, we ramped our investment spending on key brands, and made strategic decisions to ramp our marketing efforts and support the more rapid and planned geographic expansion of Redneck Riviera Whiskey. We also feel that this substantially helped develop our platform, and positions us for long-term success, particularly as we work to expand other key products both regionally and nationally.

Equally important as we move forward, we expect to see improved efficiencies with the anticipated growth, and our ability to leverage the infrastructure now in place. G&A expenses for the period totaled $2.68 million, an increase of 121% from last year, which was a result of additions to key personnel in order to support our larger footprint, similar to the point on advertising, selling, and marketing costs. However, we also incurred a number of one-time expenses in the period, part of which related to the Craft acquisition.

Net loss for the period totaled approximately $2.9 million, or $0.32 per share, compared to a net loss of $1.3 million, or $0.27 a share last year. Our adjusted EBITDA during the quarter was a loss of approximately $2.2 million, which compared to a loss of $780,000. We ended the period in a strong working capital position. Cash at the end of the quarter totaled $4.2 million. Inventories totaled just over $11 million. We also saw a large amount of the business close in the final weeks of the quarter, both for our branded and co-packing activities, which caused us to end the period with just over $1.8 million in receivables. The bulk of those receivables turned within a 45 day period. We closed the year with a positive working capital position of $15.2 million.

I would like to take a minute to run through a couple of the key numbers as they compare to our internal goals we set for ourselves going into the quarter. In terms of gross sales, we came right in line with a $20,000 higher figure than our internal forecast. Gross profit was off by $94,000 from our goal. This was almost entirely due to the production efficiencies we mentioned. Our EBITDA loss was $572,000 higher than our internal plan. A major portion of that, nearly $500,000, was related to the one-time costs we do not expect to repeat, with the balance being those production and efficiency that affected the gross profit. So, on balance, we feel good about how we performed versus our internal goals.

We had very high, or maybe better classified as exciting expectations for ourselves, and our internal goals for the balance of this year. Business is good, and we believe we can start driving improved efficiencies with our existing infrastructure as we further ramp the top line. The co-packing business is surging currently as they have entered their heavy busy season, and we are operating at full capacity, working quickly to bring additional capacity online. And the branded business continues to be strong in its key areas. We look forward to reporting our upcoming progress.

That concludes the financial highlights for the quarter. Further details are available in our 10-Q. And with that, I think we'll open it up for questions.

QUESTIONS AND ANSWERS

Operator
We will now begin the question-and-answer session. To ask a question, you may press star then one on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. At this time, we will pause momentarily to assemble our roster.

And our first question comes from David Bain of ROTH Capital. Please go ahead.

David Bain
Thank you. First, Grover, congratulations on your execution of CEO and transition. I know we look forward to analyzing your continued leadership as Executive Chairman.

I think our first question, this would be for Robert, I was hoping to follow up on Burnside’s moving to California through the platform that was built. We look at that as a pretty big milestone, and I'm wondering how we should think about the Burnside rollout in terms of — I don't know how you want to capsulate it, but additive cases, perhaps, in the national rollout. I understand some of this may be more art than science, but if you can kind of give us a sense as to what Redneck has built, in terms of the opportunity, and then look at the Burnside opportunity.

And then related to that same question, how we should think about the rollout differences with other brands that may go through the system, like the RTD, with Redneck, or wholly-owned lines that may come on line going forward.

Robert Manfredonia
Thanks, David. Your first question was on what's the anticipated potential volume of Burnside, and to be quite frank, I don't have that yet. I don't have that yet. But if you want to look at it in the larger context of what we're trying to do, Redneck, we spent last year developing the Redneck portfolio, and really sort of the infrastructure of the brand, which built the platform that you mentioned. It's in 46 states now, plus DC. The way that we see Burnside is, it's not going to be a 46 state type of brand, right, it's a Craft brand. It's going to be a large metro focus sort of brand. So, going into California, with Los Angeles and San Diego, and obviously San Francisco, we're going to focus a little bit differently on that brand than we do with sort of Redneck, which is a suburbia rural type of brand in a general way. Okay?

So, but what we see very exciting about Burnside is: one, all of the accolades that the brand has won; two, craft whiskey and bourbon is extremely, extremely hot at this point in time. In fact, one of the areas in which we think we can grow is the rye area. Rye is one of the fastest growing sub-segments in the whiskey category, and Burnside Rye is a double gold-winning product at the right price point. So we think we can scale that up in four-to-six markets very quickly. So I didn't answer your question direct, but I wanted to give you sort of the context of how we see Burnside.

And then the second part of the question is, as you said, the platform is really, really important. We've said to the market that the gateway effect is really part of our strategy, and that's what we're going to be doing over the next couple of months. It may be an RTD, and maybe it could be something that we see from a transactional standpoint, consumer behavior standpoint, intel from retail and from distributors, and we'll develop it on our own, or it'll be something that we may have in Oregon, be it way away that potentially can go out. We're still finalizing sort of the way that's going to look and feel. But that's going to be a big part of where as we nationalize and scale up a lot of the items we have, or we can develop, or we will acquire as we move forward.

So hopefully I answered your question enough without giving you a final answer on what I think the volume is going to be.

David Bain
No, that's great, that's a lot of color. Thanks, Steve. Steve, I guess I'm trying to capsulate current cash. If we could, so essentially, near-term receivables are close to $2 million, so if we're closer to $6 million prior to 2Q results, I guess that's how we should look at. And then, could we get a sense as to the $11.6 million of inventory you mentioned at cost. I mean, can you maybe opine to the true value, and, I mean, how liquid — no pun intended — how liquid that inventory actually is?

Steve Shum
Yes, I mean, if you look at the breakdown on inventory, a significant portion of it is in raw material, which means a lot of it is still in bulk form in barrels, and when it's in that form it is — no pun intended -- highly liquid in the market place. The other dynamic, a lot of that is obviously the brown spirits, and brown spirits generally show a trend that, as they get older they do improve in value, sometimes fairly substantially. So obviously, we keep all of our inventory held at cost, but we certainly have inventory in there that should have a higher street value than what we originally paid for as it is ageing.

So, like I said, it's over $10 million in the raw format and in the bulk spirits, and like I said, a big significant portion of that is the brown spirits. And I would also make note that we even have some inventory deposits out, probably a little over 400,000 worth in our prepaid, so the inventory is actually even a little bit higher, but nonetheless, we have a very strong inventory position.

We may whittle that back a little bit in the next quarter or two, just to be able to have inventory also as a source of cash, just let it bleed down a little bit. Of course, part of our long-term goal, as everybody knows, is we want to continue to maintain strong inventory balances, and ultimately grow them for our future, which is important as we build out key products like our single malt program, now that the new still is up and running. So that'll be an important dynamic longer term, is to continue to actually build inventory, but for the next quarter or two, we might bring that back down a little bit.

Grover Wickersham
Dave, I'm just going to jump in real quick and make just a quick add to that, is that I was actually kind of the lead guy on acquiring inventory, and if you recall, back when we did our uplisting, the focus was Burnside. So we acquired an awful lot of aging Bourbon, and like Steve said, that's a liquid market. And with the emphasis on Redneck, where incidentally, where again, we acquired a whole lot of new still, and we're really in a currently really good position right now with our Redneck Whiskey inventory. But because we really focus on Redneck, we have a bourbon that aged that we're not really taking full advantage of.

So, Richard Wolf, one of the things he's done, which is very helpful, is like when he was running Buffalo Trace, he has sort of a model for looking at basic, coordinating the aging of inventory with the projected sales. So I would expect we actually will be surplussing a significant amount of our bourbon inventory, and I would hope a lot of that's appreciated. And that would still leave us with plenty to take advantage of what Robert's suggesting that we're going to be doing, rolling out in the Redneck platform with our bourbon.

I will say, at the time, David, we were aware that we were definitely overcommitting, but with brown spirits appreciating 20% to 30% a year, it just seemed like a good place to put our cash.

David Bain
Right. So with the drawdown, if there's a little bit of a drawdown for additional cash, then the true value of the inventory is pretty much close to the same perhaps, or we can rebalance that maybe offline at the time, but I just wanted to get a better idea. Okay, fantastic. Thank you so much.

Operator
Again, if you have a question, please press star, then one.

And our next question will come from Ian Gilson of Zacks Investment Research. Please go ahead.

Ian Gilson
Good morning, gentlemen. If we look at Granny Rich as being an extension, how is that doing as compared to the rest of the Redneck Whiskey?

Robert Manfredonia
I can answer that, Steve, if that's okay.

Steve Shum
Yes, no, no, I was going to say for sure, that's your court, Robert.

Robert Manfredonia
So good morning, Ian. Really, I think I'd like to step back and talk about the purpose of Granny Rich. Granny Rich price point alone is a $39.99 suggested EVLP priced item where Redneck, as you're aware, is $24.99. So it's sort of a tiered approach. Granny Rich is a softer sort of rollout type of item. What we're trying to do is capture off of the back of Redneck, and then bring it to an elevated point where some consumers are looking for an aged brand. So, the purpose of the brand is not the same scale model as the, I'll call it the original is meant to be, right? It's an additional SKU that's going to fit a need, and a growing need, within a higher price point. So it's in 15 states roughly across the country. The early adoption has been fantastic. It's exceeded our expectations. But the purpose alone is not to be that scale typed item like the original is.

Now, 175s, which I mentioned earlier, are going to be a scale item, Ian. That's going to be something that we think we could do very, very, very well with, even in 2019. We brought it in early, it was meant to be a 2020 item. But we brought it in early just based upon what we saw in the marketplace, and based upon early demand, and you'll see a substantial announcement coming in the following weeks.

Ian Gilson
Okay. You've spoken a lot about the brown spirits, but not so much about the vodka, which everybody has talked about for doing as well as the brown spirits. So why is that? Is vodka basically just a local product? Can you roll that out down with the brown sprits in California, for example?

Robert Manfredonia
I'll answer that one too, Ian. You want me to take that, Steve, or do you want to handle that one?

Steve Shum
Yes, I think, and Grover might want to make comment on it, but go ahead first, Robert, please.

Robert Manfredonia
Okay. So really when you look at Portland Potato Vodka, that's outperforming our model in 2019, at least early on, and in '18 it far exceeded our expectation, but I think we look at it a little bit differently. And last week, in fact, I just went through, I just scrubbed all the transactional data nationwide, and just looked at what vodkas in general are doing by price segmentation. There is not a category within vodka nationally, nationally, that is in the black. Every single price point, every single SKU level, except for where Tito's is, and right now it's a one-driver market within vodka, everything's in the red. So for us to take it out it would, one, we would be fighting the data, and number two, we would have to pay disproportionately to drive through what the data is saying.

So, at this point in time, even though Portland Potato Vodka is exceeding plan in Oregon, it's not the right time to bring it to the national platform.

Ian Gilson
Okay, fine, that does—

Steve Shum
I'm going to jump in, Ian, and I'm just going to say that, having said that, it's really on a tear right now, and I think, I mean, in fact, actually, people ask me why are we doing so well with it all of a sudden, and this year has been really strong for that product, but I think we've added to the sales team. Also, I think it's kind of becoming, maybe through our advertising or something else, it's kind of hitting critical mass, but I would—as I mentioned, we beat December in Q1. Normally December's 40% above whatever your best number in Q1. And we're adding a few extra SKUs. We're doing a rebrand, we've been talking about for a while, that's coming out with Sandstrom momentarily. The additional SKUs I think help a bit. So that's a good product.

Ian Gilson
Okay. Is there a price sensitivity that you can take advantage of when demand is so high?

Steve Shum
Is the question about national, Ian, about expansion, or is it about Oregon specifically?

Ian Gilson
Well, where the bulk of your sales are, whatever — like if you ex out Riviera —

Robert Manfredonia
Guys, let me just jump in on that one. I think, Robert, we do have with our Portland Mule, either the Portland Mule, which is our new RTD with the Portland Potato Vodka, or something similar to that I think would be a pathway to going into Northern California, but right now the focus is on the brown spirits.

Steve Shum
Ian, I'll just reiterate the point of, what we want to try to do is ride where the transactional data is saying we should go, because that is the, I'll take it, the path of least resistance for major retailers. If we want to scale up, we have to follow the data. And Grover mentioned it, really if we follow what whiskey's doing, and the sub-segments of bourbon and rye, which we have in Burnside, so we fit where the data is going. RTT development, which we've already started in Oregon, we can bring out to the national platform. Trying to go against it with vodka, at least at this point in time, we're better served to, I always say follow the data, and it makes those calls with Walmart, Kroger, Albertsons, a heck of a lot easier, and that's sort of why we rationalize it that way.

Grover Wickersham
Hi, guys, I'm worried we're going to run out of time to take some more questions.

Grover Wickersham
Thanks, Ian. Should we go to the next question?

Operator
Our next question comes from Harold Weber of Aegis Capital. Please go ahead.

Harold Weber
Hi, guys, how are you doing? I have a couple of questions for you. The gentleman had touched on it before in regard to the inventory issues. Would you say that the majority of the inventory is the brown

stuff that has been talked about in the past, that's had a — I'm using numbers out there of 20% a year appreciation with that. Would you say that at 11 million, 12 million, that's most of it, half of it? Just to get an idea, when we're looking at the asset value of your real wholesale product, just to get a better idea. Is there any way to look at that on a cumulative basis, one way or the other?

Steve Shum
Yes, Harold, I would say that probably over 75% of the inventory is in bulk brown spirits, so a significant portion of it.

Harold Weber
Okay. So that's a real-time view of what the market's been doing in the current timeline; is that about right?

Steve Shum
Yes. The market has definitely saw a big surge in appreciation, and there's been some slowdown in some of that growth, but what we do see is, again, as Grover often points out, is that you can buy earlier spirit, which we have done a lot in our portfolio over the last year and half or so, and there's usually a pretty good step up in value in the first couple of years, when it gets to a point where you can then take it from bulk and put it into a bottle, that usually starts at two, and then for bourbon four. So definitely you still hit those key timelines, and you get an increase in value in the spirit.

Harold Weber
Okay, so that's reasonable. So wanted just to get a view of, you guys have made timely, and where are the investments in your main business, raw materials, and it's clearly you seem to have paid off pretty well at this point. If you're going to monetize some of that, it sounds like a good thing to help grow the rest of the business.

As far as, at this point, it looks like going into the next quarter we could be at full production. So if that's the case, and you're looking to ramp up some additional, where does that put us as far as, what do you feel is — are we going to continue to grow revenues 50%, 100% quarter-over-quarter, are we going to start to show some profitability here? Our margins should be improving because we had a whole lot of one-time expenses in this quarter, right?

Steve Shum
Yes. Well, again, we certainly think the trends are in our favor on the top line, like I said. The Craft business is really in their heavy busy season, they're doing fantastic. The Redneck Riviera product and our other branded products are doing well. So we're certainly looking forward to continued strong topline growth. And you're right, we certainly feel that we'll start really demonstrating the leverage in the infrastructure, and on top of that, removing some of these one-time expenses. We think we can show some pretty meaningful improvement in EBITDA as we go forward from here.

Harold Weber
We should be starting to make some money if our costs are down and our revenues are up, our margins should be improving, what's the problem?

Grover Wickersham
Harold, just to kind of put a point on the advantage of the Craft acquisition, is that they almost acquired us really, because they're really taking over our production. They have a huge team, and all they do is focus on putting things in cans and bottles extremely efficiently. So a lot of our margins are related to the overall cost per facility, or manufacturing costs and direct labor, which are part of the cost of goods sold. But as our volume goes up, and as they continue to put some discipline and real efficiencies into the process, you would expect margins to improve as the cost per unit dropped.

Harold Weber
Okay, that perfectly makes sense, but that's one thing. The branded stuff is a whole different ballgame. You're increasing sales tremendously —

Grover Wickersham
Harold, I'm putting the branded products, because they're essentially using the same discipline on manufacturing Redneck Riviera, the bourbons, and the vodka, and everything else. Our cost per bottle should be dropping. Our goal is to drop it pretty dramatically this quarter, and continuing on through the year.

Harold Weber
Is it reasonable to say that as time goes forward, you're going to be able to, let's say, separate or differentiate to some degree, branded product sales, which has a much higher, obviously, profit margin versus packaging, pre-shipping, case sales, which is a large part of the business, but it's a contract manufacturing, which is obviously a whole different scenario. How do you see this?

Grover Wickersham
Well, I mean, it's very possible —

Robert Manfredonia
That's kind of a question for Steve, but it is — there's a huge demand right now for co-packing, especially wine, but also beer in the Pacific Northwest. There's also, frankly, we've been approached by a number of people to co-pack CBD beverages, since we can do that legally in Oregon. So I think the co-packing actually is one of the main drivers of the business, alongside some of the other things like Redneck. I don't know, Steve, did you want to say anything or?

Grover Wickersham
Steve, no? Okay.

Harold Weber
And do you have any type of a, I don't know, a foresight of how much CBD product you'll be able to actually manufacture over the next, let's say couple of quarters, 6, 12 months? It sounds like you're starting to produce it now, or whether for distribution, I'm just asking, I'm not sure.

Robert Manfredonia
Yes, I mean, we're talking to some leading distributors. Harold, we know it's a huge market and we know there's a lot of demand, but it's too early for us to say that we're anything other than extremely optimistic. I mean, we're very optimistic, and the initial feedback on sampling has been very, very positive. I'm hoping we'll have some more color on that when we roll out of Q2.

Harold Weber
Okay, I'm just hoping to see. I mean, you guys have some real premium brand opportunities, and hopefully we should be able to get some good margins out of that so that we can have benefits. Appreciate it.

Robert Manfredonia
Yes. Harold, if I could interject one more time. I think your last comment, that's why we're very excited that we've released the first non-Redneck brand into the national platform. This is where we're going to be able to help our brand utilize all the work that we put forth in 2018. So this is priority one, to move into this national platform, and Burnside is the first of a few brands that will be coming out in 2019.

Harold Weber
Okay, great, thank you.

Operator
Our next question comes from Geoffrey Gwin of Quad Group. Please go ahead.

Geoffrey Gwin
Great, thanks for taking the question, and congratulations on a great quarter, and Grover, as well, on building such an amazing platform. My question is really wanted to focus on the second quarter. Can you recap for us the distribution, just growth quarter-over-quarter, but also year-over-year, I mean, what we should be expecting on the national platform stage? Specifically, how many incremental doors we're expecting, incremental points of distribution?

Grover Wickersham
Robert, you want to take that one?

Robert Manfredonia
Yes, I can. Good afternoon, Geoff. So, the way we look at it again, early stage brand, right, with Redneck Riviera. I'm looking at the numbers. We actually, in the third quarter, we doubled our placement in quarter three versus quarter four in the on-premise and the off-premise. We've added, as we mentioned, almost 2,400 points of distribution just in national accounts. We're going to have another large onboarding of incremental distribution in the second quarter. Then it will, I won't call it flatten out, but it will start to build off of our organic business substantially more than just the incremental piece, and then the next large ramp of business will be the first quarter of 2020. So it's sort of a timing mechanism of how the market works and how accounts onboard new distribution.

The first trimester is usually a large portion of when new business is seeded, and then you start to work through displays in the summer, and then obviously the fourth quarter with driving sort of seasonality with that part of the year, and then we'll have a large surge next year. So you'll see a substantial ramp up in early part of this quarter, and then what we're going to try to do, Geoff, and I'll bring it in a little bit of a different direction. We're going to try to start going deeper with our business, meaning where we have Redneck Riviera 750s, our objective is to start putting the 175s next to the 750s, and where applicable put the Granny Rich brand beside that, so we're starting to build a billboard effect for the Redneck Riviera brand. That's in part what we're trying to do. So it's not about as many new doors, it's about depth within the existing business that we have now, so the old one plus one equals four approach, by the way that we look on the shelf, is part of what we're going to be driving in the second and the third quarter.

Geoffrey Gwin
Right, right. So the SKUs growing, doors growing. So a following question I that had. I'm sorry, go ahead.

Robert Manfredonia
No, a combination of both. Just to say that it won't be just 750s just being incrementally grown only, we want to start utilizing all of the work the team has done in 2018 and start to build off of that with depth within the existing account base.

Geoffrey Gwin
Right. So like, for example, Florida, where you have outstanding distribution, and probably would take up the products from the one SKU to multiple SKUs. As that happens, what happens to the on-premise distribution? Have you seen any notable changes in on-premise as the masses pick the brand up?

Robert Manfredonia
Yes, that's really a good point. I mentioned earlier in the call that account buys in the first quarter were 91% above what we did in the fourth quarter. That's been a concerted effort, that we know that we need to have on-premise availability for awareness, but also trial. So we're trying to be a little bit more complete. We took a nontraditional path with just corporate accounts being the focus, but we're trying to make sure that we have balance with the general market off-premise, and then add on-premise availability and features, and drink features, and start bringing people to understand the brand a little bit further, above and beyond all the hard work that John Rich does with above-the-line pressure coming down. We want to make sure that we have availability in the on-premise, and Florida has been — I'll have to go back through it, but I don't think I'm too far off on this — is by far where we're exponentially growing to be on-premise, above and beyond Illinois and Texas, but Florida, we've had a lot of success, and the team's doing a great job down in that marketplace.

Geoffrey Gwin
Okay, great. And then lastly, the Craft acquisition looks like it's just been an amazing acquisition, and you've mentioned on the call that you're going to add capacity there. And so, when we think about rolling out these next products, Grover, you mentioned the Portland Mule RTD, and in prior calls you've also mentioned a Redneck Riviera RTD, that, I'm assuming you now have the capacity to package that and distribute that yourself with these new assets.

Robert Manfredonia
Yes, Geoff, I mean, that's our strategy. There are some people who have really focused on developing products and their marketing, and then having other people co-pack them. But I think the co-packing business that we're in right now with Craft, within five years could be a $30 million business. The growth in the Pacific Northwest is huge. So, not only do we get to participate in that growth, quite frankly, co-packing is a resource, it's very hard to come by. For our 187 can that we've been pounding the drum on and saying, well, that's the new slimline can, is really — I mean, we're not exactly the only game in town, but we pretty much are in the Pacific Northwest. And so, we're running that equipment full out.

So I think our ability to take a Sandstrom-branded product, and something like CBD, where you don't even have to clear it with the TTB that approves label for alcoholic beverage. You just basically go to the printer, and you come out with it as fast as you can. So the ability to go directly from a product concept to a product that Mel Heim — and I want to do a shout out to her, she's fantastic — that Mel Heim can put together, and then run it on our own equipment. I think that's a competitive advantage, it also improves our Costco problem.

Geoffrey Gwin
Great, great, that's exciting, thanks.

Operator
Our next question comes from Shawn Willard of Orca Investment Management. Please go ahead.

Shawn Willard
Good morning. I'll be interested in reading your cue. When you do an acquisition the size of the canning business that you picked up, it's always kind of a blind guess of where that's going to roll in. But one of the things that you said in the quarter that I'd like to know kind of where it falls is, in your commentary, you said there was roughly $500,000 of one-time expenses, and you didn't really delineate what that was specifically for. But did that happen at the gross margin line, or was that buried somewhere down in operations?

Steve Shum
Shawn, most of that was in the G&A line.

Shawn Willard
Okay.

Steve Shum
I mean, I would say that what I referred to in terms of production efficiencies and where we were off from our internal goal of about 90 some thousand in our gross profit target, that is probably related to some of those getting situated, bringing their operations into the fold, and at the same time, Craft was going through a rapid growth cycle themselves, trying to bring on new equipment, hire new bodies, get prepared for some big customers we took on right at the end of the quarter. So, that certainly drove some of those inefficiencies in the production facilities.

Shawn Willard
So on a go-forward basis, did Q1 look like a somewhat normalized gross margin with the new business just having a higher overhead cost to it, or was there anything that was artificially lowering that?

Steve Shum
Yes, I think that we still had some higher bourbon stock we were still sort of bleeding through a little bit of the quarter, so that contributed, but if you look at those production inefficiencies, I think, mathematically, it's a couple to three points on the gross margin line, and then some of the material costing that was a little bit higher in the quarter that we think — we've mentioned this on the last call, as we start getting into some of our additional stock and the bulk spirit inventory, we think that will improve as some upward bias in the margin, too. Yes and no, to answer your question. It's not perfectly normalized, but pretty close.

Robert Manfredonia
Yes, Shawn, also, keep in mind Craft Canning, we didn't get a full quarter with Craft Canning, and they didn't really get hands-on so that we could start picking-up the efficiencies until well into Q1, and that's an ongoing process. So I think I would expect us to see cost improvements definitely in Q2, and I think that's going to continue on into Q3, based on the manufacturing efficiencies that we're getting because of that acquisition.

Shawn Willard
So basically, January, February were transitioned for the business you acquired. It was probably up and running at seasonal rates in March. And then the same thing with your core business that rather than the — and I'll look for the exact term — but the sample stocking that you've been providing to some of the large retailers was migrating over to replenishment, and permanent placement inventory was also again in March, right?

Robert Manfredonia
Right, yes, those are correct statements. And I think, also, as we previously said, Craft added some high-capacity equipment midway through the quarter. That equipment hit the ground running. It's fully utilized. And as Steve mentioned, he's looking to acquire more equipment, and plus they're beginning to really maximize utilization of the existing Motherlode equipment that we have. So all of that's affecting our manufacturing efficiencies, not just for the co-packing, but also for our product cost, and you're going to see more of that in Q2 I would expect.

Shawn Willard
So one more question and then I'll stop. But it looks to me like, based on what I'm seeing for volumes of the core business, your volumes are going to be such that you're going to use the entire tax credit for the Craft business that's allowed probably by third quarter or sometime this year; is that reasonably fair?

Steve Shum
Yes, we will be bumping up against the 100,000 proof gallons limit at the lower tax rate for sure.

Operator
Our next question is a follow-up from David Bain of Roth Capital. Please go ahead.

David Bain
Great, thanks, I know it's a long call. But just, if I could, just follow up on, I believe one of Ian's question, and, Robert, your discussion with Geoff on depth. Still trying to get our hands a little bit around the product extension potential into the Redneck gateway, as you termed it. I understand myself for Granny Rich, but the 1.75, is that close to like a 1.1 potential in terms of the Redneck flagship, or a form factor in terms of dollar sales potential? And then, if we look at the RTD Redneck that's coming out, how do you think about that in terms of either volume or sales potential versus what's out there right now?

Robert Manfredonia
So the way I look at it, David, is in 2020, I think we're going to have a mix of business getting close to the 750 business, meaning half gallons, 1.75s and 750s will be getting close. You have to remember when you look at 750s, a lot of that is a byproduct of timing with national corporate accounts. So, as an example, we will be pitching half gallons in September of this year for spring of 2020. We did the same thing with

750s, spring of 2018 for onboarding in this period of time. So a lot of the volume in large chunks will be coming spring of next year. So you're going to start to see an exponential lift in 1.75s next year. However, there are accounts in Texas, and I can go around the country, that don't have sort of a very tight windows of time for presentations that we're going to start our onboarding the 1.75s, Spec's, Goody Goody in Texas, Twins in Texas, are all accounts that we feel pretty good about at this point in time.

RTDs, we mentioned that on our last call, that's something that we're really excited about back to riding the data, and we think we have something that is very unique and different versus a lot of the mainstream RTDs that are being developed right now, especially with Redneck Riviera. And then we're going to have some other non-Redneck related brands that are going to be coming out to the national platform.

But we will start bringing in volume of RTDs in the third quarter, and then we will be presenting to the large box stores, again in the fall of this year or next year. So we will receive incremental volume and revenue in the back half of the year, but most of that growth, David, is going to be in 2020, early 2020.

David Bain
And when you add that and all these products with the Burnside mix into the national platform, I mean, what's the average number of SKUs you need to begin to get incentives to kick in for even more distribution potential, I mean …

Robert Manfredonia
So, in part, I think you bring up a really good point, which is, when you have several brands within a portfolio, your ability to have favorability efficiency with, let's call it discounting as one example of it, becomes exponentially better. So when we can walk into an Albertsons, or we can walk into a distributor in California, and we have a Redneck, and the lines of Redneck, and a Burnside in another area, our costs starts to go down incrementally.

So part of what we're trying to do is utilize the national platform gateway strategy, but also, we start to cut costs a little bit on just sort of the below-the-line costs that we have that we are occurring right now. The model becomes a lot more efficient. So we're going to start to recognize and see those efficiencies in the coming months as we start to add new brands on to the platform.

David Bain
Great, thank you.

Robert Manfredonia
You're welcome.

CONCLUSION

Operator
This concludes our question-and-answer session. I would like to turn the conference back over to Steve Shum for any closing remarks.

Steve Shum
Great. Thanks, everyone, we really appreciate your time today. Speaking on behalf of the whole management team, we're very excited about 2019. We think that all of the investments that we've made in our infrastructure and our people over the last year and a half will really start to show themselves as we move through the balance of this year, and show the power of the platform that we've created and built for the organization.

So feel free to reach out to any of us with any follow-up questions, be happy to take your call, and answer any remaining questions you might have.

And, Grover, I don't know if you want to say any last remarks as well, otherwise we'll wrap up the call.

Grover Wickersham
Well, I'd just like to echo what Steve just said, and also say that I'm really looking forward to my new role of Executive Chairman, because hopefully what I'll be able to do, working with the board, is to focus on strategic acquisitions and deal making, and also get involved very heavily in the strategy on the CBD launch. So I'm excited that Steve handing over day-to-day operational duties to Steve and Robert definitely frees me up, and that opens up a lot of possibilities for creativity that I'm excited about.

But, I want to thank everyone. I know we have investors on the call that have been with us since 2016, like Shawn, for example, and we appreciate the support that we're getting from all our investors, shareholders. We really appreciate the support that we've gotten from ROTH Capital as well. So I just want to end on a note of thanking everyone, and I think the best is still ahead.

Steve Shum
Great, thank you.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.