

2021 Shareholder Letter

Cheers Health, Inc.

Preface:

Dear Cheers shareholders,

This is not only Cheers' first ever shareholder letter, it's mine as well.

The responsibility of reporting through an annual shareholder letter falls squarely on the shoulders of the CEO. It is no small task, as I am reporting to over 1,500 Cheers investors about the state of a business that they own. Whether you invested a few hundred dollars in this recent round, or a few hundred thousand dollars in previous rounds, you are a part-owner in this business and your management team feels the full weight of that responsibility.

During up years, we realize that we may be regarded as heroes. But during down years, we are fully aware that we may be regarded as bums.

Of course, as fate would have it, my first-ever shareholder letter requires reporting to you on a down year — one in which both revenues and net income declined due in large part to the recent, abrupt, and immense changes in the digital advertising industry caused by iOS 14.¹ Fate can be a cruel mistress!

In many ways, a shareholder letter is a rite of passage for CEOs as it is neither regulated, nor required, and thus allows them to speak more freely than other forms of investor communications. It gives a unique window into the leadership of a business, going not only into the what, but the why and the how. These letters are as much about how management thinks and feels about the business as it is about what they have done and plan to do.

To prepare for such an endeavor, I have read annual shareholder letters from a number of different companies and CEOs that I admire. Chief among these are Amazon (Jeff Bezos), Southwest Airlines (Herb Kelleher), and Berkshire Hathaway (Warren Buffett). Of course, as clued by my favorite book which I have referenced in investor communications often — *The Outsiders: Eight Unconventional CEOs and Their Radically Rational Blueprint for Success* — Warren Buffett is my favorite.

When it comes to these shareholder letters, a few key things have stuck out to me so far:

- *The best letters are clear.* They get down to the basics of explaining where both the threats and opportunities lie within the business. This doesn't mean they are

¹ By "iOS 14", I am (and will be throughout the rest of this letter) really referring to iOS 14.5 and beyond. iOS 14.5 was released on April 26, 2021. The feature of concern within that release is a privacy feature called "App Tracking Transparency" which, according to Apple's website, lets users "control which apps are allowed to track [their] activity across other companies' apps and websites for ads or sharing with data brokers." I just use "iOS 14" as shorthand here because it's simpler to say and it is how that particular new privacy feature is commonly referred to in the digital advertising space.

either concise or short, as they are often the opposite (at the turn of the millennium, most Berkshire letters were 12,000+ words), but it does mean that they explain the root issues with particular clarity. (For example, because insurance float is so critical to Berkshire's business, Buffett spends a page explaining how it works in simple terms in every shareholder letter in the 2000s.)

- *The best letters are candid.* They are not so much of a sales pitch for investors to buy the stock tomorrow, but rather a sales pitch to find like-minded people who want to invest in the vision and team for the long-term — good, bad, and ugly. Throughout the years, these letters build trust among that group of people. Candor is the language of partnership. If someone talks only of sunshine and rainbows, then they are either a fool or a crook — neither of whom you should want to do business with.
- *The best letters are insightful.* While the business is the primary focus of these letters, readers end up learning about all kinds of tangential subjects that matter to the business and its leadership as well. These topics range anywhere from types of decision-making and their speed (Bezos) to moral implications of leverage (Buffett). In fact, Buffett often spends as much as a quarter of his letters dealing with systemic business issues that are only partially related to Berkshire's affairs.
- *The best letters have personality.* At the end of the day, there are few places where a CEO has as much legal freedom to express their thoughts to owners in their own style as a shareholder letter. This freedom allows for both originality and fun. Many of Warren Buffett's famous quotes — which almost always involve some colorful imagery (e.g., "Only when the tide goes out do you discover who's been swimming naked.") — come from shareholder letters. In fact, you can hardly get through a page of a Berkshire letter without encountering a witty joke.
- *The best letters tell a story.* Rather than being stuffy business analysis, full of MBA-esque jargon and structure, great letters draw you into the business as an active reader of an enthralling story. A business is ultimately a journey, and journeys are typically communicated through the literary form of narratives. These letters help the reader understand what the leadership team is going through and gives them an observer seat at the decision-making table. While readers of shareholder letters might not agree with the conclusions, they can at least better understand how they were made.
- *The best letters get better.* These executives have held the mantle of their businesses for quite some time — at least over a decade. As you read through their annual letters, you will see not only the businesses growing, but the executives growing as well. You can see where they were right or wrong — and how they handled that information. You can see where their opinions on

subjects changed and where they stayed consistent. And ultimately, great shareholder letters show not only the yearly transformation of the business but its leadership as well.

As you dive into Cheers' first-ever shareholder letter, please remember our "[House Rules](#)", which were initially laid out in a blog post on our website (cheershealth.com) on November 3rd, 2021. Of these, there are two that are fitting to restate here, along with another that I will add:

1. *We will not give away any information that we believe could help our competition.* A shareholder letter is public. And because of this, it has a major downside... anyone can read it — including competitors. We don't want to make it any easier for them to copy us, because they always try. Cheers is closing in on nearly 100 copy-cats that have entered the market since our founding. We built this industry and we would like to stay its leader.
2. *We will not give away any information that we believe is legally risky.* For example, suppose someone wants us to answer, "what will the stock price be next year?". This question is essentially impossible to answer because we can't predict the future. Additionally, we can't give specific guidance without it potentially becoming misleading if we don't hit what we say, either above or below. Only trouble can come from such a statement — and as investors ourselves through the daily act of capital allocation — we don't like anything that has limited upside but significant downside.
3. *Everything we say is our current best guess and will probably change as we encounter additional information.* When challenged about some of his inconsistencies, the famous economist John Maynard Keynes stated: "When I find new information, I change my mind; What do you do?" Business factors often change both abruptly and intensely. It is very possible that something I say today about Cheers could be obsolete tomorrow because of new information we encounter. If a bus tour company sells a trip with an itinerary that takes passengers over a certain bridge, then comes to find it broken and missing a section, ought they drive right off the edge to stay true to their plans? Personally, that's not a bus that I'd like to be on.

In this letter I will do my best to explain everything going on with Cheers and how we think about the past, present, and future. My goal is not to just inform you, but to instill in you the faith that Cheers' management team will make the most of what is possible with the resources we have, all by using candor as one of our primary tools.

This letter is intentionally long. It discusses concepts that are unique to how we manage Cheers and will be helpful for you to understand going forward as an investor. In future letters, we will likely refer back to these concepts, allowing us to save word count on giving them a full overview such as we are doing here.

A now-famous Galilean man said two millennia ago: “Whoever can be trusted with very little can also be trusted with much, and whoever is dishonest with very little will also be dishonest with much.” I believe that this statement about the human condition regarding responsibility and stewardship is still true. And therefore, I and my team strive to uphold the highest of standards no matter the size of our business or what has been entrusted to us.

On behalf of the Cheers team, I can’t thank you enough for throwing in your lot with us. You have our word that we are doing everything we can to make it worth more!

“Cheers,”
Brooks Powell, Founder & CEO

To the Shareholders of Cheers Health, Inc.:

In 2021, Cheers generated \$8.7m in revenue with \$0.9m in net income. For reference, in 2020, Cheers generated \$10.4m in revenue with \$1.7m in net income. This means that from our high watermarks in 2020, Cheers' revenue is down 17% and its net income is down 46%. On a positive note, Cheers' cash position has improved significantly over the past two years. At the end of 2019, Cheers had \$0.6m in cash on hand and \$2.1m in total assets. At the end of 2021, Cheers had \$4.5m in cash on hand and \$5.9m in total assets – gains of 7.8x and 2.9x, respectively.

When looking back to 2019, Cheers' revenue was \$8.2m with -\$352k in net income, so 2021's results are well above that. When speaking with one of Cheers' board members about the disappointing 2021 results, they said: "If 2020 wouldn't have existed, would you be happy with the final 2021 numbers?" To which I replied: "Of course, the business would have had its first profitable year, still grown, and improved its cash position significantly."

In some regards, the disappointment of 2021 is related to our success in 2020. The maxim that an executive is only as good as their last quarter feels true. While you might not think of us that way, that's the devil we're fighting in our minds. We have to remind ourselves that what ultimately matters is not the value created in the short term (months, quarters, or even a year or two), but the value that is created over the course of a number of years. It takes discipline to optimize for the long term—and so far, that's a game we have been winning. Cheers is worth much more than it was five years ago at the end of 2016 when the company had no profit and the yearly revenues were only about \$50k.

One thing to point out when comparing the 2021 calendar year with 2019/2020 is that 2021 was the first year in which Cheers had to pay corporate income tax due to our carried losses being completely used up by 2020's profits. 2021 saw over \$200k in corporate taxes that 2020 did not see. 2020 also had other sources of unique income, such as restitution from Amazon when a truck carrying ~\$240k in revenue worth of Cheers' products had a mechanical malfunction and all of that inventory was left stranded in the back of truck for an entire Texas summer. In the words of one of Cheers' early investors: "It's an honor to pay taxes. Only companies that actually make money pay taxes. Given the choice, you would rather pay taxes than not."²

When it comes to comparing apples-to-apples by using net operating income as the barometer, 2020 was \$1.4m (13.7% operating margin) while 2021 was \$1.2m (13.8% operating margin) — which is a difference of 16%. The fact that operating margin was stable between 2020 and 2021 means that revenue and net operating income moved more or less proportionally. While this is a decline, it's not all gloom and doom, as Cheers has built up a nice war chest over the past two years to tackle its next stage of business — brick-and-

² This does not mean that we don't try to be as tax efficient as possible through every legal method available to us. But, it does mean that if we can't spend money on something with a worthwhile ROI in a calendar year, we'd rather hold the cash and take the tax hit. Saving 28% in taxes on a 100% loss is a bad trade by 72 percentage points... which is something many people don't understand about "tax write-offs".

mortar retail expansion. This move is critical for turning Cheers into a household name and an enduring American brand. In fact, I can't think of a single enduring American consumer packaged goods (CPG) brand that isn't sold in retail. (Even the largest direct-to-consumer (DTC) brands are rapidly expanding into retail to correct for problems they are experiencing in their online businesses.)

In 2001, Berkshire Hathaway reported its first loss in per-share book value since it started being recorded in 1965. It was the first time the company lost money in a given calendar year in over three decades. When Berkshire's average annual gain from 1965–2000 was 23.6%, the -6.2% in 2001 was a huge blow, resulting in about a 30-percentage point negative swing from the company's average.

How did Buffett respond to such a loss? He did three things.

First, he points to the fact that he keeps 99% of his net worth in Berkshire — essentially saying: “Look, this bad year may hurt your portfolio. But it has hurt mine even more! I have all my eggs in this one basket.” In other words, this bad year doesn't hurt anyone more than him, and he's fully invested in making the company a success — quite literally.

Second, he explains the problem in *excruciating* detail and takes full responsibility for it. He admits that he actually recognized the problem, but “didn't convert thought into action.” He finishes this thought with his classic wit, this time directed against himself: “Predicting rain doesn't count; building arks does.”

Third, he explains what he is going to do about the problem. And is *very* candid that the problems will potentially span several years before being fully rectified. He doesn't sugarcoat either the diagnosis or its treatment.

When it comes to Cheers' first materially down year since its inception in 2014, a period of about seven years, I would like to do the same thing. This will be structured as: 1) how Cheers' management is very much incentivized to increase the value of its stock, 2) what caused the decrease in both revenue and earnings in 2021, and 3) what we can do about it now and how we plan to increase the value of Cheers' stock over the long haul.

Beyond that, I will touch on a few ancillary topics that may be on our investor's minds, such as new products that are soon to be released, our switch from glass to plastic packaging, and even competition.

1) Stock value is what Cheers' management team cares about.

Like Buffett, 99% of my theoretical net worth is held in Cheers shares. There is no one who has more eggs in this basket than me. If Cheers struggles, that hurts me more than anyone.

Cheers is nearly a decade in the making since when I first came across the beneficial properties of dihydromyricetin (DHM) in 2013 while doing my undergraduate studies at Princeton University. It is very much my “baby”. This use of paternal language is intentional, as my wife and I have put off having kids to build this company through its money-losing years, which spanned from 2014 through 2019. Then 2020 hit, causing us to wait even longer to see what would happen next. Only recently have we been able to even consider the possibility of kids! If that doesn’t give you some level of comfort about our belief in the future of Cheers, I don’t know what else will.

From mid-2014 through mid-2017, Cheers was an LLC and we paid ourselves nothing. Then Cheers became a C-Corp to be able to raise money through selling stock, and mid-2017 through mid-2018 we paid ourselves about \$25k a year each — which at the time Cheers’ lawyers said was the legal minimum for salaried C-Corp employees in Texas. It wasn’t until 2019 that our calendar year household income went above \$100k. If you’re curious, my total current cash compensation is \$90k. For context, this is the [low end](#) for what most venture-backed CEOs pay themselves. That number typically ranges from \$75-250k, with the average being around \$150k for companies around Cheers’ stage. While I hope to increase my cash compensation in future years — primarily so I can think even more about Cheers’ finances rather than my own — one thing will remain true: *Cheers’ stock is the way I plan to make the vast majority of my wealth.*

With a few exceptions, this is the case for most of the Cheers management team. Cheers loves to compensate heavily with stock in lieu of cash because we believe in fighting overhead obligations like the plague.

Large overhead expenses relative to income are arguably the greatest risk to any business startup. It reduces the margin of error and makes even the smallest bumps in the road potentially fatal to a small company. Revenue is often far less predictable than overhead. As a result, if your revenue numbers are off, you may not be able to pay your overhead. And to make matters worse, increasing overhead, especially payroll and benefits, is a bit like hell — easy to get into, but almost impossible to get out of. When was the last time someone’s salary was ever cut without relationship-killing ramifications? Typically, needing to cut payroll leads to either terminations or resignations, with not many elegant solutions in between.

Bonuses could be a good option to solve for this problem in most companies. I looked into implementing them a few times in Cheers’ history. However, as a startup, we have found it too difficult to predict Cheers’ goals in each calendar year other than increasing intrinsic equity value over the long haul. Our goals can change too quickly and the capital is too valuable. For example, Cheers originally planned to raise money in 2020 and have a year of aggressive growth in retail. Then the pandemic hit, venture capital firms jumped onto the sidelines, retailers paused taking in new products, and all of Cheers’ efforts were transitioned to maximizing cash flows. A bonus structure that calendar year would have become completely obsolete at no fault of the team... and no one wants to be in a company that’s always changing the goalposts when it comes to compensation.

Our way of matching compensation to the task at hand has been primarily through stock. Using stock as compensation in a private company with limited present-day liquidation options is only expensive if the company does well and has favorable liquidation opportunities in the future — the two of which are often tied together. Like buying insurance, which helps safeguard the business at the expense of total long-term earnings (insurers want to make an underwriting profit, of course), paying with stock helps safeguard the business at the expense of future stock value. But both future earnings and future stock value are arbitrary if a company is dead... which is the whole point of insurance. Plus, stock compensation has two major advantages that cash salary does not: 1) it preserves liquid assets for use in the business, and 2) it gets management committed to the same things that private investors are committed to — increasing stock value and finding liquidation events.

The outcome of taking stock in the form of stock options instead of cash is that Cheers' team members are effectively becoming investors themselves. And much like an investor, our team is taking financial risks to be here at Cheers. While we love the company, this isn't only out of goodwill. Management wants the upside of their stock to come to fruition.

Here's a highlight using one of our executives as a case study: Hank Holcomb, our phenomenal CTO, started in mid-2017 and had a salary of just \$30k for over a year until we raised our first sizable round of funding. To make up for such a low salary and the risks he was taking, Hank was given a large stock grant. To give you a sense of the value he brings to Cheers I could give many stories, but a recent one sticks out in my mind.

Last year one of our venture capital investors reached out to us telling us about problems at one of their portfolio companies that had recently raised in excess of \$10m in total funding. In fact, one of the investors actually switched from a role at the VC firm to become the VP of Product at the portfolio company to help them out. Being an online subscription company selling physical products, they decided to build out a custom subscription portal, and really screwed things up in the process... to the level they couldn't even take new orders. This was a company with a dedicated VP of Product, multiple California-based engineers, and a team of 5 outsourced developers in Argentina. Altogether, the yearly overhead expense of their technical department was probably an order of magnitude larger than ours — i.e., Hank.

In under an hour, Hank was able to walk them through the potential solutions and give them his recommendation. I remember coming out of this meeting reminding myself about how fortunate we were to have Hank on Cheers' leadership team. For the record, while writing this letter I looked up this company to see what they ended up doing, and it looks like they took his advice and have successfully pulled their car out of the ditch.

The financial resources of their company, the pedigree of their employees, and the salary overhead of their team in comparison to ours were extraordinary. And yet, despite all of that, they were coming to us for help. One of Cheers' core values is "doing more with less" (codename for capital efficiency) and this story exemplifies that pillar. My goal as CEO is

to bring out the best in people and help them achieve their fullest potential. Doing more with less is good not only for shareholders, but managers as well.

Like many people at Cheers, Hank wears multiple hats, and his brilliance isn't one-dimensional. Early on in the business, he once singlehandedly figured out a way to get a frivolous lawsuit filed in the state of Florida dismissed through a small detail that even our stupidly expensive lawyers hadn't caught. He's an expert on subjects as diverse as dietary supplement laws and USPS shipping tiers. And given that the vast majority of his compensation is comprised of stock compared to the cash he could make elsewhere, he also sees his role as increasing the value of Cheers' stock.

Think about it this way: for someone paid in part with stock, every increase in stock value is like a pay increase and every decrease in stock value is like a pay decrease.

With a few exceptions where cash is a unique need for someone, this is the case for most managers at Cheers. For example, Seth Hazleton, our excellent VP of Operations and Cheers' de facto Charlie Munger, initially took a \$80k+/year cash compensation cut to join Cheers. One way to think about this is that Seth has very real skin in the game (e.g., \$80k+/year) by virtue of taking less cash to be here compared to what he could get elsewhere. In this way, Seth is as much an investor in Cheers as he is a manager.

Seth isn't the only example of this. We have plenty. Dalia Steichen, Cheers' Creative Director, opted to take a gamble on Cheers rather than start her own creative agency — which she could have done, especially as we were already a frequent purchaser of her services! The point I'm making here is very simple. Most of Cheers' managers could be making more cash compensation elsewhere and instead, they are here. This says something about our belief in Cheers' stock and the opportunity of the company in general.

Even in a down year, several motivations keep us planted. These are all mostly rooted in the belief that Cheers' best years are ahead of us. Looking at our careers with Cheers through the lens of an investor in our own lives, we believe that our "return" here will be greater over the course of the next few years of our lives than it could be anywhere else. By using the word "return", I do primarily mean financially. But I also mean "return" in non-financial aspects. Lifelong friendship, fun memories, hard challenges, unique experiences, new skills, interesting opportunities, novel insights, being part of something cool, etc. are all part of the return from one's work. And that's where Cheers and its culture offer something truly unique.

I say all of this to help our shareholders understand that from the beginning we have been intentionally building Cheers in such a way that management is inherently aligned with shareholders on the goal of increasing our stock value. This is the case for me personally and for our management team as well. So, when you hear about Cheers having a down year, you don't have to worry about us not caring, as it is *very* much something we care deeply about.

2) iOS 14 marks the end of an era for DTC companies.

The metrics of DTC.

Casper, Allbirds, and Blue Apron are all examples of VC-backed DTC darlings. They were all VC investors could talk about at one point in time. I still remember one VC that we were pitching in early 2018 saying they didn't like certain aspects of our business and that we should be more like Casper. I drank the Kool-aid so hard that I even went out and bought a king-sized Casper Wave so that my wife and I could "sleep on success."

I didn't get my first look at Casper's financials until Q1 2020 when they went public. In 2019, Casper had \$439m in revenue and a whopping \$93m net loss. I immediately thought: "why would anyone want to be more like Casper?"

All of these DTC darlings have had major problems in recent years, especially once their financials were revealed to investors in public markets. Since their IPO, or their highest private market valuation, Casper was down 70% (now taken private again at a fraction of the total money they had raised), Allbirds is down nearly 80%, and Blue Apron is down 97%. Besides their stock value, none of these companies have even come close to making more money than their carried losses over the course of their business existence so far. Relatively speaking, these are losses of biblical portions that ought to be understood.

When it comes to understanding how DTC businesses typically work, I believe that their financials can be simplified into three key metrics:

1. CAC ("customer acquisition cost") — i.e., the amount of marketing money it takes to convert someone into a paying customer.
2. LTV ("lifetime value") — i.e., the amount of contribution margin that a company makes from each customer over the course of their lifetime.
3. Overhead (fixed costs) — i.e., the amount of money that a company must spend to either maintain or improve upon CAC and LTV (variable costs).

With these 3 metrics, you can get a very good understanding of a DTC business. If these numbers look really good, then the business is probably really good. And if these numbers look really bad, then the business is probably really bad. Of course, most businesses lie somewhere in the middle, and that's where things start getting more complicated.

Complications of such metrics can, *and should*, be made. An example of this would be the "payback window", which is essentially the amount of time it takes for your LTV to "pay back" your CAC. If you had infinite free money, you wouldn't care about this. But, because

businesses can't get infinite free money and thus need cash flow, this is of critical importance as it affects growth rate potential and other critical measures like debt.

A metric that we often look at within Cheers, but many other companies don't, is LTVaCAC — which is “lifetime value after customer acquisition costs” and simply measures how much contribution margin after marketing that Cheers makes on a per-customer basis (our lawyers told us to mention that this isn't a GAAP metric). We typically add time windows to this as well, such as at 6 months, 12 months, and 24 months.³

We have even gone so far as to create a custom metric (again, not GAAP) that we call NI+PLE — which is “net income plus projected lifetime earnings”. (We pronounce it “nipple”, which, with a name like that, is something you will never forget.) In fact, this is the metric that we have optimized our business for since when the COVID-19 pandemic began. At that point in time, we believed we might not ever be able to raise external capital again, and so, the goal became to maximize internally generated cash over the long haul of the business. Thus, rather than spending capital on some “growth story” at all costs for future institutional investors — an activity more akin to speculation (i.e., building for what someone else might pay) than investing (i.e., building intrinsic value) — we needed some way of measuring how today's growth actions were affecting future absolute cash creation.

In *The Outsiders*, Thorndike points out that the outsider CEOs' leadership in regards to capital allocation was marked by “careful analysis and often expressed in unusual financial metrics that were distinctly different from industry or Wall Street conventions.” I share this quote only to point out that there's nothing wrong with using a business metric that's not taught in business school. In our eyes, NI+PLE is not meant to be contrarian, it's meant to help our team get a full picture of how our actions today affect the long-term economic realities of our online business unit, which as of today, accounts for 99% of our revenue.

This metric can get a bit complicated, with a few different ways of dicing it up. But it can be understood intuitively at a high level. When many companies (specifically DTC companies) are growing, they often show large losses to pursue that growth. Vice versa, while some companies are stable or declining, they may show large earnings that stem from slowing down growth. The reason for this is that most DTC companies have to invest in CAC, typically losing money on first orders with each new customer, then waiting to make a return on that investment (ROI) when each customer comes back to buy again. This is where the “pay back” comes from in the “payback window”.

In a perfect world, a business would be efficient enough to grow both revenue and earnings together (like Cheers did in 2020)... but most companies don't have that luxury at all, much less every year. This begs the question, what are the absolute lifetime earnings created during a period of time? This metric would reveal whether the growth or the earnings were worth it so as to maximize earnings of the business over its total lifetime because it is

³ *Some companies chalk this up to “LTV:CAC ratio”, which is important, but misses out on absolute values — and in the world of money... makes a big difference.)*

measuring both earnings collected today and projected earnings that were created today but should be collected tomorrow.⁴

One way to think about this is that net income (“NI”) measures the earnings that your company is collecting in the present, but were created in the past, *minus* what you are investing into the future. Projected lifetime earnings (“PLE”) measures the earnings that were *created* in the present but will be *collected* in the future. The way this is done is by taking your present net income, and then adding to it your LTVaCAC on an aggregated level from all customers acquired in the present measured period. After that, you can then add to this metric assumptions about future overhead costs and other layers of complexity. (This can all be done for different periods, such as monthly, quarterly, or yearly.)

Why is this so important? Because it helps to show that if an investment into growth—such as marketing—doesn’t increase PLE in the future by more than the NI is costing in the present, then that current investment is not worth making. And vice versa, if taking the NI in the present is less than the PLE could be worth in the future by current investment into growth, then taking that NI today is not worth it. (Unless there are other unique business needs, such as a cash crunch where you need the money now.)

For Cheers’ online business, absolute NI+PLE is the metric that we optimize for. This is the number — the combination of net income plus projected lifetime earnings — that we are trying to grow year after year. It’s the north star of our online business.

In practice, this has an interesting effect... revenue growth and earnings numbers are lumpy. If CACs are good, we spend heavily on advertising, which leads to a lower NI today, but a higher PLE tomorrow. But if CACs are bad, we pull back on advertising, which leads to a higher NI today, but a lower PLE tomorrow. This functions like a pendulum swinging one way or the other based on CAC prices. In the words of Buffett in a shareholder letter: “Charlie and I would much rather earn a lumpy 15 percent over time than a smooth 12 percent.”

In the case of companies like Casper and Blue Apron, each appears to have invested their raised capital into their own business operations at a negative ROI. They were spending more cash (e.g., \$2) to create less NI+PLE (e.g., \$1). In other words, their CAC, LTV, and overhead was a money-losing combination. Like a Ponzi scheme, a company can actually grow top-line revenue this way until it runs out of incoming investor money. Over time, this typically leads to a situation where the company has an accumulated deficit greater than their market cap — i.e., they have spent more money than the company is actually worth... which means they would have been better off never having never spent any money at all.

It’s for this very reason that when Cheers’ online business can’t find cheap enough CACs to increase NI+PLE by more than the investment we’re putting into it, we decide to hold onto

⁴ For the most part, cash flow and earnings at Cheers are tied quite closely together, and because liquidity hasn’t been an issue for quite some time, we typically just measure the earnings as it’s currently reflective of long-term cash generation.

the money instead of spending it on marketing — even if that means taking a tax hit on the retained earnings.

What keeps me up at night? The Buffett Test. Here's the oracle explaining it in his own words: "We feel noble intentions should be checked periodically against results. We test the wisdom of retaining earnings by assessing whether retention, over time, delivers shareholders at least \$1 of market value for each \$1 retained." In other words, if you're going to hold the money, you better figure out how to use it to increase the market cap by more than that over the long haul! The same should go for raising money.

Buffett, throughout his career, has maintained a bit over \$2 in market value per \$1 of earnings retained. Other "outsider CEOs", as profiled by Thorndike, maintained over \$3 throughout the course of their tenures. This is something that gets harder the larger a business grows. And as Cheers retains earnings, deploying capital in ways that boost market value is of the utmost priority.

The problem of CACs in a post-iOS 14 world.

One thing that has remained true over the years is that Cheers' LTVs have stayed more or less constant. It's quite rare for DTC CPG companies to be able to improve LTVs significantly. LTVs are typically stable at best but decline at worst. This is usually because the fittingness of a customer for a particular brand of products declines as the size of the customer pool increases. Even growing the product lineup sometimes only works to offset this reduction in fittingness as the customer base expands from niche to broad.

If LTVs are a constant, then that leaves you with two other levers: CACs and overhead. As far as overhead is concerned, the goal here is pretty simple: be more efficient as you scale so that your overhead grows slower than contribution margin after marketing—thus leading to boosts in operating margin. In other words: "Do more with less." For Cheers, we have been able to accurately predict overhead expenses as it is determined primarily by payroll, insurance, legal/accounting fees, and office/warehouse leases — all things that we have some control over. This makes them more or less stable in relation to our predictions. Very rarely do we have major surprises in the overhead bucket.

This leaves us with CACs. And unlike LTVs and overhead, CACs have been anything but stable throughout the life of Cheers. We have tried almost all major forms of advertising. Every time, digital advertising (auction-based channels) creates better returns whereas non-digital forms of advertising (non-auction-based channels) create lesser returns. The problem with this is that it has made us dependent on digital advertising supplied through Facebook, Google, and Amazon. Of these, Facebook (and its owned property, Instagram) has always been our favorite.

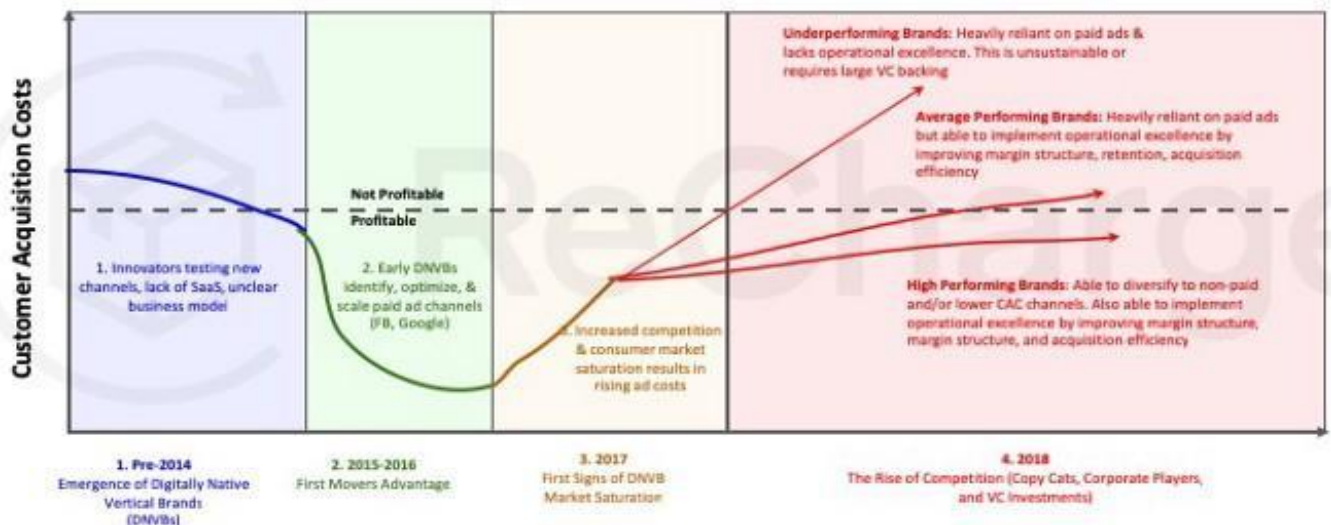
In fact, one of Cheers' advisors (Josh Hix, co-founder of Plated), wrote an entire [blog post](#) dedicated to the subject of "CAC is the net rent" in regards to his own company. It's worth the read. Other great articles on this subject include [The Law of Shitty Clickthroughs](#), [Why](#)

[premature scaling fails: The Traction Treadmill](#), and [Over 400 Startups Are Trying to Become the Next Warby Parker](#).

From 2014 through 2022, auction-based channels have been getting slowly, but significantly more expensive. Wilson Hung, Director of Growth at Kettle & Fire, wrote an article in Q4 2021 titled: [“How & why you need to improve LTV:CAC ratio”](#). In this article, Hung shares this chart with hand-drawn lines.

Survival of the LTV:CAC

the “easy” golden days are over & the bar has risen



This chart, while based on anecdotal evidence, feels true based on everything I have seen in the DTC industry. While I have never spoken with Hung personally, I believe that he would agree that we are a “High Performing Brand” given that we have been able to achieve profitable LTV:CAC ratios through our online channels for multiple years after many companies started getting capped out.

Recently, Apple’s iOS 14 software change has sunk its teeth into the efficacy of digital advertising. This has been especially problematic for Facebook, and by extension, Instagram. In short, Facebook tracks activities that occur off its app, such as your GPS and your internet purchases. This made it wildly effective at predicting the products you might want. Apple’s iOS 14 rollout made it mandatory that Facebook users volitionally choose to “opt-in” to this kind of activity rather than having the ability to “opt-out” in the settings menu as it was before. The choice of privacy was not new, it was just given a more prominent place.

As people started downloading and installing the new iOS version over the course of a few months they were hit with the opt-in prompt and then had to make a choice on the spot.

Word on the street is that about 95% of people decided not to opt in to off-app tracking, thereby picking privacy over personalization — the two of which are at odds with one another. It wasn't that big of a deal initially, as Facebook's algorithm for sending the right product ad to the right person at the right time still had plenty of fresh off-app data to use. However, as this off-app data has started getting stale, the efficiency of Facebook as a platform has only gotten worse.

Before the iOS 14 rollout occurred, Facebook's abilities likely looked something like this: If your brother just bought a cool pair of new Allbirds shoes, and then you hung out with your brother, chances are your brother is probably bragging to you about his new shoes and you're likely admiring them. Humans love to talk about what they spend their money on. Then a few hours later when you get home, voila, there's an ad for Allbirds on your Facebook/Instagram feed! Was Facebook eavesdropping on your conversation?! Probably not. Through browser tracking, Facebook probably knows that your brother just bought Allbirds, and through your GPS, probably also knows that you both hung out together that afternoon. The app likely made a guess that your brother would brag about them to you and thus primed you for being interested in buying a pair yourself.

Facebook was doing this at an extreme scale. Hundreds of millions, if not billions, of ads every single day. It was doing this for shorts, bicycles, toothbrushes, airline tickets... you name it. And it was likely connecting all kinds of weird dots, such as people who start going to the gym having a higher likelihood of buying keto products. Went to the gym and now see a keto product ad? That's probably not a coincidence.

It's impossible to know how this was working in Cheers' favor. Was it because the app knew who went to bars on Thursday evenings? Was it because it knew who had recently bought tickets to go on vacation? Was it because it knew who had just got engaged and would have a series of parties ranging from bridal showers to bachelor parties? Did those factors make them more likely to buy Cheers? Who knows!

None of this stuff was available to Cheers. It was pretty much a black box for us advertisers and it worked fantastically. Now that Facebook has lost ~95% of this off-app data to optimize off of, and with each month is moving further away from their last off-app data (a problem of "aging data"), the degradation of Facebook advertising performance has accelerated significantly. I believe that this will continue to be the case in 2022. Therefore, in my opinion, 2022 marks the end of the digital advertising era, which was the reason for the explosion of DTC startups in the first place.

If someone asked me: "If you could have done one thing differently so far as CEO of Cheers, what would it be?" My answer would be simple: "I would have been born in 1989 rather than in 1993!"

I didn't raise money or start full-time work on Cheers until I graduated from Princeton in 2017. We didn't know it at the time, but that meant Cheers missed out on the bulk of the golden era in digital advertising that spanned from 2015 through 2017. I know of one friend who built his business to about 5x our current size from 2014–2017 before it started getting

stuck in 2018 with the rising CAC prices — which was actually our largest growth year. And we kept growing well for the next few years beyond that! It suggests that our business may actually be more efficient than theirs had they competed in the same time period. (It's kind of like comparing Tiger Woods to Jack Nicklaus, or LeBron James to Michael Jordan, each of whom competed at different times and with different fields of players. You'll never really know who was better or what the other would have been capable of if they switched time periods.)

It's painful to think about how big Cheers would be if we had raised money, started full-time work on Cheers, and went “all in” on digital advertising in 2014 rather than 2017. Would it be \$25m in revenue? \$50m like my friend's company? More? Who knows... but such thoughts are unprofitable.

Instead, what we have realized is that we are very blessed to have gotten in on the tail end of the digital advertising era at all. Our recent attempt to launch a second brand, [Lightspeed](#), has failed miserably because the CACs are simply too high now to get the business off the ground, much less get it to profitability. We're currently trying to sell through our remaining inventory and discontinue the brand once the product expires. We have determined it best just to focus on the Cheers brand.

When looking on the bright side, high CACs help incumbents — i.e., Cheers — who have already acquired large sums of customers and established significant brand equity in the consumer's mind. For smaller, copy-cat competition that is just starting out, a high CAC environment should be far more expensive to acquire customers and close the gap between the scale of our two businesses.

As alluded to above, the plan is for us to expand into brick-and-mortar retail now that we're convinced that online growth is unlikely. Our beloved metric for our online business, NI+PLE, declined in 2021 and likely will in 2022 as well. You might be wondering: “Why didn't they think of going into retail sooner?” The answer is that we did, and tried.

In late 2019, Cheers started laying the plans for retail expansion the following year. In Q1 of 2020, Cheers was in full fundraising mode, pitching VC firms in NYC with the plan of using Series A funding to go towards launching Cheers in brick-and-mortar retail stores. Based on the dates, you can probably guess how this story ends. Shortly after returning from our NYC trip, around March 15th the world came to a halt because of some novel disease that no one knew anything about called “the coronavirus”. At that time, VC firms weren't interested in investing until the “dust settled”, retail stores weren't taking meetings until things were “more normal”, and we ultimately decided to postpone our retail ambitions.

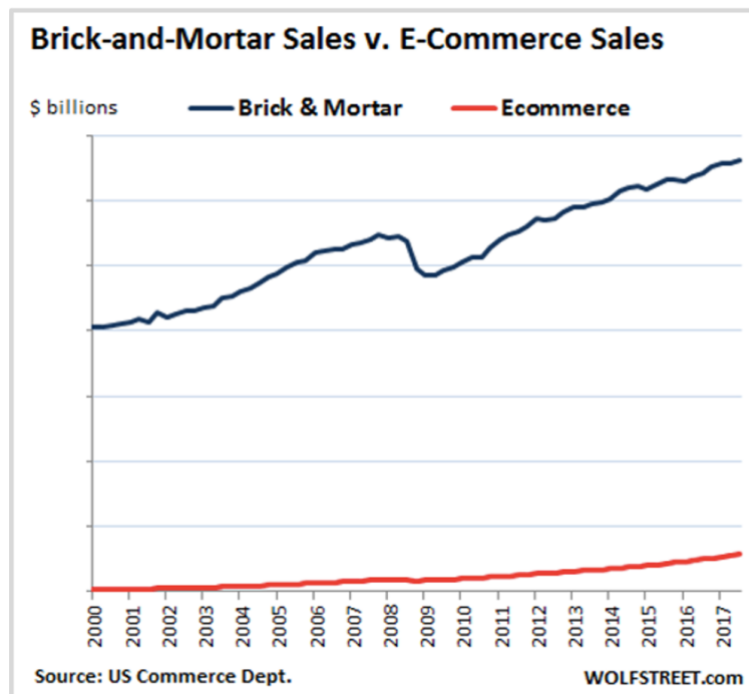
For us, iOS 14 isn't the end of the world. It is not causing us to pivot. Retail distribution has always been part of the plan and rising CAC prices are simply making us more focused on the original plan — albeit with more speed.

3) Brick-and-mortar retail is Cheers' next frontier of growth.

The time is now.

Riding on the backs of the rise of digital advertising and social media giants, DTC companies shot onto the scene in the 2010s promising customers lower prices and investors greater returns because they were able to “cut out the middleman” of traditional brick-and-mortar retailers. Over the past decade, especially as we have entered the 2020s, we have seen one major problem develop with this strategy — CAC prices have risen. Hence the coining of the phrase: “CAC is the new rent.” DTC companies didn’t actually get rid of the middle man, they simply replaced them with a different middle man, namely “FAMG” — “Facebook, Amazon, Microsoft, and Google” — as well as FedEx, UPS, and the USPS. And as it turns out, these new middlemen are often worse than the original! (My father-in-law often reminds me that if FedEx and UPS had a merger, “FEDUPS” would make a great name.)

I have had some associates say to me: “Why spend so much trying to get into brick-and-mortar retail? eCommerce is the future!” I agree with the premise, but the conclusion is flawed. eCommerce may be the future... but it’s not the near future.



It is true that each year eCommerce will take a larger percentage of the total commerce pie. In fact, eCommerce is taking about 1% more of the total US retail revenue pie each year.

Because of this, it is likely that eCommerce will be more important in the future than it is today.

There is however one major problem with believing that eCommerce is the “future” and brick-and-mortar retail is the “past”... eCommerce only currently makes up about 15% of all US retail sales—even during the height of a global pandemic! In other words, 85% of product revenue is still generated in physical stores. Even if eCommerce takes 1% more of the total retail sales pie each year, a fantastic growth rate, it will take another 35 years to get to a 50/50 split where eCommerce is equal to brick-and-mortar retail in terms of absolute volume. And even then, why would anyone want to leave half of all US retail sales untapped?

When I founded Cheers in 2014 brick-and-mortar distribution was always the long-term goal. The reason we pursued eCommerce first was because it represented a cheaper, faster, and lower-hanging fruit for initial growth. Brick-and-mortar is a long, expensive journey, and we weren’t going to get very far very quickly with the \$20k I started the business with in mid-2014, or the \$200k that we had raised in mid-2017. For all the reasons stated during our CF raise, we believe the time is now for Cheers’ expansion into brick-and-mortar retail.

Examining outsized acquisitions.

In 2017, the international alcohol conglomerate Diageo purchased Casamigos Tequila for \$700m in cash plus a \$300m “earn out” potential based on the performance of the brand over the next 10 years. This means the total sale price of the brand is somewhere between \$700m and \$1b. Other brands, such as Ryan Reynolds’ Aviation Gin have received similar deals. Casamigos is a mid-tier priced tequila that retails to the end consumer for around \$50/bottle (~\$300 case). The brand was founded in 2013 by George Clooney (actor), Rande Gerber (entertainment industry businessman), and Mike Meldman (real estate tycoon).

In a [press release](#), Diageo points out that Casamigos sold 120k cases in 2016 and then was on track to sell 170k in 2017. They said that Casamigos had a compound annual growth rate (CAGR) of 54%. This comes out to around \$36m in retail sales in 2016 and \$51m in 2017 — maybe a little more or less depending on which cases were selling the best.

My estimates are corroborated by comments from Morgan Stanley in a [Reuters article](#): “Diageo did not disclose revenue or profit figures, but Morgan Stanley estimates the deal’s enterprise value was about 20 times annual turnover, which an industry source said would make it much pricier than other spirits deals, which he said often get done at about 4 to 6 times sales.”

Assuming some pretty standard retail margins and distributor markups in the alcohol industry, and giving it a *super* wide range, this would put Casamigos’ revenue around \$9–18m in 2016 and \$13–25m in 2017. From what I can tell in other press releases and the level of their advertising, Casamigos likely wouldn’t have been profitable. This would especially be the case if Clooney was charging cash for the use of his likeness rather than

just benefitting from the appreciating stock. Even once pumped into the Diageo distribution network, Diageo [said](#): “Casamigos would be neutral to earnings for the first three years.”

Whether it’s \$13m or \$25m, it doesn’t matter much because the business ended up selling for \$700m-\$1b! That’s a whopping 28–77x revenue. In either case, this is a freakishly outsized acquisition price for the scale of the Casamigos business. For context, that would have been like valuing Cheers somewhere around \$300–\$800m... which would be a fantastic outcome based on our current levels of funding.

Is this outsized acquisition price explained by the CAGR of Casamigos, as the Diageo press release suggests? I don’t believe so. Frankly, having pockets and connections as deep as the Mariana Trench between the wealthy three star-studded founders, getting to ~\$20m in revenue in 5 years isn’t that impressive. Especially when one of those founders is George Clooney, and he is slapping his face all over delivery trucks and advertising, pumping the brand via his social media, and getting other “earned media” from his press industry friends. I would have suspected far greater numbers... After all, Cheers got to about half of this in a similar time frame without any of the star-studded running start that Casamigos benefitted from.

As reported by Reuters, North American president of Diageo, Deirdre Mahlan, told the press that high-growth companies like Casamigos were ‘notoriously challenging to value under traditional methods.’’ “Notoriously challenging” is corporate PR lingo for saying that the deal doesn’t make any sense using the company’s P&L or other financials. So, what could explain this acquisition price, besides the fact that George Clooney was a primary owner? If we assume that Diageo is a competent buyer and of sound mind — something which is always an assumption in the corporate world during a bull market — then we have to speculate that Diageo saw a metric they *loved* that isn’t reflected under standard financial accounting.

Here’s my guess: Casamigos was seeing phenomenal per-store economics. People wanted to try the product, and those who did became repeat buyers. Together, this led Casamigos to become a big revenue driver per point of distribution relative to other liquor brands. E.g., If Casamigos is beating Patron 2-to-1 at the relatively few stores it’s in... imagine if these numbers scaled to every store that Patron is in!

For a company like Diageo, which has an “in” with hundreds of thousands of locations, this could mean big money. If Casamigos is only in a few thousand stores, and Diageo has the ability to put them into a few hundred thousand stores, then there is a whole lot of meat left on the bone to scale the brand upon acquisition. If you believe that the brand is going to succeed throughout your network—which could be as large as an enterprise value of many billions—then you’re not going to be as cost-sensitive in the acquisition price, leading to an outsized valuation “under traditional methods”.

Cheers’ approach: Win the per-store economics

At Cheers, we have always seen a difference between a business' "metrics" and its "financials". Metrics are things that managers use to understand the unique underlying characteristics of their business like "CAC". Financials are things that are found on standard financial statements such as the "net operating income" on the company's Statement of Operations. One could argue that a company's metrics are what ultimately determine a company's financials. E.g., for most DTC businesses, how strong their P&L is ends up being is closely related to how good or bad their CAC and LTV metrics are.

Cheers' management currently believes that per-store economics — which is what we like to call the business' "micrometrics", are currently more important than other metrics such as the business' total CAGR of sales — which is what we like to call the business' "macrometrics". A company's macrometrics are simply the sum of its micrometrics. As we begin our retail endeavor, we will lean towards going slow and getting our micrometrics right prior to scaling them to the macrometrics level of the business. This means that in the early stage of our brick-and-mortar expansion, these efforts are unlikely to have large positive impacts on our financials.

One of my mentors at Princeton once told me: "When Ray Kroc was building the McDonald's empire, he was excited about the initial per-location economics of the first few locations. Once he saw that the per-location economics could successfully be replicated in different markets, he didn't need to be a genius to understand how valuable the business would likely become." If the per-location economics of McDonald's didn't make sense at the first few locations, what would be the point of scaling them? The fact of the matter is that poor micrometrics almost always scale into poor financials. And on the other hand, great micrometrics usually have the ability to scale into great financials, and typically with far less fundraising dilution and risk—which is great for shareholders.

Many VC-backed companies have fallen under the trap of scaling poor micrometrics and hoping they can figure out how to cure the poor underlying fundamentals at a later date once they are larger. Just because you can raise funds and spend more money doesn't mean you should. The problem with this strategy is that small problems, when scaled, become even larger problems—and usually even harder to get out of! Just look at what has occurred to companies such as Casper when they tried to scale poor per-customer micrometrics. Scaling crappy business metrics only makes sense if you're in the manure industry.

One of our investors, Founder Collective, has written an *excellent* piece on this subject called [Toxic VC and the marginal-dollar problem](#). It was [articles from their partners](#) like this that drew us to accept a check from them in our seed round.

Cheers is currently laser-focused on finding good per-location metrics for our brick-and-mortar business prior to stepping on the gas. In the past few quarters, we have been testing different types of locations ranging from bars, to liquor stores, to grocery stores, to convenience stores. We hope to test even more types of locations in the coming months. The collection of more data will help us further inform our retail expansion strategy and how best to get an ROI on both the funds we have raised and the earnings that we are

retaining. As stated above, my belief is that Casamigos got such an outsized acquisition because Diageo must have *really* liked some of their per-location metrics.

There is, of course, one downside to this strategy... It involves the appearance of moving slower. This strategy comes at the expense of short-term financials and growth. It is our expectation, however, that this investment of time and funds is well worth it over the long haul. We believe that picking the right numbers to scale will save both time and money over the course of the business' total history. We have worked really hard to build a balance sheet that gives us the time and resources to get this new business expansion right.

I'll end with some 3,000-year-old wisdom from King Solomon: "If the iron be blunt, and he does not whet the edge, then must he put to more strength: but wisdom is profitable to direct." Many quotes have been adapted from this, but the significance is all the same. If you're going to do something and your tool is dull, then it's smart to sharpen your tool before getting started as it will ultimately save you time and energy.

Like all things, this advice is not black and white and there is some discernment necessary. Sharpening something eventually has diminishing returns. So, wisdom is required to know when to stop sharpening and when to start cutting! This is something that Cheers will have to figure out over the coming year as we continue to explore brick-and-mortar retail expansion.

Miscellaneous Topics:

New Products.

We are in the process of launching two new products: Cheers Relief and Cheers Multi. Cheers Relief is a next-day alleviant designed to be taken the day after consuming alcohol to help you feel better. Cheers Multi is a multivitamin designed specifically with drinkers in mind—and to our knowledge, is the first multi-vitamin ever created for those who drink. The launch of these two new products represents the first additions to the Cheers lineup since Cheers Protect in 2019. We are very excited about both and have *loved* using them in the R&D process. (One of the many perks of working at Cheers...)

Cheers Relief contains around 25mg of cannabidiol (CBD) (each lot will be +/- a few), 1000mg of ginger (the same clinically tested amount as Dramamine Non-Drowsy), 130mg of organic caffeine (the same as in 2 caplets of Excedrin Extra Strength), 162.5mg of l-theanine (the stuff in green tea that makes the caffeine less intense), and a typical dose of b-vitamins. As you can see, we didn't hold back when it came to making this product. There is a whole lot of firepower in there!

Cheers Relief is a product that has been on my personal wishlist since 2018. I began exploring the development of this product in 2019, experimenting with everything from compounding pharmacies to purified salicin from white willow bark — i.e., "nature's aspirin". We weren't happy with the results from any of these experiments... and life is too short to make any products that we aren't proud of. It wasn't until we started combining fast-acting CBD and high doses of ginger inside strong green tea that we found something that would really take the edge off. We then worked to get this product into multiple form factors: pills and beverage—just like Restore. Initially, the beverage will only be available through retail.

The use case for Cheers Relief is two-fold: 1) if you forget to take Cheers Restore, or 2) if you took Cheers Restore, feel 50% better, but still really need that next 50%! Even as Cheers' founder, I'm not too proud to admit that both happen to me with some regularity.

My favorite memory during R&D was waking up for an early Saturday round of golf with Seth feeling queasy and miserable from purposely not using Restore the night before. (I regularly volunteer as a product tester!) I chugged a can of Relief before hopping in the car for a 30-minute drive, and by the time I was pulling into the parking lot, I realized that all my misery had left me at some point during the drive. I carded two birdies on the front 9 in the pouring down rain before they shut the course down. My golf game has suffered miserably once I used up all of the testing samples and have had to wait for our first shipment to be delivered from our manufacturing facilities! I hope that you'll experience the magic for yourself sometime soon.

Manufacturing and selling CBD involves a ton of laws and logistics. It has not been an easy process. Hank Holcomb (CTO), Dalia Steichen (Creative Director), and Kelsey Mathews (Operations Manager) all deserve a huge round of applause for turning this product into a reality. Inventing the product was easy, but getting it to market has been a marathon.

Cheers Multi was born from our Liver Habits Score research. What we found is that just like an athlete needs more protein than the average person, people who drink — such as 2–3x per week — also have different nutritional needs than the average non-drinker. Two of the big necessities here are choline and b-vitamins.

Originally, we were looking at launching another product similar to Cheers Protect that could go along with a multivitamin. However, we were weary of how many pills this meant someone would need to take. Therefore, it made the most sense for us to formulate these findings into a multivitamin. That way, if someone is already taking a multivitamin, they can simply replace their current multivitamin with ours if they are someone who drinks alcohol with any regularity.

I personally use all of Cheers' products, as do most of the people on Cheers' team. In many ways, we're making products for ourselves. We have found that if we like our products, the market tends to as well! We're currently in the process of working on R&D for more products. With the dropping of Lightspeed, we have more time and energy to focus on our further expansion of products that fall under the category of alcohol-related health.

Plastic Packaging.

If you have ordered any Cheers recently, then you may have noticed we've switched from glass to plastic packaging. There are three major advantages that plastic jars have over glass jars that led us to this decision: 1) it saves shipping weight, 2) it doesn't break, and 3) it's what retailers want. Plastic does all of this while still being recyclable. With inflation having been rampant over the past 2 years, saving funds on shipping and breakage is very important in our goals of trying to keep our prices the same. Historically, about 1% of all Cheers packages break in transit and Cheers either has to send a replacement or refund the order. Not only is this expensive and leads to a bad customer experience, it's also wasteful.

While we're excited for the opportunities that the switch to plastic jars will afford us moving forward, the transition has not been 100% seamless thus far, as some of you may have experienced. Our biggest screwup in supply chain this year occurred in the production of the first lot of Cheers Hydrate with the new plastic packaging. Long story short, Hydrate powder is finding its way into the threads of some of these jar/lid connections during transit, crystalizing, and then making them virtually impossible to open. I say virtually impossible, because of the affected jars sent back to us, I've witnessed Hank (who has arms like pythons) open jars that no one else on the team could. It's what I imagine watching King Arthur pull Excalibur out of the rock must have looked like.

We didn't know that this was a problem with Cheers Hydrate until customers started emailing us saying that they couldn't get their jars open. We don't yet know the exact rate that these jars are being affected in transit, but our solution has been to do the right thing and refund and/or replace them when people have an issue. Future Hydrate jars will be fixed by including a seal inside between the jar and the lid rather than just encapsulating the outside of the jar. In fact, we've already received a subsequent lot of Hydrate for which this issue has been eliminated. If you have received an affected Hydrate jar, please let us know and we will make it up to you.

Competition:

Friends, family, and investors send us pictures of both old and new competitors on a regular basis. This shouldn't be surprising, as mentioned earlier, Cheers' success has spawned an industry of copy-cat products that's closing in on 100. We expect in the coming years for this number to continue to grow.

We won't lie... it is annoying. We watch them copy our products, website elements, ads, emails, product descriptions, and even vocabulary terms that we have invented — e.g., “hangxiety”. Dalia even goes so far as to keep a whole folder of screenshots on her computer labeled “cheaters” in case we ever find it prudent to build a case against any of them. We also keep folders for patent infringement.

Personally, I don't get the appeal. You only live one life, are you really going to spend it copying someone else's work?

If they're not copying our work, you will often see them doing some things that are very problematic. One brand, in particular, is running a series of ads showcasing people binge drinking (e.g., one girl having 20 shots in an evening) and then using the products and feeling totally fine. Besides Cheers' mission to promote fun, responsible, and health-conscious alcohol consumption, the FDA has taken the position that alcohol intoxication is a disease. Run long enough, these companies will probably receive a warning letter from the FDA. For both moral and legal reasons, Cheers stays away from all references to alcohol intoxication and other potential promotions of binge drinking. If you have just been hired to Cheers, this is one of the first things that gets drilled into your head throughout onboarding.

For the companies that compete on price alone, almost all of them have formulas hidden behind proprietary blends so as to save money by reducing their use of expensive ingredients. One popular brand on Amazon is about half the price of Cheers Restore. It also happens to contain about half the amount of DHM that's in a dose of Restore's capsules — but most people wouldn't know that because they purposefully hide the amount of DHM in their formula behind a proprietary blend. There are bad ways to save money in the dietary supplement industry, and most of them involve watering down the product or cutting corners when it comes to manufacturing and testing. Therefore, when it comes to efficacy, quality, and safety, we believe that Cheers is well worth the nominal increase of a few bucks against other lower-priced offerings in the market.

Of course, compared to other competitors, such as those sold for \$5–7 per 3.4oz shot... Cheers is clearly a steal. One competitor even goes so far as to sell their liquid shot for \$9–12 per bottle!

In Berkshire's 2000 letter, Buffett goes on to explain one of the factors behind why State Farm had more market share than GEICO, which is owned by Berkshire. Buffett writes: "State Farm had an underwriting loss last year from auto insurance (including rebates to policyholders) of 18% of premiums, compared to 4% at GEICO. Our loss produced a float cost for us of 6.1%, an unsatisfactory result. (Indeed, at GEICO we expect float, over time, to be free.) But we estimate that State Farm's float cost in 2000 was about 23%." A year later, in a section about General Re — one of Berkshire's other insurance businesses, Buffett further says: "If 'winning,' however, is equated with market share rather than profits, trouble awaits. 'No' must be an important part of any underwriter's vocabulary."

I believe that Buffett is implying here that oftentimes companies will make uneconomic moves to grow their business or "beat" competition. We have experienced this in the past and will likely experience it in the future. To our knowledge, one of Cheers' largest competitors has raised roughly 4x more capital than Cheers to achieve a similar amount of revenue over the same time period. Cheers' mantra of "doing more with less" leads us to keep a discipline of only spending on growth when we believe that it makes economic sense to do so. Ultimately, this sometimes will come at the expense of the business shrinking or competition getting "ahead" of us. It usually doesn't pay to win a race that finishes over a

cliff. We are only focused on the race we want to win, which is ultimately increasing the stock value of Cheers through creating the best possible products and creating fundamentally sound distribution for them.

Closing thanks.

If you made it to the bottom of this 10,000+ word letter, kudos to you! I have quoted the Roman philosopher and statesman Marcus Tullius Cicero before, and I will quote him again: “If I had more time, I would have written a shorter letter.” This letter has explained a lot of concepts unique to Cheers, many of which can be referred back to in future letters, ideally making them shorter. I hope that it helps you understand how we think about Cheers and how we are being faithful to steward your support.

There are many people that are deserving of gratitude that were not included in the body of this letter. Throughout the years, I hope to highlight more that make up the DNA of Cheers’ team. Two that stand out today include Rebekah Hazleton and Cole DeVilliers, both of who are doing an excellent job leading the charge into retail. And of course, it wouldn’t be fitting to end this first letter without mentioning Leah Nguyen, who joined Cheers shortly before Cheers pursued Regulation Crowdfunding and is ultimately the reason we ever got any funding at all! The reason you’re reading this letter today is in a large part because of her. We’re also very thankful for our warehouse staff, which is such a well-oiled machine that we hardly ever hear from them unless HQ screws something up. (Sorry!)

On behalf of Cheers’ management team, I sincerely thank all the shareholders for their support of this company and its future.

Sláinte! (“Cheers” in Irish),

A handwritten signature in blue ink, appearing to read 'Brooks Powell', with a stylized, flowing script.

Brooks Powell (Founder & CEO)