BCP Research: Aurora Cannabis Inc (ACBCN)- 1Q21 Results, Mixed – Maintain Neutral

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Summary: Canadian-based cannabis producer, Aurora Cannabis Inc (Aurora) released 1Q21 results showing increased sales y/y but lower sales q/q. Average net selling price of dried cannabis came down y/y, but improved q/q. Net revenues were lower y/y and q/q, but exceeded guidance, aided by growth in Cannabis 2.0 products and international medical sales. We highlight additional progress in Aurora's European markets, with EU-GMP certification achieved at Aurora's Nordic 1 production facility. Adj. EBITDA was negative US$43 mm, driven primarily by US$32 mm in one-time costs related to the cancellation of Aurora's contract with UFC, and US$3 mm in costs related to the companies ongoing transformation plan. Excluding these charges, adj. EBITDA showed y/y and q/q improvement, reaching negative US$8 mm, in line with the company's minimum adj. EBITDA threshold for 1Q21 under certain financial covenants. Free cash flow was negative US$83 mm, attributable primarily to the one-time cancellation costs and working capital outflow. Cash decreased to US$113 mm at 56% cash to LTM revenue, with cash outflow balanced by the inflow of US$86 mm in net proceeds from the company's At-the-Market (ATM) program. Net debt stayed flat at US$371 mm. pro-forma total available liquidity of ~US$375 mm, and includes US$119 mm in undrawn secured credit facilities, and additional ATM program net proceeds raised post-1Q21.

Looking ahead, the company intends to focus on the sale of higher margin premium quality flower, vape and pre-rolls, while de-emphasizing focus on lower-potency value branded products. Management is targeting 35,000 kg in production per quarter, measurably reduced from recently documented output (44,406 kg 4Q20), and tied to the planned closure of five (5) facilities, already underway. This rationalization of production alongside reduction of operational costs is expected to translate into positive adj. EBITDA generation in 2Q21 (Dec. '21). Nevertheless, the sharp q/q increase in inventory levels and inventory days in 1Q21 imply the company has not yet brought its supply chain under control. Therefore, we maintain our 'Neutral' rating on ACBCN 5.5% 24s at 57c, awaiting more tangible evidence of industry consolidation and improved supply v. demand balance, which could help the credit emerge from distressed pricing levels.

	Amt Out (US$ MM)	Mid Price	Mid YTW	Conv. Price	ACB US Price
ACBCN 5.5% 2/28/2024	345	57.0	25.74%	$86.72	$11.21

Source: Equity information sourced from Bloomberg. Stock price as of close November 9, 2020. Convertible pricing as of open November 10, 2020.

<u>1Q21 (9/20) Financial Results:</u>

- Production volumes were not disclosed in 1Q21. Most recent disclosures (4Q20) show the dislocation between production v. sales widening, balanced by forward looking guidance from management, targeting an average of 35,000 kg per quarter with 65%+ meeting top quality flower standard
- Sales increased 29% y/y, but decreased 4% q/q to 16,139 kg, balanced by a decrease of 25% y/y and increase of 7% q/q in average net selling price of dried cannabis to US$2.79/gram
    - The company has emphasized its intention to pivot its focus to the sale of higher margin premium quality flower, vape and pre-rolls, while de-emphasizing focus on lower-potency value branded products
- Cannabis inventory was 26% higher y/y and 28% higher q/q at US$91 mm, driven primarily by increase in harvested cannabis (+13% y/y, +57% q/q) and extracted cannabis (+190% y/y, +8% q/q)
    - We anticipate the planned closure of five (5) facilities, already underway during 1Q21, will results in lower production output
    - However, the elimination of production volumes from disclosures and sharp q/q increase in inventory levels implies the company has not yet brought supply/demand under control

- Inventory days, totaling 251, decreased 5% y/y, but increased 29% q/q following the charge to inventory which occurred in the prior quarter, and providing further evidence for implications surrounding supply/demand chain management

APHACN (US$MM)	1Q21	4Q20	3Q20	2Q20	1Q20	y/y	q/q
Kilograms produced, net	n/a	44,406	36,207	30,691	41,436	-	-
Kilograms equivalent sold	16,139	16,748	12,729	9,501	12,463	29%	(4%)
Average net selling price of dried cannabis	2.79	2.60	3.45	3.49	3.71	(25%)	7%
Cash cost to produce dried cannabis / gram (USD)	n/a	0.64	0.91	0.78	0.80	-	-
Harvested Cannabis	48	31	62	52	42	13%	57%
Extracted Cannabis	30	28	36	24	10	190%	8%
Capsules	-	-	-	-	3	-	-
Hemp Products	1	1	12	12	7	(91%)	(33%)
Supplies, Consumables & Other	12	12	12	10	9	30%	2%
Cannabis Inventory	**91**	**71**	**123**	**99**	**72**	**26%**	**28%**
Cannabis COGS *	32	33	35	22	25	32%	(1%)
Cannabis Inventory Days	**251**	**195**	**312**	**403**	**264**	**(5%)**	**29%**

** 4Q20 cost of goods sold adjusted to exclude US$76 mm (CAD 106 mm) non-cash charge related to charge to net realizable value of inventory*

- Net revenue of US$51 mm (-9% y/y, -4% q/q) exceeded guidance of US$45 mm (CAD 60-63 mm), with improvements in medical and consumer cannabis revenue balanced by higher excise taxes and the elimination of auxiliary revenue
  - Consumer cannabis net revenue of US$26 mm was 13% higher y/y and 1% higher q/q, with net revenue growth for Cannabis 2.0 products outweighing sequential decline in consumer dried cannabis net revenue as a result of market share losses related to the influx of value brands into the domestic consumer markets
  - Medical cannabis net revenue of US$25 mm increased 9% y/y and 8% q/q, driven primarily by growth in international medical sales
- SG&A expenses were US$33 mm (-39% y/y, +5% q/q), slightly higher than company guidance of below US$29 mm (CAD 40 mm) for the quarter as a result of ongoing divested business and severance and benefits costs associated with the company's transformation plan
- Adjusted EBITDA of negative US$43 mm was higher y/y but lower q/q, following higher improvements to operating loss y/y and q/q balanced by a US$32 mm one-time legal settlement and termination fee tied to the cancellation of Aurora's contract with UFC, and US$3 mm in costs related to the aforementioned transformation plan
  - Excluding these charges, Adj. EBITDA was improved y/y and q/q at negative US$8 mm, within the company's minimum EBITDA threshold of negative US$8 mm, in line with financial covenants under Aurora's credit facilities
- Free cash flow was negative US$83 mm in the quarter, attributable primarily to the one-time legal settlement and termination fee and working capital outflow
  - Working capital use was US$27 mm in the quarter, mainly driven by a US$10 mm increase in A/R and US$16 mm increase in biological assets
  - Capex was US$12 mm in the quarter, 52% lower q/q v. 4Q20, and in line with company guidance
    - The company plans to deploy less than US$30 mm (CAD 40 mm) in capex in FY21
  - Lease liability payments were US$1 mm

- Cash (incl. marketable securities) decreased 9% q/q to US$113 mm at 56% cash to LTM revenue, with cash outflow in the quarter balanced by US$86 mm (CAD 114 mm) in net proceeds raised from the company's At-the-Market (ATM) program
    - The company raised an additional funds under its ATM program in October '20 (post-1Q21), increasing cash to ~US$200 mm (~CAD 270 mm), including reported marketable securities as of end-1Q21
- Liquidity (cash + A/R) decreased 3% q/q to US$169 mm at 84% liquidity to LTM revenue
    - Pro-forma total available liquidity, including the US$119 mm undrawn portion of the company's US$195 mm secured credit facilities and above mentioned ATM program net proceeds, is estimated to be US$375 mm
- Gross debt decreased 2% q/q to US$484 mm, driven by debt and lease obligation payments, while net debt stayed flat q/q at US$371 mm
    - Debt is comprised of the US$375 mm senior unsecured convertible ACBCN 5.5% 24s, US$76 mm drawn portion of Aurora's secured credit facilities and US$63 mm in lease liabilities
        - The US$195 mm secured credit facilities (US$76 mm drawn) are senior to convertible bonds and subject to certain financial covenants under agreements with syndicate banks, including Bank of Montreal and other lenders
            - Aurora reached an agreement with syndicate banks in the quarter to amend certain financial covenants, including the extension of positive adj. EBITDA attainment to 2Q21, and reducing the size of its secured credit facilities to US$195 mm
            - Other revised financial covenants include:
                - Total funded debt to shareholders' equity ≤ 0.25:1 from Dec. 31, 2020 forward
                - Total senior funded debt to EBITDA ≤ 3:1 at June 30, 2021
                - Minimum unrestricted cash maintenance of US$35 mm
                - Minimum EBITDA threshold of: -US$8 mm (-CAD 11 mm) for 1Q21, US$3 mm (CAD 4 mm) for 2Q21, US$7.5 mm (CAD 10 mm) for 3Q21, US$13 mm (CAD 17 mm) for 4Q21, and US$15 mm (CAD 20 mm) for FY21
- We note prior results were restated to exclude certain discontinued operations, as well as changes in accounting policies relating to by-products inventory costing and the allocation of salaries related to production staff

APHACN (US$MM)	1Q21	4Q20	3Q20	2Q20	1Q20	y/y	q/q
Net Revenue	**51**	**53**	**56**	**42**	**56**	**(9%)**	**(4%)**
Adjusted EBITDA	**(43)**	**(23)**	**(38)**	**(60)**	**(25)**	**74%**	**87%**
Adjusted EBITDA margin	*(85%)*	*(44%)*	*(67%)*	*(143%)*	*(45%)*	*(4,051bps)*	*(4,156bps)*
Interest Paid	n/a	n/a	n/a	n/a	n/a	-	-
Taxes Paid	n/a	n/a	n/a	n/a	n/a	-	-
Working Capital	(27)	35	(41)	(36)	(35)	(22%)	(177%)
Accounts receivable	*(10)*	*13*	*12*	*7*	*9*	(210%)	(180%)
Biological assets	*(16)*	*(4)*	*(23)*	*(7)*	*(11)*	42%	268%
Inventory (1)	*(3)*	*2*	*(24)*	*(22)*	*(10)*	(74%)	(255%)
Prepaid and other current assets	*5*	*19*	*(10)*	*4*	*(13)*	(141%)	(72%)
Accounts payable and accrued liabilities	*(2)*	*4*	*9*	*(22)*	*(6)*	(72%)	(148%)
Deferred revenue	*(1)*	*(1)*	*(2)*	*4*	*(0)*	1,318%	60%
Provisions	*(0)*	*3*	*(3)*	*-*	*(3)*	(87%)	(114%)
Capex	(12)	(25)	(62)	(97)	(81)	(85%)	(52%)
Lease Liability Payments	(1)	6	(7)	(3)	(2)	-	(118%)
Free Cash Flow	**(83)**	**(7)**	**(148)**	**(196)**	**(143)**	**(42%)**	**1,139%**
Cash (2)	**113**	**125**	**172**	**130**	**145**	**(22%)**	**(9%)**
Accounts receivable	56	40	57	59	69	(19%)	39%
Liquidity	**169**	**165**	**229**	**188**	**214**	**(21%)**	**3%**
Loans and Borrowings	139	150	191	214	213	-	(8%)
Convertible Debentures (3)	345	345	345	345	345	0%	0%
Total Debt	**484**	**495**	**536**	**559**	**558**	**(13%)**	**(2%)**
Net Debt	**371**	**371**	**363**	**429**	**413**	**(10%)**	**(0%)**
Cash to LTM Revenue	**56%**	**60%**	**76%**	**59%**	**66%**	***(1,042bps)***	***(419bps)***
Liquidity to LTM Revenue	**84%**	**80%**	**101%**	**86%**	**98%**	***(1,451bps)***	***406bps***

(1) Excludes non-cash charge to net realizable value of inventory
(2) Includes cash and equivalents, ST investments and marketable securities
(3) Convertible debentures valued at par

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