4 Emerging Trends as Aurora Cannabis (TSX:ACB) Targets Operating Profitability

Description

Marijuana player **Aurora Cannabis** (TSX:ACB)(NYSE:ACB) released its fiscal third-quarter earnings on May 14, and management reiterated an earlier promise for an operating-earnings-positive quarter in the next installment.

The company had reported ever-widening operating losses over several quarters in the past, as management went all out on an aggressive acquisitions-led growth spree, but there have been some notable emerging trends that investors may find encouraging, as the company tries to prove that its operations can indeed become profitable.

Here are some of the notable moving parts in the company's earnings and emerging trends that could affect positive EBITDA this quarter.

Medical cannabis on strong show

The company's higher-margin medical sales segment recorded some impressive growth numbers during the first three months of 2019 with a 12% sequential increase in net revenue to $29 million. Segment revenue growth had significantly stalled just prior to recreational sales launch last year, and the recent return to double-digit growth is encouraging.

Fueling the strong return to growth was a 5% quarter-over-quarter increase in medical patients over 77,000 patients during the last quarter, and the company has reported a further 7% jump in active patient count to nearly 83,000 patients by mid-May 2019.

This segment may continue to deliver strong margins in the future and support low sales volatility, as patients aren't likely to switch products as much as recreational consumers may.

Production costs decline

The cost of producing a gram of product declined by 26% over three months to $1.42 per gram — the lowest reading in four consecutive quarters. Costs per gram are expected to continue declining over the near term as low-cost Aurora Sky harvest constitutes the bulk of harvested inventory.

Technological efficiencies and production economies of scale are already kicking in nicely to drive costs lower, and that will support gross margin safety, even if average prices were to continue to decline as the market matures.

Gross margins expansion

As production and cash cost of sales decline, the gross margin before fair-value adjustments has grown marginally too, even as average selling prices weakened over the first quarter of this year.

Medical cannabis gross margin before fair value expanded to 60% from 59% in a previous quarter, while recreational marijuana gross margin marginally increased to 50% from 47% previously.

Margins could have been even better had the company sold more extracts, which fetched up to 68% in adjusted gross profit margins during the quarter. Management highlighted extraction capacity constraints, which are being attended to as the company invests in higher extraction capacity, while the arrangement with **Radient Technologies** has already started delivering fruits, leading to a potential margin expansion

Operating expense containment

The most critical operating costs, namely selling, general, and administrative expenses, only increased marginally by 1% over the first three months of this year, as compared to a quarter ago. This was an impressive achievement for a high-growth company that has been significantly increasing its bills as it rapidly expanded globally.

Cost containment will be critical factor towards an operating earnings quarter.

Foolish bottom line

There’s a good chance that the company could manage to report positive operating earnings this quarter if it manages to contain cost escalations, expand its medical patient base, and drive more recreational sales into its channels as production expands and per-unit production costs decline.

Adjusted EBITDA losses narrowed by 20% last quarter, and the company could reinforce this trend if the recent 40% jump in high-margin export sales could be maintained as this, and higher extract sales, could help defend profit margins.

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brianparadza