Watch This as Aurora Cannabis (TSX:ACB) Targets Positive Earnings This Quarter

Description

Last month, **Aurora Cannabis** (TSX:ACB)(NYSE:ACB) management reiterated its guidance for a positive EBITDA beginning this current quarter ending June 30. Such an achievement could be a huge confidence booster to the marijuana investing public, which has placed astronomical valuation multiples on the growth stock. Could this noble target be achievable this quarter?

There are a lot of moving parts that require investor attention, as the company finally targets operating profitability, but a reduction in the company's quarterly operating expense bill for a rapidly growing cannabis operation isn't likely one of them.

I would expect the achievement of operating profit to come from a few of the following sources.

Accelerated medical revenue growth

Although the company reported steadily growing revenues in a previous quarter, sales are nowhere near an operating breakeven point, and more top-line growth is still required to narrow the $36 million adjusted EBITDA loss to zero.

The recent 5% sequential growth in registered patient numbers during the last quarter to 77,000 patients and a further enrollment to nearly 83,000 patients in May is encouraging, but Canadian medical sales growth may still be insufficient to pull the overall adjusted EBITDA out of the red by this month-end.

Aurora Cannabis registered an impressive 40% sequential growth in export sales last quarter, as the company ramped up production from its flagship facility and had more product from its E.U. GMP-certified facilities to feed into Europe export sales, which fetch higher prices per gram to generate better margins.

That said, E.U. sales were a mere $3.1 million last quarter — too low to significantly drive the company to positive EBITDA, while Latin American operations are still in a slow growth mode.

Although medical sales bring better adjusted gross margins, I'm more convinced that the bulk of the required revenue growth this quarter will come from another source that investors need to watch out for.

Watch recreational sales!

Aurora Cannabis still has a huge delivery order to fulfill on its provincial supply agreements signed in 2018.

Disclosed initial annual supply volumes into provincial supply agreements topped 63,000 kilograms per annum last year, with critical volumes for Ontario and other provinces still undisclosed. However, by end of last quarter, the company had only recognized consumer sales volumes of around 9,300 kilograms ever since the adult use market sales began.

Thus, the company has to deliver over 53,700 kilograms of marijuana to satisfy its contracted obligations. That's a tall order, but that's a massive opportunity, too.

Management expected the company to have more than 25,000 kilograms of marijuana ready for sale during this quarter, encouraged by the 15,000 kilograms produced last quarter.

By the end of March this year, management only had a small window of just two quarters to push massive volumes into these contracts, and by end of this month, that window will narrow to just three months!

The company is likely to heavily push more product into the consumer market this quarter for it to achieve the EBITDA target and will likely do the same next quarter to sustain the position, but I'm worried about the sustainability of such volumes.

National retail sales contracted across the provinces at the beginning of this year to February, with a welcome small recovery in March, but channel inventory volumes are growing way too fast. The recreational sales channel may become clogged soon if consumer demand growth slows while product volumes continue building, and that may negatively affect producer wholesale prices going forward.

Can the EBITDA target be achieved?

Production costs per gram are coming down, as the flagship facility at Edmonton Airport ramps up production and targets producing marijuana at a cash cost below $1 a gram. Declining cash costs will boost margins significantly.

Increased productivity also avails more product for oil extraction, and the company may sell more of high-margin extracts this quarter as extraction capacity was reported to have increased subsequent to the last quarter. Operating margins may expand.

It seems like management has adopted an operating cost-containment focus while still growing the revenue base to improve corporate earnings, making the realization of a positive EBITDA quarter a potential reality, given falling production costs per gram.

However, given the recent average selling prices, and assuming a flat adjusted gross margin and constant sales mix, the company may need to sell between 21,000 and 24,000 kilograms of product this quarter to achieve operating breakeven, giving a required revenue of close to $130 million for the quarter!

That looks like a very tall order given prior quarterly achievements.

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