Are Pot Stocks Like Aurora Cannabis (TSX:ACB) and Hexo (TSX:HEXO) Running Out of Cash?

Description

We know that cannabis companies have been struggling with structural and regulatory issues for a while. Most pot companies have reported less-than-impressive quarterly results over the last year, resulting in an extended bear run for investors.

The recreational marijuana industry has been rattled by illegal sales that still account for 40% of total Canadian cannabis sales. The slower-than-expected roll-out of retail stores in major provinces have resulted in high inventory levels.

Further, high capital expenditures and related investments have meant that pot companies are struggling to stay afloat and might very well run out of cash. According to a report from boutique investment bank Ello Capital, several cannabis companies, including heavyweights such as **Aurora Cannabis** (TSX:ACB)(NYSE:ACB) and **Hexo** (TSX:HEXO)(NYSE:HEXO), would need to raise additional capital sooner rather than later.

Several pot stocks are still reporting a negative EBITDA and operating cash flow. This suggests it will be difficult for companies to raise debt, forcing them to raise additional equity capital and resulting in the dilution of existing shareholder capital.

Aurora Cannabis

According to Ello Capital, Aurora Cannabis has about 2.3 months of leeway left before its cash balance is down to zero. Aurora ended the December quarter with a cash balance of $182.5 million. It has a total debt of $602 million, while its operating cash flow stands at -$288.9 million and free cash flow is at -$695 million.

Aurora Cannabis is grappling with several other issues. It announced the exit of founder and CEOTerry Booth recently. The company also had to stop construction for two key projects and announcedclose to $1 billion in balance sheet write-offs.

Aurora Cannabis stock has been pummeled in the last year. The stock is trading 84% below its 52-week high, and now with liquidity concerns, there is a chance that investors will continue to bleed in 2020 as well.

The massive correction for Aurora Cannabis has meant the stock is trading at a price-to-book ratio of 0.66. With a market cap of $2.55 billion, it is valued at 8.35 times forward sales.

Hexo is down 83% from 52-week high

Hexo is another company under the scanner. Ello Capital estimated Hexo's cash balance to be enough for 6.5 months. Hexo already has raised about $100 million since October last year by equity offerings as well as convertible debentures.

Hexo ended the October quarter with a cash balance of $65.4 million. It has a total debt of $55 million, while its operating cash flow stands at -$138 million and free cash flow at -$246 million.

Hexo stock too has burnt investor wealth. The stock is currently trading 83% below its 52-week high. Shares fell 20% in January 2020 after Hexo's acquisition of Newstrike came under the scanner. Newstrike was reportedly growing cannabis products illegally at its Beamsville facility in Niagara.

In fiscal 2020, Hexo aims to reduce operating expenses by 25%. Like most pot companies, Hexo is also banking on Cannabis 2.0 to drive product demand higher. Its partnership with **Molson Coors** can also help Hexo to stay afloat, which will give the firm a chance to make a comeback.

The verdict

There is a chance that Aurora, Hexo, and others may be able to issue additional capital in the upcoming months. However, there is also a chance that these companies will crash and burn considering the current pessimism surrounding pot stocks.

The cannabis industry is still at a nascent stage and can be likened to the dot com bubble of 2000. While **Amazon** and **Alphabets's** Google rose from the ashes to generate millions of dollars in returns, there were hundreds of internet stocks that were wiped out without a trace.

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