



Cannabis Retailer Gives Stock Investors an Early Christmas Present

Description

Canadian cannabis retail giant **Fire & Flower Holdings** ([TSX:FAF](#)) saw its stock price rise over 2% on Tuesday after reporting record quarterly revenue and positive Adjusted EBITDA for the first time ever. Sustained positive operating cash flow wraps up the early Christmas present to FAF stock investors

Fired-up Fire & Flower's strong sales performance

During the 13 weeks ending October 31 this year, Fire & Flower generated third-quarter 2020 revenues of \$33.1 million, up 142% year over year and 15.8% sequentially. Strong revenue growth was reported in all three of the company's reporting segments.

Retail segment revenue growth of 123% was enabled by an increase in retail store outlets from 31 stores by October 31, 2019, to 54 outlets by the same date this year. Retail sales growth was also aided by an 11% increase in same-store sales. A successful Cannabis 2.0 products rollout offset the negative impact of increased competition from new retail stores across the provinces.

Wholesale distribution revenue growth at 19% sequentially was impressive after the Saskatchewan market opened up during the quarter.

Most noteworthy, the company's Hifyre digital retail segment is on steroids after a strong 55.8% sequential growth. Interestingly, the company reports that its Hifyre IQ platform, a data analytics package, has enjoyed massive adoption by major cannabis licensed producers. The platform has made inroads into investment banks, consultancy firms, and equity analyst establishments. That's some success and strong market endorsement there.

FAF achieved a significant milestone: Positive adjusted EBITDA

The company's sustained revenue growth this year and notable success in containing costs and

maintaining healthy gross margins has paid off in a big way.

As revenue increased by triple digits and gross margins remained flat at 34.7%, operating costs rose by a smaller margin of just 12%. Operating losses declined from a staggering \$5.9 million last year to just \$467 thousand. This enabled the company to report an adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) of \$1.2 million, its first-ever positive adjusted operating earnings quarter.

Positive adjusted EBITDA is a favourable attribute on any company, as it means the company is capable of generating some cash-based earnings from business operations. Businesses that consistently generate positive adjusted EBITDA can be more sustainable than those that don't.

Should you buy the cannabis stock?

This is a big question.

Fire & Flower is now Canada's largest cannabis retailer with 71 retail store licences. Sales [have continued to grow](#), even as competition from new nearby locations took some volumes away. The company could sustain its growth momentum after recent acquisitions and strong uptake of its data analytics package, which could penetrate the global market.

Further, FAF continues to generate positive cash flow from operations. The company reported cash generated from operations of \$4.18 million during the first nine months of the current fiscal year. Significant cash working capital was freed up when it started receiving inventory supplies on credit from licensed producers. This was a positive development, as the company can deploy that capital to investment projects.

That said, there are a few concerns about the buy decision. Provinces are issuing out new retail licences by boatloads right now. Newly licensed outlets will compete for a pie that is growing at a slower-than-desirable rate. Same-store sales growth could become negative, and operating margins could shrink as competition intensifies.

Further, I noted that the book value of equity in FAF shrank significantly this year. Shareholders' equity was \$46.9 million, or 31% of assets, in February this year. It's down to just \$2.7 million, or 2% of assets, by October 31. Liabilities have grown by double digits as debentures, loans, and derivative liabilities increased by 80% this year. Notably, total assets remained essentially flat.

Declining equity balances could be a significant cause for concern for equity investors. As far as the numbers are concerned, equity investors' claim on the assets of the company has been reduced substantially. Equity in Fire & Flower is now of little significance. It appears as if **Alimentation Couche Tard** has essentially snatched the company away from retail investors.

CATEGORY

1. Cannabis Stocks
2. Investing

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