Is HEXO (TSX:HEXO) a Buy After its Impressive 2nd-Quarter Performance?

Description

Yesterday, **Hexo** (TSX:HEXO)(NYSE:HEXO) reported its second-quarter earnings of fiscal 2021. The company's top line beat analysts' expectations and reported positive adjusted EBITDA for the first time in its history. However, the company's net losses increased from $4.2 million in the previous quarter to $20.8 million amid some non-recurring expenditures. The increase in net losses appears to have let investors down, dragging the company's stock price down by 6.3%. So, should you buy HEXO right now? Let's first look at its second-quarter performance and its growth prospects in detail.

HEXO's second-quarter performance

For the quarter, HEXO's top line came in at $32.8 million, representing sequential growth of 11.6% and year-over-year growth of 93%. Along with Quebec, the company is also strengthening its market share in Alberta and Ontario. The revenue contribution from outside Quebec has increased from 44% in the first quarter to 49%.

During the quarter, the company had relaunched the UP brand, with higher THC content, which appears to have resonated well with the customers. It generated $3.2 million of revenue during the quarter. Further, the company continues to strengthen its market share in the cannabis-infused beverage segment, thanks to its joint venture with Molson Coors, Truss Canada. Meanwhile, the revenue from its beverage segment grew 11%, sequentially.

Further, HEXO has reported a positive adjusted EBITDA of $0.2 million during the second quarter compared to a loss of $0.42 million in the previous quarter. It was the company's seventh consecutive quarter of adjusted EBITDA improvement. The improvement in gross margins and lower SG&A expenses drove the company's adjusted EBITDA.

Meanwhile, HEXO's net losses increased during the quarter due to non-recurring expenses, such as the revaluation of its currency warrants and unfavourable foreign exchange. The company'soperational cash usage excluding working capital stood at $2.9 million. With over $250 million ofworking capital on its balance sheet, its financial position looks strong.

Outlook

Amid increasing legalization and expanding medical usages, the cannabis industry offers high growth prospects. Meanwhile, HEXO has also taken several initiatives to take benefit from the growing cannabis market. It is looking at improving its distribution network in other provinces also to make its products readily available.

Meanwhile, the company focuses on expanding its footprint in the United States and has appointed Charlie Bowman as General Manager of its U.S. operations. In January, the company, in partnership with Molson Coors, had launched CBD-infused beverages in Colorado. After receiving positive customers response, the company is focusing on expanding the product to other states.

Further, HEXO had signed an agreement to acquire Zenabis Global for $235 million in an all-stock deal last month. The acquisition could position HEXO as one of the top three players in the Canadian recreational market and provide access to the European medical cannabis market. The transaction could deliver $20 million savings within one year of closing the transaction, given the two companies' synergies. HEXO's management is hopeful of completing the transaction in the fourth quarter of fiscal 2021. So, the company's growth prospects look healthy.

Bottom line

By posting a positive adjusted EBITDA in its second quarter, HEXO is at an inflection point and can only grow from here. The company has returned close to 94% this year. Despite the increase in its stock price, its forward price-to-sales and price-to-book multiples are lower than its peers, **Canopy Growth** and **Aphria**. So, given the sector tailwinds and its growth initiatives, I believe HEXO could continue its uptrend and deliver superior returns this year.

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