

Lowell Farms (US OTCQX: LOWLF: \$0.71): Q3 Weakness on Pricing Pressure; Maintain view that can be a Winner in CA

November 16, 2021

Lowell Farms reported Q3/21 results of \$12.5M in revenues and an adjusted EBITDA loss of \$5.2M. Results for the quarter compared with our estimates of \$15M in revenues and a \$1M adjusted EBITDA gain. Guidance had called for \$14M to \$16M in revenues.

The underperformance for the quarter stemmed from persistent wholesale pricing pressure in California with flower prices down nearly 50% from where the company anticipated and 60% from the levels of Q2/21. Compounding results, due to unfavorable pricing, management also held off selling roughly \$1M worth of flower that would have otherwise been sold. The unsold flower will be sold in either Q4 or early 2022. We expect pricing pressure to persist for the foreseeable future dragging both top line results and margins in the process. The pricing drag on results only furthers our positive view on Lowell's brand acquisition completed earlier this year and the launch of the third-party flower processing business this summer. Both mitigate some pricing risk longer term and provide additional sources of revenues that differentiate the company from other flower producers in California which will be disproportionately challenged as undiversified entities. Importantly, Lowell recognized initial revenues from both its licensing agreement (made possible by the Lowell brand acquisition) and the processing business. We are confident that each can scale in 2022 contributing at a combined run-rate of between \$20M and \$30M in revenues at some point next year. Ultimately, we believe licensing arrangements can also be a catalyst to drive greater interest in Lowell as a takeout candidate as the company proves the strong demand for Lowell pre-rolls outside of California.

We adjust our estimates on Lowell to reflect updated guidance for Q4 (between \$15M and \$17M in revenues and positive adjusted EBITDA) and a continued drag on pricing next year. The reported weakness is disappointing particularly given the scale of Q3 underperformance vs. what was expected to be conservative guidance provided in August, however we continue with our positive view on Lowell believing that the company can be a winner in California on its innovative wholesale offering and strong brand recognition. Our rating remains Buy while we reduce our price target from \$1.60 to \$1.20 noting that the updated target still reflects meaningful upside from current levels.

Licensing arrangement could drive future M&A

As mentioned, Lowell reflected initial contributions from its licensing agreement with Ascend in Q3/21. Lowell pre-rolls were sold in Ascend stores and through Ascend's wholesale business in Illinois and Massachusetts beginning late in Q3 with the business generating roughly \$700K in revenues for Lowell. In connection with the earnings call, Lowell also announced plans to expand the licensing agreement to Michigan with Ascend selling Lowell pre-rolls in its six Michigan dispensaries and eventually the wholesale market. We expect continued expansion of licensing opportunities both with Ascend (company also in Ohio and New Jersey and will soon be in New York pending the MedMen asset acquisition) and other licensing partners.

Viridian Capital Advisors

www.viridianca.com

Jonathan DeCoursey

Director Equity Research

jdecoursey@viridianca.com

(781) 724.6869

Lowell Farms

Rating: Buy

Price Target: \$1.20 (was \$1.60)

Investment Highlights

- Q3/21 miss on pricing pressure.
- Expect lower flower pricing to continue into 2022. Pricing pressure furthers our positive view on LOWLF's differentiated initiatives put in place by management including brand acquisition, buildout of processing business and decision not to acquire additional cultivators.
- Initial contributions reflected from new processing business and licensing arrangement with Ascend. Expect both to scale in 2022.
- Believe could be a takeout candidate by an MSO looking to gain California exposure and sought after brand.

Click the Link to Subscribe to the [Viridian Cannabis Deal Tracker](#)

Ultimately, we believe the partnering with licensing partners could drive a takeout of Lowell given that licensing agreements give companies the chance to work closely together and ultimately reduce the level of integration risk involved in any transaction. As we have previously stated, we believe Lowell should be a sought-after takeout candidate from any company looking to scale production capabilities in California while also bringing the Lowell Herb Co. brand into other state markets either through sales at owned stores and the wholesale channel or licensing relationships.

In the short term, we also believe Lowell could be in the market to acquire smaller branded players in California that are challenged in the current pricing/distribution environment like the Lowell Herb Co. was prior to Lowell's acquisition earlier this year. Given the company's distribution footprint and cultivation and production capacity any brand acquisition could likely provide immediate returns in California while also allowing Lowell to further its licensing opportunity.

We revise our estimates and reduce our price target

- Revenues: Q4/21 from \$20M to \$16M; 2021E from \$61.2M to \$54.7M; 2022E from \$84M to \$77M.
- Adjusted EBITDA Q4/21 from \$3.6M to \$100K; 2021E from \$900K to (\$8.9M); 2022E from 18.6M to \$10.1M.

Our \$1.20 Price Target reflects an EV/EBITDA multiple of 32.3x our 2022 estimate and EV/Sales at 4.2x.

FY Income Statement (\$M)

	2020	2021					2022				
	2020	Q1 '21	Q2 '21	Q3 '21	Q4 '21E	2021	Q1 '22E	Q2 '22E	Q3 '22E	Q4 '22E	2022
	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Dec-22
Revenue	42.7	11.0	15.2	12.5	16.0	54.7	15.0	19.0	22.0	21.0	77.0
Gross Profit	19.1	(1.5)	5.7	0.1	6.1	10.4	5.7	7.4	9.5	9.2	31.8
G&A	11.8	2.5	3.8	4.2	3.9	14.4	3.6	3.5	3.5	3.6	14.2
Sales & Marketing	5.2	1.4	2.2	2.5	2.4	8.6	2.2	2.3	2.3	2.3	9.1
Depreciation	3.7	0.3	0.2	0.3	0.3	1.1	0.3	0.3	0.3	0.3	1.2
Opex	20.6	4.2	6.2	7.0	6.6	24.1	6.1	6.1	6.1	6.2	24.5
Income from operations	(1.5)	(5.7)	(0.5)	(7.0)	(0.5)	(13.6)	(0.4)	1.3	3.4	3.0	7.3
Total Other Expense	7.2	(1.0)	1.3	(1.7)	(1.4)	(2.8)	(1.4)	(1.4)	(1.4)	(1.4)	(5.6)
Pre-tax Income	(8.8)	(6.7)	0.8	(8.6)	(1.9)	(16.4)	(1.8)	(0.1)	2.0	1.6	1.7
Taxes	0.2	0.1	0.1	0.1	(0.3)	(0.1)	(0.3)	(0.0)	0.3	0.2	0.3
Net Income	(9.0)	(6.7)	0.7	(8.7)	(1.6)	(16.3)	(1.5)	(0.1)	1.7	1.4	1.5
EPS	(0.3)	(0.1)	0.0	(0.0)	(0.0)	(0.1)	(0.0)	(0.0)	0.0	0.0	0.0
Shares	33.4	53.6	201.3	202.3	203.3	165.1	204.3	205.3	206.4	207.4	205.8
Adjusted EBITDA	(9.8)	(4.6)	0.7	(5.2)	0.1	(8.9)	0.3	2.0	4.1	3.7	10.1
<u>% Revenues</u>											
Gross Margin	45%	-13%	38%	1%	38%	19%	38%	39%	43%	44%	41%
Opex	48%	38%	41%	56%	41%	44%	41%	32%	28%	30%	32%
Operating Income	-4%	-52%	-3%	-56%	-3%	-25%	-3%	7%	15%	14%	9%
Net Income	-21%	-61%	5%	-70%	-10%	-30%	-10%	0%	8%	7%	2%
Adjusted EBITDA		-41%	5%	-42%	1%	-16%	2%	11%	18%	18%	13%
<u>Growth Rates</u>											
Revenues											
Y/Y	15%	17%	53%	-12%	74%	28%	36%	25%	76%	31%	41%
Q/Q		20%	37%	-18%	28%		-6%	27%	16%	-5%	

Source: Company Reports, Viridian Capital Estimates

Required Research Disclosures

Distribution of Ratings/IB Services				
Rating	Count	Percent	IB Services in Past 12 months	
			Count	Percent
Buy (Buy)	12	100%	0	0%
Hold (Hold)	0	0%	0	0%
Sell (Sell)	0	0%	0	0%
Not Rated (NR)	0	0%	0	0%

Analyst Certification

The research analyst responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers and were prepared in an independent manner, including with respect to Bradley Woods & Co. Ltd.; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by the research analyst in this report.

Meaning of Ratings

Bradley Woods & Co. Ltd.'s rating system of **Buy, Hold, Sell, Not Rated** reflects the analyst's best judgment of risk-adjusted assessment of a security's 24-month performance.

Buy: A Buy recommendation is assigned to stocks with low risk and approximately 10% expected return or stocks with high risk and approximately 25% expected return. The analyst recommends investors add to their position.

Hold: A Hold recommendation is assigned to stocks with low risk and less than 10% upside or less than 15% downside or to stock with high risk and less than 25% upside or less than 15% downside.

Sell: A Sell recommendation is assigned to stocks with an expected negative return of approximately 15%. The analyst recommends investors reduce their position.

Not Rated: A Not Rated recommendation makes no specific Buy, Hold or Sell recommendation.

Compensation or Securities Ownership

The analyst(s) responsible for covering the securities in this report receives compensation based upon, among other factors, the overall profitability of Bradley Woods & Co. Ltd. including profits derived from investment banking revenue and securities trading and market making revenue. Unless noted in the Company Specific Disclosures section above, the analyst(s) that prepared the research report did not receive any compensation from the Company or any other companies mentioned in this report in the previous 12 months, or in connection with the preparation of this report. Unless noted in the Company Specific Disclosures section above, neither the analyst(s) responsible for covering the securities in this report, nor members of the analyst(s)' household, has a financial interest in the Company, but in the future may from time to time engage in transactions with respect to the Company or other companies mentioned in the report.

For compendium reports (a research report covering six or more subject companies) please see the latest published research to view company specific disclosures.

Other Important Disclosures

This report is provided for informational purposes only. It is not to be construed as an offer to buy or sell a solicitation of an offer to buy or sell any financial instruments or to particular trading strategy in any jurisdiction. The information and opinions in this report were prepared by registered employees of Bradley Woods & Co. Ltd. The information herein is believed by Bradley Woods & Co. Ltd. to be reliable and has been obtained from public sources believed to be reliable, but Bradley Woods & Co. Ltd. makes no representation as to the accuracy or completeness of such information.

Bradley Woods & Co. Ltd. is regulated by the United States Securities and Exchange Commission, FINRA, and various other self-regulatory organizations. This report has been prepared in accordance with the laws and regulations governing United States broker-dealers.

Opinions, estimates, and projections in this report constitute the current judgment of the author as of the date of this report. They do not necessarily reflect the opinions of Bradley Woods & Co. Ltd. and are subject to change without notice. In addition, opinions, estimates and projections in this report may differ from or be contrary to those expressed by other business areas or group of Bradley Woods & Co. Ltd. and its affiliates. Bradley Woods & Co. Ltd. has no obligation to update, modify or amend this report or to otherwise notify a reader thereof in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate.

Bradley Woods & Co. Ltd. does not provide individually tailored investment advice in research reports. This report has been prepared without regard to the particular investments and circumstances of the recipient. The securities discussed in this report may not be suitable for all investors and investors must make their own investment decisions using their own independent advisors as they believe necessary and based upon their specific financial situations and investment objectives. Estimates of future performance are based on assumptions that may not be realized. Furthermore, past performance is not necessarily indicative of future performance. Investment involves risk. You are advised to exercise caution in relation to the research report. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

Bradley Woods & Co. Ltd. salespeople, traders and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed in this research. Bradley Woods & Co. Ltd. may seek to offer investment banking services to all companies under research coverage. Bradley Woods & Co. Ltd. and/or its affiliates expect to receive or intend to seek investment-banking related compensation from the company or companies mentioned in this report within the next three months.

This research report (the "Report") is investment research, which has been prepared on an independent basis by Bradley Woods & Co. Ltd., a member of FINRA and SIPC, with offices at 805 Third Avenue, 18th Floor, New York, NY USA, 10022. Electronic research is simultaneously available to all clients. This research report is provided to Bradley Woods & Co. Ltd. clients and may not be redistributed, retransmitted, disclosed, copied, photocopied, or duplicated, in whole or in part, or in any form or manner, without the express written consent of Bradley Woods & Co. Ltd. Receipt and review of this research report constituted your agreement not to redistribute, retransmit, or disclose to others the contents, opinions, conclusion or information contained in this report (including any investment recommendations, estimates, or target prices) without first obtaining express permission from Bradley Woods & Co. Ltd. In the event that this research report is sent to you by a party other than Bradley Woods & Co. Ltd., please note that the contents may have been altered from the original, or comments may have been added, which may not be the opinions of Bradley Woods & Co. Ltd. In such case, neither Bradley Woods & Co. Ltd., nor its affiliates or associated persons, are responsible for the altered research report.

This report and any recommendation contained herein speak only as of the date of this report and are subject to change without notice. Bradley Woods & Co. Ltd. and its affiliated companies and employees shall have no obligation to update or amend any information or opinion contained in this report, and the frequency of subsequent reports, if any, remain in the discretion of the author and Bradley Woods & Co. Ltd.

Bradley Woods & Co. Ltd. may effect transactions in the securities of companies discussed in this research report on a riskless principal or agency basis. Bradley Woods & Co. Ltd.'s affiliated entities may, at any time, hold a trading position (long or short) in the securities of the companies discussed in this report. Bradley Woods & Co. Ltd. and its affiliates may engage in such trading in a manner inconsistent with this research report. All intellectual property rights in the research

report belong to Bradley Woods & Co. Ltd. Any and all matters related to this research report shall be governed by and construed in accordance with the laws of the State of New York.

This report is not directed at, or intended for distribution to or use by, any person or entity who is a citizen or resident of, or located in any locality, state, country, or other jurisdiction where such distribution, publication, availability, or use would be contrary to law or regulation or which would subject Bradley Woods & Co. Ltd. and its affiliates to any registration or licensing requirements within such jurisdictions.

The Bradley Woods Form CRS, Client Relationship Summary, can be accessed [here](#).