

Trulieve Cannabis Corporation^{1,6}

BUY

TRUL-CSE

November 21, 2018

 Last: **C\$12.73**
 Target: **C\$26.00**

Q3 delivers on expectations; outlook remains solid

Trulieve reported Q3/18 results largely in line with expectations. Revenues came in at \$28m, up 22% QoQ, and slightly ahead of our forecast of \$27m, driven by slightly better same-store-sales growth and new store openings. Adj. EBITDA of \$12.6m (44.4% margin vs. 49.2% est.) was slightly lower than our \$13.3m forecast as SG&A expenses came in ~\$1m higher than our \$7m estimate.

Market share loss slightly better than forecasted. We had expected TRUL's market share to be pressured in Q3/18 as competitors expanded their networks by a combined 10 new stores during the quarter. However, TRUL fared better than expected, with market share reaching an estimated ~55% in Q3/18, slightly better than our ~53% forecast, but down from ~63% in Q2/18. Despite TRUL's sequential share decline, we note the company still holds a commanding position in FL, with the next closest competitor's market share estimated at below 20%.

SG&A may trend higher, as expected. We believe a 50% increase in SKUs offered (120 total), combined with a slightly more competitive environment during Q3/18 explain TRUL's higher operating expenses. TRUL's aggressive store expansion plans should also drive higher SG&A costs in coming quarters. However, we have previously included in our forecasts a step-up in spending correlated with TRUL's growing footprint and increasing competitiveness in Florida alongside new entrants to the market. Hence, an expected ramp up in TRUL's SG&A was expected, and does not materially change our outlook for coming quarters.

Continuing aggressive store rollout bodes well. TRUL has accelerated its store openings following Q3/18 with five new FL locations, bringing its total network to 22 stores, and matching the pace of growth of its closest competitors in the state. Our prior forecasts called for TRUL to reach 22 stores only by end of Q4/18, hence we have slightly boosted our forecasts to reflect this more rapid growth. TRUL's speedy network expansion highlights continuing solid execution in our view, and could put the company in a position to reach its goal of 30 FL stores by Jan. 2019.

Valuation and recommendation

Maintain BUY and \$26.00 target. While TRUL's market share lost some ground in Q3/18, this was expected and therefore does not change our outlook. Q3 EBITDA margins of 44.4% still make TRUL the most profitable public US cannabis operator, and reinforce the company's strong execution by demonstrating it can expand operations and maintain strong profitability. Lastly with TRUL's store rollout accelerating post Q3, the company is well positioned to capitalize on the high growth of the FL market. Given the above we maintain our positive stance, and our price target based on 15x (unchanged) our 2020 EBITDA forecast of \$143m.

What's Changed	Old	New
Rating	BUY	n.c.
Target (C\$)	\$26.00	n.c.
Revenue FY18E (m)	\$97.6	\$100.8
Revenue FY19E (m)	\$219.5	\$227.3
Revenue FY20E (m)	\$308.9	\$306.9
EBITDA FY18E	\$44.1	\$43.9
EBITDA FY19E	\$106.2	\$108.6
EBITDA FY20E	\$146.0	\$143.6

Share Data

Share o/s (mm, basic/f.d.)	109.8 / 110.3
52-week high/low (C\$)	22.2 / 9.98
Market cap (basic,m)	\$1,075
Market cap (f.d.,m)	\$1,081
Net debt & NC interest (m)	(\$7)
Net debt & NC interest (f.d.,m)	(\$7)
EV (f.d.,m)	\$1,073
Projected return	104.2%

Financial Data

FYE Dec 31	FY18E	FY19E	FY20E
Revenue (m)	\$100.8	\$227.3	\$306.9
EBITDA (m)	\$43.9	\$108.6	\$143.6
EV/EBITDA	24.4x	9.9x	7.5x
Adj. EPS (f.d.)	\$0.15	\$0.57	\$0.81
P/E	nmf	17.1x	12.1x
CFPS	\$0.26	\$0.57	\$0.78
P/CF	nmf	17.3x	12.5x
Net debt (m)	(\$26)	(\$54)	(\$139)
BVPS	\$0.86	\$1.59	\$2.39
P/BV	11.4x	6.1x	4.1x

Pro-forma recent financings and M&A activity

All figures in US\$ unless otherwise noted

[Current Chart](#)
[Previous Research](#)

Robert Fagan, CFA (514) 288-0318
rfagan@gmpsecurities.com

Andrew Partheniou, B.Eng, MBA (514) 288-2256
apartheniou@gmpsecurities.com

Figure 1. TRUL's Q3/18 earnings results

Y.E. Dec-31 (US\$, 000's)	Q3/18A	Q2/18A	Chg. QoQ	GMP Q3/18E	Diff.
Revenues	28,326	23,299	21.6%	27,172	1,153
Adj. COGS	7,710	5,645	36.6%	6,793	917
Adj. gross profit	20,616	17,654	16.8%	20,379	236
Gross profit margin	72.8%	75.8%	-299bps	75.0%	-222bps
Adj. SG&A expense	8,041	6,031	33.3%	7,000	1,041
Adj. EBITDA	12,574	11,623	8.2%	13,379	(805)
margin	44.4%	49.9%	-549bps	49.2%	-485bps
Depreciation & amortization	932	576	61.7%	470	462
Net financing costs (income)	369	782	-52.8%	963	(594)
Taxes	8,153	5,402	51%	4,891	3,262
Adj. net income	3,120	4,862	-35.8%	7,055	(3,935)
Adj. EPS (f.d.)	\$0.03	\$0.74	nmf	\$0.06	-\$0.04
Shares outstanding (f.d.)	110,344	6,578	nmf	110,344	-

Note: Q3/18 adj. EBITDA excludes \$1.4m of listing expenses

Source: Company reports, GMP Securities

Forecasts

Minor tweaks to forecasts. In light of TRUL's more rapid FL network expansion, we have slightly modified our forecasts to bring forward some store openings. This has a minor positive impact on our FY18 and FY19 revenue estimates, and a slight negative impact to our FY20 sales estimate. Some higher SG&A expenses going into Q4/18 and Q1/19 were already included in our estimates, however we have bumped up slightly our SG&A expense assumptions for future periods to reflect expected ongoing rapid store network expansion in FL, as well as in MA post TRUL's acquisition of Life Essence Inc.

Figure 2. Summary of changes to our forecasts

Year-end Dec-31 (US\$,000's)	FY18E		FY19E		FY20E	
	New	Old	New	Old	New	Old
Consolidated sales (net)	100,817	97,643	227,273	219,532	306,919	308,875
Gross margin	73,680	72,777	164,030	158,314	198,643	200,078
Gross margin %	73.1%	74.5%	72.2%	72.1%	64.7%	64.8%
SG&A expenses	29,744	28,672	55,438	52,138	55,088	54,125
SG&A expense ratio %	29.5%	29.4%	24.4%	23.7%	17.9%	17.5%
EBITDA	43,936	44,105	108,592	106,177	143,555	145,953
EBITDA margin %	43.6%	45.2%	47.8%	48.4%	46.8%	47.3%

Source: GMP Securities

Recommendation

Our positive stance on TRUL is supported by the following:

- 1. Strong execution track record.** Trulieve has demonstrated strong operational expertise by performing the fastest dispensary network expansion amongst all peers in Florida. Since receiving its dispensing licence, Trulieve has opened a new store every 1.2 months on average, ~7% faster than its closest competitor, Curaleaf, and ~50% quicker than Surterra Wellness. Trulieve has also proven its ability to effectively compete by maintaining market share of ~88%–90% during 2017, and ~67% over the first nine months of 2018, despite competitor store count increasing from two stores, to 38 stores over the same period. The above highlights a strong track record of execution for Trulieve, giving us confidence that the

company can effectively penetrate markets in new states, and reproduce the success experienced in the Florida market.

2. **Robust value creation.** Most cannabis companies undergoing rapid expansions have yet to generate meaningful profitability as expense growth exceeds revenue growth while operations are being scaled up. Trulieve by comparison has demonstrated a proven capability to expand profitably with EBITDA margins of ~44% representing the strongest profitability levels amongst all US public peers. The company has historically allocated capital in a highly efficient manner, translating into robust ROIC generation, which we estimate at a rate of ~60–70% currently. This not only highlights stronger value creation by Trulieve than any other US public peer, but also provides the company with an important advantage in the ability to re-invest higher cash flows earlier to drive future growth.
3. **Florida market could offer revenue upside of ~\$100–175m.** We believe there is a high likelihood that smokeable dried flower and edibles are introduced as new product forms, and opioid replacement therapy (ORT) is added as a new qualifying condition in Florida sometime over the next ~18 months. Under such a scenario, we estimate this could boost Florida's market size in 2020 by as much as ~\$500m–900m (~60%–110% over our \$800m forecast). Under a conservative assumption of 20% market share for Trulieve in 2020 (well below our ~35% forecast), we estimate this could translate into potential revenue upside of ~\$100–175m. Assuming EBITDA margins of ~40%–50%, this could translate into ~\$7–\$15 of upside to our target price.

Financial statements

Figure 3. TRUL's income statement

FYE Dec. 31 (US\$, 000's)	FY2016A	FY2017A	Q1/FY18A	Q2/FY18A	Q3/FY18A	Q4/FY18E	FY2018E	FY2019E	FY2020E
Consolidated revenues	161	19,778	15,247	23,299	28,326	33,946	100,817	227,273	306,919
<i>Growth YoY %</i>				946.6%	468.3%	191.9%	409.7%	125.4%	35.0%
COGS (excl. IFRS adjustments)	2,706	10,734	4,447	5,645	7,710	9,335	27,137	63,243	108,277
Adj. gross margin	(2,545)	9,044	10,800	17,654	20,616	24,611	73,680	164,030	198,643
<i>Gross margin %</i>	<i>nmf</i>	45.7%	70.8%	75.8%	72.8%	72.5%	73.1%	72.2%	64.7%
Operating expenses	1,458	8,307	4,672	6,031	8,041	11,000	29,744	55,438	55,088
<i>% of sales</i>	905.0%	42.0%	30.6%	25.9%	28.4%	32.4%	29.5%	24.4%	17.9%
Adj. EBITDA	(4,004)	737	6,128	11,623	12,574	13,611	43,936	108,592	143,555
<i>Margin %</i>	<i>nmf</i>	3.7%	40.2%	49.9%	44.4%	40.1%	43.6%	47.8%	46.8%
Depreciation & amortization	113	558	394	576	932	671	2,572	3,489	4,412
EBIT	(4,117)	179	5,735	11,046	11,643	12,940	41,364	105,104	139,143
Financial expenses (net)	362	857	321	782	369	597	2,068	2,387	2,387
EBT	(4,479)	(678)	5,414	10,265	11,274	12,344	39,295	102,717	136,756
Income taxes	(670)	4,738	3,762	5,402	8,153	5,168	22,486	39,367	47,674
<i>Tax rate (%)</i>	<i>nmf</i>	<i>nmf</i>	69.5%	52.6%	72.3%	41.9%	57.2%	38.3%	34.9%
Adj. Net income (before M.I.)	(3,809)	(5,416)	1,652	4,862	3,120	7,175	16,810	63,350	89,082
EPS (f.d., before M.I.)	\$0.00	\$0.54	\$0.25	\$0.74	\$0.03	\$0.07	\$0.15	\$0.57	\$0.81
Total one-time items (after-tax)	-	8,970	5,212	3,021	14,382	(3,993)	18,622	17,281	(1,647)
Reported net income (before M.I.)	(3,809)	3,553	6,864	7,883	17,503	3,182	35,431	80,631	87,435
<i>Net income attributable to TRUL</i>		3,553	6,864	7,883	17,503	3,182	35,431	80,631	87,435
Reported EPS (f.d., after M.I.)	\$0.00	\$0.54	\$1.04	\$1.20	\$0.16	\$0.03	\$0.32	\$0.73	\$0.79
Shares outstanding (f.d.)	-	6,578	6,579	6,578	110,344	110,344	110,344	110,344	110,344

Source: Company reports, GMP Securities

Disclosures

GMP FirstEnergy is a trade name and division of GMP Securities L.P. ("GMP"), and a trade name of FirstEnergy Capital LLP (together with GMP referred to as "GMP/FirstEnergy"). The information contained in this report is drawn from sources believed to be reliable but the accuracy or completeness of the information is not guaranteed, nor in providing it does GMP/FirstEnergy assume any responsibility or liability whatsoever. Information on which this report is based is available upon request. This report is not to be construed as a solicitation of an offer to buy or sell any securities. GMP/FirstEnergy and/or affiliated companies or persons may as principal or agent, buy and sell securities mentioned herein, including options, futures or other derivative instruments thereon. Griffiths McBurney Corp. ("GM Corp."), an affiliate of GMP accepts responsibility for the contents of this research subject to the foregoing. U.S. clients wishing to effect transactions in any security referred to herein should do so through GM Corp. GMP Securities L.P. will provide upon request a statement of its financial condition and a list of the names of its Directors and senior officers.

The superscript(s) following the issuer name(s) mentioned in this report refers to the company-specific disclosures below. If there is no such superscript, then none of the disclosures are applicable and/or required.

Company-Specific Disclosures:

- 1 GMP/FirstEnergy has, within the previous 12 months, provided paid investment banking services or acted as underwriter to the issuer.
- 2 RESERVED
- 3 GMP/FirstEnergy owns 1% or more of this issuer's securities.
- 4 GMP Securities, LLC ("GMP LLC"), an affiliate of GMP/FirstEnergy, discloses the following in relation to this issuer as required by the Financial Industry Regulatory Authority ("FINRA") Rule 2241: as applicable.
- 5 The analyst is related to an officer, director or advisory board member of this issuer, but that related individual has no influence in the preparation of this report.
- 6 The analyst has viewed the operations of this issuer and the issuer paid all or a portion of the travel expenses associated with the analyst's site visit to its operations.
- 7 The analyst has viewed the operations of this issuer.
- 8 The analyst and/or a member of their household has a position in this issuer's securities.
- 9 A member of the Board of Directors of this issuer is also a member of the Board of Directors of GMP Capital Inc., but that individual had no influence in the preparation of this report.
- 10 The analyst owns this issuer's securities in a managed account but has no involvement in the investment decisions for that managed account.

Each research analyst and associate research analyst who authored this document and whose name appears herein certifies that:

(1) the recommendations and opinions expressed in the research report accurately reflect their personal views about any and all of the securities or issuers discussed herein that are within their coverage universe; and (2) no part of their compensation was, is or will be, directly or indirectly, related to the provision of specific recommendations or views expressed herein.

GMP/FirstEnergy Analysts are not registered and/or qualified as research analysts with FINRA and may not be associated persons of GMP LLC and therefore may not be subject to FINRA Rule 2241 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account as defined by FINRA but are subject to the applicable regulatory rules as mentioned below.

All relevant disclosures required by regulatory rules (including The Investment Industry Regulatory Organization of Canada, and Financial Conduct Authority), GMP/FirstEnergy's recommendation statistics and research dissemination policies can be obtained at www.gmpsecurities.com or by calling GMP's Compliance Department at 416-367-8600.

GMP/FirstEnergy Analysts are compensated competitively based on several criteria. The Analyst compensation pool is comprised of several revenue sources, including secondary trading commissions, new issue commissions, investment banking fees, and directed payments from institutional clients.

The GMP/FirstEnergy research recommendation structure consists of the following ratings:

Buy: A Buy rating reflects 1) bullish conviction on the part of the analyst; and 2) typically a 15% or greater return to target.

Speculative Buy: A Speculative Buy rating reflects 1) bullish conviction on the part of the analyst accompanied by a substantially higher than normal risk, including the possibility of a binary outcome; and 2) typically a 30% or greater return to target.

Hold: A Hold rating reflects 1) a lack of bullish or bearish conviction on the part of the analyst; and 2) typically a return of 0 to 20%.

Reduce: A Reduce rating reflects 1) bearish conviction on the part of the analyst; and 2) typically a 5% or lower return to target.

Tender: Clients are advised to tender their shares to a takeover bid or similar offer.

Country Specific Disclaimers:

Canada: GMP is a member of IIROC and a participant of the TSX, TSX Venture and the Montreal Exchange. 145 King Street West, Suite 300 Toronto, Ontario M5H 1J8 Tel: (416) 367-8600.

UK and Europe: This material is distributed by FirstEnergy Capital LLP to persons who are eligible counterparties or professional clients. FirstEnergy Capital LLP is authorised and regulated by the Financial Conduct Authority. 85 London Wall, London, EC2M 7AD Tel: +44 (0)20 7448 0200

Other countries: circulation of this report may be restricted by laws and regulations in other countries and persons in receipt of this document must satisfy any relevant legal requirements in that country.

© GMP. All rights reserved. Reproduction in whole or in part without permission is prohibited.