



Biotech Daily

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Daily news on ASX-listed biotechnology companies

Dr Boreham's Crucible: Cronos Australia

By TIM BOREHAM

ASX Code: CAU

Share price: 60 cents

Market capitalization: \$332.6 million

Shares on issue: 554,370,703

Chief executive officer: Rodney Cocks

Board: Dr Marcia Walker (interim chair), Mr Cocks, Dr Ben Jansen, Guy Headley

Financials (12 months to June 2022): revenue \$67 million (up 208%), earnings before interest, tax, depreciation and amortization \$10.5 million (up 390%), net profit \$6 million previously a \$4million loss), cash \$16.1 million (up 673%), maiden dividend one cent a share (fully franked).

Major identifiable shareholders: Guy Headley 23%, Ben Jansen 23%, Cronos Global 10%, Matua Jansen 10%

In a vast green field of ASX-listed cannabis flame-outs, Cronos Australia stands out as a rare beacon of meaningful revenue and - gasp ! - profitability.

And here's where you really pick yourself off the floor: the company last month delivered a one cent a share maiden dividend - the first time an ASX pot stock has ever dispensed such a return to investors.

At the heart of its success is its markedly different business model: rather than enduring the heavily-regulated drudgery of cannabis cultivation and extraction, Cronos is a medical dope marketplace that links patients, doctors and pharmacies on the one platform.

Specifically, the Canview platform links 700 authorized prescribers (mainly general practitioners), 2,800 dispensing pharmacies and 7,000 regular patients. The platform sources around 160 products from 28 local and Canadian suppliers.

The asset-light, virtual platform has been likened to the sector's version of Amazon or Ebay, although it's not quite as easy as clicking and collecting an aromatherapy candle you never knew you needed.

In August, Cronos reported a net profit after tax of \$6.05 million for the full year to June 30, on a 208 percent revenue uptick to \$67.0 million.

"We're really happy that we have a differentiated business model and a differentiated financial outcome as a result," says Cronos chief Rodney Cocks.

About Cronos

Cronos Australia was originally a 50:50 venture between Canadian medical cannabis giant Cronos Group and a private equity fund owned by Mr Cocks.

Mr Cocks was awarded Victoria's Australian of the Year gong in 2005, for tending to injured bombing victims in Bali and Baghdad's UN Headquarters. He has held roles at Linfox and Boston Consulting Group.

Cronos Australia listed on the ASX in late 2019, having raised \$20 million at 50 cents apiece. Originally, the group's sales plans revolved around Cronos Group's in-house products, under the Peace Naturals banner. The company also sold the Adaya brand and continues to do so.

Cronos had planned to build a cannabis manufacturing facility in Smeaton, Victoria, but its hue changed radically after September 2021, when it announced plans to merge with CDA Health Pty Ltd in a cash-scrip deal.

CDA - as in Cannabis Doctors Australia - operates under a telehealth model, but has face-to-face clinics in Brisbane, the Gold Coast and the Sunshine Coast.

Via its Burleigh Heads Cannabis subsidiary, CDA owned Canview, a "compliant prescription pathway to access high quality medical cannabis product". CDA also owned Healthy Not High, which sells hemp products.

Post the circa \$60 million deal, CDA shareholders own roughly 74 percent of Cronos.

The company also has a 50:50 partnership with the founders of the Sukin skincare brand, in view of developing cannabidiol (CBD) based skin unguents.

Musical board chairs

CDA was founded by cannabis doctor Ben Jansen and the commercially-oriented Guy Headley, who has been installed on the Cronos board.

The merger resulted in a wholesale board reshuffle, with original directors Daniel Abrahams, Jason Adler, Michael Gorenstein and Anna Burke leaving the building. (Yes – Ms Burke is the former Labor MP and House of Representatives speaker).

Cronos Global CEO Kurt Schmidt also joined the board in December 2021, but the stint was short-lived after he left his day job in March 2022.

Health sector veteran Shane Tanner chaired Cronos but stepped down in April this year.

Canview? Can do !

Launched in 2020, Canview is automated and works on artificial intelligence.

Via Canview, the patient books a doctor's appointment. The doc then sends the prescription via Canview to one of 2,800 participating chemists (representing half of Australia's pharmacies).

The pharmacy orders the medicine (also via the platform) and a follow-up consultation is arranged.

Dr Cocks says current access arrangements are slow and dis-jointed (excuse the pun).

Currently, medicinal access is available mainly through the Therapeutic Goods Administration's Special Access Scheme B on a case-by-case basis, or authorized prescribing doctors. Access is heavily weighted to the latter channel.

With the exception of the approved cannabis drugs Sativex (multiple sclerosis) and Epidiolex (epilepsy), pot treatments are restricted substances and thus can only be dispensed via these means.

"With those modalities there is a massive compliance burden which sits behind it," Mr Cocks says. "Our system solves the problem for the doctors. It also gives prescribers visibility over inventory and their ability to prescribe."

Sky-high demand

While the listed ASX medical cannabis trip has been difficult generally, use has soared from virtually nil in 2018 to more than 100,000 active patients.

Mr Cocks says anecdotal evidence from the clinic visits suggests that 80 percent of medicinal cannabis is used for chronic pain, often as an alternative to opioids. Mental health (anxiety) and epilepsy are also often mentioned.

But according to research company BMC's latest survey, only 13.3 percent of patients are using prescribed products which implies most are obtaining their hooch illicitly.

Nearly half the sample reported the prescribed stuff was too expensive, while some respondents said it was too hard to find a prescribing doctor.

Encouragingly, 95 percent reported an improvement in their condition.

Cronos reports the vast majority of medication sold via the platform is whole flower bud (ground and vaporized), as opposed to extracted oils.

Finances and performance

The source of most of Cronos's revenue, the Canview platform sold a record 486,000 products last financial year - a 270 percent increase on the previous corresponding period.

Cumulatively, the company is approaching its one millionth sale.

Cronos gleans its revenue from a margin on the goods sold, with an average prescription value of \$130. Chemists don't pay to be involved and Cronos pays their shipping costs.

Chief finance officer Tom Howitt says the company's gross margin averaged 36 percent for the year, reflecting low fixed costs and the absence of production facilities.

"We are confident we can keep that consistent for the next financial year at least."

Cronos appears well-placed to continue to pay dividends, but Mr Howitt says payouts will be considered alongside other measures such as acquisitions or growing the existing assets.

"We are working in a fast-moving industry and it's hard to predict anything with certainty," he says. "Everything we do is patient-centric, but in a way that maximizes value for shareholders."

Cronos shares jumped 45 percent to 32 cents on July 25, when the full-year numbers in effect were pre-announced in the June quarter results.

Last Monday, the stock whooshed up nine cents, or 19 percent to a record 55 cents on little obvious news.

The lowest the shares have traded in the post-merger era is 11 cents, in mid-September 2021.

Surveying the pot-holed landscape

Without harping on the point, pretty much every other ASX pot stock has encountered some sort of strife and most have tweaked their business direction.

Many of them have merged and have had more transitions than David Bowie, such as sector pioneer Phytotech Medical which has morphed into the cannabis investment group MMJ.

The \$400 million market cap Incannex Healthcare is what one would politely call pre-revenue, but it's taking a serious approach to developing drugs to treat sleep apnoea and traumatic brain injury. It's also got a keen interest in psychedelics, which is proving a popular expansionary - and mind expanding - pursuit.

Little Green Pharma has done well to forge a European focused cannabis oils export business, although production now centres on an acquired Danish facility

Cann Group is producing from a facility near Mildura in northern Victoria, having earlier ditched a plan to build a cultivation factory in Tullamarine at a sky-high cost. The company planned its first commercial harvest in June.

Cann Group recently was busted when Mildura locals noticed an eerie pink glow over the town, which was traced to LED lights at its facility at a hitherto secret location. The quirky incident made world news.

Formerly The Hydroponics Company and then THC Global Group, Epsilon Healthcare is ramping up output at its Southport factory, the biggest compliant cannabis factory in the Southern Hemisphere.

We'll also call out the worthy performance of Althea Group, which managed customer receipts of \$22 million for the 2021-'22 year, up 113 percent.

Althea's quirk is that roughly half its revenue derived from recreational cannabis in the (growing) markets where pot is legal.

What's next?

Management's focus will be on enticing more doctors, chemists and patients to join the platform.

A key priority is to convert the occasional-prescribing doctors into more ardent ones.

"We are trying very hard to offer more functionality and make it a simpler and better product," Mr Cocks says. "We don't rest on our laurels ... we work to deepen our competitive moat [position]."

He notes a network effect as more parties join the platform, because the scale of activity increases to the benefit of all.

While overseas expansion is possible, the North American market is muddled by the spread of legalized dope, which means the stuff can be obtained at the corner store or even home delivery. The European market has its own peccadillos.

Acquisitions are possible, but not in upstream growing and cultivating activities.

"M&A can be a huge source of shareholder value but it can also destroy it," Mr Howitt says.

Quite.

Dr Boreham's diagnosis:

With medicinal dope use soaring from a very low starting point and only two percent of general practitioners involved, we agree with management's assertion of an "amazing opportunity".

Freshleaf Analytics reckons the local market was worth \$230 million in 2021, growing to \$423 million by the end of 2022.

"It's really interesting to see that the companies that have made it did a strategic shift away from cultivation," Dr Cocks says. "It's something we've taken lessons from and vindicates ... our strategy around being asset-light."

Mr Cocks says there's been a distinctive "mainstreaming" of cannabinoid therapies as more doctors become comfortable with dispensing the stuff.

Of course, with 31,000 general practitioners in the country there's a long way to go. The other challenge - or opportunity - is to convert the illegal users to kosher ones.

Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort. He is the joint owner of a home-mortgage, but please don't call him a dope.