

urban-gro, Inc.

United States / AgTech
 Nasdaq
 Bloomberg: UGRO US
 ISIN: US91704K2024

Q2/23 report

RATING
BUY

PRICE TARGET
\$ 6.40

Return Potential 476.6%
 Risk Rating High

EARNINGS IMPROVED BUT WORK STILL TO BE DONE

Second quarter reporting featured a solid sequential uptick in sales and earnings. The Q2 AEBITDA loss narrowed to \$-2.0m vs \$-3.4m in the January-to-March period, thanks largely to overhead cost reductions. An uptick in cash and liquid assets to \$8.6m (Q1: \$7.3m) should also cheer investors concerned that the company might have to tap the markets to replenish cash. Management reiterated on the earnings call that UGRO is on a solid financial footing. However, the order backlog was revised downwards from \$105m in Q1 to \$79m after a cannabis project had to be idled when the client ran into financing issues. Despite this setback, we think the company has found a path out of the loss-making woods, and we remain Buy-rated on urban-gro. Updated 2023 FBe and a recalibrated DCF now point to a \$6.4 TP (old: \$7).

Earnings improved but still work to be done urban-gro brass kicked off the earnings call reemphasising their quest to bring adjusted earnings into the black. The AEBITDA loss narrowed to \$-2.0m in Q2 (Q1: \$-3.4m), and the company expects this negative result to be pared down even further in Q3 setting up potential for a positive number in the October-to-December period. UGRO continued to slash overhead expenses in Q2 and sees around \$2.9m in SG&A savings going forward, while several senior staff members also stepped up by offering to accept stock grants in lieu of portions of their salaries for 3 months.

Other Q2 takeaways Operating cash flow totalled \$3.6m in Q2 and was helped by the conversion of a large receivable into cash. The combined working capital effects boosted the cash position to \$8.6m (+18% Q/Q). The business mix was also encouraging in a still tricky environment for the cannabis and produce markets. UGRO began to diversify into other industrial, commercial, and healthcare sectors a year ago, and this is paying off (overleaf). Some two thirds of Q2 sales stemmed from these new sectors. Although the pause in the cannabis project is disappointing, the contract remains open and the company is demonstrating its ability to apply its expertise to other sectors. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2020	2021	2022	2023E	2024E	2025E
Revenue (\$m)	25.84	62.11	67.03	90.07	120.95	161.45
Y/Y growth	6.8%	140.4%	7.9%	34.4%	34.3%	32.0%
AEBITDA* (\$m)	-0.65	2.68	-3.90	-5.87	1.38	3.87
AEBITDA margin	-2.5%	4.3%	-5.8%	-6.5%	1.1%	2.4%
Net income (\$m)	-5.07	-0.88	-15.28	-11.91	-3.77	-1.67
EPS (diluted) (\$)	-1.06	-0.09	-1.44	-1.19	-0.38	-0.17
DPS (\$)	0.00	0.00	0.00	0.00	0.00	0.00
FCF (\$m)	-3.81	-9.90	-17.06	-9.28	-1.03	1.70
Net gearing	-83.7%	-71.8%	-23.5%	-10.1%	-6.3%	-12.6%
Liquid assets (\$m)	0.18	34.59	12.01	2.54	1.51	3.21

* adjusted EBITDA

RISKS

Risks include but aren't limited to regulatory, financing and market cyclicality, particularly in the cannabis sector.

COMPANY PROFILE

urban-gro, Inc is a provider of professional turnkey facility services to the CEA industry and various commercial sectors. Headquartered in Denver, Colorado, the company now operates six offices across North American and one in Europe. Operations are executed by a staff numbering 140 employees.

MARKET DATA

As of 16 Aug 2023

Closing Price	\$ 1.11
Shares outstanding	11.61m
Market Capitalisation	\$ 12.88m
52-week Range	\$ 1.11 / 5.21
Avg. Volume (12 Months)	87,330

Multiples	2022	2023E	2024E
P/E	n.a.	n.a.	n.a.
EV/Sales	0.1	0.1	0.1
EV/AEBITDA	n.a.	n.a.	5.2
Div. Yield	0.0%	0.0%	0.0%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2023

Liquid Assets	\$ 8.56m
Current Assets	\$ 34.52m
Intangible Assets	\$ 4.87m
Total Assets	\$ 61.29m
Current Liabilities	\$ 31.82m
Shareholders' Equity	\$ 26.73m

SHAREHOLDERS

Insiders	28.9%
Institutional Holdings	28.0%
Free Float	43.1%

**Table 1: Q2 vs FBe and prior year period**

All figures in USDm	Q2/23	Q2/23E	variance	Q2/22	variance	H1/23	H1/22	variance
Revenue	18.8	21.5	-12%	16.3	16%	35.6	37.3	-4%
Gross profit	2.9	3.6	-21%	3.5	-18%	5.7	8.4	-32%
Margin	15.2%	16.9%	-	21.5%	-	16.0%	22.6%	-
AEBITDA	-2.0	-1.2	-	-0.5	-	-5.4	-0.1	-
Margin	-	-	-	-	-	-	-	-

Source: First Berlin Equity Research; urban-gro

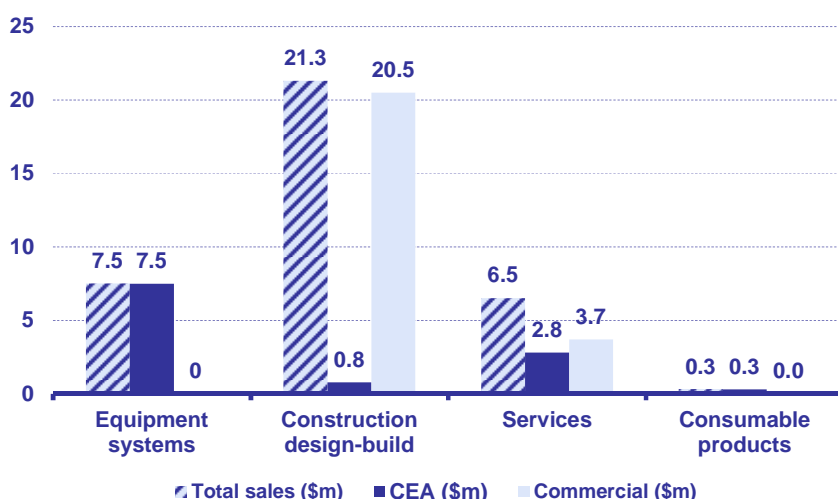
Revenue up 12% Q/Q The company racked up nearly \$19m in revenues for the quarter (+16% Y/Y). The improvement was led by a welcomed 59% sequential uptick in the higher margin Equipment Systems sales to \$4.6m, while Construction Design-build contributed \$11m to the topline (+8% Q/Q). The 12% miss to our revenue target owes chiefly to a shortfall to our Construction Design-build figure occasioned by the aforementioned cannabis project delay.

Table 2: Revenue by segment

All figures in USDm	Q2/23	Q2/23E	variance	Q2/22	variance	H1/23	H1/22	variance
Equipment systems	4.6	4.0	14%	10.1	-54%	7.5	27.1	-72%
Services	3.0	3.3	-8%	3.0	0%	6.5	6.7	-3%
Construction Design-build	11.0	14.0	-21%	2.9	279%	21.3	2.9	634%
Other	0.2	0.2	0%	0.3	-	0.3	0.6	-50%

Source: First Berlin Equity Research; urban-gro

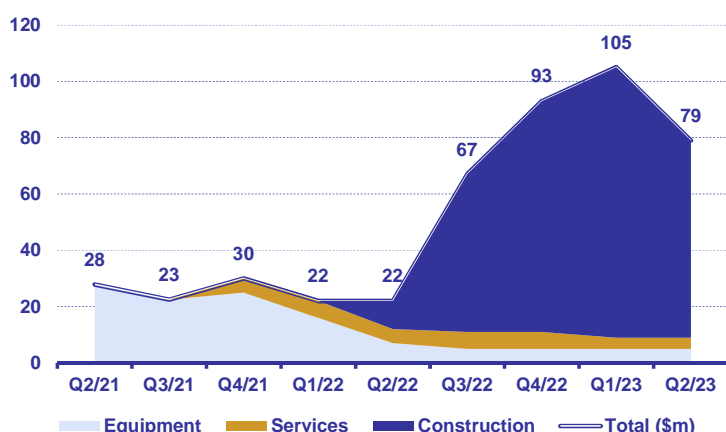
Meanwhile, commercial clients accounted for some 66% of Q2/23 revenue compared to 20% in the prior year period. The new revenue split underpins management's effort to reduce exposure to the still choppy cannabis and vertical farming markets.

Figure 1: H1/23 revenue breakdown of CEA vs Commercial

Source: First Berlin Equity Research; urban-gro



Figure 2: Order backlog developments



Source: First Berlin Equity Research; urban-gro

Order backlog takes a hit The Q2/23 backlog tallied \$79m (-25% Q/Q) and comprised 32% commercial (non-CEA) projects valued at \$25m. The sequential decline is traced to a cannabis cultivation project that had to be paused when the client encountered funding issues. The project remains open, but management prudently removed the project to maintain high backlog integrity. Construction Design-build accounted for 89% of the backlog at the end of H1, and the company believes several small deals deep in discussion will be inked H2. Management adjusted their 2023 guide accordingly (table 5 overleaf).

Table 3: Financial highlights

All figures in USDm	Q2/23	2022	variance
Cash & liquid assets	8.6	12.0	-28%
Financial debt (short- and long-term)	1.9	3.8	-50%
Net debt / (net cash)	-6.7	-8.2	-
Total assets	61.3	62.1	-1%
Shareholders' equity	26.7	34.7	-23%
Equity ratio	44%	56%	-

Source: First Berlin Equity Research; urban-gro

urban-gro exited the six month period with cash and liquid assets of \$8.6m vs \$7.3m at the end of Q1. The 18% Q/Q increase stems from lower working capital consumption with the collection of a large outstanding receivable in Q2. An increase in accounts payable meant UGRO ended the period with negative working capital of roughly \$2.8m.

Table 4: Cash flow developments

All figures in USDm	H1/23	H1/22	variance
Operating cash flow	-0.7	-4.9	-
Cash flow from investing	-0.2	-3.1	-
Free cash flow (FCF)	-0.9	-8.0	-
Cash flow from financing	-2.6	-3.8	-
Net change in cash	-3.4	-11.8	-

Source: First Berlin Equity Research; urban-gro

**Table 5: Revised guidance vs our forecasts**

	Unit	Guidance		FBe
		Old	New	
Revenue	\$m	100 - 120	90 - 95	90.1
Growth	%	49 - 79	34 - 42	34
AEBITDA	\$m	-3 to break even	-5 to -6	-5.3

Source: First Berlin Equity Research; urban-gro

We have adjusted 2023 FBe to account for: (1) the paused cannabis project in the Construction Design-build backlog; (2) the cost cutting measures that will save some \$2.9m in overhead; and (3) the shortfall to our Q2 earnings targets. In terms of sales and earnings cadence in H2/23, we look for the topline to improve sequentially and for AEBITDA to show another incremental improvement in Q3 with a break-even result for this KPI in Q4.

Table 6: Revisions to FBe and target price

	old	new	revision	upside	dividend yield	total return
Price target (\$)	7.0	6.4	-8.6%	476.6%	0.0%	476.6%
All figures in USD '000	2023E			2024E		
	old	new	revision	old	new	revision
Revenue	97,192	90,068	-7.3%	129,588	120,945	-6.7%
Gross profit	15,507	14,315	-7.7%	21,184	20,301	-4.2%
Margin (%)	16.0%	15.9%	-	16.3%	16.8%	-
AEBITDA	-3,014	-5,865	-	265	1,377	419.3%
Margin (%)	-3.1%	-6.5%	-	0.2%	1.1%	-

Source: First Berlin Equity Research estimates



VALUATION MODEL

We remain Buy-rated on urban-gro Although the company is not quite out of the loss-making woods, we think UGRO is on a solid path to reach its profitability targets by YE23 with a business mix less exposed to the volatile cannabis and nascent vertical farming sectors. Our TP moves to \$6.4 (old: \$7) after adjusting our DCF model for the Q2 performance.

Table 7: DCF model

In USD '000	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E
Sales	90,068	120,945	161,450	198,583	234,328	269,477	299,120	329,032
NOPLAT	-10,217	-3,768	-1,666	2,822	6,950	10,528	12,534	14,675
(+) depreciation & amortisation	811	605	807	794	703	808	808	804
Net operating cash flow	-9,407	-3,163	-859	3,616	7,653	11,336	13,342	15,479
(-) Total investments (CAPEX and WC)	1,978	-1,857	-2,433	-2,482	-2,407	-2,212	-2,016	-2,118
(-) Capital expenditures	-730	-738	-985	-1,013	-961	-835	-927	-1,020
(-) Working capital	2,707	-1,120	-1,448	-1,469	-1,446	-1,377	-1,088	-1,098
Free cash flows (FCF)	-7,429	-5,020	-3,292	1,134	5,246	9,124	11,326	13,361
PV of FCFs	-7,077	-4,203	-2,422	733	2,980	4,555	4,968	5,151

In EUR '000	WACC	Terminal EBIT margin	Terminal growth rate
PV of FCFs in explicit period	10.8%	6.1%	1.0%
(+) PV of FCFs in terminal period	11.8%	6.6%	1.5%
Enterprise value (EV)	12.8%	7.1%	2.0%
(+) Net cash / (-) net debt	13.8%	7.6%	2.5%
(+) Investments / minority interests	14.8%	8.1%	3.0%
Shareholder value	15.8%	8.6%	3.5%
Fair value per share (\$)	16.8%	9.1%	4.0%

	WACC	Terminal EBIT margin	Terminal growth rate
Cost of equity	10.8%	6.1%	1.0%
Pre-tax cost of debt	11.8%	6.6%	1.5%
Tax rate	12.8%	7.1%	2.0%
After-tax cost of debt	13.8%	7.6%	2.5%
Share of equity capital	14.8%	8.1%	3.0%
Share of debt capital	15.8%	8.6%	3.5%
WACC	16.8%	9.1%	4.0%

*Please note our model runs through 2035 and we have only shown the abbreviated version for formatting purposes



INCOME STATEMENT

All figures in USD '000	2020	2021	2022	2023E	2024E	2025E
Revenues	25,838	62,113	67,030	90,068	120,945	161,450
Cost of goods sold	-20,122	-47,353	-52,824	-75,753	-100,645	-133,571
Gross profit	5,716	14,760	14,206	14,315	20,301	27,879
SG&A	-6,658	-13,124	-20,971	-22,190	-21,528	-26,316
Stock-based compensation	-1,803	-1,841	-2,572	-2,342	-2,540	-3,229
Operating income (EBIT)	-2,746	-205	-12,637	-10,217	-3,768	-1,666
Net financial result	-1,498	-334	274	-192	0	0
Other non-operating result	-831	-337	-577	-1,500	0	0
Impairment loss	0	0	-2,661	0	0	0
Pre-tax income (EBT)	-5,074	-876	-15,600	-11,909	-3,768	-1,666
Income taxes	0	0	322	0	0	0
Minority interests	0	0	0	0	0	0
Net income / loss	-5,074	-876	-15,278	-11,909	-3,768	-1,666
Diluted EPS (in \$)	-1.06	-0.09	-1.44	-1.19	-0.38	-0.17
AEBITDA	-652	2,679	-3,904	-5,865	1,377	3,870
Ratios						
Gross margin	22.1%	23.8%	21.2%	15.9%	16.8%	17.3%
EBIT margin	-10.6%	-0.3%	-18.9%	-11.3%	-3.1%	-1.0%
AEBITDA margin	-2.5%	4.3%	-5.8%	-6.5%	1.1%	2.4%
Net margin	-19.6%	-1.4%	-22.8%	-13.2%	-3.1%	-1.0%
Tax rate	15.0%	21.0%	21.0%	21.0%	21.0%	21.0%
Expenses as % of revenues						
SG&A	25.8%	21.1%	31.3%	24.6%	17.8%	16.3%
Stock-based compensation	7.0%	3.0%	3.8%	2.6%	2.1%	2.0%
Y-Y Growth						
Revenues	6.8%	140.4%	7.9%	34.4%	34.3%	33.5%
Operating income	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
Net income/ loss	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.



BALANCE SHEET

All figures in USD '000	2020	2021	2022	2023E	2024E	2025E
Assets						
Current assets, total	5,245	59,480	34,558	18,693	20,878	26,783
Cash and equivalents	185	34,591	12,008	2,536	1,508	3,209
Trade receivables	915	13,126	15,380	8,637	11,598	15,481
Inventories	537	515	320	623	827	1,098
Other ST assets	3,609	11,248	6,849	6,897	6,945	6,994
Non-current assets, total	2,915	14,675	27,508	27,479	27,664	27,894
Property, plant & equipment	129	208	1,307	1,316	1,328	1,344
Goodwill & other intangibles	991	9,568	21,023	20,933	21,054	21,215
Financial assets	1,710	4,210	2,559	2,585	2,611	2,637
Other LT assets	85	690	2,619	2,645	2,671	2,698
Total assets	8,161	74,155	62,066	46,171	48,542	54,677
Shareholders' equity & debt						
Current liabilities, total	14,546	25,005	24,256	17,794	21,253	25,680
Trade payables	654	6,067	9,960	6,226	8,272	10,978
ST debt	5,271	0	0	0	0	0
Customer deposits	4,879	13,345	2,571	3,455	4,639	6,124
Provisions	1,799	3,878	3,197	3,325	3,458	3,596
Other current liabilities	1,944	1,716	8,527	4,788	4,884	4,982
Long-term liabilities, total	1,021	983	3,078	3,212	3,351	3,496
Long-term debt	1,021	0	0	0	0	0
Deferred tax liabilities	0	441	1,033	1,085	1,139	1,196
Other non-current liabilities	0	542	2,045	2,127	2,212	2,300
Shareholders' equity	-7,406	48,167	34,732	25,165	23,938	25,501
Total consolidated equity and debt	8,161	74,155	62,066	46,171	48,542	54,677
Ratios						
Current ratio (x)	0.4	2.4	1.4	1.1	1.0	1.0
Quick ratio (x)	0.3	2.4	1.4	1.0	0.9	1.0
Equity ratio	-91%	65%	56%	55%	49%	47%
Net debt	6,197	-34,591	-8,175	-2,536	-1,508	-3,209
Net debt / EBITDA (x)	-9.5	-12.9	2.1	0.4	-1.1	-0.8
Net gearing	-84%	-72%	-24%	-10%	-6%	-13%
Return on equity (ROE)	69%	-2%	-44%	-47%	-16%	-7%
Capital employed (CE)	1,016	9,357	12,498	9,710	10,962	12,588
Return on capital employed (ROCE)	-270%	-2%	-101%	-105%	-34%	-13%



CASH FLOW STATEMENT

All figures in USD '000	2020	2021	2022	2023E	2024E	2025E
Net income	-5,074	-876	-15,278	-11,909	-3,768	-1,666
Depreciation and amortisation	258	495	1,483	811	605	807
Amortisation of financing instruments	558	104	0	0	0	0
Stock-based compensation	1,803	1,841	2,572	2,342	2,540	3,229
Other non-cash items	1,016	500	3,427	0	0	0
Tax result	0	0	-322	0	0	0
Net interest expense	0	0	-274	192	0	0
Operating cash flow	-1,438	2,064	-8,393	-8,565	-623	2,370
Change in working capital	-2,195	-3,628	-4,220	39	358	342
Tax paid	0	0	0	0	0	0
Net operating cash flow	-3,633	-1,564	-12,613	-8,526	-265	2,712
Cash flow from investing	-176	-8,337	-4,452	-755	-764	-1,011
Free cash flow (FCF)	-3,809	-9,901	-17,065	-9,281	-1,028	1,701
Equity inflow, net	0	57,747	30	0	0	0
Debt inflow, net	4,183	-5,756	0	0	0	0
Interest expenses paid	-638	0	0	-192	0	0
Stock buyback	0	-7,684	-4,362	0	0	0
Other adjustments	0	0	-1,186	1	0	0
Cash flow from financing	3,545	44,308	-5,518	-191	0	0
Net cash flows	-264	34,407	-22,583	-9,472	-1,028	1,701
Cash, start of the year	449	184	34,591	12,008	2,536	1,508
Cash, end of the year	184	34,591	12,008	2,536	1,508	3,209
EBITDA/share (in \$)	-0.14	0.27	-0.37	-0.59	0.14	0.39
Y-Y Growth						
Operating cash flow	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
Free cash flow	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
AEBITDA / share	n.m.	n.m.	n.m.	n.m.	n.m.	181%

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UST-Id.: 251601797

Ggf. Inhaltlich Verantwortlicher gem. § 6 MDStV

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The production of this recommendation was completed on 17 August 2023 at 09:49

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ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

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RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	27 June 2023	\$1.21	Buy	\$7.00
2	Today	\$1.11	Buy	\$6.40

INVESTMENT HORIZON

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Legally required information regarding

- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <https://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Marie-Curie-Straße 24-28, 60439 Frankfurt am Main

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