

This is Auxly / Q2 2024 Letter to Shareholders

# Auxly

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Dear Auxly Shareholders,

As we reach the halfway point of the year, I am thrilled to share the exceptional results of our recent quarter, marking another period of unprecedented success and growth for our company.

We started the year with a very clear focus on sustainable profitability which we expected to deliver through increased teamwork and operational efficiency; prudent cost management; and focused and deliberate growth in our three core product categories of vape, dried flower and pre-rolls. By prioritizing these areas, we sought to not only enhance our market position but also build a solid foundation for long-term success. Our commitment to this strategy has so far proven successful and has allowed us to streamline operations, optimize our resource allocation and drive significant improvements to our financial and commercial results.

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Foray

KOLAB PROJECT

BACK FORTY



Parcel

## Record-Breaking Financial Performance

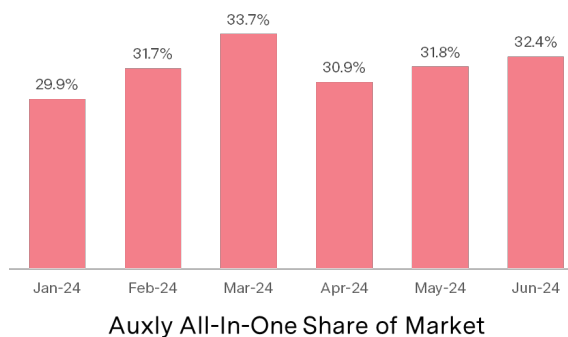
Because of the collective efforts of dedicated and talented employees, we have been able to deliver the best Q2 in Auxly's history and also reach new all-time high milestones across key metrics:

- Net Revenues of \$29.2 million, an increase of 33%, year-over-year and 16% compared to the previous quarter;
- Gross Margins on Finished Cannabis Sold reached an all-time high of 41% compared to 27% in Q2 2023, representing an incredible 1400 bps (14%) improvement;
- Adjusted EBITDA also reached an all-time high of \$5.2 million for the quarter, a remarkable 580% year-over-year improvement;
- SG&A remained essentially flat quarter-over-quarter and approximately \$0.2 million lower than Q2 2023 net of one-time, non-recurring restructuring costs of \$0.7 million
- Net Income and Positive Cash Flow of \$2.0 million and \$2.9 million respectively, setting another Q2 record for Auxly.
- Debt decreased by 48% overall compared to the end of 2023.

The improved topline performance was driven by successful innovations and improved consistency and quality resulting in increased sales in our core categories of dried flower, vape and pre-roll. Continued improvements in operational efficiency and overhead cost management enabled our record-breaking bottom-line results.

## Market Leadership and Performance

We are passionately committed to our consumers; our mission as a company is to help our consumers live happier lives! Our increasing sales are a testament to our commitment to product quality and innovation. We continue to deliver products that consumers trust and love. For example, this quarter our recently launched Liquid Imagination 28g dried flower SKU was a top 10 SKU nationally, despite not being available in Quebec. We also continued to innovate in the pre-roll segment launching several new SKU's, including the large format 0.75g three-pack pre-roll, and we continued to increase distribution for our pre-roll portfolio.





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During the quarter we made market share gains across all three of our key product categories and, of note, we dominated the rapidly growing all-in-one vape category. Our product development and vape manufacturing teams continue to demonstrate why they are the best vape team in the country. Our 4 Back Forty all-in-one vape SKUs finished the quarter as the top 4 all-in-one vape SKUs nationally, securing over a 32% share of all-in-one vape market. Our momentum in the vape category resulted in Auxly finishing the quarter as the 2nd largest manufacturer of cannabis vapes in Canada by total sales. We

plan to build on this momentum by launching new and exciting flavour profiles under our Back Forty brand, while also launching a new innovative vape format under our Kolab Project brand throughout the second half of the year.

### **Operational Highlights**

Our low-cost cultivation is an increasing competitive advantage within the current Canadian cannabis landscape. With only a few large-scale greenhouses capable of consistently producing high quality cannabis at a low cost, we are seeing increased demand and pricing for our bulk flower products. Given the significant capital outlay and amount of time necessary to replicate the scale, automation, consistency, and efficiency of our Auxly Leamington facility, we believe that Auxly Leamington provides us with a significant competitive advantage in the short and medium term. We intend to leverage this advantage to drive further growth in the Canadian adult-use market and in wholesale bulk cannabis sales to other industry participants.

Due to the increased demand for our branded and wholesale flower products, we have increased cultivation levels on a capital-light basis at our

Auxly Leamington facility, which included increasing plant density and optimizing post-harvest processes. We expect that our ongoing efforts will continue to enhance the 41% Finished Cannabis Inventory Sold Margin (an all-time record for Auxly!) that we achieved in this Q2 of 2024

We remain dedicated to improvements in product quality and innovation and look forward to introducing consumers to some of the new cultivars in our extensive genetics library, including Fire Breath, an exciting new cultivar being released this fall that we think is going to be a hit with our flower consumers.

## Looking Ahead

### Cannabis Industry Landscape

The domestic and international cannabis markets are continuing to evolve, and we are closely monitoring significant upcoming regulatory changes that could positively impact our business. Domestically, Health Canada has proposed amendments to the Cannabis Regulations, known as the Regulations Amending Certain Regulations Concerning Cannabis. This consultation closed on July 8, 2024, and we anticipate these amendments will come into force in early 2025.

The proposed changes are intended to simplify and streamline various aspects of the regulatory framework governing the cannabis industry. They aim to reduce administrative burdens

by streamlining reporting requirements and compliance obligations. Notably, these amendments could lower regulatory costs associated with excessive personnel security clearances and certain onsite monitoring devices.

Equally as important, the proposed changes will give us some increased flexibility in cannabis product packaging, including the option for transparent packaging of dried cannabis and more adaptable product multi-packs, to give our consumers a more informed purchasing experience and greater value.





## Explosive Growth of All-In-One Vape Category

The all-in-one vape category has experienced remarkable growth, now representing 20% of the total vape market, up from just 8% in July 2023<sup>1</sup>. Consumers are increasingly attracted to the discreet and convenient design, ease of use, and rechargeable features of these devices. Our Back Forty brand is dominating this segment with the top four best-selling all-in-one products nationally and a commanding 32% share of category. Building off the momentum of our Back Forty all-in-one vapes, we are excited to launch a new all-in-one format under our Kolab Project brand. In keeping with Kolab's market reputation as the highest quality vape hardware in the entire industry, our Kolab all-in-one device will marry state-of-the-art technology with convenient design. This new Kolab all-in-one device will feature our most potent extract ever at 95% THC, uses a blue ceramic coil and offers dual-heat settings to guarantee a carefully crafted experience.

## Market Trends

In today's dynamic and rapidly evolving market, the importance of innovation cannot be overstated. As consumer preferences evolve and new trends emerge, staying ahead of the curve is essential for maintaining our competitive edge. Our commitment to consumer insights and innovation ensures that we are able to anticipate and respond quickly to emerging trends and set new standards for product excellence. By fostering a culture of creativity and agility, we have been able to note several key trends shaping the cannabis market and driving our growth.



<sup>1</sup> Hifyre IQ, July 31, 2024



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### **Enhanced Flower Quality at All Price Tiers**

The modern flower consumer demands value and expects increasing quality, regardless of the price point. We continue to elevate the quality of our dried flower across all price tiers. Our focus on improving THC potency and refining post-harvest practices has driven continued quality improvements and superior product value. For example, we have introduced practices such as hang-drying, dry-trimming, 14+ day curing, and humidity packs for Back Forty flower. Additionally, our Kolab Project brand features the Exotics strain rotation, showcasing some of the finest indoor-grown flower in Canada.

### **Continuing Our Momentum**

As we celebrate these accomplishments, our focus remains firmly on continued sustainable and profitable growth. We expect to see continued revenue expansion; gross margin improvements and enhanced profitability throughout the second half of the year, driven by the excellence of our people, increased consumer demand for our quality products, an exciting pipeline of innovative new products and our commitment to continued improvement in operational efficiency and overhead cost management.

Thank you for your support and trust in our company. Your investment and engagement are vital to sustaining our momentum. We look forward to sharing more successes with you in the future.

Best,  
Hugo Alves, CEO