

# Burcon NutraScience (BU-T)

## Major Endorsement Brings Cash and Credibility – Raise Target Price

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Doug Cooper, MBA  
(416) 643-3863

[dcooper@beaconsecurities.ca](mailto:dcooper@beaconsecurities.ca)

### Major Investment

<b>BUY (Unch.)</b>	<b>\$6.50</b> (was \$3.25)
Recent/Closing Price (C\$)	\$2.29
12-month Target Price (C\$)	\$6.50
Potential Return	184%
52 Week Price Range	\$0.60 - \$2.49

	Estimates		
YE: March 31	FY19	FY20E	FY21E
Revenue (\$MM)	\$0.0	\$0.1	\$0.8
Adj EBITDA (\$MM)	(\$4.5)	(\$4.2)	(\$3.4)
Adj. EPS	(\$0.11)	(\$0.05)	(\$0.02)

	Valuation		
	FY19	FY20E	FY21E
EV/Sales	n/a	n/a	n/a
EV/EBITDA	n/a	n/a	n/a
P/E	n/a	n/a	n/a

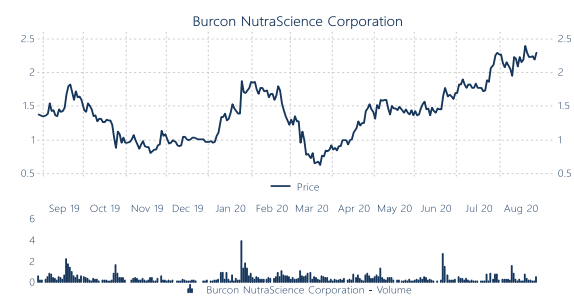
Stock Data	
Shares Outstanding (MMs)	
Basic	97
FD	116
Market Cap (C\$MMs)	
Basic	\$222
FD	\$266
Net Debt (US\$MM)	-\$13.0
EV (C\$MM)	\$248

### About the Company

Burcon NutraSciences has over 20 years experience developing and patenting processing technologies and product applications for proteins derived from crops such as soy, pea and canola among others. In Jan 2020, its JV partner Merit Functional Foods signed a collaboration agreement with Nestle and in August 2020, Merit secured an equity investment from Bunge Ltd. Merit has built and will commercialize a pea processing plant expected to be operational in early 2021.

### All prices in C\$ unless otherwise stated

#### Stock Performance



- Major Equity Partner Adds Cash and Credibility:** Last night, Merit Functional Foods announced that Bunge Limited (BG – N, NR, US\$6.5 billion market cap) has bought \$30 million of treasury stock in Merit. It also bought stock from the 3 Merit principals of Merit, which brings BG's stake in the company to 25%. We believe this is very important for 2 reasons:
  - Bunge is one of the world's three major agricultural processors along with ADM and Cargill (the "ABCs" of agribusiness). This not only provides Merit with capital to expand its plant as well as a major credibility endorsement but also secures Merit's supply of raw materials. These points in aggregate should lead to a material decline in the discount rate applied to BU's anticipated royalties.
  - This is the second major endorsement by a world leader in the food industry. Recall its partnership with Nestle (world's largest CPG) who will be buying ingredients from Merit. Nestle has been very vocal about its commitment to the plant-based food market and has a number of new product launches based on pea-based proteins (which it will buy from Merit). We believe it views Merit as an out-sourced R&D hub with Merit working "hand in glove" with Nestle to tailor its plant-based proteins for specific products. We would expect to hear more from Nestle, as well as other CPGs, in the coming months on this.
- What Does This Mean for BU stock? Much Higher:** BU's stock price is valued on its equity investment in Merit (33% ownership after the BG transaction), the royalty stream from the revenue derived from Merit and BU's 100% ownership of the technology for plant-based proteins other than pea and canola (licensed to Merit). Let's look at each:
  - Equity Investment in Merit:** We believe the combination of the new \$30 million from BG as well as the cash Merit has already (significant government loans/grants) means that Merit can significantly expand the scope of the plant. Recall that Phase 1 is virtually complete with the plant expected to start generating revenue in January. With this new capital (as well as future access to debt financing), we believe the facility will be increased to a \$200 million revenue run-rate at a 25%+ EBITDA margin. Given its participation in one of the world's most secular trends (electric vehicles being the other), we believe it will receive a premium multiple. At 20x that \$50 million EBITDA run-rate, that would imply a \$1 billion valuation. BU's 33% stake would therefore be worth \$330m (\$3.35/share). Furthermore, we believe BG will likely want to increase its stake and build more plants. This could drive BU's equity value further.
  - Royalty:** We believe BU has an ~6% royalty on sales, which on \$200 million in revenue would be \$12/year. Based on the 20-year term of the license, that would equate to \$240 million. Given the visibility on the partnerships and funding, we believe a low discount rate on this future royalty stream is merited. As such, just based on this one plant, BU's discounted royalty could be worth \$200 million or \$2.00/share. Again, if/when more plants are built, this royalty stream would grow and be accretive to the aforementioned per share value.
  - Value of Technology Outside Pea and Canola:** BU retains the rights to other plant-based proteins including hemp, flax, soy, etc. As the company has created significant value from pea and canola, we believe the market should value other proteins. Value \$1/share.
- Raising Target Price:** As noted earlier, the plant-based protein market is one of the major secular trends of our generation. There is a serious "scarcity" factor for companies who are best positioned to benefit from it. Burcon is one of those. Our "sum-of-the-parts" valuation above implies a \$6.50 target price, albeit could be higher with expansion beyond the single plant. **Maintain Buy.**

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As at July 31st, 2020	#Stocks	Distribution
BUY	54	69.2%
Speculative Buy	11	14.1%
Hold	1	1.3%
Sell	1	1.3%
Under Review	11	14.1%
Tender	0	0.0%
<b>Total</b>	<b>78</b>	<b>100%</b>

BUY Total 12-month return expected to be > 15%  
 Speculative Buy Potential 12-month return is high (>15%) but given elevated risk, investment could result in a material loss  
 Hold Total 12-month return is expected to be between 0% and 15%  
 Sell Total 12-month return is expected to be negative  
 Under Review  
 Tender Clients are advised to tender their shares to a takeover bid or similar offer

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