



Aphria's (TSX:APHA) Surprise Profit Brings Hope to Beaten-Down Cannabis Stocks

Description

Despite the range of issues that have emerged in recent months and impacted cannabis stocks, including **Canopy Growth's** [horrendous](#) fiscal 2019 results and **CannTrust's** regulatory investigation, cannabis cultivator **Aphria** (TSX:APHA)(NYSE:APHA) delivered an unexpected profit.

This surprising result comes on the back of the controversy that has surrounded the company since an adverse research report was released in late 2018, which claimed that Aphria was essentially a fraud. Those results have sparked speculation that now is the time to acquire the legal cannabis grower, because even after spiking sharply after those positive results, Aphria has only gained 5% over the last year.

Better-than-anticipated results

While Aphria reported a full-year fiscal 2019 loss of almost \$17 million, it reported a fourth-quarter net profit of \$16 million compared to a \$5 million loss a year earlier. This surprised many analysts because of the spate of losses reported by cannabis cultivators over the last two years. For the full year and fourth quarter 2019, the cultivator reported an impressive adjusted gross margin of 53%.

What stood out the most was Aphria's ability to grow sales. It reported record fourth-quarter net revenue of \$75 million, which was a 75% increase over the prior quarter, while revenue from adult-use marijuana sales rocketed upwards by 158%.

That impressive sales growth was, however, responsible for increased operating expenses. Costs of goods sold shot up by 74% quarter over quarter to \$87 million, although production costs as represented by all-in sustaining costs (ASICs) for the period fell by 18% to \$2.35 per gram produced, making Aphria one of the lowest-cost major Canadian cultivators. The 47% year-over-year increase in AISCs can be attributed to increased spending on the Aphria Diamond expansion.

Importantly, Aphria finished its fiscal 2019 in a solid financial position with \$551 million of cash,

providing it with enough capital to continue building its operations and expanding the all-important global distribution network.

For fiscal 2020, Aphria is expecting net revenue to more than double compared to 2019 to between \$650 and \$700 million with adjusted EBITDA expected to be \$88 to \$85 million.

The Aphria Diamond facilities, when complete, will add 1.3 million square feet of licensed cultivating space with cultivating capacity of 140,000 kilograms annually, lifting the company's total Canadian production capacity to 255,000 kilograms. That will position Aphria to take full advantage of the expected growth in demand for legal marijuana products globally with analysts expecting the market to be [worth](#) US\$66 billion by 2025.

Aphria is building a global distribution network which already reaches North and South America, Western Europe, and Australia. A key part of that network is its agreement with **PAX Labs** to supply cannabis pods for that company's vaporization devices. PAX has sold over 500,000 oil concentrate devices and continues to expand its U.S. market share. Aphria is expected by some analysts to become a leading provider of various cannabis administration systems with Aphria estimating that PAX devices could represent 30% of the Canadian recreational market by 2021.

Foolish takeaway

It hasn't been smooth sailing for Aphria after it was rocked by the 2018 allegations of fraud. The company has, however, cleared the decks, including taking a \$58 million write-down on the value of its Latin American assets, making it an appealing play on the burgeoning legal cannabis industry. That attractiveness is boosted by its growing cultivation footprint, expanding distribution network, and surprise fourth-quarter 2019 profit. When those factors are considered in conjunction with its tempting valuation metrics, including a price of 10 times sales, 1.4 times book value, and 34 times projected 2020 earnings, it is apparent that Aphria is attractively valued.

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