



Aphria (TSX:APHA) Earnings Drives Cannabis Stocks Higher

Description

Shares of leading cannabis company **Aphria** (TSX:APHA)(NYSE:APHA) gained over 15% yesterday after its fiscal first quarter of 2020 (ended in August) results were released. Aphria reported sales of \$126.1 million with adjusted earnings per share (EPS) of \$0.07.

Analysts estimated the firm to post revenue of \$132.2 million with EPS of -\$0.02. Though Aphria revenue missed estimates, it crushed the earnings forecast, driving the stock higher on October 15.

According to one *Bloomberg* report, Aphria is the first major pot stock to post two consecutive quarters of profits. Aphria was one of the first cannabis producers to increase greenhouse cultivation, resulting in a sustainable operating margin.

Aphria's earnings also drove investor optimism higher. Stocks such as **Aurora Cannabis** and **Canopy Growth** increased by 2.3% and 3.4%, respectively. **Horizons Marijuana Life Sciences ETF** rose by 5.1%.

Aphria stock had declined 13% last week

Aphria investors lost 13% in market value last week [after the company was impacted by Hexo's](#) tepid preliminary forecast. Investors were also worried after Aphria announced that its supply agreement with **Aleafia Health** was scrapped. Aleafia was one of Aphria's largest customers.

However, during the first-quarter earnings call, Aphria management reiterated the outlook for fiscal 2020. The company estimates sales between \$650 million and \$700 million in 2020. It expects adjusted EBITDA between \$88 million and \$95 million, indicating a margin of 13.6% at the midpoint.

Analysts estimated Aphria to post revenue of \$645 million in 2020 with EBITDA of \$86.8 million.

What drove Aphria sales in the first quarter?

Aphria sales rose by an impressive 850% year over year, up from revenue of \$13.29 million in the first quarter of 2019. This growth was driven by several partnerships. It has signed supply agreements with all Canadian provinces and the Yukon territory and claims to have access to 99.8% of the domestic population.

Aphria signed an exclusive distribution agreement with Great North Distributors. The latter is a subsidiary of Southern Glazer's Wine & Spirits and will provide Aphria with a sales force and channel expertise, resulting in an efficient distribution of cannabis products.

Aphria also signed an agreement with We Grow BC, a Vancouver-based licensed cannabis producer. Further, it also has a five-year supply agreement with Shoppers Drug Mart.

Expansion strategy in the U.S. and overseas

Aphria has claimed that as cannabis is illegal in the U.S. at the federal level, it has hindered expansion efforts in the country. All cannabis manufacturers have to create cultivation centres in each state they operate in.

This not only increases costs but impacts operational efficiency as well. Aphria will most likely expand significantly in the U.S. once cannabis becomes legal at the federal level.

The legal cannabis market continues to grow at a fast pace. Europe is considered to be the largest medical marijuana market in the world and Aphria's international strategy is to gain traction in medical cannabis in countries with a stable economic and political jurisdiction.

Will Aphria's bet on vapes backfire?

Aphria has stated that vape sales in the United States market account anywhere between 17% and 30% of total cannabis sales. We know that Canada is getting ready for Cannabis 2.0, where marijuana-based edibles, vapes, and concentrates will be legalized this week.

Aphria has invested capital and resources in product research, development, and production of these emerging categories. However, the recent vaping scandal in the U.S. has driven down demand for vape products, and this sentiment may very well spill over to Canadian markets.

Aphria's press release states, "The company believes edibles and beverages will collectively represent a much smaller proportion of the market and has a strategy established to meet this demand, which will be implemented after vapes have been introduced."

So, is Aphria over-estimating demand in the vaping category? Will these estimates result in the company missing its revenue forecast for fiscal 2020?

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