



Is Aphria (TSX:APHA) Stock a Buy After its Potential Merger With Tilray (NASDAQ:TLRY)?

Description

Cannabis stocks have experienced a strong rally since Joe Biden won the presidential race in late 2020. Investors expect the Democrats to decriminalize or even legalize cannabis at the federal level in the U.S., which will generate massive demand for pot products. Further, cannabis companies will also have access to traditional forms of finances.

Shares of **Aphria** (TSX:APHA)(NASDAQ:APHA) are trading at \$10.9 and have gained over 80% since November 2020. Let's take a look if the Canadian cannabis giant remains a top bet for investors in 2021 as well.

Aphria merges with Tilray

Last month, Aphria announced a merger with **Tilray** ([NASDAQ:TLRY](#)) in an all-stock deal likely to close in the second quarter of 2021. After the merger, the combined entity will generate \$874 million in sales, making it the largest Canadian cannabis company.

Aphria and Tilray will not be able to enter the highly lucrative U.S. market unless marijuana is legalized at the federal level. It means they are allowed to sell only hemp-based products south of the border.

The two companies [expect to generate](#) \$100 million in pre-tax cost savings after the merger. However, similar to most other mergers, Aphria and Tilray will also have to grapple with redundancies and short-term pains associated with mergers.

Another matter of concern is the negative profit margins of both Tilray and Aphria. In the first three quarters of 2020, Tilray's net loss stood at US\$268 million, significantly higher than the US\$102 million it lost in the prior-year period.

While Aphria has achieved a positive EBITDA [for six consecutive quarters](#), it has reported a net loss in three of the last four periods. In the last reported quarters, Aphria's sales fell 4% on a sequential basis

while Tilray's sales were flat year over year.

What's next for investors?

Aphria investors will own 62% of the combined entity at the end of the merger. Historically, the buyer's stock price is negatively impacted in the short term after an acquisition or merger takes place. But over the long term, the stock prices gain momentum if the combined entity manages to benefit from cost synergies and produce a diverse business that consistently increases shareholder return.

Tilray is one of the largest producers of hemp and this business generated US\$61.5 million in sales in the first nine months of 2020. This suggests hemp sales account for 40% of the company's top line and was higher than the US\$58.5 million it generated via cannabis sales.

Aphria can gain traction in the U.S. hemp market via this merger. Further, the company also acquired Sweetwater Brewing Company for US\$300 million in a cash-and-stock deal, allowing it to enter the cannabis beverage segment in the U.S.

The cannabis segment is still at a very nascent stage and investors should brace for further consolidation in this sector. Right now, it seems Aphria's merger with Tilray will provide the company with enough ammunition to become one of the largest pot players in the world.

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