Is Tilray Too Dangerous?

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"Tilray is too dangerous," said CNBC's "Mad Money" host Jim Cramer. "It is a spec stock that is losing money, and we don't recommend stocks that are losing money."

Cramer isn't the only one shying away from the Canadian cannabis producer. Kerrisdale Capital called the company a "failing cannabis player" in a recent report.

> We are short shares of Tilray Brands, a $2.4bn failing Canadian cannabis player running a familiar playbook for unsuccessful businesses trading in the public markets: given structurally unprofitable operations, the company has resorted to ongoing, shameless and massive dilution to stay alive, even as management compensates itself generously while operating metrics further deteriorate.

But is this true? Is Tilray a failing cannabis player? Is Tilray too dangerous for investors?

CNBC is not a Reputable News Organization

Of course, CNBC is not a reputable news organization. It's corporate press, the entertainment division of the military-industrial complex.

Likewise, Jim Cramer has been wrong so many times that it's surprising people still take him seriously.

But Kerrisdale Capital doesn't share Cramer's reputation. Following their report, Tilray's shares dropped 12% to around $2.75 per share.

Of course, it's not all Kerrisdale's fault. The other week, Tilray requested shareholders approve raising common stock shares from 980 million to 1.208 billion.

Tilray argues that the dilution is necessary to remain flexible in response to market uncertainty. But, as indicated by declining stock prices, shareholders weren't happy.

But is Tilray too dangerous for investors?

Among Canadian cannabis producers, Tilray stands out as the dominant player, having succeeded where others have failed. Its global presence in pharmaceuticals and craft beer industries bodes well for future cannabis distribution.

But if Tilray is diluting its share to mask its fiscal health, is the company too dangerous to invest in?

Is Tilray Too Dangerous?

Kerrisdale Capital's report isn't a single-page newsletter. It's a comprehensive takedown of Tilray's fiscal and operational health. But is it accurate? Is Tilray too dangerous for investors?

"Tilray has a dilution problem," the report reads. It refers to Tilray's cash payments to a partner named Double Diamond Holdings. These are "recurring cash obligations" that Tilray has been increasingly

using its stock for payment.

This means Tilray is giving away ownership to fulfill its financial obligations.

Likewise, the report highlights that these payments have grown from $24 million in cash to $100 million in shares. The report suggests Tilray is undervaluing its stock when making these payments to Double Diamond Holdings.

The report also criticizes Tilray for not being transparent about these payments during their quarterly calls.

Kerrisdale Capital calls the adjusted EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization) and free cash flow figures provided by Tilray "materially misleading."

They criticize how these stock payments are missing from Tilray's definition of free cash flow. The report says if you strip away "accounting gimmicks" and "other one-time benefits," Tilray's underlying financial performance is not improving but steadily (and significantly) deteriorating.

What About Craft Beer & USA Legalization?

Kerrisdale Capital's report is critical of how rescheduling cannabis in the United States might benefit Tilray. It's less of a question of "Is Tilray too dangerous," and more of "Is this relevant to Tilray's success?"

Or even detrimental to it?

The report suggests rescheduling cannabis to Schedule III will benefit pharmaceutical companies looking to patent cannabis-based FDA-approved drugs. There are also tax benefits for state-level operators.

But since Tilray doesn't have significant U.S. cannabis operations, what benefit is there? Consider that rescheduling favors U.S.-based companies. It's a net negative for a Canadian cannabis company like Tilray as it empowers its competitors with no tangible benefit to themselves (like cross-border trade).

The report also criticizes Tilray's acquisition of brands from beer giant Anheuser-Busch InBev (ABI). Kerrisdale Capital says the acquisition lacks strategic clarity, and the lack of financial details about the purchase is a huge red flag.

And it gets worse.

According to Nielsen data, the retail sales of these acquired brands have been declining. Looking at the numbers, it appears ABI was happy to sell off its lackluster brands.

Do Investors Consider Tilray Too Dangerous?

Is Tilray too dangerous? Is the company diluting its stocks to mask its financial health and maintain operations? If you're a Tilray fan, consider taking a second look, suggests Kerrisdale Capital's report.

While Tilray's rationale for acquiring ABI brands was for future distribution into the THC-infused beverage market, Kerrisdale Capital's report questions this logic.

They argue that the brands require significant investment, marketing and distribution. Without the support of ABI, Tilray has created more work for themselves. Exploiting the distribution opportunities is not as cut-and-dry as Tilray has made it sound.

Likewise, the report expresses concern about Tilray's valuation, even before the news about

rescheduling cannabis spiked their shares.

The report points out that on the news of a potential rescheduling, Tilray’s shares were trading 36 times higher than their EBITDA and three times higher than their revenue.

But ultimately, the report is concerned about near-term dilution risk related to refinancing. It mentions the payment patterns to Double Diamond. It suggests that over $40 million in stock will be paid to the supplier ahead of the $127 million in convertible notes set to mature on October 1.

Not exactly what you want to hear if you’re a Tilray shareholder. Which brings us back to our central question: Is Jim Cramer right? Did Kerrisdale Capital hit the nail on the head?

Is Tilray too dangerous?