Is Canopy Growth Corp. (TSX:WEED) Stock a Buy After a 20% Plunge?

Description

After having soared almost 400% over one year, **Canopy Growth Corp.** (TSX:WEED)(NYSE:CGC) shares plunged 20% from their peak reached on June 22. The pot producer's latest quarterly results played a big role in the sharp decline in share price.

Sales are rising fast, but losses are widening

The cannabis giant reported its fourth-quarter results on June 27, which disappointed investors. Indeed, while its revenue rose significantly, Canopy reported a loss much larger than expected.

Canopy's revenue rose 55% to $22.8 million in the fourth quarter of 2018 as compared to the same quarter last year. For the whole year 2018, its revenue increased 95% from 2017 to $77.9 million.

The marijuana producer's net loss amounted to $61.5 million ($0.31 per share) in the fourth quarter of 2018, while it was $12 million ($0.08 per share) in the last quarter of 2017. Analysts had expected a loss of $12.8 million.

For the year 2018, the net loss amounted to $70.4 million ($0.40 per share) compared to a net loss of $7.5 million ($0.06 per share) in 2017.

Canopy incurred a large loss in its latest quarter, because the company increased its expenses significantly to be ready for the Canadian recreational cannabis market, which will start on October 17. Overall operating expenses surged 149% to $58.2 million in the quarter ended March 31 as compared to the same period in 2017.

As Canopy expects that the legalization of recreational marijuana will increase demand for its products, the cannabis producer is increasing its production to be able to supply large quantities of cannabis and generate significantly higher revenues starting in the second quarter of fiscal 2019. The company expects to be profitable by the end of its fiscal third quarter.

Canopy expects to have at least 18 retail cannabis stores open in Canada by October 17 and should have about 220,000 kilos available in the first year of recreational marijuana sales.

Canopy continues its expansion in the medical market

While Canopy is preparing for the recreational cannabis market, it is not losing sight on the medical market, which represents a bigger market globally. Canopy wants to be a global leader in medical cannabis and has now a foot on the five continents with its recent expansion in Africa.

Canopy also continues to expand in Europe and is keeping an eye on Germany in particular, which legalized medical marijuana last year. Canopy had $2.3 million in sales in Germany in the fourth quarter, amounting to nearly 10% of the company's overall sales.

Canopy keeps innovating and developing products for the medical market. The company recently launched Spectrum Cannabis Softgels, and Canopy Health, its research segment, will start "in-human" clinical trials this summer to evaluate medical marijuana's potential to treat insomnia.

Bottom line

The market is too focused on the short term. Yes, Canopy is incurring large losses in the short term, and that's not what investors want to see in a stock. But Canopy is still in its high-growth phase: it's normal in that stage for the company to incur losses, as it is investing heavily to gain market share. To decide if Canopy is a good investment, you need to look at the long-term potential of the company.

Canopy could experience very strong growth in the coming years because of the recreational marijuana market, which has strong revenue potential.

Indeed, in Canada, recreational cannabis sales could generate up to $4.34 billion in sales, while the medical cannabis market will account for between $770 million and $1.79 billion.

For Canopy, this should translate into a jump of 316% in sales and 70% in earnings for the current year and into a rise of 170% in sales and 467% in earnings next year. That means the pot producer is expected to generate over $800 million in sales and earn $0.44 per share two years from now.

Nevertheless, investing in a pot company is still risky at this point, and you shouldn't invest more than you are ready to lose. You need a solid stomach to tolerate high levels of volatility and uncertainties related to the marijuana industry.

But I think that patient investors will be rewarded considering the strong potential of the recreational market. Canopy is one of the best pot stocks to own, as it is well prepared for the increased demand in cannabis. I expect there will be another run in weed stocks before legalization, so I think Canopy is a buy on the dip.

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