

Canopy Growth Corp. (TSX:WEED): Why This Analyst Says Demand Will Disappoint

Description

In 2019, [cannabis stocks](#) have continued their unbelievably explosive upward climb, hitting levels that are approaching 2018 highs in the sector.

Canopy Growth Corp. (TSX:WEED)(NYSE:WEED) stock, for example, is 57% higher year-to-date, and only 16% off its October 2018 highs.

Aurora Cannabis Inc. (TSX:ACB) stock is 34% higher year-to-date, and while it's still 37% off of its 2018 highs, its comeback has also been impressive.

But do you ever worry about the unbridled, sky's the limit optimism in this sector?

Well, you wouldn't be alone if you did.

I have fallen in this camp, and now we have some of the major brokerage firms also expressing concern.

Most recently, a [healthcare](#) analyst at Raymond James has publicized his concern related to the market's assumptions of explosive demand, questioning whether this is accurate.

For all the talk about the medical benefits of marijuana, it seems that there have not really been many convincing studies backing up the many claims — the kind of studies that we witness, expect and demand to see from biotech and pharmaceutical companies before we see approvals.

At this time, shareholder capital is being used for these clinical trials in order to prove out the thesis of all the medical benefits that marijuana offers.

But, if we look more closely at the clinical trial process, we can see that the failure rate is extremely high and it is a long and arduous process.

So if marijuana is not approved for many of the indications it is being tested for, it becomes a wellness product, which is a much smaller market subject to fads and big competition.

So where would that leave Canopy Growth and Aurora? Companies that are already struggling with turning a profit from their operations, and stocks that are trading at sky-high valuations?

Canopy is losing money at a feverish pace, as losses continue to mount as expenses increased dramatically to fund the company's growth plans. For example, SG&A expense represented 54% of net revenue versus 43% last year.

While this is to be expected, as the company is embarking on a very aggressive growth strategy, it's nevertheless something investors should watch, as it is falling to the bottom line, reducing earnings,

and cash flow numbers.

Possible weakness in medical demand presents another path to weakness as lower-than-expected medical marijuana use would take marijuana demand away, and while companies would still have the massive recreation market, it would still be a setback.

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