Scratch Out This Weed Stock From Your Shopping List

Description

The anxiety of investors in the cannabis space heightens every time a sordid tale about a cannabis company comes out. On March 28, it was the turn of **CannTrust Holdings** (TSX:TRST)(NYSE:CTST) to report Q4 2018 and full-year earnings. While the both the top-line and year-over-year growth were impressive, the stock still fell 18.95%.

CannTrust's sales growth is stellar but is analogous to the situation of the bigger industry players. Again, investors are frustrated about the bottom line, which is the real gauge of performance. The fourth-quarter sales growth yielded a net loss of $25.5 million and a dismal $6.2 million net income. The saga of discontent continues.

Eroding gross margins

Investor confidence in the cannabis sector continues to erode. You can't blame others who see weed stocks as nothing more than a pump-and-dump play. While nearly all cannabis producers reported astronomical growth sales, losses are enormous as well. There's still no solid business case at the start of Q2 2019.

On a full-year basis, CannTrust's net loss amounted to $13.5 million versus a $6.8 million net income in 2017. In terms of EPS, the company reported a loss per share of $0.26 in the fourth quarter compared to $0.08 for the same period in 2017. Judging by the reported earnings of industry peers, the losses were somewhat expected.

The declining gross margin is adding insult to injury. CannTrust's gross margins in the fourth quarter barely improved (34% to 35%) from a year ago. But on a full-year basis, the 6% contraction in gross margins (from 63% to 57%) was quite telling. CannTrust's cash cost per gram fell sharply from $5.16 in Q4 2017 to $2.94 in Q4 2018.

On the wholesale side, which includes recreational cannabis, CannTrust sold about 1.2 million grams of dried cannabis during the fourth quarter and extracts of about 104 thousand grams. For the first time, the wholesale segment brought in sales Q1 2019. Dried cannabis and extracts were sold for

$4.20 and $3.90 per gram, respectively.

But pricing can become a major factor in the future. The only way to achieve economies of scale is to double or triple production capacity, which the company is currently working on.

Across the border, investors also punished the stock of the newly listed weed company on the NYSE. The erosion in gross margin didn't sit well with them despite the revenues doubling year over year.

Not a strong buy

Back home, there are bullish sentiments. Some analysts see a potential +29.07% increase to $12.74. The recommendation trend is a buy but not a strong buy. The current price is at par with its 200-day moving average of $9.94. However, blowing past the 50-day moving average of $11.72 might be a struggle.

Caution is advised as the cannabis sector appears more volatile than the general market. As for CannTrust, profitability can come sometime late 2020 when peak annual output reaches 200,000 kilos. Thus, be circumspect and scratch out the stock from your shopping list for now.

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