Contrarian Alert: Should You Buy CannTrust Holdings (TSX:TRST) or Canopy Growth (TSX:WEED) Stock?

Description

The meltdown in the prices of marijuana stocks in recent months has contrarian investors kicking the tires on pot stocks that could potentially deliver big returns.

Let's take a look at **CannTrust Holdings** (TSX:TRST)(NYSE:CTST) and **Canopy Growth** (TSX:WEED)(NYSE:CGC) to see if one deserves to be on your buy list today.

CannTrust

CannTrust trades at $2.20 per share at the time of writing. That's down from $13 in March and nearly $15 last October.

The entire sector is off roughly 50% since late April, but CannTrust is facing some unique challenges that are keeping investors away from the stock.

The company ran into trouble with Heath Canada in early July after the government agency determined that CannTrust had grown pot plants in unlicensed rooms. This led to CannTrust halting all sales of its product while Health Canada continued its investigation. A follow-up report indicated Health Canada had uncovered non-compliant activities at a second facility.

CannTrust fired its CEO at the end of July. In addition, the chairman — who is also the CannTrust founder — left the company after the report was released.

The Ontario Cannabis Store, the Ontario Government's marijuana retail operation, has sent back $2.9 million worth of cannabis products. Health Canada has put 5,200 kilograms of CannTrust production connected to the unlicensed facilities on hold and the company has voluntarily set aside another 7,500 kg.

CannTrust is still waiting for a Health Canada decision on how to deal with the situation. If it simply applies a fine of up to $1 million, CannTrust could see its stock soar on what would likely be perceived by investors as a slap on the wrist.

In the event Health Canada forces the unlicensed product to be destroyed, CannTrust says it would take a material financial hit.

However, Health Canada could also suspend or revoke the company’s federal licences, which would potentially be the end of CannTrust.

The longer the ordeal drags on, the worse things will be and the more likely it is that CannTrust will be unable to recover. Pundits are already speculating that the stock could be removed from the **S&P/TSX Composite Index** due to its plunge in market value.

A buyer could emerge for the assets, but it’s unlikely a sale of the entire company will occur, at least until the liabilities are fully known.

Canopy Growth

Canopy Growth trades at $32 per share at writing, compared to its closing high of roughly $70 in late April.

Canopy Growth fired its founder, chairman, and co-CEO Bruce Linton, in July. You might ask how that would be possible, but it was linked to a major investment in the company the previous August.

Last year, **Constellation Brands**, a beer, wine and spirits giant based in the United States, spent $5 billion to boost its stake in Canopy Growth to 38%. Constellation Brands changed its CEO after the deal was done, and rumours suggest the new boss was not happy with the size of the losses Canopy Growth continues to rack up as it rapidly expands in an effort to become the global leader in the emerging cannabis industry.

The departure of Linton, the former face of the company and arguably a core part of the firm’s brand, might be the reason that investors have decided to take a step back and wait to see what direction Canopy Growth will now take regarding expansion and market focus.

Constellation Brands paid more than $48 per share for the stock last year, so the investment is currently under water.

Canopy Growth reported lower quarter-over-quarter revenue in the most recent earnings filing, and the buzz might be coming off the whole sector as investors start to cut back growth expectations.

Is one attractive today?

At this point, I would avoid CannTrust. The risks are simply too high right now.

Regarding Canopy Growth, the stock is more attractive at the current price than it was a few months ago, and a rebound could quickly take it back above $50, as we have witnessed a couple of times in the past 18 months.

As such, long-term cannabis bulls might want to start nibbling, but I would keep any position small until the sector is clearly back in rally mode.

There is a chance we could see another extensive leg to the downside before bargain hunters come in and put a floor under the stock.

Other options exist, however. The Canadian government is about to open the cannabis edibles and drinks market, which could provide an opportunity for investors through some companies that are not producers but will play a key role in the expansion of the sector.

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