



Hexo Corp's (TSX:HEXO) Weak Outlook Drags Cannabis Stocks Lower

Description

Shares of **Hexo Corp.** ([TSX:HEXO](#))(NYSE:HEXO) were hit badly yesterday. The stock fell 23% on October 10, 2019, to close trading at \$3.77. Hexo announced its preliminary fourth-quarter of 2019 (ended in July) results yesterday which were below estimates. The company also withdrew its financial outlook for fiscal 2020.

This not only crushed Hexo stock, but impacted the entire cannabis sector. **The Green Organic Dutchman** fell over 20%, while **OrganiGram Holdings** fell 13.7%. Other top pot stocks such as **Aphria**, **Canopy Growth**, and **Aurora Cannabis** also lost 14.1%, 10.3% and 8.8% in market value in a single day. The **Horizons Marijuana Life Sciences Index** fell over 7% as well.

Hexo estimated Q4 revenue between \$14.5 million and \$16.5 million

In the July quarter, Hexo expects revenue between \$14.5 million and \$16.5 million. This will mean it estimated sales between \$46.5 million and \$48.5 million in fiscal 2019. The preliminary results were way below analyst estimates. Analysts [expected Hexo to post revenue](#) of \$25.28 million in the July quarter while sales for 2019 were estimated at \$59.08 million.

Hexo Corp's CEO Sebastien St-Louis attributed the revised forecast to lower than expected product sell-through. He stated:

While we are disappointed with these results, we are making significant changes to our sales and operations strategy to drive future results. Over the past quarter, we began re-configuring our operations to focus on high-selling strains and initiated a new sales strategy that we believe will meaningfully improve performance. We plan to discuss these in more detail on our upcoming earnings call.

Hexo stated that the cannabis industry is impacted by slower roll-outs, pricing pressure, and a delay in government approval for cannabis derivative products. There is also uncertainty over the type of

derivative cannabis products that are regularized which has resulted in Hexo withdrawing its outlook for fiscal 2020.

Hexo had earlier estimated sales to reach \$400 million in 2020, while analysts expected sales of \$316.8 million. Both these estimates seem way beyond reach looking at the company's revised forecast for the July quarter.

Hexo is now looking to focus on profitability and increase operational efficiencies. It aims to leverage expertise to grow low-cost, innovative, and quality-oriented cannabis products.

Hexo stock is now trading 66% below its 52-week high

The significant pullback witnessed by Hexo investors has meant the stock is now trading 66% below its 52-week high. Hexo shares are down 55.5% since October 2018 and have declined over 40% in 2019.

Prior to Hexo's revised guidance, analysts had a 12-month average target price of \$10. Investors can expect this price to be revised significantly lower driven by the company's tepid outlook.

Hexo stock was trading lower in the last week as well after the company's then chief financial officer, Michael Monahan, announced his resignation on October 4. Monahan had released a statement saying that the CFO profile requires him to be largely available at Gatineau and Ottawa which is currently not possible due to family reasons.

What next for Hexo investors?

The cannabis stocks have witnessed a bloodbath in the last year. While high stock valuations were a key reason for the sell-off after the legalization of recreational cannabis in Canada, investors and analysts were still optimistic about high growth in this segment.

However, these estimates need to be revised and re-assessed after leading cannabis producer Aurora Cannabis too reported sales below its own forecasts last month. Is there enough demand to sustain the high valuations or are companies going to be hit by rising inventory levels that will further impact profit margins?

Several cannabis stocks are still reporting losses but investors were banking on the growth potential in marijuana to drive profitability over time. The uncertainty in this sector continues to haunt investors by significantly driving down their portfolio value.

CATEGORY

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Date

2025/08/25

Date Created

2019/10/11

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