Is Canopy Growth (TSX:WEED) Stock a Contrarian Buy at $20?

Description

The downward spiral in the share price of **Canopy Growth** (TSX:WEED)(NYSE:CGC) and other pot stocks continues.

What's going on?

Canada's largest marijuana company just reported disappointing results for its most recent quarter ended September 30, 2019. Canopy Growth lost $374 million for the quarter, representing a 13% increase in losses compared to the same period last year. Management says the hit is mainly due to rising operating costs.

Cannabis producers have increasingly warned of weaker-than-expected for the current quarter and into and 2020 due to a lack of retail outlets in Ontario and Quebec. In fact, there is growing concern that the marijuana industry has switched from a shortage of product that hit the sector a year ago to an oversupply.

Canopy Growth booked a $32.7 million charge on returned products and a $15.9 million write-down on inventory in the latest results. The problem appears to be connected to weak demand and lower sales of oil and softgel products in the recreational market.

CEO Mark Zekulin specifically targeted Ontario as a major pain point. The province is dragging its heels on allowing an increase to the number of physical stores that can sell recreational cannabis products.

Net revenue from the quarter came in at $76.6 million, down from $90.5 million in the previous three months.

Investors had hoped the company would get spending under control after the board fired Bruce Linton, the former founder, chairman, and CEO this summer. Canopy Growth's largest shareholder, **Constellation Brands**, recently put its CFO into the chairman role.

Constellation Brands invested $5 billion in August 2018 to boost its ownership to 38%. The investment was done at a share price of $48.60.

At the time of writing, Canopy Growth's stock price is down to $20.20 per share. That's a 17% decline on the day and well below the high near $70 the stock hit in April.

Upside potential

Cannabis bulls say the total Canadian medical and recreational market is more than $5 billion, and the opening of hundreds of new retail locations in Ontario and Quebec in the next two years should boost sales of legal pot products.

In addition, Canopy Growth is positioned well to benefit from rising demand for medical marijuana in Europe and South America, where it has established production and distribution operations.

The wildcard remains the United States. Selling cannabis products is currently illegal at the federal level, but many states have allowed the sale and consumption of the products. Canopy Growth has an agreement in place to acquire **Acreage Holdings** in the event marijuana is legalized federally south of the border.

Acreage has production and distribution operations in at least 20 states.

Should you buy Canopy Growth today?

The company now has a market capitalization of $7 billion, which still appears expensive based on annualized revenue of less than $400 million and no clear path to profitability.

Contrarian investors might want to start nibbling on the hopes of a near-term bounce, but I would keep any new position small right now. There is a risk we could see further downside across the sector before the dust clears and bargain hunters put a new floor under the stock.

Other oversold stocks in the TSX Index might be better options to consider today.

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