Are Cannabis Revenues Leveling Off?

Description

Cannabis stocks are popular among many TSX investors in Canada, and for a good reason. High revenue growth is a crucial driver for strong price performance on the stock exchange. Because the marijuana industry is new, cannabis companies should experience increasing revenue growth post-legalization.

This week's earnings didn't turn out quite as well as shareholders would have hoped. Instead of continued surges in revenue, cannabis stocks, including **Neptune Wellness** (TSX:NEPT) and **Canopy Growth** (TSX:WEED)(NYSE:CGC), reported declines in revenue, which sent the stock prices lower. What happened?

Canopy Growth accredited lower-than-projected new store growth and already high province inventory levels for the lower revenue. Meanwhile, Neptune Wellness — a cannabis company more focused on health products — cited order timing as the primary driver for the lower income.

Canopy Growth

Canopy Growth's net revenue came in lower than expected at $76.6 million — a 15% decrease from the previous quarter's revenue of $90.5 million.

"The last two quarters have been challenging for the Canadian cannabis sector as provinces have reduced purchases to lower inventory levels, retail store openings have fallen short of expectations, and Cannabis 2.0 products are yet to come to market," said Mark Zekulin, the CEO of Canopy Growth.

Provinces purchase marijuana from Canopy Growth, but they began accruing high inventory levels. In response, the regions purchased less new inventory. Once many of the new stores open, the provinces will build up stocks once again, and revenue will rise.

However, international medical cannabis revenues soared last quarter by 72% to $18.1 million from 10.5 million. The company is expanding quickly overseas, and that should offset seasonal fluctuations in the North American market.

Neptune Wellness

Neptune Wellness reported a year-over-year decrease in revenue on Monday for the quarter ended September 30, 2019. Net revenue was 8% lower at $6.52 million compared to $7.1 million for the same quarter last year, right after the first wave of marijuana legalization.

The company credits the timing in the orders for the decrease in revenue. Order timing can affect orders between quarters, which is why six-month and yearly averages can be more helpful when assessing changes in demand for a specific brand.

Neptune Wellness is different from other marijuana corporations in that it sells hemp-derived nutrition products. The marijuana industry has taken a few hits recently, beginning with lung injuries from THC vaping products. Neptune has been largely shielded from this tragedy because it markets ingestible chewables, soft gels, roll-ons, sprays, and oils.

Foolish takeaway

It may be counter-intuitive to think that marijuana is a seasonal industry, but it is an agricultural product. Planting cycles create harvest seasons where supply will start booming — and that is when the retailers will make significant purchases.

Canadian investors will want to take note of the rise and fall in inventory orders to make counter-cyclical purchases in stock. When the stock price falls along with revenue, it would be a good idea to pick up new positions.

Timing the market is difficult and not recommended, but on seasonal stocks, find dependable companies that you don’t mind owning for the next 30 years and buy when the shares are low to make the most out of your retirement savings.

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