Prediction: Canada's Cannabis Market Will Recover in 2020

Description

2019 was a rocky ride for marijuana investors, the first real losing year since the sector rose to prominence.

A number of different factors hit the industry hard. Retail struggles dominated the story during the first half of the year, with the leading pot suppliers unable to keep up to demand.

Then, the narrative changed. Suddenly, everyone focused on oversupply issues, with analysts predicting we'll soon be awash in more legal marijuana than we know what to do with. Various pot producers missed on growth expectations. And investors woke up to some major issues, like realizing that despite all the fancy branding, marijuana is still a commodity product.

The declines were staggering. From its peak of over $70 per share in May 2019, **Canopy Growth** (TSX:WEED)(NYSE:CGC) has lost some 60% of its market value, with shares currently flirting with $25 each. Remember, Canopy is considered the safest and best in the sector, meaning many of its competitors did even worse.

After such dismal results, it's understandable investors might be bearish on the sector. I know I sure was. But I've since softened my stance. Here's why I think the sector could see a recovery in 2020.

Sentiment change

When it comes down to valuing an industry without any earnings, it all comes down to sentiment. But unless you're a momentum trader, the key is to do the opposite of what every other investor is doing. Taking this contrarian approach is a key step to successful investing, especially in something like the marijuana sector.

Everyone is so bearish on pot stocks that just a few pieces of good news can really move the sector.

Recent trading

In fact, I think the sentiment around marijuana isn't as bearish as you might think. It may have already turned the corner.

Just look at Canopy Growth's stock chart if you want proof. It bottomed out in the $25-per-share range back in November and has been forming a base ever since. It looks to me like the bad news floating around the sector has already been priced in and isn't getting any worse. That's good news for investors looking for a breakout in the other direction.

I'm no short-term investor, but that doesn't mean we can't use some simple trading strategies to help our long-term investments. Shares making a base is a good beginning step. If the stock breaks out, then that's likely a good time to start buying.

The best way to invest in pot

Marijuana is still a speculative industry, so you'll want to limit your investment dollars to the best names in the sector. And despite some of its struggles — including disappointing results and the ousting of former CEO Bruce Linton — Canopy Growth is still the class of the sector.

Canopy's balance sheet is in good shape, with nearly $3 billion in cash and short-term instruments and a very manageable debt level. Investors don't have to worry about it running out of money anytime soon.

The company also has significant international operations, with assets in 12 different countries spread over five separate continents. These markets aren't suffering from the same issues plaguing Canada and represent nice upside potential if these nations ever take the next step and fully legalize marijuana.

And remember, cannabis edibles were quietly legalized last month, with hardly any fanfare. This new source of demand could really help with some of the excess supply in the system. As the largest producer, Canopy is well positioned to be a supplier of choice to these manufacturers.

Finally, there's potential in the U.S. market. If a Democratic nominee wins the presidential election later this year, it'll pave the way for marijuana to become legal in the United States. That's a huge opportunity for Canopy and would certainly represent a big change in sentiment.

The bottom line

2020 could be a good year for Canada's leading marijuana stocks. The market is simply too bearish today; just a few things need to go right for investors to have a nice year.

But be warned. It's doubtful dreams of 500% or 1,000% returns will be realized. There's still good upside potential, but it'll be a little more limited than the stellar results posted from 2015 to 2018.

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