Contraction Is the New Trend for Cannabis Stocks

Description

A year ago, many investors in Canada's cannabis industry were boasting of their incredible returns. Investors were doubling or tripling their money in a short amount of time on any company that planted a cannabis plant with a licence from Health Canada.

Since a year ago, most of these same companies have been halved three times over. The broader **Horizons Marijuana Life Sciences ETF** (TSX:HMMJ) has dropped nearly 70% from its peak.

The incredible hysteria around growth in this sector has now been replaced with some semblance of sanity. Various cannabis producers have announced significant layoffs, greenhouse/production facility closures, and significant writedowns on assets. Also, they have slashed forward-looking revenue and profit expectations.

Therefore, these announcements come as revenue growth has stagnated. The market is beginning to understand how ridiculous the implied growth projections of Canadian pot players were.

Canopy Growth

Companies like **Canopy Growth** (TSX:WEED)(NYSE:CGC) have felt significant pressure to show profitability. They have largely shifted gears from a "growth-at-any-cost" mandate toward a "get-profitable-quickly" strategic focus.

Canopy remains the largest publicly traded cannabis producer in Canada by market capitalization. However, Canopy recently announced production facility closures, including two greenhouses in Ontario totalling roughly three million square feet. This makes Canopy the third-largest company in terms of production capacity. Canopy now falls behind **Aurora Cannabis** and **Aphria**.

Canopy had a much slower growth rate in recreational cannabis than initially expected pre-legalization. This is something anyone who read my commentary from 2017/2018 would have anticipated. Canopy cited the slower growth rate, which lead to a significant supply glut, as the reason for shuttering production for now.

The cannabis being produced at these two Ontario facilities was slated for "Cannabis 2.0" products. These include infused beverages and chocolates. This indicates that the entire Cannabis 2.0 rollout may indeed fall flat, as I predicted in a recent piece.

The speed at which companies like Canopy Growth have had to "grow up" and shift from being "edgy startups" to real companies capable of generating real profits and shareholder value has accelerated of late.

Both cofounders of Canopy Growth were fired last year, including CEO Bruce Linton. Mr. Linton was replaced with David Klein, the former CFO of **Constellation Brands**, which owns a massive chunk of Canopy. Mr. Klein's new role in Canopy Growth has perhaps been the key for this corporate transformation.

Bottom line

I would advise investors to steer clear of Canopy, and all other cannabis producers, for that matter, right now. I believe the pain has only just begun.

Stay Foolish, my friends.

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2. Cannabis
3. Canopy Growth

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