Why Canopy Growth Stock May Be in for Some Downside Pressure From Here

Description

Despite an incredible start to the year, **Canopy Growth** (TSX:WEED)(NYSE:CGC) has waned in recent months. Shares of this Canadian cannabis juggernaut have fallen nearly 60% from their peak earlier this year. Indeed, the entire cannabis sector, particularly in Canada, has felt this pain.

Unfortunately, more pain may be on the horizon for these stocks. And Canopy's current position as a dominant Canadian cannabis player puts this stock more in the limelight than its peers. Here's why I'm more bearish on this stock than I have been in some time.

Fourth-quarter earnings did not meet expectations

As with any publicly traded company, earnings matter. While one could argue that earnings have taken a back seat for cannabis companies in recent years, investors are largely assessing these equities on the basis of how profitably they're growing in addition to how fast they're growing.

For investors in Canopy, the numbers simply don't look great.

The company reported lower-than-anticipated earnings this most recent quarter. Both revenue and EBITDA failed to meet analyst expectations. In fact, the company's EBITDA loss of $94 million was the highlight many investors seem to have jumped on. Despite a series of cost-cutting measures, Canopy hasn't been able to stem the bleeding thus far. There's a lot of work to be done to get this company to operate with a positive operating margin. Accordingly, many fundamental investors remain on the sidelines with this stock.

Now, Canopy has announced a cost-cutting plan of reducing $150 million of expenses by fiscal 2022. That's good. And the company's recent acquisitions of **Supreme** and **Ace Valley** could provide some EBITDA growth (positive). That would be good as well.

However, analysts remain fuzzy on how to quantify or project positive EBITDA for Canopy from here. Some suggest the company needs to drastically reduce costs or cut out its M&A activity. After all, Canopy is burning through cash at a rate of approximately $400 million in 2022 and $125 million in

2023. This cash will need to come from somewhere, leading many to believe more debt and/or another equity issuance could be on the horizon for investors.

Such moves may be difficult for investors to stomach over the short term. Accordingly, it’s hard to be bullish on this stock over the next 12 months, in my view.

Bottom line

Besides these rather disappointing fundamentals, the U.S. legalization catalyst many investors were banking on appears to be less of a sure thing than it once was. There happens to be no shortage of negative catalysts for cannabis players like Canopy right now.

Accordingly, this is a stock many investors may do well to stay on the sidelines with. There’s simply too much near-term uncertainty with this stock to warrant an investment today, in my view.

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