Will Canopy Growth Corp. Crash as Hard as Valeant Pharmaceuticals Intl Inc.?

Description

Canopy Growth Corp. (TSX:CGC) has been taking a beating lately! The stock has pulled back about 39% from its high just a week ago. Investors who'd jumped on the ship late got hurt really bad, and the stakes still remain as high as ever, even at current levels.

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The stock is risky, and if you're a momentum trader, then you've probably had Canopy on your radar. If you're a contrarian, then you're probably sitting back and waiting for a huge pullback to jump into the stock. Good move. The stock is falling hard, and you may have an opportunity to pick up shares of this promising company at a much better price.

Why is the stock crashing this hard, this fast?

As I've mentioned in a previously, the business is great and has very promising growth potential, but the stock is a speculative trader's playground. There simply is no long-term investing with Canopy at current levels, as the stock has soared way too high in a short period of time. This kind of short-term action has attracted every short-term trader and will cause volatility that is only seen in penny stocks.

With the massive amount of speculative traders holding Canopy, all it takes is one piece of bad news to send the dominoes falling. All of the good news and tailwinds are already baked into the stock. A violent correction would happen should there be any negative news released in the press.

A piece of bad news was released, and it could cause shares of Canopy, as well as any other marijuana stock, to lower levels over the next few weeks.

What kind of bad news could send marijuana stocks tumbling?

News was released that the federal government could be putting a limit on the volume of medical marijuana that veterans can be reimbursed for. It's not clear how much this news will affect Canopy or any other marijuana company's long-term growth potential. But what doesn't make sense is the pullback of 39% in just a week; there's no way that this news would cause such a correction in the stock.

As we've learned in the case of Andrew Left's short analysis of **Valeant Pharmaceuticals Intl Inc**. (TSX:VRX)(NYSE:VRX), it just takes is one piece of bad news to end the party. All traders and short-term thinkers will jump ship. However, unlike the case of Valeant, I do not believe Canopy will receive an endless series of short attacks, scandal investigations, and a swarm of bearish pieces in the months following the first piece of bad news. Canopy is not Valeant; in fact, I believe Canopy is a great company, but it's a stock plagued by unheard-of volatility.

Canopy will not face the same fate as Valeant in terms of it having its stock lose over 93% of its value, but it could still fall a lot farther from here. It's never a good strategy to catch a falling knife, so if you're going to buy Canopy, at least wait until the volatility subsides as bad news usually comes in bunches.

I'm not going to tell you that there's a fundamental reason why you should own Canopy for the long term right now, because it's a speculative bet, but with huge risk comes huge reward, as we've seen by the massive returns that the stock has given its investors over the past few months.

If you're a long-term investor looking for a core holding, then Canopy is not for you. This company is only for the young investor who can afford to take risks. The stock is ridiculously overvalued, even after the 39% crash. However, it doesn't make much sense to use traditional valuation metrics with such a small-cap growth name anyways, but be warned, you could lose your shirt if you don't play Canopy right.

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