



3 Reasons to Think Twice About New Cannabis ETF

Description

How do you know when you might be in a market bubble?

Well, for starters, you start hearing from 24-year-olds about how much money they're making off one of this country's hottest stocks: **Canopy Growth Corp.** ([TSX:WEED](#)) — a company with a \$2 billion market cap despite just \$30 million in revenue over the past 12 months.

Hey, before you send out a lynch mob, I'm a [big believer](#) in the cannabis industry and see a huge future for Canopy and all the other players currently growing medical marijuana in this country.

That said, the proposed Emerging AgroSphere ETF from ETF Managers Group LLC (ETFMG) in the U.S. is merely an ETF provider trying to capitalize on a popular investment trend.

Consider that ETFMG closed the Restaurant ETF before Christmas after just 14 months. Gathering US\$1.4 million in assets over a little more than a year, the ETF with the catchy stock symbol couldn't cut it with investors.

In October, ETFMG came out with another niche ETF called the **Spirited Funds/ETFMG Whiskey and Spirits ETF** — a great idea in theory, because who doesn't like the idea of investing in some of the world's biggest whiskey producers? — but it's got a tough road ahead of it, just like its deceased ETF stablemate.

So, before you invest in this ETF, which is still going through the SEC approval process, here are three reasons you might want to think twice.

Won't consider recreational cannabis market

The ETF will track the Emerging AgroSphere Index: a group of 69 companies which do three things, according to Alan Brochstein of New Cannabis Ventures:

1. Engage in lawful medical research intended to lead to the production of government-approved prescription drugs which use natural or synthetic versions of the cannabidiol CBD and other cannabis-

based extracts;

2. Are involved in the production or sale of products which are legal derivatives of industrial hemp; and
3. Are involved in the supply chain of either category of company.

Only if the recreational use of marijuana becomes legal in the U.S. or Canada will the index be able to stray from its focused investment strategy.

Canada expects to legalize the recreational market sometime in 2018 or 2019; who knows about the Federal Government in the U.S.? Maybe never.

Canopy Growth weighting

Canopy Growth is the largest cannabis producer anywhere in the world. Yet if you look at the index's holdings, you will see that 14 of the 69 holdings have at least one share held by the index, including **Aurora Cannabis Inc.** (TSXV:ACB), one of Canopy's biggest rivals.

I've yet to figure out Canopy Growth's actual weighting, but the list of constituents suggests it would be no more than 1-2% at the most and rebalanced quarterly.

Investors on this side of the border are not going to be happy about the home-grown Canadian content with the majority of holdings U.S.-listed companies with smaller market caps or a few big businesses, such as **Abbot Laboratories**.

Canopy Growth should be a bigger piece of the pie.

ETFs getting bigger

There's no question that investors will be very interested in this new ETF. However, there's a big difference between buyers and tire kickers.

The fact is, successful ETFs are getting bigger, not smaller.

Down in the U.S., the top 10 ETFs in 2016 took in US\$87.1 billion in net flows through December 6 — 39% of the overall total; much of the funds were directed to S&P 500 ETFs.

You can be sure that the same domination applies here in Canada to S&P/TSX ETFs, whether that's based on the broader S&P/TSX Composite or the S&P/TSX 60.

Bottom line

The best use of this ETF might be as a hedge against any drop in Canopy Growth's stock price or one of the other big Canadian marijuana stocks.

You could go long WEED and short or buy put options on the ETF, hoping to reduce your paper losses on Canopy Growth should it fall in price.

If you're a long-term investor I'd forget about any insurance and just hang tight through the ups and downs over the next two to three years, buying a little whenever it drops below \$10.

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2. TSX:WEED (Canopy Growth)

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