

3 Things You Should Know Before Buying a Marijuana Stock

Description

If there's one high-flying sector that's sure to be a fan favourite in the Canadian markets these days, it would have to be the newly minted marijuana industry. With marijuana expected to become legal in Canada by July 1, 2018, many investors are chomping at the bit to get a piece of the action. But with great expectations for rewards also come great risks.

The first thing any prospective investor in the marijuana industry should try to understand is what expectations are already being priced in by the market. A recent report from Deloitte estimated that sales from recreational and medicinal marijuana would reach \$5 billion annually by 2018.

While this figure is considerably higher than the \$869 million of marijuana sales registered legally in 2016, it's important to keep in mind that the combined market capitalization of Canada's three biggest marijuana producers, **Canopy Growth Corp.** ([TSX:WEED](#)), **Aphria Inc.** (TSX:APH), and **Aurora Cannabis Inc.** (TSXV:ACB), comes in at a staggering \$3.1 billion today, meaning that much of the anticipated growth is likely already reflected in these companies' current valuations.

While appropriately discounting market expectations can be a difficult task at the best of times, a more straightforward exercise would be to understand the pertinent risks facing a prospective investment in marijuana shares, and there are several that should be considered.

One risk is the fact that even if legalized, marijuana will remain tightly regulated by government bodies such as Health Canada. This means that producers like Canopy Growth, Aphria, and Aurora Cannabis will be restricted as to the prices they can charge for their products.

What's more, there are many questions that remain unanswered as to how the Canadian government will allocate distribution channels and award government licences. Still yet to be determined, pricing, distribution, and regulations will do much to shape the marijuana industry in Canada.

For those who are unfazed by market hype or red tape, there's only last word of advice this author can offer.

Marijuana stocks are not for the faint of heart. Investors in Canopy Growth, for example, enjoyed a 30% gain during the first two weeks of February, only to see those gains all but evaporate over the next five weeks. Investors who bought Aphria shares at the start of November enjoyed gains of 24% over the first two weeks, only to lose 17% of that investment over the following five weeks. Investors considering a purchase should be careful to note the extreme price swings associated with these high-flying pot stocks.

Should you buy?

There are still many uncertainties facing Canada's emerging marijuana industry, but there is also tremendous opportunity for growth with experts expecting the size of the market to quintuple over the next few years as legalization kicks in. While some brave souls may decide to step their foot in the ring,

investors should be cautious of a stampede for the exits should the bubble burst.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:ACB (Aurora Cannabis)
2. TSX:WEED (Canopy Growth)

PARTNER-FEEDS

1. Msn
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