Just How Much Risk Should Investors Take With Marijuana Stocks?

Description

After a tumultuous past year, shares of Canada's marijuana companies have begun to find a trading range, while the selection process among investors has continued to evolve.

Trading near the $3 mark approximately one year ago, shares of **Canopy Growth Corp.** (TSX:WEED) were held mainly by investors with high risk tolerances and the willingness to bear large fluctuations in their investments. As things progressed throughout the year, more investors became aware of the rapidly developing industry. Following the euphoria, the "followers" continued to pile in to the security until the share price had been bid up to a high of $17.86, only to experience a pullback to a current price of approximately $8.

Although volatility is to be expected, investors may still want to take a step back and evaluate who their peers really are. Presently, the shareholder base is still one of the most retail driven (individual investors) on the market. It would seem the credo of "invest in what you enjoy/know" has been practiced by many investors — some who have more investment knowledge than others.

While the fundamentals can be argued late into the night with no clear winner, there is one thing that must be weighed by each investor before taking a position in the security: how much should be bought?

The question of how much does not revolve around a total dollar amount or a total share amount; instead, how much one buys is measured as a function of the entire investment portfolio. While every investors will build their portfolio differently, it is important to keep in mind a few important characteristics of the marijuana industry.

First, as the industry is still very new and developing, investors must be aware that the capacity is still being increased by a number of competitors, while the potential to buy marijuana across the board (without a prescription) is not yet available. Sometimes paying for potential can lead to a bad result as the potential can be overstated.

The second thing to consider is the track record of each company in the industry (or, in this case, the lack of track record). While there is a tremendous amount of potential for the scaling of many companies in the sector, the reality is that without a track record of sustainable and profitable growth it will be difficult for companies such as Canopy Growth Corp. to deliver for shareholders on a consistent basis.

While many investors clearly believe in the possibility of scaling the business and providing positive returns over the long term, it is worth considering how much of one's portfolio should be invested in a stock that is arguably still in the "speculative" category. While the total allocation for certain investors is probably well over 10%, the more popular amount for the majority of investors will be no more than 5%.

When investing in a growth stock, we must never put in more than we are willing to lose.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:WEED (Canopy Growth)

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