Marijuana Stocks: What Could Push Canopy Growth Corp. Stock to $40?

Description

Canopy Growth Corp. (TSX:WEED) stock has been trading in a range for the past month, and investors, who were witnessing explosive gains in marijuana shares, are now wondering what might take this top marijuana stock to the next level.

Though Canopy Growth stock is down ~10% this year, it's still up more than 140% during the past year — a performance that's hard to match by other growth stocks.

Going forward, it appears that investors are not exactly keen to speculate on marijuana stocks, especially when the deadline for the legalization of recreational pot is fast approaching. The price action in the marijuana space suggests that stocks of Canada's largest pot producers have lost their momentum of the past year.

I believe that investors who are still hoping to make massive gains by speculating on marijuana stocks are a little late to the pot party. With valuations soaring, it's tough for rational investors to put their money on this trade.

Lofty valuations

The average price-to-book ratio of Canopy, for example is 5.2, or about three times the **S&P/Toronto Stock Exchange Composite Index'** P/B ratio of 1.8. Its price-to-sales ratio is 83, a staggering 49 times the Index' P/S ratio of 1.7.

With these lofty valuations, marijuana companies must be extremely smart in order to execute their sales strategies once the recreational market is ready. Canopy Growth, however, is well positioned to benefit from a potential surge in demand. Canopy's latest earnings report showed that the company already has a great deal of momentum.

Ontario-based Smiths Falls said its revenue rose to $21.7 million for the quarter ended December 31 — more than double the $9.8 million earned in the last three months of 2016.

The company also reported a 138% jump in its active registered patients to 69,000, up from 29,000 a year ago. The growth came as Canopy's profits attributable to the company narrowed to $1.6 million, or one cent per diluted share, up from nearly $3 million, or two cents per diluted share, a year ago.

The bottom line

In 2017, investors' psychology last drove a remarkable rally in pot stocks, which tells us that investors usually overreact in both positive and negative situations.

As I've discussed in my earlier articles, all the good news has already been priced into marijuana stocks, and it would therefore be unrealistic to expect a similar performance this year. As the market focus shifts to the execution, it's better for investors to wait on the sidelines.

For long-term investors, however, Canopy Growth stock could prove to be a good investment if we don't see too much competition from new entrants. Trading at $28.99 at the time of writing, Canopy stock is still expensive. I would therefore wait for a more attractive level before taking any position.

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