



3 Reasons the Party is Over for Canadian Cannabis Stocks

Description

The **Horizons Marijuana Life Sciences Index ETF** ([TSX:HMMJ](#)), which tracks many of the top Canadian cannabis producers, has plunged 17.5% month over month as of close on April 4. The ETF is down 19.3% in 2018 thus far. The broader cannabis market has faced major turmoil since the initial global stock market rout hit in early February. There are a number of factors contributing to this precipitous decline.

Market overvaluation comes home to roost

Experts and analysts have long been sounding the alarm with regard to overvaluation in the cannabis market. Enthusiasm peaked in the final months of 2017 and in the first month of 2018 as the top producer raced to consolidate.

Aphria Inc. (TSX:APH) found itself embroiled in controversy over its \$425 million acquisition of Nuuvera Inc. On March 22, Hindenburg Research, a U.S.-based account known for its connection to short-sellers, called its aggressive strategy into question, as Nuuvera had “almost no revenue.” It also drew attention to potential conflicts that have now [plagued Aphria](#). Shares of Aphria have plunged 28% since that report was published.

Beyond these isolated cases, the market has come under fire for company valuations soaring beyond \$5 billion despite comparably low revenue. **MedReleaf Corp.** (TSX:LEAF) reached an all-time high of \$31.25 in early January, but has since plummeted to \$15.74 as of close on April 4.

Anxiety over the execution of recreational legalization in Canada

In February, it was revealed that recreational cannabis legalization would [fail to meet the July 2018 deadline](#) originally set by the federal government. Although this didn't spook the market at the time, there are concerns that public officials may move more aggressively to stifle the industry.

There is a belief that the early shortage of legal weed will drive sales in the black market. Some have suggested that the government should curb supply and restrict advertising to start. More recent research has called this strategy into question and instead lobbied to keep supply high and prices low.

Consumer advocates and others have also criticized the decision from some provinces to turn to the government for distribution and sales.

To add to the concern, data released from Statistics Canada early this year indicated that the potential market may not be as large as optimists had hoped. Canadians reportedly spent \$5.7 billion in cannabis in 2017. **Canopy Growth Corp.** CEO Bruce Linton projected that the number will be closer to \$10 billion once the market truly gets underway. However, moves to curb advertising and growth could frustrate investors in the early phases.

Spillover from a broader economic issues

The **S&P/TSX Index** has plunged 6.4% in 2018 as of close on April 4, and U.S. and global indexes have also fared poorly as shifting monetary policy and rising trade tensions have rattled markets. The frothy cryptocurrency and cannabis markets have been the first victims of what could turn out to be a steeper correction as we move ahead to the spring and summer.

CATEGORY

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