



Reality Bites As Canadian Pot Stocks Plummet

Description

Aurora Cannabis Inc. ([TSX:ACB](#)) has plummeted 35% year-to-date, while **Canopy Growth Corp.** ([TSX:WEED](#)) has plummeted 22% year-to-date and 37% from its January highs.

In my view, this was to be expected, as [pot stocks](#) were and are reminiscent of the early 2000s internet or the [dot-com bubble](#).

As the internet expanded, excitement grew, and the optimism in the market knew no bounds. More and more analysts were projecting bold and optimistic growth numbers, and stocks skyrocketed accordingly. Some investors made a great deal of money, while others lost a great deal of money.

It seemed that new internet companies surfaced every other day, with their stocks trading at double-digit multiples of sales.

Until they didn't. And in 2000, everything came crashing down.

The NASDAQ fell from a high of over \$5,000 in March of 2000 to lows of just over \$1,200 in July of 2002. That's a two-year decline of 76%.

Does any of that sound familiar?

The very nature of a bubble is that stocks are trading on hype, excitement, and hope rather than fundamentals. When this happens, the risk/reward profile of a stock becomes skewed.

That is, the risk inherent in the investment far outweighs the potential reward because the stock is reflecting unrealistic and wildly optimistic scenarios.

Unwinding the hype

I believe the pot bubble is bursting. Is it being triggered by trade wars, the crashing real estate market, or the general sense of unease in the market due to rising debt levels and declining risk tolerance? It doesn't really matter *what* the trigger is, only that it's happening. This can be viewed as an exciting

thing, because as valuations become more realistic, we can focus on the real business of investing.

In summary, I'm in agreement with the excitement surrounding the marijuana industry. I'm just not a fan of the valuations and buying into hype, and with Canopy trading at 90 times sales and Aurora trading at 142 times sales, there is clearly still a lot of hype.

As investors, it's a good idea to take a longer-term view of things and, when we witness these situations, to be confident enough to stay on the sidelines and wait for reason to return.

All with the goal of making sure we buy low and sell high — and not the opposite.

So let's wait for the stocks to trade on fundamentals rather than hope and wildly optimistic expectations. In other words, we should wait until these stocks represent a good investment thesis rather than a gamble.

As we've witnessed so far in 2018, those investors who bought the stocks recently are having a hard time watching their investments tank.

CATEGORY

1. Investing

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

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Author

karenjennifer

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