An In-Depth Reading for HEXO (TSX:HEXO) Stock Indicates a Strong Sell Signal

Description

Watching pot stocks fizzle last week was both unsurprising and disappointing. While I have been bearish on the green stuff since the get go, seeing so many excited investors watch the polish come off their shining growth stocks on the day of legalization was a little disheartening.

One of the things that has made the beginning of the industry's boom turn to bust so saddening has been the misselling of these stocks to hopeful investors who could not – and do not – grasp the complexities behind legalization, nor the difficulties faced in rolling out legal marijuana as a product.

I'm not going to go back over these issues, though I mention them here; suffice is to say, the bust is happening. Let's take a popular pot stock to illustrate what this looks like in terms of data.

HEXO (TSX:HEXO)

With a market cap of $1 billion, HEXO looks like a proper stock. It has a ticker, it trades on the TSX, it has a share price that rises and falls. Other pieces of data confirm that this is, indeed, a stock that can be invested in: bought, cherished, or sold. But if you run it through a stock screening tool, such as the one below – which has been tested successfully on different types of stocks to ascertain buy or hold signals – it doesn't come out the other end in one piece.

I use a three factor system, the first factor of which is value. A negative P/E combines unfavourably with a P/B of 4.1 times book, (which, while high for the TSX index, actually signifies good value for the Canadian pharmaceuticals industry). HEXO pays no dividends as yet, leaving it with a value scoring of 4 /33.

HEXO is poor value, low quality, and highly volatile

A negative past-year ROE and disappointing EPS make for a mixed quality reading – the second factor – when combined with a massive 143.1% expected annual growth in earnings, (which will be great for shareholders should it actually materialize, but it's unlikely).

The latter ought to even out this portion of our in-depth reading, though post-legalization profitability doubts cast a palpable shadow here; overall, HEXO gets 8/33 for quality.

HEXO is showing very high downward momentum at the moment, the third factor in my screening system, which should come as no surprise to those who were bearish on the so-called pot-com boom. To put a figure on it, HEXO shed 20.97% in the last five days. Its beta of 2.65 indicates high volatility, but that's going to fall as investors start to lose interest in the fizzled green gold rush.

Further, its share price is overvalued by 5.5 times its future cash flow value. This gives a momentum score of 20/33, and a total of 32%, indicating a strong sell signal.

The bottom line

A negative PEG ratio isn't much of a surprise, after everything, but next time you see one, look for verifiable growth. If you want to keep this stock, weigh the following: HEXO is a debt-free company, which adds to the overall quality of this stock, though it has seen more inside selling than inside buying over the last 12 months. Personally, I think this stock is worth selling – the sooner the better.

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