Are Pot Stocks Getting Cheaper?

Description

Cannabis investors have been paying some big premiums in recent years to own stocks that offered little in the way of earnings and just relied on promises of future growth. However, now that we've seen marijuana companies start to report some strong sales numbers, those valuations might not be as astronomical as they once were. Let's take a look at some of the bigger names in the industry to see if that's really the case today.

Aurora Cannabis (TSX:ACB)(NYSE:ACB) had sales grow to $54 million in its most recent quarter, which was more than four times the revenue it had a year ago. That put its sales for the trailing 12 months at $119 million. With a market cap of $12 billion, that puts the stock at a price-to-sales (P/S) ratio of around 100.

Back in June of last year, I had noted that Aurora was trading well over a P/S of 100 and that was only because it had been declining at that point. In Aurora's case, its valuation has certainly come down, despite the fact that its share price has risen 45% since then. Rising sales have contributed to the lower P/S ratio, and that's a trend that's likely to continue as we see companies report post-legalization sales that are sure to send their top lines soaring.

In its most recent earnings, Aurora still didn't include a full three months of recreational sales, so in its next earnings release we'll likely see an even stronger revenue number. While it's still an expensive stock, we can definitely see that its valuation has improved since last year.

Cronos Group (TSX:CRON)(NASDAQ:CRON) is another expensive pot stock, which was trading at more than 250 times its sales back in December. Since then, its share price has risen by more than 80%, and that's after it has come down in price in the past month. For Cronos, the company's results have not kept up with its rising sharing price.

Over its past four quarters, sales have totalled just $16 million. And with a market cap of $7.5 billion, investors are paying a mammoth 480 times the company's sales. Cronos was an expensive stock back in December and things have only gotten worse since then. While the stock might have some great prospects for growth, investors might be wise to wait until some of that is realized before jumping on board.

Cronos is heavily overvalued even compared to other pot stocks. It would have to see a significant decline in price for it to be comparable to one like Aurora which has much more substance behind its share price.

Bottom line

Pot stocks are still very expensive. And while Aurora may have come down in price in the past year, paying even 10 times sales is still a lot for a stock. However, the good news is that at least in Aurora's case, the multiple is going in the right direction. Although there is some semblance that prices are coming down to reality, you've still got stocks like Cronos that have reached even more obscene levels.

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