



Why Cronos Group (TSX:CRON) Is Still Too Expensive, Even at \$14/Share

Description

The deepening cannabis rout has brought down valuations across the sector, and even lavish names like **Cronos Group** ([TSX:CRON](#))([NASDAQ:CRON](#)) are [beginning to look a lot more attractive](#), now that they're trading at half of where they used to be. However, Cronos's market cap only tells part of the story: even at these levels, Cronos remains a richly valued stock, whose near-term future hinges almost entirely on its CBD ambitions.

Last quarter was largely in line

Cronos delivered no surprises in the second quarter, with total kilos sold climbing to 1,584 up from 1,111 kilos in Q1 of 2019. As far as prices go, Cronos managed to outperform its peers, with average net selling price for dried cannabis climbing to \$6.19/gram from \$5.14/gram in the same period, and average net selling price of oils also rising to \$7.69 from \$7.16/gram.

The increase in kilos sold and realized prices translated to net revenues of \$10.2 million, which works out to a 58% sequential increase. While these numbers are certainly laudable, bear in mind that Cronos trades at 16 times consensus sales. That means that if you buy Cronos, even at these levels, you are paying \$16 for every \$1 of expected revenues that Cronos will make, which is a very lavish price to pay, considering that names like **Canopy Growth** trade at roughly 10 times forward sales.

So, what exactly are you paying for when it comes to Cronos? Quite simply, CBD.

Will CBD be Cronos's key to domination?

In July, Cronos announced that it would be entering the U.S. CBD market in the next six to 12 months. With Wall Street analysts calling for a \$16 billion valuation in 2025 for the CBD space south of the border, it's easy to see why Cronos's has caught the attention of investors.

Moreover, Cronos recently announced intentions to acquire Redwood Holding Group, owner of popular CBD brand Lord Jones, which sells CBD-infused gummies, oils, topical lotions, and bath salts. The

\$300 million acquisition, which will be mostly paid in cash, signals Cronos's dedication towards gaining a U.S. foothold — a fact that is made even more bullish, given that Cronos's has the full backing and scale of **Altria** behind it, through their lucrative partnership arrangement.

But is CBD really worth *that* much?

While last quarter's sales came in above estimates, \$10.2 million is still a fraction of names like Canopy, which delivered nine times that amount, even on a weak quarter. Internationally, we also see competitors like **Aphria** branch out into lucrative European markets, whose growth mirrors that of the U.S. CBD space.

And while the Altria partnership grants Cronos unprecedented scale and branding expertise, I just cannot justify Cronos's extremely premium valuation.

So, despite the recent selloff, I feel that Cronos's future is too predicated on the flawless execution of its CBD strategy, and because of that, I cannot recommend buying Cronos, even at these prices.

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