Now Is the Perfect Time to Buy Pot Stocks

Description

Pot stocks were soaring last year on speculation and short selling. Canada became the first country to pass liberal recreational marijuana laws. Canadian pot stocks have been throwing so much financing into acquisitions to quickly expand that their balance sheets are not pulling in the profit investors were hoping for.

Quickly growing pot stocks initially saw the rise in stock price, because their expensive acquisitions and business development strategies were killing investors with hopes of finding the one pot stock that would make them millionaires. Instead, they got caught up in a speculative bubble at the peak.

Here's a breakdown of the worst-performing pot stocks this year and how to invest without getting burned by the downward correction.

Canopy Growth

Canopy Growth has been losing heavily this year after speculative traders drove the stock price up to $70.98 at the start of the last 52 weeks. The current stock price is now $19.08, which means investors who purchased new positions at its peak have lost around 53% of their initial investment.

Levered free cash flow for Canopy Growth is negative $1.22 billion. When levered free cash flow is negative, investors can expect more of the company's earnings to go to servicing debt than given back to them as a return on their investment. If you see a company's stock price going up drastically when it is reporting negative free cash flow, it is likely the case that shareholders are creating a speculative bubble.

Financial statements can be daunting to look at for shareholders who don't have as much experience or accounting knowledge. Despite this, it isn't that difficult. Every investor can learn how to look up a company's financials to make good investment decisions.

Cronos Group

The Cronos Group has lost 75% of its value in the past 52 weeks and is now $8.13 per share at the time of writing. The Cronos Group was also a pot stock that investors shorted and a part of many short-squeeze rumours, which fueled even more long positions.

A short squeeze is a substantial stock price increase caused by growing short positions. When a stock is sold short, the broker must also take a long position in the stock to lend the shares to the customer. Likewise, to guard against the losses of a short position, investors must take a long position in the stock.

Understanding all this, many speculative traders will look for stocks with significant short positions and then take a long position in the hopes that the stock price will hit the max pain price or the price at which the stock will cause the most financial losses.

Foolish takeaway

I don't recommend long-term investors look for stocks with a lot of speculative trading or short selling. Adopting this kind of investment strategy will cost you more time and cause more stress than what it is worth.

Instead, try to avoid stocks caught up in these cycles. Look for pot stocks with positive levered free cash flow, as it will guarantee the highest return on your initial investment.

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Author
debraray