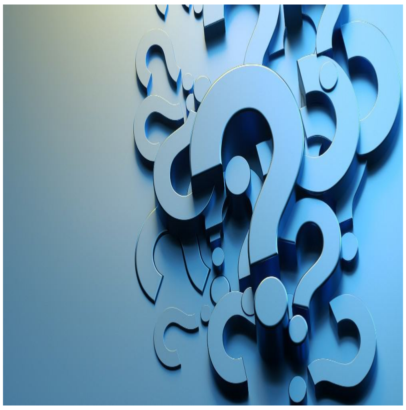

Should you Short Cannabis Stocks or Just Avoid Them?

Description

The past two months have been surprisingly kind to cannabis stocks. Since March 18, the **Horizons Medical Marijuana Life Science** ETF has risen 58%, compared to just 32% for the **TSX** in the same period. True, marijuana stocks have been lifted by a broader market rally. But the cannabis sector is rallying harder than most, posting massive gains in a short amount of time.

The question is: *why*?

Cannabis stocks still face the same problems they always did: huge losses, questionable goodwill and decelerating revenue growth. For example, in its most recent quarter, **Aurora Cannabis Inc** (TSX:ACB)(NYSE:ACB) posted a $137 million net loss and lower revenue growth than in prior quarters. Other cannabis companies are posting similar results, so it's not clear why this sector is rallying right now.

In light of this, it's tempting to consider shorting cannabis stocks, which are still as overpriced as they ever were relative to sales. Now their revenue growth is slowing down. Certainly, there are some opportunities to be had by shorting them.

Right?

Maybe — and maybe not. While most marijuana stocks appear overpriced right now, it's probably not a great idea to short them. An irrational rally can last a long time, and the potential losses are unlimited. In light of this, you're probably better off avoiding marijuana stocks rather than shorting them.

Why shorting is dangerous

Shorting stocks is dangerous because of the potential for unlimited losses. When you buy a stock with your own money, your loss is limited to the amount of money you invested.

When you short a stock, you borrow it, which means you have to pay back the shares later. There's no limit to how high a stock could go, so your potential losses when shorting have no theoretical limit.

While hedge funds frequently use shorting and other complex strategies, these are not generally recommended for retail investors. Even marijuana stocks, which appear poised for another dip, could rally unexpectedly. So shorting them could cost you some big money.

What to do instead

If you're bearish on cannabis stocks, your best bet is to avoid them and invest your money elsewhere.

When we look at a marijuana stock like Aurora Cannabis, it seems fairly evident that its future isn't great. The company is losing money. Its revenue growth is slowing down. It's facing billions of dollars in impairment charges. Its acquisitions haven't panned out. Basically, apart from its *historical* revenue growth, it has almost every factor working against it. That's reason enough to avoid the stock.

But *short* it?

No way. Marijuana stocks are extremely volatile, and while their long-term trajectory is grim, they could spike massively in a bull market. Unless you have the intestinal fortitude to hold on during something like that, you're likely to lose money.

Leave shorting to the hedge funds. In your own brokerage account, it's enough to just avoid marijuana stocks entirely.

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Date
2025/07/21
Date Created
2020/06/07

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