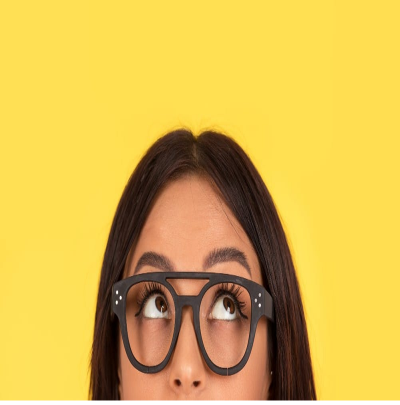

Penny Stocks: Gold Mine or Complete Scam?

Description

A popular option that many new investors might consider are investing in penny stocks. These stocks are referred to as penny stocks, because they're usually under a $5, or at least close to it.

There are some obvious benefits right off the bat that Canadian investors might think of when considering penny stocks. If you made a large investment and the stock moves up even slightly, you could be swimming in cash.

But the reverse is also true. Should you make a large investment, it can be relatively easy for those shares to plummet, and all your funds with it. So, what should Motley Fool investors consider before getting into penny stocks?

What's a penny stock?

First off, let's identify what exactly penny stocks are. Penny stocks are those with a market capitalization between $50 and $300 million. Shares trade at $5 and under. They tend to be small businesses with not to much history and therefore don't operate at a profit most of the time. This means they rely on debt based on their business models that have yet to be proven.

If you're getting into penny stocks, it means you *really* believe in the company's future. And while it's great for some investors to hop on board, penny stocks are really for large investors. These are people getting a large piece of the action and work with the company to see it succeed.

Motley Fool investors, however, are simply bystanders who can merely hope that the company does well. You don't get a real say, and that's a problem. Many of these companies can easily go bankrupt, and most don't see stable long-term growth.

Are all penny stocks alike?

There are certainly penny stocks out there that actually do have a history behind them. Take **Bombardier**

(TSX:BBD.B) for example. The company recently had a reverse stock split, but before that it traded at about $2 per share. It had a long history behind it, but not a great one.

That started to change this year, but a market correction has undone the company's growth. That is likely the reason for the reverse stock split. By doing this, it remains on the **TSX** without the risk of delisting.

And that's a big consideration. If you find these stocks on the TSX, they'll be over $1. You'll have to invest in "over-the-counter," or OTC, penny stocks elsewhere, usually through a broker.

Industries to consider

There are a few industries that are filled with penny stocks right now. Some are risky; others, less so. Some of the more risky ones include cannabis, mining, and technology right now. Oil and gas and pharmaceuticals can still be risky but don't have the sheer numbers that some of these other areas do.

That's why it can be good to think outside the box when looking for these stocks. You want to identify companies that perhaps aren't in these areas and therefore have less competition.

One I would consider right now is **StorageVault Canada** (TSX:SVI). This was a favourite penny stock, and it's now just above the $5 range. It operates storage facilities throughout Canada and has been growing through acquisitions and increasing its online offerings.

Storage is a huge industry given the rise in small businesses and e-commerce. People will store their items long term in this case. But there's also the fact that people will always need storage thanks to major life events, like divorce, displacement, death, and downsizing.

Bottom line

Penny stocks have the potential to make Motley Fool investors rich. I'm not going to say they don't. But I also don't want to say that you *will* get rich from these companies. It's incredibly risky, and there are better options.

If you're adamant about penny stocks, look for strong companies with stable growth paths in areas where there's little competition. But otherwise, stick to finding undervalued stocks that offer long-term potential, no matter the price.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:BBD.B (Bombardier)
2. TSX:SVI (StorageVault Canada Inc.)

PARTNER-FEEDS

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2. Koyfin
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1. Investing

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