



Canadian Penny Stocks: Can You Get Rich?

Description

If you're looking for a bargain on the stock market, or you have little money to invest, penny stocks can be a tempting venture. After all, with a low barrier to entry — by definition, \$5 or less per share — penny stocks may seem like a safe way to invest your money.

But don't be fooled. When it comes to penny stocks, the old saying couldn't be more true: you get what you pay for. Cheap as they are, penny stocks have dubious prospects for growth, not to mention low market valuations, and if you're looking to build wealth, penny stocks aren't the "rags-to-riches" venture many make them out to be.

So, before you start adding penny stocks to your portfolio, let's take a step back. What are penny stocks, and are they truly worth the money? Let's look closely and see.

What are penny stocks?

Penny stocks are small companies whose [market capitalizations](#) are between \$50 and \$300 million (also known as a [micro-cap company](#)) and shares trade for \$5 or under.

Penny stock companies are typically young, small businesses (usually start-ups) with a little fire but no proof their business model will work. They also don't have deep cash reserves to support them. They typically rely heavily on debt—or unproven technology they hope will propel them forward.

Whatever the reason for their small size, penny stock companies often take huge risks to get off the ground. When you invest in them, you're essentially betting the company will do the impossible and overcome these major challenges.

It's a steep bet. **Penny stock companies often fail.** Unlike [growth stock companies](#), which are fast-growing companies with potential for success, it's doubtful penny stock companies will exhibit long-term growth. You can lose money on a growth stock venture, sure. But the danger with penny stocks is losing your entire investment, as these companies can easily go bankrupt.

Top Canadian penny stocks

While we don't recommend penny stocks as a principal [investing strategy](#), a few companies could be viable for beginning investors. Here's just a few penny stocks that have crossed our radar.

Penny Stock	Description
Hive Blockchain Technologies (TSXV:HIVE)	Crypto mining company specializing in Bitcoin and Ethereum
5NPlus (TSX:VNP)	Specialty metals and chemical company
Cloud MD Software & Services (TSXV:DOC)	Telemedicine company offering health technology solutions

All data accurate as of November 21, 2022

1. Hive Blockchain Technologies

HIVE is a crypto mining firm. Simply put, they specialize in mining and selling cryptocurrencies, such as Ethereum and Bitcoin.

With its IPO in 2017, HIVE became the first publicly traded crypto miner on the TSX. Since then, the stock has performed mediocorely. Though it had an opening price of \$12, it immediately plummeted. By 2020, you could have literally bought the stock for a few pennies. After a brief, but hopeful, spike in 2021, the stock now trades at around \$2 per share.¹

One good thing about HIVE: it's one of the old crypto mining companies. That's not saying much (crypto is still young), but it does have more stability and experience than most penny stock companies.

2. 5NPlus

Headquartered in Montreal, 5NPlus is a metal supplier that engineers specialty metals and chemicals.

Many of the metals that 5NPlus produces are critical for other industries. For example, 5NPlus makes metals and chemicals that are used in semiconductors, solar cells in satellites, solar panels, and detectors for certain medical imaging equipment. The company also has a heavy "sustainability-first" approach, which involves using recycled metals as raw materials rather than making them from scratch.

5NPlus first went public in 2007 for \$3 per share.² Since then, it has mostly traded below its initial value, with a brief spike in 2011.

3. CloudMD Software & Services

Cloud MD is a health technology company that provides healthcare facilities with new digital services, such as an online patient portal, cloud-based EMR (electronic health record), and telemedicine.

Riding on "shelter in place" mandates from the pandemic, CloudMD demonstrated impressive growth

in 2020 and 2021. Like other tech companies, however, CloudMD has stagnated significantly in 2022, falling to its lowest price since its IPO—a whopping \$0.20 per share. It's unlikely the stock will see significant growth in the short-term—especially since telehealth isn't as necessary as it was in the pandemic—but could be a company to watch for in the long run.

Can you get rich from penny stocks?

Penny stocks are, well, stocks. As such, you can earn money by investing in them. That said, it will be a real challenge if you expect to earn significant wealth, let alone get rich, on penny stocks alone.

To understand why, consider the most common way penny stock investors make money: short-term gains. Unlike growth and [value stock investing](#), which involve looking for companies that will demonstrate long-term upward growth, penny stock investors want companies that will hit it big in a short period of time. When that spike comes (if it does), the penny stock investor typically sells their shares to make a quick gain.

The problem with this? For one, we're talking about penny stocks. Even if a penny stock worth \$5 hit a 100% gain, you'd still only earn \$5. To get rich off penny stocks, you have to trade at high levels, and even then, you probably won't earn as much as you would in a good growth stock.

The second problem is consistency. You may earn a quick profit off a handful of penny stocks, but rare is the investor who can do this frequently over long periods of time. Those that do are professionals, meaning they invest significant amounts of time and money (even professionals lose) in penny stock ventures. Unless you're prepared for that kind of investing style, you shouldn't expect to earn wealth off penny stocks alone.

If you have extra money and you want to try penny stocks, by all means — give it a whirl. But if your goal is to [invest for retirement](#), or you're new to investing, penny stocks aren't the smartest option for you.

How to find penny stocks

Because of their size, most penny stocks don't meet the requirements to be traded on major market exchanges, such as the [Toronto Stock Exchange \(TSX\)](#). Instead, penny stocks are sold over-the-counter (OTC), such as on an over-the-counter bulletin board (OTCBB) or "pink sheets."

When a penny stock company is listed on an OTCBB, it must meet certain requirements. For instance, it must keep up-to-date information on its finances and make financial records available for traders to review. Pink sheets are a different story.

When listed on pink sheets, penny stock companies don't have to reveal information on their finances. For this reason, buying penny stocks on pink sheets is considered extremely risky, as you won't know much about the companies you're buying.

How to trade penny stocks in Canada

Here are four steps to trading penny stocks in Canada:

1. Open a brokerage account that buys and sells penny stocks

Since penny stocks are traded OTC, you'll have to find an [online brokerage](#) that will buy and sell penny stocks on your behalf. Many will offer this service, but check your online brokerage ahead of time if this is something you're interested in.

2. Buy penny stocks

Once you have a broker who will conduct penny stock trades, you buy penny stocks as you would normal stocks: fund your account, choose your penny stock company, and place an order.

3. Sign a risk disclosure

Because of the risks that penny stocks impose, you typically may have to sign a disclosure with your broker before you start buying them. They'll usually send you a document detailing the risks, and once you review and sign it, your broker will allow you to trade penny stocks.

4. Make sure you aren't charged commissions

Finally, if you're serious about trading penny stocks, make sure your broker doesn't charge commissions on penny stock transactions. Since you probably won't earn much on penny stocks anyway, you don't want to give away your precious gains to extra investing fees.

What sectors are penny stocks usually in?

In Canada, you'll likely find most penny stocks in the following markets:

- [Cannabis](#)
- [Mining](#)
- [Oil & gas](#)
- [Technology](#)
- [Pharmaceuticals](#)

How risky are penny stocks?

Short answer: very, very risky. The risks of penny stocks are numerous and include:

- **Insolvency** – Penny stocks are little-known companies that have yet to prove themselves on the larger market. They can (and often do) go out of business.
- **Highly speculative** – Often, you're investing in an idea or concept, not a company with solid fundamentals.

- **Traded “over the counter” (OTC)s** – The OTC market lacks the same rigorous reporting as larger exchanges, and you could have less visibility into your company’s operations.
- **Thinly traded** – There could be less liquidity in penny stocks, meaning it could be difficult to sell your shares at the time that you want.
- **Target of scams** – Many con artists will build up a penny company—through social media or some other means—to artificially inflate the stock price. When the price is high enough, they’ll sell their shares. Called “pump and dump,” this scheme could bamboozle investors into buying a bad stock for a terrible price.

How long should you hold penny stocks?

At The Motley Fool, we recommend you hold a stock for a minimum of 5 years. But penny stocks are a different beast—they require a short-term strategy, which is why we *don’t* recommend investing in them.

Common investing advice would tell you to hold a penny stock for no more than 6 months. Some investors, however, might recommend holding a penny stock for no more than 6 *seconds*. Penny stock investors sell so quickly because they’re only waiting for a very minuscule gain—a few pennies will do. Once the penny stock reaches that “height,” the investor sells. That could be 6 minutes, 6 hours, or 6 days.

Again, at The Motley Fool, we believe in [long-term investing](#). If you’re a long-term investor, you look for great companies that have strong business fundamentals and will likely increase in value over time. If you have some extra money to play with penny stocks, that’s okay, as long as penny stocks don’t make up a large portion of your holding.

What’s a better alternative to penny stock investing?

A better approach to stock investing, especially for [beginner investors](#), is to invest for the long term. That means finding high quality stocks, such as undervalued stocks, good growth stocks, or even stocks that pay out consistent dividends, and holding onto them for the long haul. Additionally, you could diversify your portfolio by investing in a solid fund, such as an [exchange-traded fund \(ETF\)](#).

Another alternative to penny investing is to buy fractions of a stock. You may not have thousands of dollars to buy a full share of Shopify or Amazon. But with fractional investing, you can buy a small amount and still benefit from the company’s growth.

TICKERS GLOBAL

1. TSX:VNP (5N Plus Inc.)
2. TSXV:DOC (CloudMD Software & Services Inc.)
3. TSXV:HIVE (Hive Blockchain Technologies)

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2025/06/28

Date Created

2021/09/24

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