



The Bridge Research Article: The Emerging Cannabis Market

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The Emerging Cannabis Market

The US cannabis market has been a confusing ride for investors. There is a huge market that is not quite legal and is not quite illegal. The size of the opportunity in the U.S. alone is large. Colorado, which has been a legal market for over 5 years, sells over \$1.5B in legal products (not including the black market). Multiply that by usage rates and population across 50 states and you get a market opportunity north of \$85B, even before you take into consideration the expanding medical cannabis market opportunity.

A recent Gallup poll said 66% of Americans support legalization. Nine in ten think it will be legal at the Federal level within 10 years. This is why cannabis is an important growth industry for investors to watch.

What are the biggest impediments to the U.S. legal marijuana industry aside from being illegal at the Federal level?

- Lack of banking access
- Varied regulatory structures on a state level
- High state taxes keep the black market flourishing
- High capital requirements

Recreational cannabis may only be legal in 11 US states and D.C. thus far but over 25% of the population lives in those states. A major reason marijuana stocks are currently trading at lows is because additional cannabis legalization has not occurred at the pace expected. If you want to invest in public marijuana companies, you need to think about long duration investing.

Venture capitalists (VC) invested a record \$1.2 billion of capital into US marijuana companies in 2018.

In 2019 YTD, \$1.7 billion has been invested. VC companies continue to pile into the space even as public equity valuations have collapsed. Since VC companies typically have a 5-year window to monetize their investments, that's a vote of confidence in the sector.

What cannabis compound do you think offers the most upside for growth: CBD (non-psychoactive therapeutic benefits) or THC (psychoactive/mood-altering)? There are numerous use cases for CBD and THC when it comes to treating various ailments from insomnia, pain, anxiety, depression, inflammation and seizures. Because cannabis was and still is classified as a Schedule I narcotic, pharma companies have invested little in researching its therapeutic benefits, yet they could eventually disrupt their core drug therapies. Because of CBD's non-psychoactive properties it has a larger addressable market. CBD is currently being used in everything from food, drink, health/wellness, sport and beauty products.

Liquor, tobacco and healthcare companies understand this is a disruptive threat with effects that will play out over the next decade as more legalization and medical studies occur.

Liquor companies especially understand this dynamic, which is why they have been the biggest movers to invest in the legal cannabis industry. The poster child for this is Corona owner Constellation Brands' (STZ) stake in Canadian marijuana producer Canopy Growth (GGR). Cannabis gives liquor companies a way to diversify their product offerings as a hedge against softening sales of alcoholic beverages.

A new academic study found that recreational marijuana legalization hurts online search and advertising click-through rates for alcohol brands. The research looked at online searches and ad impressions related to cannabis, alcohol and tobacco



products in 6 states that had legalized recreational marijuana between 2014 and 2017 to determine the effects of the legalization on internet browsing activity. Researchers found alcohol searches declined about 11%. Tobacco findings were the opposite with marijuana legalization increasing tobacco related searches by 8%.

For tobacco companies that have invested in cannabis, early research shows counterfindings. Altria (Marlboro/Juul) has had a big stake in Cronos, a Canadian producer. With the current vaping health crisis, Altria's diversification moves may or may not prove profitable.

Legal marijuana is still a new industry but the effect of this disruptive market on other industries has only begun to play out.

Sources:

*Conallen, Bill. "Recreational Cannabis Legalization a Substitute for Alcohol, Not Tobacco." *Whitman Voices*, 9 July 2019.*

*Jones, Jeffrey M. "U.S. Support for Legal Marijuana Steady in Past Year." *Gallup*, 23 Oct. 2019, news.gallup.com/poll/267698/support-legal-marijuana-steady-past-year.aspx.*

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