

What Canadian Cannabis Investors Can Learn From Colorado's Legalization

Description

For Canada, nationwide legalization has been in the cards for quite a while now, but, unfortunately, there have been endless delays due to the many issues that premiers still have. There's uncertainty regarding what may happen if cannabis is legalized, but I don't think there are critical concerns, especially considering that some states in the U.S. have already pulled the trigger on legalization.

Cannabis is legal in Colorado; it's worth it to take a look at what happened in the state in its post-legalization era to see if there are real concerns that Canada may want to consider. After all, sometimes learning from the mistakes of others is the best way to move into uncharted waters. Although the geographies are different, many legalization effects and other patterns will be the same.

What happened to Colorado when cannabis was legalized?

John Hickenlooper, the governor of Colorado, was recently interviewed by BNN regarding the state of legalization in Colorado and gave some ideas on how Canada can be successful with its legalization. Although the pros of legalization heavily outweigh the cons, there are small adjustments that could be made to ensure a smooth transition.

Many Canadian premiers are worried about the negative impacts of legalization, but these concerns may be overblown, and further delays may not be necessary. On legalization, Mr. Hickenlooper stated, "...we made a lot of mistakes, most of them were corrected [and] they weren't significant. We didn't see a big spike in teenage consumption or overall consumption, but things like the grey market did kind of seep out."

Taxation and pricing are major question marks

Taxation and pricing will play a big role in the elimination of a grey market. To reduce such a grey market, the Federal Government may initially want to keep taxes low and gradually increase them in the years following legalization.

Producers such as **Canopy Growth Corp.** ([TSX:WEED](#)), **Aurora Cannabis Inc.** ([TSX:ACB](#)), **Aphria Inc.** ([TSX:APH](#)), and **MedReleaf Corp.** ([TSX:LEAF](#)) will likely see a surge in demand once legalization day comes, and the price per gram of cannabis is likely to be at its high point. As more producers get growing licences, and the existing producers become more efficient, demand will eventually meet supply, and the price per gram of cannabis will gradually decrease.

Analysts at **Canaccord Genuity** stated that \$8 per gram of cannabis can be expected until 2019 or 2020, and the average price will gradually drop to the \$7 level in 2024.

If many prospective producers are given the green light over the next few years, then cannabis prices may drop below \$7 per gram, and this is probably a great time for the government of Canada to raise taxes on the sale of cannabis.

What does that mean for Canadian marijuana producers?

What the Federal Government will do regarding taxation is a huge question mark right now. If they want to attempt to eliminate the grey market in the initial stages, producers will benefit, but even if taxes are kept high initially, I don't think producers will be too negatively impacted, but pot stocks may take a short-term hit because the general public may treat such news as a negative.

I believe the grey market will eventually be phased out years down the road, especially since companies like Aphria and Aurora are aggressively investing in efforts to reduce operating costs.

Bottom line

While the premiers' concerns are warranted, I don't think they are enough to delay nationwide legalization by another year or more, especially because nothing horrible happened after legalization in Colorado. Many may think that legalization will continue to be delayed to 2019 or beyond, but in reality, it may come sooner than we think.

When legalization occurs, I believe headline risk will increase, and cannabis stocks will be as volatile as they were last year. If there are further delays to legalization, then trading volumes on cannabis stocks are likely to be low, and it'll be very difficult for traders to make a quick profit.

Cannabis is a commodity, and competition is going to get ridiculously fierce as more producers start popping up on the TSX. Everybody wants to get in on the Canadian green rush, and we may witness a market similar to the tech surge of the late 1990s. There will be a few winners in an ocean of losers, so investors should be very careful when buying shares of any cannabis stock.

If you do want to get in on the green rush, then it'd be a very wise move to buy efficient companies that show operational improvements on a consistent basis. Aurora and Aphria are two solid long-term companies that come to mind. Don't trade them though; own them for the long haul.

Stay smart. Stay hungry. Stay Foolish.

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2. TSX:WEED (Canopy Growth)

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