



Canopy Growth Corp.: Could a Hemp Strategy Support Exponential Growth?

Description

Canopy Growth Corp. ([TSX:WEED](#)) recently increased its exposure to the hemp business line with its November 2017 acquisition of the assets and operations of Green Hemp Industries Ltd., including the intellectual property held by its principal, Jason Green, in an all-stock transaction. Investors may be wondering why Canopy would deepen its investment in hemp after a significant write-down of hemp-based inventory in a previous quarter messed up its gross margin.

Hemp and cannabis belong to the same biological species. Before the latest hemp acquisition, Canopy already had a significant hemp exposure after its acquisitions of Groupe H.E.M.P.CA and Mettrum Health Corp. in November 2016 and January 2017, respectively. Mettrum Health had Mettrum Originals, a hemp-focused subsidiary under its umbrella.

Canopy wrote down the \$0.7 million off the carrying value of its hemp products during the quarter ended September 30, 2017 due to discontinued product lines; the company appears to be refocusing its hemp strategy.

Refocused hemp strategy

Canopy appears to be refocusing its hemp market strategy from simple hemp health foods and industrial product business units toward a new corporate strategy that closely combines hemp with Canopy's core cannabis business line in a unique and brilliant way.

The company signed a deal with Skinvisible Pharmaceuticals, Inc. in the September 2017 quarter involving hemp-based topical creams to be launched by Canopy Hemp Corporation in Canada as well the development of cannabis-based topical products after the federal legalisation of cannabis infused products in the country.

The acquisition of Green Hemp Industries is a massive, high-level strategic move that allows the company to boost its cannabidiol (CBD) extracts product line. It is expected that with the recreational marijuana legalisation approaching in July of 2017, new federal regulations covering hemp will allow companies to harvest and extract high volumes of CBD from hemp leaves and flower.

Current “industrial hemp” regulations only allow hemp farmers to harvest hemp stalk and seeds and never to touch the valuable, CBD rich, hemp leaf and flower. New flexible regulations to be introduced later this year could lift that prohibition and allow Canopy to exponentially grow its cannabis oil and capsules product volumes from low cost, organically grown hemp plants.

Canopy’s aggressive competitor, **Aurora Cannabis Inc.** ([TSX:ACB](#)) made a [similar strategic move](#) through its conditional and highly negotiated investment in then financially distressed **Hempco Food and Fiber Inc.** last year.

The hemp plant is a significantly cheap source of CBD extracts, and Green Hemp Industries could offer Canopy a cheap supply of the product from its vast farmland and efficient extraction technology.

The high level strategic thrust

I don’t expect Canopy to become a hemp food giant anytime soon; the company may not be that enthusiastic about creating a dominant hemp food business. Hempco faced serious challenges in its Korean market due to an influx of cheap and low quality hemp products from Asian producers, and I don’t even see any hemp revenues from Canopy’s financial statements released in November last year.

However, Canopy seems to have something up the sleeve with the hemp strategy.

The regulated hemp market could potentially allow for more robust consumer-facing brand marketing, advertising, and retail channels, which will serve to strengthen the company’s consumer-facing brands in the future.

Canopy could thus be able to elevate consumer awareness for its brands in the hemp market. I believe the strategy could exponentially grow its cannabis market share in a regulated recreational marijuana market, as the company channels massive advertising dollars and floods the consumer market with loosely regulated hemp products carrying its brands.

Investor takeaway

Canopy Growth Corp. is keen on keeping its pole position in the global cannabis market, and the recent hemp investment is a critical part of the strategy that will afford the company a cheap supply of CBD extracts while allowing Canopy to aggressively market its consumer-facing brands in markets where cannabis regulations strongly prohibit advertising.

The company’s long-term growth prospects are seemingly even more visible in the global market at it executes its aggressive expansion strategy.

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