Almost Halfway Through the Year, This Is Where Marijuana Investors Need to go!

Description

With almost half the year already on the books, the marijuana industry has been a mixed bag for investors, with the **Horizons Marijuana Life Sciences Index ETF** (TSX:HMMJ) declining by close to 15%. In spite of being six months closer to legalization, investors are not valuing the sector with the frenzy and exuberance they once did. The reality is starting to catch up with investors, as they're now better able to project the future cash flows of these companies. For those who continue to hold these investments, rest assured that there is nothing to worry about: there is still a lot of money to be made.

For those who think that a 15% decline is too much however, don't feel bad. Investors in bitcoin have lost approximately 50% of their investment since January 1 of this year. Things could have been worse.

Consistent with the index are shares of **Aurora Cannabis Inc.** (TSX:ACB), which declined by close to 25% as the company agreed to buy competitor **MedReleaf Corp.** (TSX:LEAF) for close to $3.2 billion after completing another smaller acquisition for $1.2 billion. The smaller purchase price for CanniMed Therapeutics Inc. earlier in the year goes to show that the industry is not very traditional — a scenario that will potentially bring about major risks for investors.

What major risks?

In a traditional setting, consolidation occurs only once companies have become fully mature and have little room to grow market share and increase profits. At this point, there is often excess cash available that is used to fund the acquisition of a competitor. In the case of the marijuana industry, the acquisitions are coming with a lot of uncertainty. In spite of a significant amount of potential, the industry has yet to become profitable.

The main reason that many smaller firms are acquiring their competitors is to be able to reach better economies of scale and acquire some degree of pricing power. With many competitors to choose from, the governments will have the pricing power and no firm will be able to make any amount of excess profit. By consolidating, the government will have fewer choices, which may pressure them to pay a little more for each purchase.

Case in point: **Canopy Growth Corp.** (TSX:WEED)(NYSE:CGC), which has increased in value by close to 20% since the beginning of the year. As the company was first into the market and has enjoyed the appearance of “first mover” advantage, there is no doubt that governments will want to have the product of this company on their shelves. For anyone trying marijuana for the first time (or for the first time in the past 20 years), the company that has been in the news most often may just be the go-to supplier.

In spite of the traditional rules not applying to this industry, the best bet for investors may just be found in shares of Canopy Growth Corp., as the company has momentum on their side and in many cases it is the only company known to consumers. Sometimes things are just not that hard!

CATEGORY

1. Investing

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2. TSX:ACB (Aurora Cannabis)
3. TSX:HMMJ (Horizons Marijuana Life Sciences Index ETF)
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