

This Cannabis Company Is Leapfrogging the Competition

Description

While growth prospects remain massive, the cannabis market has been a double-edged sword for many producers.

On one hand, markets in both the U.S. and Canada continue to be strong. In 2018, the Canadian government legalized recreational use for adults, instantly creating a multi-billion dollar market. South of the border, some analysts predict the U.S. marijuana market will grow to \$80 billion by 2030.

But with huge near-term demand, producers have been scrambling to create new capacity. That's caused damaging over-supply, putting pressure on selling prices. For example, in January, the *New York Post* reported that Oregon has more than one million pounds of excess weed.

"We're looking at hundreds of millions of dollars of local capital that is at imminent risk," said Adam Smith, founder and director of the Craft Cannabis Alliance.

Many investors are worried that while growth prospects remain attractive, over-supply will commoditize prices to a point where margins collapse for nearly every grower. And because cannabis is still illegal at a federal level in the U.S., it can be difficult to move excess capacity across state lines to under-supplied regions.

Some companies like **Cronos Group Inc** are beefing up their competitive edges by partnering with deep-pocketed tobacco companies like **Altria Group Inc**. Still, if over-supply becomes a permanent reality, the market will remain a race to the bottom.

However, one company has decided to bypass the competition completely. Instead, the company is focusing on value-add products with similarly large potential but less risk of commoditization. Here's what you need to know about **Hexo Corp** ([TSX:HEXO](#)).

Branded cannabis will win

In the rush to bring large amounts of supply to the market quickly, expect prices to collapse over the long term. To succeed in the cannabis space, investors must focus on companies with differentiated edge capable of providing pricing power. The easiest way to do this is to find companies capable of branding their products.

While some competitors are attempting to brand dry flowers or other THC-infused products like oils or vapes, these areas will largely be commoditized. Value-add products like cosmetics, beverages, and food will be a completely different story. Already, we have countless examples of branded items in these categories that generate impressive profits through trusted branding, the most famous of which being **The Coca-Cola Co**.

That's why Hexo's focus is so intriguing. Late last year, it struck a deal with **Molson Coors Canada Inc**.

to form a joint venture aiming to bring cannabis-infused beverages to North American markets, starting with Canada. Molson has a 57.5% controlling interest while HEXO owns the remaining 42.5%.

These partnerships will be the key to success in adjacent markets like beverages. Molson has decades of experience designing, branding, manufacturing, and distributing beverages throughout the world. In a joint statement, the two companies said the partnership will allow them to “hit the ground running,” thereby building market share more quickly than any other competitor.

Focus on other cannabis categories

Cannabis companies simply focused on building capacity are touting future revenue potential based on current prices. As those prices become commoditized, any producer without a differentiated competitive edge will suffer.

Other companies are having difficulties creating partnerships in the traditional beverage industry. Shares of **Tilray Inc** fell 16% in one day last year after it failed to secure a tie-up with **PepsiCo**, Inc, while **Aurora Cannabis Inc** dropped its rumored talks with Coca-Cola.

“The difficulties in investing in that category, particularly in the U.S., where federally these things are still not legal, are quite a considerable challenge,” one Pepsi executive said.

Armed with a valuable partnership in a cannabis category with significantly better pricing power, Hexo is a contrarian pick in an increasingly competitive market.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:HEXO (HEXO Corp.)
2. TSX:TPX.B (Molson Coors Canada Inc.)

PARTNER-FEEDS

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2. Newscred
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