Why Health Canada's Recent Announcement Could Be Bad News for Canopy Growth (TSX:WEED)

Description

We could be seeing a lot more competition in the cannabis industry very soon.

Health Canada recently announced that it would be making it easier for companies to obtain cannabis licenses. Previously, applicants didn't have to have their sites ready to go before submitting their applications, which has created a lot of back-and-forth that wasn't necessary that the government felt resulted in a lot of inefficiencies and bottlenecks along the way.

With a supply shortage of cannabis in Canada, there's definitely an incentive to expedite the process. By requiring applicants to have a site already built and in compliance with regulations right at the start, it will help streamline the process and ensure that time isn't being wasted on applicants that still have a long ways to go.

More competition could be bad news for industry leaders

While a company like **Canopy Growth Corp** (TSX:WEED)(NYSE:CGC) might be enjoying its place atop the industry today, more competition will make it more difficult for the company to keeps its advantage and strong market share. With advertising in the industry being limited, there's not much of an advantage Canopy Growth can have over its rivals, especially in Ontario, where restrictions around store ownership mean it will have limited say in the retail side of things.

And with an increase in competition, that will help drive down prices and give consumers more options to choose from. Both of those consequences will have a negative impact on Canopy Growth's financials, which aren't all that strong to begin with. While some of the more promising competitors have been acquired by Canopy Growth and other big cannabis companies, further acquisitions will require cash being spent or a company having to issue new shares, resulting in dilution for existing shareholders.

Industry leaders don't want to see too much competition, as it will result in more effort being needed to win market share by driving costs and prices down as much as possible. Although Canopy Growth has managed to turn a profit in two of its past five quarters, operationally it has been nowhere near break even as it has been other income that has been able to land the company into the black.

Bottom line

For consumers, the news from Health Canada is a big win. By getting more growers and producers out there, it'll help the industry meet demand and hopefully keep more customers from having to go to the black market. However, with the possibility for even more fragmentation in an industry that already has lot of small companies vying for market share, it's going to make it more difficult for a single company to dominate the market.

The key will lie in acquisitions, and that's where having a strong balance sheet and lots of cash on hand is going to be paramount to staying near the top of the industry. For Canopy Growth, that could be a problem, especially with the company focusing on the U.S. market lately.

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