



3 Warning Signs for Cannabis Investors

Description

Boy, what a year 2019 was for investors in Canada's new cannabis industry. The mood among many has certainly shifted, and the euphoria with which companies were gobbling each other up has abated. **Horizons Marijuana Life Sciences Index ETF** is now down 65% from its 52-week high in early 2019 (not its overall peak).

Questions about where the bottom is remain, and with cannabis stocks continuing to slide with seemingly no end in sight, investors remain cautious with respect to these names, and deservedly so.

Here are three of the biggest question marks, or warning signs, if you will, that investors need to keep an eye on in 2019 when considering if/when to jump back into the fray.

Inventory levels

I've pointed to this in the past — there's a glut of inventory out there, and it's killing margins. Companies are being forced to destroy product; cannabis is a natural product, and has a shelf life. It's also a commodity, and supply and demand is a real thing that drives prices.

With provincial distributors the main customers of most cannabis producers, the "price taker" reality for producers is starting to kick in (and it appears investors are starting to notice this issue).

As of mid-2019, the glut was approximated at [150,000 kg](#) of the green stuff — a truly staggering sum.

Black market is alive and strong

The black market is unregulated.

This fact alone is enough to make anyone understand the disadvantage any large-scale licensed cannabis producer has when competing against some guys growing plants in their basement. I've gone into detail about [a few of the key hurdles](#) producers face and given readers a taste of some of the red

tape cannabis producers have to fight through to get their product to market.

You can bet the Canadian government will want to take bigger and bigger tax bites out of the profit pie that producers are able to consume most of right now. As margins shrink and taxes rise, expect to see profit expectations continue to drop, hurting share prices further. I still do not believe the true impact of future taxation and over-regulation are built into these producers' share prices.

Cannabis retail is failing consumers

Having cannabis packaged in a similar fashion to cigarettes is killing the retail experience. Having product at government stores locked behind an opaque cabinet, with consumers having to guess what they are going to get, is mind boggling.

The retail experience at most government stores across the country is lacking. The guy on the street corner has the advantage at this stage in the game, and while the government talks a big talk about getting rid of the black market across the country, the abysmal way in which cannabis is retailed at this point in time is likely to lead to continued problems with black market penetration in 2020 and beyond.

Ontario has realized this issue, and there are seemingly plans to privatize retail in that province; questions remain, however, as to what regulations will be put in place for these retailers (if they're held to the same standards as government stores, it won't help). The one hope for cannabis investors is that private stores will roll out quicker, as this has been another major pain point for the industry — the true lack of physical retail locations, again, due mostly to government regulation.

Stay Foolish, my friends.

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