



Will Cannabis Companies Ever Pay Dividends?

Description

Canadian cannabis companies have not yet established themselves as consistently profitable companies. The biggest names in the sector have reported net losses for years. However, as the sector expands, some investors may be wondering whether Canadian cannabis companies will ever pay dividends. Let's take a deeper dive into that question.

What does it take to be a consistent dividend payer?

Some of Canada's best-known companies have remarkable dividend histories. For example, **Royal Bank of Canada** ([TSX:RY](#))([NYSE:RY](#)) ("RBC") has been paying a dividend for over 100 years and is Canada's largest bank. The bank enjoys consistent profitability due to the relatively concentrated nature of Canada's banking sector and the diversified range of financial services businesses operating under the RBC banner.

RBC is able to pay consistent and growing dividends for a few reasons. First, the business model is stable because banks make money on interest rate spreads. If rates go up or down, RBC passes on changes to customers. RBC still profits by being able to borrow for less than what the bank charges customers.

Second, RBC operates in a business with steep barriers to entry. Furthermore, it would take tens, if not hundreds, of billions of dollars to build a bank that would be able to compete with RBC.

RBC demonstrates the types of traits that make for reliable dividend payers. Notably, two of these traits are a stable business model that delivers profit in all (or almost all) business environments, and high barriers to entry.

Some cannabis companies in the United States already pay dividends

Strictly speaking, there is no company that directly produces and sells cannabis and currently pays a regular dividend. However, **Innovative Industrial Properties** ([NYSE:IIPR](#)) ("IIP") is as close as you will come to a dividend-paying cannabis company, at least for now.

IIP is a [REIT](#), in the United States, focussed on cannabis production assets. IIP's business model involves owning the vital production space that producers operate in and leasing it to producers at contractually-set rates. In many cases, IIP engages in sale-leaseback transactions where the REIT's client already owns and operates a production facility, and simply wants to lease that space instead of owning it.

IIP buys the property from the client and immediately leases the space back to that same client, allowing producers to free up huge amounts of capital tied to production facilities with no business interruption.

This business model is stable. The rents that producers pay are contractually set, and thus IIP enjoys predictable and recurring cash flows. While the barriers to entry are not necessarily as high as they are for banks, it is not cheap to continuously be acquiring new industrial properties.

Additionally, REITs are required to pay out 90% of income to shareholders in the form of dividends. These factors allow IIP to pay a generous dividend.

Production and brand development are not cheap

Companies such as **Canopy Growth** ([TSX:WEED](#))(NYSE:CGC) have certain unique expenses that companies like IIP do not. For example, Canopy actually has to produce cannabis. This costs [money](#), especially given that Canopy has a large indoor-cultivation footprint.

Second, Canopy has to brand and market products. There is a huge financial risk that comes with carrying inventory of specific strains or products. If that strain or product does not sell, it not only means potential markdowns on prices, but also that Canopy is not generating cash flow very quickly.

Additionally, developing brands, advertising, and paying royalties to third party collaborators all eat into profit margins as well.

Ultimately, Canopy is likely a decade or more away from paying a dividend if the company ever does. Canopy has significant costs that must be budgeted for because these costs play a vital role in revenue and profit growth. In the end, Canopy is better suited for growth investors.

Takeaway

Some companies in the cannabis space will eventually pay a dividend. However, don't focus exclusively on the dividend. Focus on profitable business models with high barriers to entry. Stock price gains, and often dividends, will follow.

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1. Bank Stocks

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POST TAG

1. Cannabis Stocks
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3. Dividends
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TICKERS GLOBAL

1. NASDAQ:CGC (Canopy Growth)
2. NYSE:IIPR (Innovative Industrial Properties)
3. NYSE:RY (Royal Bank of Canada)
4. TSX:RY (Royal Bank of Canada)
5. TSX:WEED (Canopy Growth)

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