

A Timeline for Decriminalization of Marijuana

Even though KellyAnne Conway claims otherwise, a fact is a fact, and there can be no 'alternative facts'. And it is a fact that unless you have a medical exemption, your use of marijuana in Canada is illegal. The loosening of social mores does not change the fact of illegality.

The price of the shares of public marijuana companies have risen and fallen in tandem with Supreme Court decisions, the *Allard* decision out of the Federal Court, and policy announcements from Health Canada. The companies' only real value is in the licence – the real estate and cash exist only because of the licence. In such a highly regulated space, being an intelligent investor demands a knowledge of the legal arena.

One need look only at Canopy Growth, the largest such company in Canada. Its shares took an insane streak up to almost \$18 in November, creating a market cap of roughly \$1.6B. The unaudited six month revenue number ending Sept 30/16 was \$15M, implying a full year run-rate of \$30M, or a bit under 2% of that market cap. That was a valuation equal to 50 times go-forward revenue, reminding us of the ludicrous and eventually unsupportable valuations of the dotcom era.

Canopy Growth's share increase was directly attributable to market expectations that the federal government would loosen restrictions for medical purposes, and would soon introduce legislation to decriminalize marijuana in Canada. That would increase the size of CGC's market and cash flow. Shareholders were giddy. Then reality intruded. Health Canada actually announced certain restrictions on how much marijuana would be

funded for veterans, the reality of which brought the stock back to a more defensible value. Over the course of a month, roughly \$800,000,000 was ground off CGC's market cap.

This isn't to pick on CGC. It's the largest and likely best known Licenced Producer, so it stands as a good proxy for the industry as a whole. The shares of other LP's and applicants endured similar roller-coaster rides in their respective share prices, for similar reasons.

So what's next on the legal front? With each of *Smith* and *Allard* affirming patient rights, and the new ACMPR regulations reflecting those expanded rights despite international treaties governing the sale of marijuana, investors' sights should be set on the timing of decriminalization.

Note there is a massive difference between the introduction of legislation to decriminalize, and the actual final act of decriminalizing. Decrim will be a slow political process, not an event. There likely will be an uncertain number of years between the introduction of proposed legislation and the final date of enacting the statute.

Even the federal Health Minister, Dr. Jane Philpott, doesn't know. Earlier this month she was specifically asked if marijuana would be fully legal and available in Canada before the next federal election in 2019. She answered, "At this point, I can't give you a specific timeline."

She added, "We need to make sure that there is a strict regulatory process in place and that there are restrictions in terms of access. We also have work to do on the public education front."

It's clear from the rest of her interview the feds aren't in a rush to push the legislation through the system.

In Canada at the federal level, here is how a new statute is created under that system. The process involves many stages

and many different forms of review.

A new bill is first proposed in the House of Commons, usually but not always by the party then in power. That bill is introduced to the House and is deemed to have been given a 'First Reading', almost always without debate. The Second Reading involves a more detailed look at the proposed statute by the House, including a review of the philosophy behind the bill and an overall review of the actual wording used in the bill to express that philosophy. There is public debate at this stage among the members of the House.

After edits, the bill is sent to a Committee of the House for a much more granular examination of the bill, its intents, the precise wording, and the impact it may have on other existing statutes. The Committee can seek the advice of the public and of outside experts, and can make proposed amendments to the bill. This can be a lengthy process.

After the Committee stage, the bill goes back to the House for Third Reading, debate and amendments before a final vote is called on the final wording.

That's halfway through the process. The bill then has to follow the same byzantine routine through three readings and a committee in the Senate. The Senate as a house of sober second thought is supposed to look at the proposed legislation from a less partisan viewpoint.

Assuming the bill makes it all the way through that, it is then submitted to the Governor-General for royal assent and to convert that bill into a law. It is a lengthy process, and will be especially complicated for as sensitive an issue as marijuana.

This timeline has an additional complication, which is the the thorny issue of the Single Convention, a treaty signed by Canada and 180-some other countries governing international marijuana laws. The government has not given any indication

how it intends to escape that treaty.

There will likely be a small market bump in the share prices when the legislation is announced. Some insiders are expecting that announcement to come on April 20, the annual "4-20 day" which is a key part of marijuana culture. That announcement, whenever it is made, has already largely been priced into the market so don't expect a large bump. From then on, expect a multi-year experience as the bill winds its way through readings, committees, and the Senate, and as the share prices bump up and down in response.

Don't overlook the real risk that decrim may take place many years in the future. To protect your investment dollars, find public companies that can survive purely on their respective medical marijuana sales. Their survival should not depend upon near-term legalization of marijuana. If their predicted success is predicated upon an assumption of imminent decriminalization, that is a clear indicator of a weak business plan, a short-term thinking management team, and a flawed risk assessment process. Find the companies that can survive for the next several years purely on medical, and for whom decrim would be a bonus.

If pushed for a favourite, we'd point to CGC, the first and largest of the LP's, and to Aurora Cannabis.