

**INVESTING**



**CANNABIS**

**THE NEXT GREAT  
INVESTMENT OPPORTUNITY**

**DAN AHRENS**

**WILEY**



# Investing in Cannabis



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*The Next Great Investment  
Opportunity*

Dan Ahrens

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# A Note to Readers

**T**he opinions expressed in this book are those of the author alone, not the publisher, and not necessarily those of AdvisorShares Investments, LLC, AdvisorShares Trust, the AdvisorShares Pure Cannabis ETF (NYSE: YOLO), or the AdvisorShares Pure US Cannabis ETF (NYSE: MSOS). Opinions are subject to change, are not guaranteed, and should not be considered a recommendation to buy or sell any security or AdvisorShares Fund. There are risks involved in investing in evolving industries that may be adversely affected by legislative initiatives as well as changes in social and economic conditions, all of which may impact the profitability of companies.



# Preface

A book about investing in cannabis was not even possible just a few short years ago. There wasn't enough to invest in! Publicly traded and exchange-listed cannabis stocks have exploded onto the scene with legalization in Canada and a constantly growing list of locations in the United States. Cannabis includes both medical and recreational adult-use marijuana, but also hemp-based CBD (cannabidiol) and other cannabinoids with a long list of potential uses. Pharmaceutical and biotech companies are just scratching the surface of cannabis-based applications. Marijuana dispensaries are quickly opening all around the United States, Canada, and in countries across the globe. Cannabis based products are everywhere – lotions, oils, beverages, food – wellness products of all types for humans and for pets.

This book will focus of investing in cannabis through publicly traded stocks that are available to everyone. The opportunity is substantial. The new business of cannabis will have great success stories but will also have abysmal failures. As a new industry, the ups and downs will be extreme. A lot of companies won't make

it. Some may be downright fraudulent. We will discuss the state of legalization and name the top cannabis operators in the United States and Canada, in biotech and pharmaceuticals, CBD, and all the other associated businesses. I'll tell you what to look for, and what to avoid.

# Acknowledgments

**T**his book and our cannabis funds would not have been possible without contributions from a great number of people. I would like to thank AdvisorShares CEO Noah Hamman for his ideas and for his drive to get the first cannabis focused, actively managed, exchange-traded fund launched in the United States. And to everyone else at AdvisorShares, thanks for all you do. Managing Director of Distribution James Carl helped with some great data and charts. Thanks to Lynn Brautigan and Mackenzie Peterson in our marketing department for all their constant work on content. Lynn created some nice-looking charts for the book. Investment Consultant Lance Davidson – keep up the great communications. Thanks to our Chief Compliance Officer Stefanie Little. And thank you to Ryan Graham, a Vice President at JConnelly PR, for your good work with the press.

For the launch of my firm's cannabis-related funds, a great many people at partner firms and servicing firms were involved. There are too many to name but include people at trading firms, swap dealers, market makers, authorized participants, legal firms, tax and audit,

and of course the fund distributor, fund administrator, and the stock exchange.

All of the people in various groups at Bank of New York Mellon and BNY Mellon Asset Servicing for Exchange Traded Funds have been great to work with. We've been fund clients of BNY Mellon for more than 10 years and brainstormed with them about cannabis stocks for well over a year before launching our fund. I appreciate their understanding of what's legal and what's not, and how to handle our cannabis investments properly.

The Exchange Traded Products team at the New York Stock Exchange have been great partners and helped us launch dozens of funds quickly and efficiently. They've also helped us get some great ticker symbols.

Our outside counsel at Morgan, Lewis & Bockius LLP have represented AdvisorShares since our founding and always aided us in being an innovative fund company. They are the best in the business of exchange-traded funds.

The team in Global Securities Finance at Cowen Execution Services LLC / Cowen and Company LLC have been instrumental in our fund's investment process and in our access to the US multi-state operators we invest in. Cowen has been an essential firm in North American cannabis expansion.

Thanks to Kevin Harreld, senior acquisitions editor at John Wiley & Sons, for seeking me out and for support all along the way.

Thanks to my beautiful wife, Lana Ahrens. Forced to read a few of the early chapters in development, she claimed that she actually found the book interesting. Owen Ahrens and Arden Ahrens – thank you for being born and for being generally great kids. Keep making those good grades in school.

# Chapter 1

## Like Investing in Alcohol at the End of Prohibition

*“Prohibition has made nothing but trouble.”*

—Al Capone

**O**n December 5, 1933, at 3:32 p.m. local time, Utah became the 36th state (the required three-quarters of the 48 states) to ratify the Twenty-First Amendment to the United States Constitution. Prohibition ended. Only 16 years earlier in 1917, the Eighteenth Amendment had been proposed in Congress to establish a ban on the manufacture, transportation, and sale of “intoxication liquors” in the United States. Circumstances made Prohibition a failure, and the Eighteenth Amendment was the first Constitutional amendment in the history of the United States of America to be repealed. The primary reason – money.

The 1920s (the roaring twenties) were a boom time for the US economy. Life was good. Following victory in World War I, the United States was becoming a true world power. New consumer goods spread into households with the advent of mass production, and the modern automobile and airline industries were born. The US financial system was thriving without the legal sale of alcohol. But the Eighteenth Amendment had actually done little to curb the sale and consumption of liquor. It was simply transported

and sold illegally. It was done with a wink and a nod among many Americans. The Volstead Act (formally named the National Prohibition Act) was a law that became effective on January 17, 1920, to provide enforcement for the Eighteenth Amendment. It created a special enforcement unit of the Treasury Department (Bureau of Prohibition), and formally began Prohibition. For the wealthier, more powerful, or simply “connected” individuals among American society, drinking came easy. It almost turned into a game of enjoying smuggled alcohol and visiting speakeasies. In another interesting side effect of Prohibition, increasingly strong distilled spirits surged in popularity. The appeal of beer and wine was diminished. Distilled spirits were more profitable to produce, cheaper to transport, and easier to smuggle into the country.

Despite policing efforts of the Treasury Department and other law-enforcement agencies, organized crime reaped the real benefits of the illegal alcohol trade. Organized crime flourished. Organized crime became more organized. With America enjoying good fortune in the twenties, many people weren’t concerned with crime – especially crime involving alcohol. Gangsters often became glorified celebrities. Everything was fine until the economy suddenly and violently came crashing down. America’s Great Depression began with the Black Thursday stock market crash of October 24, 1929. The Great Depression happened for a host of reasons. The stock market crash followed a period of gross overconfidence and overproduction of goods. A panic in the stock market sparked a panic at the banks. A weak banking system allowed banks to fail and close. Bankruptcies and job losses snowballed.

While the United States was navigating through the Depression, the federal government desperately needed revenue if it were to help set the economy on a correct path and put jobless Americans back to work. Federal income taxes had only been created a few years earlier with the Sixteenth Amendment of 1913. It was a major shift in the federal government’s revenue system. Prior to creation of the income tax, alcohol taxes had generated as much as 40% of the federal government budget. With Prohibition, the government had quickly become incredibly dependent on income tax as its primary revenue source. The Depression changed that. Incomes suffered



and income taxes suffered. Income tax revenue dropped 60% from 1930 to 1933. The legalization and taxation of alcoholic beverages was an easy target. In the 1932 presidential election, the Governor of New York, Democrat Franklin D. Roosevelt (FDR) campaigned against the financial failures of President Herbert Hoover's administration. The repeal of Prohibition was an important part of Roosevelt's Democratic Party platform. He easily defeated the incumbent Hoover in a landslide victory on Tuesday, November 8, 1932. Just three months later in February of 1933, Congress would propose the Twenty-First Amendment to repeal Prohibition.

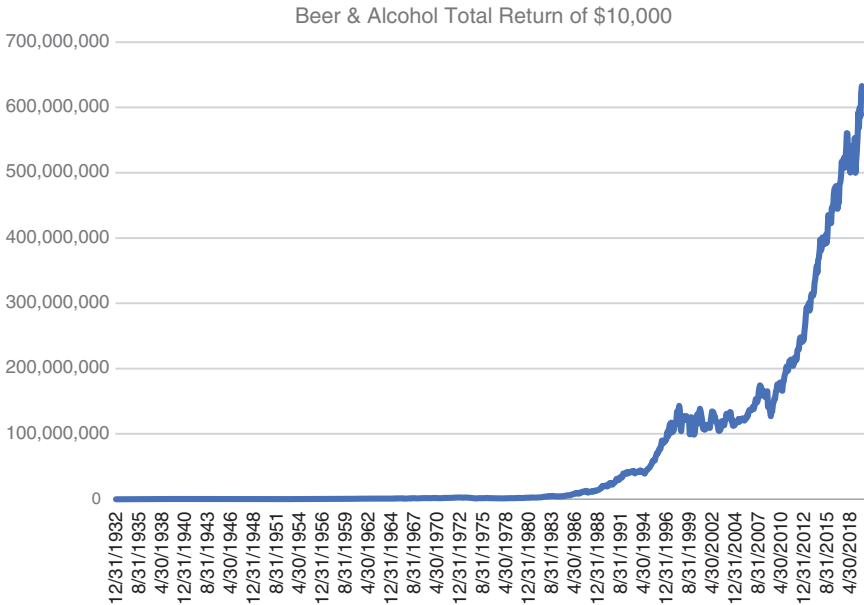
The end of Prohibition was a major financial victory for the federal government. Millions of dollars collected in alcohol taxes helped to finance President Roosevelt's New Deal programs in the years that followed. Alcohol helped to financially heal the country as it slowly recovered from the worldwide economic crisis – the most severe in the history of the industrialized world.

Any long-term investor putting money in a diversified group of alcohol stocks near the end of Prohibition would do very, very well. The performance numbers from 1933, or anywhere around that time, up to the present day, are rather remarkable.

## Time to Buy

Using US publicly traded stock price data from the well-known and publicly available CRSP (Center for Research in Security Prices) library of Dr. Kenneth French, Tuck School of Business at Dartmouth College, we looked at the exchange-listed securities of the US stock market broken down into 30 industry portfolios. Among a myriad of available data points for stock prices and dividends going back to 1926, the database provides monthly investment returns for each industry grouping. We chose to begin in 1933 – the year that Prohibition was repealed in the United States. We're certainly not the first to study this industry data. Numerous case studies have been completed and articles have been written using various timeframes and methods for crunching the data. The results are the same. From the lows of the Great Depression, alcohol stocks outperformed the other industries and outperformed the general market.

## Beer and alcohol total return of \$10,000



Source: AdvisorShares, based on data from the CRSP library of Dr. Kenneth French, December 31, 1932, to December 31, 2019

Admittedly – compounded investment performance over a long period of time (like more than 85 years) can cause a very exaggerated graph. The early years of a long-term compound return chart usually look almost flat. The stock performance of alcohol in the 1930s was anything but flat. It was extremely volatile. But the fact remains that since 1933 alcohol stocks have outperformed other industries such as chemicals, communications, construction, financials, healthcare, oil, and retail. As we started our calculations in 1933, annualized industry performance numbers may look better than expected, but please remember that we’re calculating from a seriously low point in the years following the stock market crash in 1929. Another industry performed almost as well as alcohol. It was tobacco. If you’re thinking of similarities to marijuana or cannabis, you’re right. But there is much more to follow.

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30 industries listed in the CRSP library, annualized  
performance December 31, 1932, through December 31, 2019

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Industry	%
Automobiles and Trucks	11.00
Beer and Alcohol	<b>13.54</b>
Printing and Publishing	9.45
Business Equipment	12.87
Aircraft, Ships, and Railroad Equipment	12.89
Chemicals	11.27
Apparel	11.13
Construction and Construction Materials	10.99
Coal	7.82
Electrical Equipment	12.54
Fabricated Products and Machinery	11.75
Banking, Insurance, Real Estate, Trading	11.65
Food Products	11.85
Recreation	12.57
Healthcare, Medical Equipment, Pharmaceutical Products	12.67
Consumer Goods	11.53
Restaurants, Hotels, Motels	12.66
Precious Metals, non-Metallic, and Industrial Metal Mining	9.02
Petroleum and Natural Gas	11.80
Everything Else: Sanitary, A/C, Irrigation, Cogen	9.46
Business Supplies and Shipping Containers	11.45
Retail	12.48
Personal and Business Services	12.92
Tobacco Products	<b>13.13</b>
Steel Works	8.64
Communication	9.97
Transportation	10.41
Textiles	10.69
Utilities	9.60
Wholesale	12.06

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Source: Performance calculated by AdvisorShares Investments, LLC. Average value weighted returns from monthly performance data from the CRSP library of Dr. Kenneth French.

In October of 2018, an article was published by *Barron's*, “What Alcohol Stocks During Prohibition Say About Marijuana Stocks Today,” by Al Root. The article’s main point was that the value of alcohol stocks dropped after Prohibition was lifted. While factually correct, I feel the premise of the article was all wrong. The article was pointing out that alcohol stocks were a lousy investment in the year that followed the end of Prohibition. Alcohol didn’t automatically go up beginning on December 5, 1933. What the article failed to mention was that alcohol stocks had already gone up more than 350% following Franklin D. Roosevelt’s (FDR’s) presidential victory in November of 1932 and the Twenty-First Amendment being proposed in Congress in February of 1933.

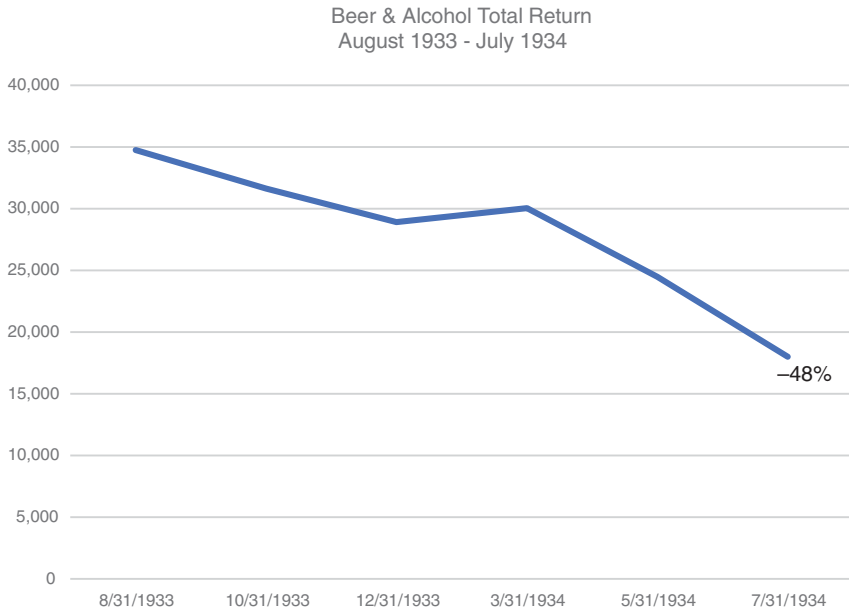


Beer and alcohol total return, February 1933–August 1933  
Source: AdvisorShares, based on data from the CRSP library of  
Dr. Kenneth French.

While alcohol’s manufacture and sale had “only” been illegal for 14 years, it was once again a new industry in the United States that

required hard work to recreate operations and infrastructure – and to replace the alcohol black market that had been operating since 1920. Extreme stock price volatility followed.

From a high point in August of 1933 to a temporary low around July of 1934, alcohol stocks as a group dropped almost 50% in value. As the *Barron's* article described – a poor investment.



Beer and alcohol total return, August 1933–July 1934

Source: AdvisorShares, based on data from the CRSP library of Dr. Kenneth French.

When investing, it's very important to understand the psychology of investing. What makes a stock go up or down? More than anything, it's about supply and demand. When investors have demand for a stock, that demand means there's more buyers than sellers. There's buying pressure. The stock price goes up. I'm pointing this out now because in June or July of 1934 there wasn't any buying pressure on alcohol stocks. After a great run-up following FDR's victory and in anticipation of Prohibition coming to an end, alcohol

stocks turned terrible again. Investors were sellers. Alcohol stocks went down in almost every month over an 11-month period. Some investors may have been selling to lock in their gains from the previous year. Other investors probably thought they were too late and had missed the boat on investing in alcohol stocks.

By October of 1935, alcohol stocks gained almost 100% from the lows in the summer of 1934. What changed? I don't know. Some wise investors must have decided that alcohol was undervalued once again and had the long-term vision to buy at low prices. Once stock prices reversed, other investors joined in. Plenty of ups and downs followed.



Beer and alcohol total return, July 1934–October 1935

Source: AdvisorShares, based on data from the CRSP library of Dr. Kenneth French.

Through truly extreme volatility at the end of alcohol's Prohibition, even the years 1933 through 1935 provided terrific investment performance to early investors.



Beer and alcohol total return of \$10,000, 1933–1935

Source: AdvisorShares, based on data from the CRSP library of Dr. Kenneth French.

While the alcohol industry in the 1930s was highly volatile, in the decades that followed it turned into one of the steadiest, most predictable industries around. The alcohol business is often referred to as recession-proof. People are going to drink no matter what's going on with the economy – no matter what's going on with the stock market. People don't stop drinking when the stock market drops. They may even drink more! The spread of coronavirus (COVID-19) in 2020 isolated people at home and caused a definite spike in alcohol sales across the board. In the longer term, when the economy slows or the overall stock market dips, investors traditionally shift to safer, more predictable investment sectors such as consumer staples – and alcohol.

The health of the alcoholic beverage industry is distinguished by three major characteristics:

### 1. Concentration