

A BVR Special Report

Excerpt from

What It's Worth:

Value and Business Challenges in the Budding Cannabis Industry

Second Edition

BVR
What It's Worth

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Value and Business
Challenges in the
Budding Cannabis Industry

A BVR SPECIAL REPORT



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What It's Worth

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Introduction

The times they are a-changin'.

—Bob Dylan

The estimated annual demand for recreational cannabis now exceeds that for wine, craft beer, and organic food,¹ according to estimates gathered for the *Marijuana Business Factbook 2016*. The vast majority of this \$40 billion to \$45 billion is spent on the black market and so is not taxed.

In the past year, Oregon, Alaska, and Washington, D.C., joined Colorado and the state of Washington in legalizing recreational marijuana. As of the fall of 2016, 25 U.S. states, the District of Columbia, and the territory of Guam allow for comprehensive public medical marijuana and cannabis programs. An additional 17 states allow “low THC” products for medical reasons in limited situations.²

Legal marijuana has become serious business. ArcView Market Research estimates that sales of legal marijuana in 2016 will grow to \$7.1 billion, an increase of 26% over 2015’s \$5.7 billion and \$4.6 billion the year before.³ One analyst, GreenWave Advisors, predicts that, in a scenario in which the momentum toward legality included all states by 2020, U.S. retail marijuana sales could reach \$35 billion.⁴ Alternatively, even if the progression were slower paced, GreenWave expects it to be a \$25 billion industry by 2020.

California, the largest state market and the first to legalize medical marijuana, in 1996, accounted for 49% of U.S. cannabis sales in 2014. That amount will grow exponentially if voters legalize adult

1 Marijuana Business Daily, *Marijuana Business Factbook 2016*, Executive Summary.

2 National Conference of State Legislatures, blog, July 7, 2016. www.ncsl.org/research/health/state-medical-marijuana-laws.aspx.

3 ArcView Market Research, *The State of the Legal Marijuana Markets*, 4th edition, Executive Summary, 2016. www.arcviewmarketresearch.com.

4 GreenWave Advisors, *State of the Emerging Marijuana Industry, Current Trends and Projections*, 2nd edition, Executive Summary, November 2015.

use of marijuana in November 2016. Legal marijuana in Colorado, the first state to allow both adult use (also referred to as “recreational”) and medical marijuana, was a \$996 million industry in 2015, generating \$135 million in tax revenue, licenses, and fees. Big players are emerging, who have warehouses with some 50,000 to 60,000 square feet of plants and 50 employees or more watering the plants and giving them nutrients. These are very much commercial, professionally run operations.

And, as with other businesses, there is real money to fight over when the owners divorce a spouse, dispute a partnership agreement, gift shares, or sell the enterprise. However, in this case, performing an accurate valuation is particularly challenging. The industry’s relatively short history, high level of risk, high volatility, and complex, quickly evolving regulatory structure are unique considerations to which appraisers, business owners, and attorneys must pay attention. Determining the subject company’s proper risk-adjusted discount rate or the valuation multiple to apply to cash flow and EBITDA can be especially problematic. And the ethical or legal issues must be considered since selling marijuana is still considered an illegal activity at the federal level.

Accountants, business appraisers, attorneys, and investors are all paying attention to this booming industry because of the opportunities it provides. The chapters here in *What It’s Worth: Value and Business Challenges in the Budding Cannabis Industry* address the important issues and provide the technical insight that business professionals need when valuing or servicing a marijuana dispensary.

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