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“Legalize it”: The Global Legal Framework on Cannabis and its implications on Recreational Market

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Abstract:

The recreational cannabis market has been under transition from the black market into a legal regulated one. This has been happening due to: an increase in acceptance rates; medical research depicting cannabis as less harmful than alcohol; the economic impact.

Uruguay tried to be a pioneer in legalization, but the over-conservatism created several barriers for trade, causing a lack of legal supply, pushing up the black market, and currently illegally selling a legal product.

Nevertheless, the industry is expected to continue its growth once more data on health issues gets released and once cannabis companies get easier access to credit and a clear road to the market.

Keywords: Legal Framework, Recreational Cannabis, Uruguay, Black Market

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Legal Overview

The recreational market for cannabis has been under the media radar for the past few years. There has been a recent trend of legalizations that makes this market expected to be worth over \$USD 50Bn¹ by 2025. This valuation comes mostly from a cannibalization of the illegal market around the world.

This legalization trend has been driven by higher acceptance rates, due to recent research that has been depicting cannabis as a less harmful² drug when compared with well-accepted ones such as tobacco or alcohol. Nevertheless, it has been a long process because there is no international rule about the subject and each country has been dealing with the topic in different ways, with different legal implications.

Countries have different legal frameworks concerning cannabis (*Figure 1*), and legalization has been experiencing different paces all over the world.

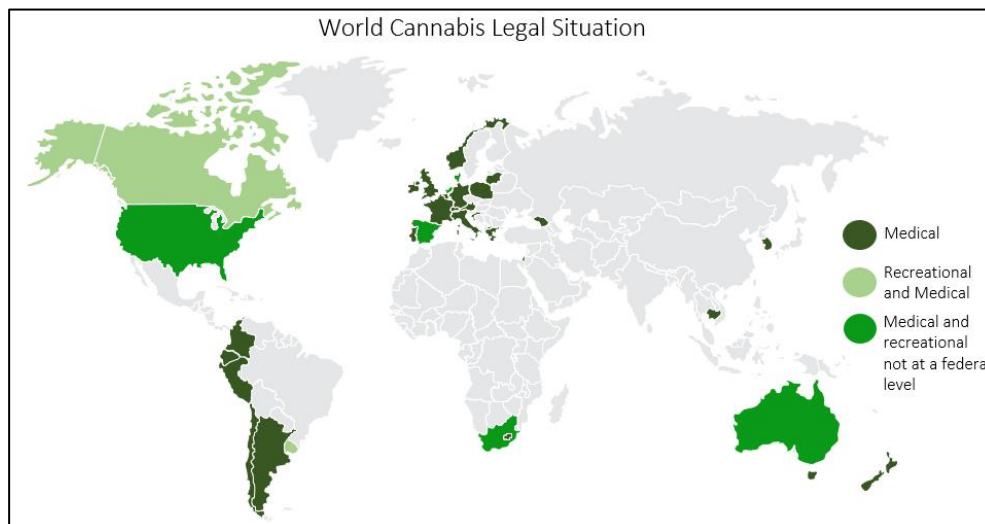


Figure 1: World panorama of cannabis legalizations; Source: Prohibition Partners

Why is the recreational legalization such a hot topic?

First, the acceptance rate.

Cannabis consumers are not the delinquents that society marginalizes anymore³, and nowadays they include CEOs of the world's largest companies (e.g. Elon Musk, Steve Jobs or Bill Gates), popstars (e.g. Miley Cyrus, Rihanna or Madonna), celebrities (Brad Pitt, Paris Hilton or Megan Fox) or even Olympic gold medalists (Michael Phelps).

Therefore, when some of the world's largest influencers are supporting (some of them publicly) the legalization of cannabis for adult use, this automatically brings the topic back into political discussion, since it is not

¹ Sources: Prohibition Partners; Global Cannabis Report; New Frontier Data; Euromonitor; UN ODC

² Source: Batista Leite, Ricardo. Ploeg, Lisa. "The Road towards the Responsible and Safe Legalization of Cannabis Use in Portugal", February 2018, Ata Médica Portuguesa

³ Source: Rolling Stone: "50 Most Successful Marijuana Enthusiasts You Should Know", April 2017

coherent from the governments to “let” so many celebrities do it, while the general population still needs to pay tremendous fines (and depending on the country it can lead to jail or even death penalty). Additionally, with high acceptance rates around the world (especially in Western countries⁴), governments know it is important to start having a position on the topic in order to gain votes.

Second, the health issue.

Although this has been mostly relevant for the boom of the medical segment, it has been important for a change in mentality about recreational consumption.

Despite being seen as a hard drug until the end of the last century, and sometimes put into the same category as heroin, recent R&D and case studies on the subject have been creating a different perspective.

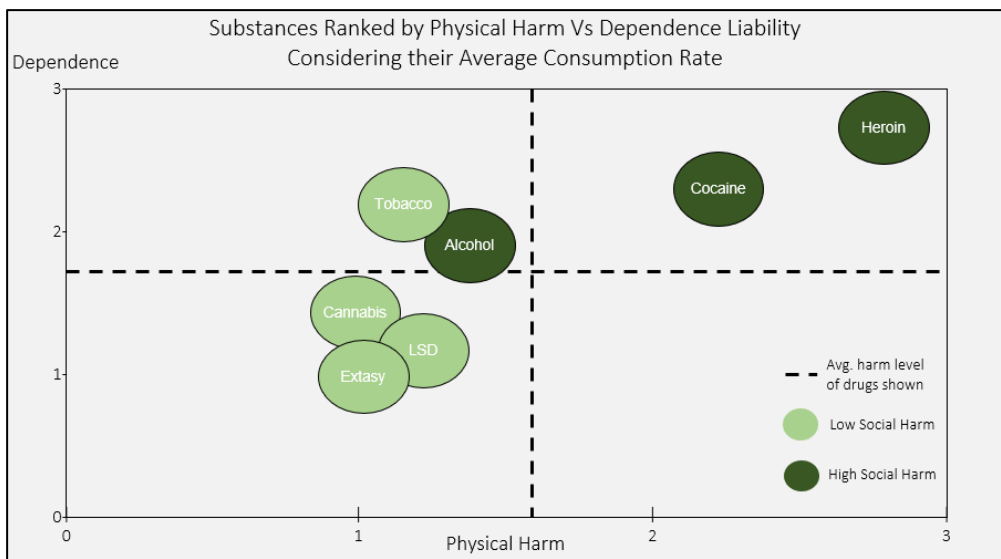


Figure 2: Substances Rank; in a 0-3 scale, where 0 represents no risk and 3 represents the maximum probability of becoming addicted or dying with overdoses; Source: Batista Leite, Ricardo. Ploeg, Lisa. “The Road towards the Responsible and Safe Legalization of Cannabis Use in Portugal”, February 2018, *Ata Médica Portuguesa*, Pages 115-125

As can be seen in *Figure 3* the use of cannabis was found to have less physical harm than socially accepted drugs such as alcohol or tobacco. Additionally, the risk of becoming addicted to marijuana is also considerably smaller when compared to its counterparts.

Adding to the reasons mentioned above, cannabis has been associated with considerable health benefits for people who have a fast-paced lifestyle or those who suffer from chronic diseases such as Parkinson or Multiple Sclerosis. Healing characteristics associated with the components of the plant (both THC and CDB) have been the reason why several doctors, physicians, and lawyers have been bringing the topic into the political agenda, creating a lobby with which the Pharma companies are starting to partner up.

Third, the economic benefits

⁴ The US has an acceptance rate for recreational use above 67%; Source: Forbes, December 2019

As if the previous reasons were not politically relevant enough, there is one last motivation that is making the governments of several countries consider the legalization. Money.

Cannabis represents a close to \$USD 100Bn opportunity that is happening in parallel economy, allowing for illegal groups to make considerable sums of money with mature distribution networks, and paying no taxes on the transactions.

For a government in power to use the people's will (high acceptance rates on the legalization for adult use and strong lobbying starting to appear) to fight the black market, and to still be able to collect taxes, a solid alignment of interests for the legalization wave to continue over the next years is needed. Nevertheless, there are still some risks to bear in mind for investors and implications for companies that are playing in this grey-zone market.

Uruguay Case Study

Uruguay is a global case study⁵ for being the first country in the world to legalize recreational cannabis for people aged 18 or more. The distribution places are regulated by the government as well as the maximum quantities, but once you registered in the national database one is allowed to buy weed in any pharmacy.

But is it really what is happening? Why is Uruguay not a 100% comparable use case to be a precedent on what could happen in other geographies?

The reason is because in Uruguay, cannabis consumption was not exactly liberalized as sold by the media, and there are still several barriers to consumption that distort the conclusions that would be taken from the data outcomes of the six years since legalization, creating statistical problems for the analysis on the impact of legalization of recreational marijuana (e.g. measuring impact on consumption, prices, demand, supply, health, among other variables).

Firstly, there are only three ways of purchasing the product, and distribution different from these ways will be considered illegal:

- i) Consumers can buy it in pharmacies. However, only 17 pharmacies⁶ sell cannabis all over the country, due to the problems with banking regulation (explained in detail below) that are causing a lack of supply.
- ii) Consumers can grow plants at home, but have limits on the number of plants they can have, and need to be registered on IRCCA⁷
- iii) Consumers can be part of a membership club. However, these clubs are strictly regulated, have limited capacity, and impose a limit on consumption.

Secondly, there are strict regulations imposed by the government that are limiting the market:

⁵ Although still a taboo topic when related with recreational use, cannabis cultivations for CBD extraction have been emerging in China. Source: "BBC: "Uruguay: The world's marijuana pioneer", 2019; EIPaís

⁶ Source: BBC: "Uruguay: The world's marijuana pioneer", 2019

⁷ (EN) Institute for Control and Regulation of Cannabis

- i) Concerning prices, every selling point is forced to sell at a fixed price⁸ per gram
- ii) With regards to consumption, it can only be done for those who are enrolled on a national list controlled by the government. Due to the bureaucracies to enroll, the majority of people⁹ is not enrolled, and tourists are also excluded from purchasing cannabis, pushing them to the black market.
- iii) Cannabis cannot be used by other businesses (e.g. a restaurant is not allowed to sell infused drinks or food), limiting the measurement of the real impact on the economy.
- iv) Not all strains are allowed, and only ones with lower THC amounts (around 12%), meaning that higher THC-level products can only be found in the black market

Thirdly, there is a short of supply caused by the lack of access to banks. This happens because several banks are headquartered in foreign countries where cannabis is still not legal (e.g. Spanish bank Santander refused to allow payments to purchase cannabis with its accounts in Uruguay, and the access to credit for companies is also limited), and therefore they preferred to be out of the market until further developments are made in their countries. The consequences were that few pharmacies in Uruguay actually decided to sell marijuana, which creates a lack of supply that will foment black market.

In conclusion, although Uruguay is a case study that should be taken into consideration when other governments decide how they will regulate the market, it is not accurate to make statistical conclusions based on the data provided from this example, because it will be biased from the source.

The restrictions imposed by the government are creating several barriers, increasing the black market (which currently is illegally selling a legal product¹⁰), and not allowing for probably the most important, which is measuring the real impact on consumption after legalization and the consequences on health levels. Therefore, although Uruguay should be studied by governments and official entities, other case studies should be considered (e.g. California policies¹¹, despite the lack of sufficient years of relevant data, will be another case study to take into consideration), to reach the best possible outcome for society.

Main Risks and Possible Implications

Health issues

The legalization spree can face some barriers due to the diseases that high-THC cannabis consumption might potentiate. It is known that consumption of cannabis with THC levels over 10% (in the Netherlands or London it is not uncommon to see 25% THC weed) can increase the risk of psychosis¹².

⁸ All distributors were imposed a selling price around 5€ per gram

⁹ Around 45K enrolled in 3.8M inhabitants. Source: Prohibition Partners

¹⁰ Similar to what happens in lower value-added industries in “rich countries” (e.g. mechanics, hairdresser) where payments are often done in cash to avoid taxes.

¹¹ Has a more liberal approach where cannabis was taken similarly to what legally happens with beer or wine

¹² Source: German Institute for Medical Cannabis

Therefore, although it is a drug usually announced as less harmful when compared with more accepted drugs such as alcohol or tobacco, cannabis is still a psychedelic drug that acts on the endocannabinoid system about which there is still not enough information and study cases to measure the impacts on human health. The major problem is that people buy their weed on the black market, not knowing what they are smoking. In other words, it is like going for a beer with friends and ending up drinking Vodka cups with a similar flavor. Although this is something that good regulation can avoid (e.g. proper product labeling with its characteristics), it is still a concern to bear in mind, especially because it has a strong impact on the social image the cannabis industry is trying to convey.

Access to Credit

The fact that cannabis is still not legal at a federal level in the majority of countries where banks are headquartered is creating problems¹³ for companies to have access to credit. Therefore, the growth of the cannabis industry has been fueled by equity issuances from companies, creating a problem of dilution of older investors, and pushing away possible future investors.

Regulatory measures are being developed to try to ease this situation, but faster developments need to be carried out for the market to have enough credibility and create liquidity for companies and interested parties.

Road to Market

Finally, and probably the most important aspect to take into consideration, is the way cannabis will be sold. One of the major concerns of the governments debating on the topic is to avoid making the same mistake they did when the same questions were raised regarding the alcohol industry. Nowadays, it is not uncommon to see kids buying alcohol in normal supermarkets, meaning that the legislation for the responsible use of that drug was not well thought though, having the severe public consequences that alcohol is responsible for around the world.

Therefore, the preferable model under discussion for the recreational cannabis distribution is the same as some countries (e.g. Sweden, Australia, Finland, among others) adopted for alcohol beverages¹⁴. The idea with cannabis was to create a place where consumers would go and be able to choose from a wide variety of products, all of them properly labeled with the components and major effects it can cause (similar to what was done in some states in the US).

In conclusion, several initiatives have been undertaken in the industry regarding regulatory frameworks and there is a higher propensity to discuss the topic at an international level. However, this process is expected to take time due to some uncertainties about the right model to use and the remaining lack of sufficient relevant data that is necessary for governments to make decisions. Therefore, the next years will be important to shape the international position with regards to cannabis, where pioneer countries will be used as case studies to allow for that discussion.

¹³ E.g. Due to a lack of access to credit in the US, Aurora is financing its growth based on equity issuances, which is creating a problem of dilution, pushing away several investors

¹⁴ Alcohol products need to be purchased in stores especially created for that reason