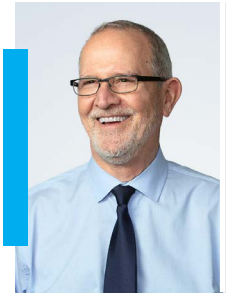
Cannabis advisory newsletter

What's up with Michigan's cannabis market? A 10,000-foot perspective

By Robert A. Hendricks



THIS MONTH'S FEATURE: ROBERT "BOB" HENDRICKS

Robert "Bob" Hendricks is Senior Counsel at Warner Norcross + Judd. Bob represents growers, retailers, processors, labs and secure transporters who directly participate in marijuana enterprises in Michigan, as well as those businesses that provide ancillary goods and services to the industry. As new growth and distribution systems are established and continue to expand, Bob helps clients smoothly navigate the process in accordance with Michigan's legal and regulatory framework.

The first commercial medical marijuana license under the Medical Marijuana Facilities Licensing Act was issued by LARA in July 2018 followed by an adult use recreational license 18 months later. The licensed and regulated cannabis market just celebrated its fourth birthday — so it's still a toddler. It's not surprising to see dramatic changes in that market. Below are a few observations on where we are, why we may be here and what the future may look like.

PRICE COMPRESSION. According to the monthly statistical report[1] issued by the Michigan Cannabis Regulatory Agency (CRA) for June 2022, the average retail price of an ounce of cannabis flower was $112 for medical and $122 for recreational. A year ago, the average price was over 40% higher or $209 per ounce. And two years ago, in June 2020, the average retail price of an ounce of cannabis flower was $512.05[2] for recreational and $276.37 for medical. What happened?

SUPPLY GLUT. Plant numbers, and potentially flower supply, exploded by five times over the past 24 months. In June 2020, based on the total number of cultivation licenses (medical and recreational) issued by CRA, the maximum number of plants that could be legally grown was 500,000. Two years later, that maximum number had increased fivefold to 2,500,000. Also in June 2020, the maximum plants for medical licenses was almost twice the number for recreational (330,500 for medical, 169,500 for rec). By June 2022, recreational plant numbers far exceeded medical[3] (1,500,000 to 990,000).

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Assuming an average of four harvest cycles per year (based on indoor cultivation) and four ounces of flower per harvested plant, the current maximum plant count could yield 1,250,000 pounds of flower semiannually.[4] But according to the CRA sales statistics for the first half of 2022, total sales for both medical and recreational flower January to June 2022 were about 225,000 pounds. In other words, the potential supply of flower exceeded actual sales by more than five times.

BLACK MARKET? And that's not all. Anecdotal observations from a variety of sources suggest that at least some meaningful percentage of the product available in Michigan (including flower, resin, distillate and other derivatives) is produced here by unlicensed cultivators/processors or is illegally moving into Michigan from high-production states like California, Washington and Oregon. Certainly, the vast majority of licensees holding the almost 3,000 CRA-issued licenses are careful to ensure their operations are fully compliant with CRA regulations, which obviously prohibit both the purchase and sale of product that has not passed through the licensed process. Licensees have invested far too much money, time and effort to risk their licenses. But as prices compress and cash flow falls to a trickle, the temptation to accept a bargain price for "unlicensed" product can increase.

CONSUMER CONFIDENCE. Consumers of licensed cannabis are said to distrust elements of the industry. A recent news report[5] examining the accuracy of THC content as listed on product labels concludes that some cannabis consumers are losing faith in testing laboratories and the state of Michigan's regulator. Part of the promised value of a legal state marketplace for cannabis was to increase the reliability and safety of cannabis products. Those factors can help drive out untested and unreliable black market products. But if consumers don't believe in the reliability and safety components of licensed products, then price will become the only driver. Ultimately, science and

compliance with reasonable regulatory requirements should support the reliability question. The sooner, the better.

THE GOOD NEWS. Against this backdrop of troubling developments, there is also much to celebrate. As laid out monthly in CRA's statistical reporting, the first six months of 2022 saw retail sales of licensed medical and recreational cannabis exceed $1 billion. Assuming steady to increasing consumer demand (which certainly is borne out in the historical sales figures), sales of licensed, tested and legal state cannabis in Michigan could exceed $2.1 billion this year. Just four years ago, that sales figure was zero. Despite supply and demand imbalances, price compression, and alleged black market interference, every indication is this market is here to stay.

Nationally, the push for state legalization of cannabis continues. Presently, 19 of the 50 states have adopted adult use legalization and 39 have legalized medical marijuana use.[6] While federal repeal of marijuana prohibition remains elusive, more and more U.S. representatives and senators are willing to talk about, and in some cases vote for, normalization at the federal level. Regression of cannabis legalization seems very unlikely.

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Public approval of the repeal of cannabis prohibition has been strong in Michigan since voters approved the Michigan Medical Marijuana Act in 2008 by more than 60%. Local governmental approval also seems to be increasing. The number of cities, villages and townships authorizing cannabis commercial activity in their jurisdictions increased by about 5% for medical and 15% for adult use cannabis in the last 12 months. Perhaps the 2022 $160 million excise tax (some of which becomes directly available to opting-in municipalities) will continue to attract more municipalities to adopt authorizing ordinances supporting commercial cannabis in their jurisdictions.

The unprecedented experiment by many individual states in the United States to repeal marijuana prohibition, despite refusal by the federal government, appears generally to be succeeding. The "sky is falling" predictions made in the early years do not seem to have come to pass. Certainly, future refinements are necessary. But from my perspective, most participants are glad our state moved in this direction.

About the author: Robert A. Hendricks is senior counsel at Warner Norcross + Judd LLP with four decades of commercial law experience. He has been cultivating a state-level leadership role and a prominent practice in the area of legal cannabis commerce since 2013. He can be reached at rhendricks@wnj.com.

Sources:

[1]https://www.michigan.gov/cra/resources/cannabis-regulatory-agency-licensing-reports/marijuana-regulatory-agency-statistical-report

[2]In the CRA June 2020 report, two values were provided, the mean and the median. Generally, the mean is closer to the "average," and is the number used in this article.

[3]Because some of the medical class C licenses are in place to support recreational "excess grower" licenses, it is likely that some of the medical Class C's are not actually planted.

[4]This is a conservative estimate. Some indoor growers say they can produce up to 8 oz. per plant, and outdoor plants typically produce even more.

[5]Super potent weed spurs distrust in Michigan marijuana industry. https://www.mlive.com/public-interest/2022/06/super-potent-weed-spurs-distrust-in-michigan-marijuana-industry.html

[6]https://mjbizdaily.com/map-of-us-marijuana-legalization-by-state/

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