Cannabis mutual fund looks to ride the sector's waves

StoneCastle Cannabis Growth Fund launches Sept. 14

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With cannabis legalization a month away, Canadian investors looking to get into the space will have a new mutual fund option.

Launching Sept. 14, the StoneCastle Cannabis Growth Fund is looking to benefit from the increased interest in the sector as recreational marijuana becomes legal across Canada on Oct. 17.

Bruce Campbell, portfolio manager at StoneCastle Investment Management, describes it as the first open-end Canadian mutual fund focused on cannabis. There are already ETFs in the space, some of them actively managed, as well as mutual funds with a medical focus with exposure to the pot sector.

Spartan Fund Management is the portfolio manager and StoneCastle is the fund's sub-advisor.

The fund will contain a mix of companies tied to cannabis, from licensed producers (LPs) to distributers and equipment makers, Campbell said. It's targeting a 60-40 Canada-U.S. split, with a maximum 50% of net asset value invested in foreign securities. On the Canadian side, LPs will make up roughly 80% of holdings, Campbell said, while the U.S. side will be more diverse.

Canadian companies like Smiths Falls, Ont.-based Canopy, which last month received a $5-billion investment from alcohol maker Constellation Brands, have the opportunity to be global players after their early exposure to a regulated recreational market, Campbell said.

"I truly believe there are going to be some Canadian companies that are leaders in the space because of their early execution here in Canada and their access to capital," he said.

In addition to Canopy, Canadian cannabis producers in the fund include Organigram, Hexo and CannTrust, while other holdings include Scott's Miracle-Gro, which produces lighting used for growing cannabis.

Producers will eventually make up a smaller portion of the overall portfolio, Campbell said, as cannabis evolves into "more of a branded consumer packaged goods type of product." Companies that produce solvents used in extraction, that buy and lease production facilities, and that produce the packaging will emerge as players in the space.

Campbell said the fund's active management is appropriate in a sector known for its swings. The fund's risk rating is high.

"It tends to have these big waves where it can be 100% up and 50% down. We'll be active to manage that process—we'll be fully invested on the way up, we'll be less than fully invested on the way down," he said.

"If we start to see some sort of change in the makeup of the market, at that point in time we'll raise cash to preserve capital and wait for the next cycle."

The approach will also allow the fund to respond to new opportunities in the U.S. and globally as they appear, he said.

The management fee for the Series A fund is 2%, with Spartan paying a 1% trailing commission to firms. There is a sales charge of up to 5% of the amount invested.

The Series D fee is 1.25%, with trailing commissions of 0.25% to the discount broker. The Series F fee is 1%.