

2020

Special Edition

Pot of gold:

How to invest in cannabis industries in 2020
in partnership with MMJ Group Holdings Limited (MMJ)

Switzer Financial Group



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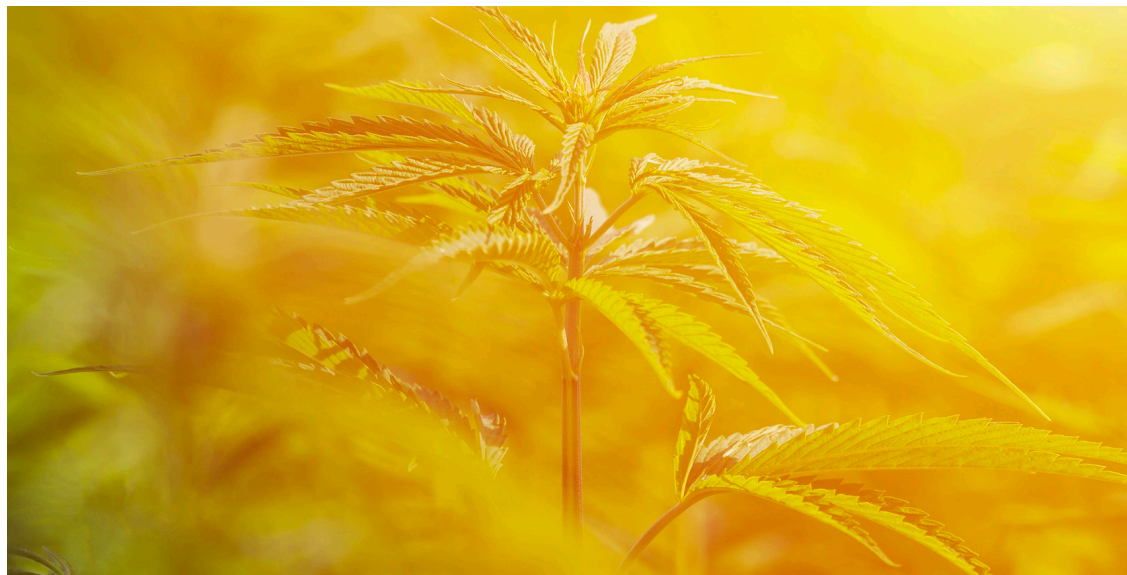
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What are 'pot' stocks?

by Sophia Katsinas



Put simply, pot stocks are publicly listed companies whose products all stem from the marijuana plant. Most products are divided into two main branches: medical marijuana and recreational marijuana. There is technically no major difference between the two, aside from the intent of use, but recreational marijuana tends to have a higher concentrate of THC - which gives 'the high'.

In regards to marijuana stocks, there are three primary categories: growers, biotechs and supply providers.

Growers are the ones who create the product and directly distribute it to consumers. Canada has seen the most noteworthy success story of a grower company, with Canopy Growth Corporation listing on the Toronto Stock Exchange in 2014. In just 3 years, the company grew to a market cap of \$1.1 billion, and this was before marijuana was recreationally legalised in Canada. Due to its popularity, Canopy Growth Corporation

has partnered with big companies like Constellation Brands (parent company of Corona, Svedka etc.) who are their biggest shareholder and plan to experiment with cannabis-infused drinks.

Biotechs are another form of 'pot stock', which are the biotech companies who develop the chemical components of marijuana, known as cannabinoids. They are mostly responsible for developing drugs for medicinal use during cancer treatments and more. Many biotechs may develop synthetic versions of these chemicals, but are still categorized as 'pot stocks'.

The third form of 'pot stock' is supply providers, which are companies that support marijuana growers by providing them with a number of resources, whether it be packaging, management, lighting systems, fertilizers, etc. These companies have nothing to do with the marijuana side of things, but provide growers with necessary supplies, which makes them a 'pot stock'.



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What is the legal position?

by Sophia Katsinas



Australia's laws surrounding cannabis use are quite hazy. At a federal level, cannabis is under the category of "illegal drugs". Though, on 29 February 2016, the federal government passed the Narcotic Drugs Amendment Act 2016, which amended the Narcotic Drugs Act 1967 to "enable applications for licences and permits for the cultivation, production and manufacture of medicinal cannabis products," as stated on the Australian Government Department of Health's Office of Drug Control (ODC) website.

The types of medicinal cannabis that are currently legal under federal law are strictly available to specific patient groups under medical supervision, and regulated under the Therapeutic Goods Administration's (TGA) Special Access Scheme (SAS). Medicinal cannabis can only be supplied by a medical professional to patients who fit a very specific category.

There are three types of licences relating to the supply of medicinal cannabis products available:

- medicinal cannabis licence authorising cultivation or production or both
- cannabis research licence authorising similar process for research purposes
- manufacturing licence authorising the manufacture of a drug or product.



Though, each state and territory also has its own legislation regarding cannabis use, and as of 31 January 2020, the ACT changed its stance. The ACT Police made it clear that “cannabis is not legal in the ACT, amendments have been made which exempt individuals from criminal liability in certain circumstances”.

Adults over 18 in the ACT can now:

- possess up to 50 grams of dried cannabis or up to 150 grams of fresh cannabis
- grow up to two cannabis plants at your home per person, with a maximum of four plants per household.

Though it is still an offence to:

- smoke or use cannabis in a public place
- expose a child or young person to cannabis smoke

“Medical cannabis is currently legal under federal law but are strictly available to specific patient groups.”

- store cannabis where children can reach it
- grow cannabis using hydroponics or artificial cultivation
- grow cannabis plants where they can be accessed by the public.

- to sell, share or give cannabis as a gift to another person

- for people aged under 18 to grow, have, or use cannabis

- to drive with any amount of cannabis in your system.

In Australia, cannabis use grew from 9.8% in 2013 to 14.5% in 2016, according to the Australian Institute of Health and Welfare.

What is happening overseas?

by Sophia Katsinas

Canada has acted as a world leader in 'pot stocks', with their consumer demand growing since cannabis became legalised in 2018.

“The marijuana market in the US should surpass \$70 billion by 2027.”

The U.S. market is also growing rapidly. According to Grand View Research, the legal marijuana market in the U.S. should surpass \$70 billion by 2027. According to analysts at Cowen Washington Research Group, they predict federal legalisation will occur by 2027, which could skyrocket 'pot stocks' into a \$100 billion market. They are not the only ones with such strong predictions of growth. New York-based investment bank Jefferies Group LLC, predicts that the global cannabis industry could be worth up to \$130 billion by 2029.

Policy around cannabis legalisation is contentious in the US, as it is one of the most solid disparities between Republicans and Democrats. Though, with nine states and the District of Columbia legalising marijuana, an additional fifteen states decriminalising it, and thirty-three states in total legalising medical marijuana, around 2/3 of Americans believe marijuana use should be legal, according to a study by Pew Research Center.



How high can pot stocks go?

by Sophia Katsinas

To bring it back to what's relevant for you, the main thing we want to focus on when investing is; what does this mean for growth?

In 2019, research by medical marijuana company, Cannvalate, suggested Australia "has the gastest-growing market for medicinal cannabis globally in terms of percentage month-on-month growth".

Ultimately, marijuana is still illegal in Australia at the federal level. There are only a handful of Australian companies with licences to grow cannabis, and most Australian marijuana companies listed on the ASX pursue medical marijuana products.

As legislation eased in Canada and the United States, the price and demand of 'pot stocks' also increased. Though, as is often the case when stocks are overhyped, cannabis stocks suffered a sharp correction in price in 2019.

But, as David Borum from Zack's reported on Nasdaq.com, in March 2020, "the marijuana industry is far from dead". The industry is in better shape today, and because of last year's threat there are a number of strong companies available to invest in at a significantly lower price than they were trading a year ago.



Q&A with Michael Curtis

Non-Executive Director, MMJ



1. Can you please give us a brief overview and history of MMJ?

MMJ GROUP HOLDINGS LIMITED (MMJ) is the only listed investment company offering Australians the opportunity to invest in unlisted, and listed, cannabis-related businesses locally and offshore. MMJ invests in cannabis related businesses in Australia and globally, which has created several international opportunities across the global market.

All MMJ shareholders have the opportunity to acquire new shares at 50% discount to the book value of our investments at no brokerage cost. These investment valuations are recent and already reflect the downturn in the Canadian cannabis investment market.

Harvest One Cannabis, one of MMJ's oldest investments has announced a strategic review, which would consider sale of assets and achieve positive cashflow. In addition, MMJ's highly experienced Board and Management Team (located in Australia and Canada), have extensive hands-on operational experience, strategic partnership development and cannabis expertise in Australia and worldwide.

In July 2019, MMJ appointed Canadian based Embark Ventures as its asset manager. EBv is headed by myself, Michael Curtis. I co-founded Dosecann along with Greg Boone and sold the company to Cannabis Wheaton for CAD38 million - MMJ generated a realised return of 2.3 times its investment in Dosecann. I also co-founded Embark Health, which is set to become one of the largest extraction companies in Canada. MMJ has generated a return of 2 times its investment in Embark Health. Investment returns in the past five years have generated a Multiple on Invested Capital ("MOIC") of 1.3 times capital invested

MMJ is a globally diversified cannabis company with multi-country presence to take advantage of new opportunities as they arise. MMJ is able to provide its shareholders with prospective higher returns from unlisted investments which subsequently publicly list.



“MMJ is the only listed investment company offering Australians the opportunity to invest in cannabis-related business, locally & offshore.”

2. Why is MMJ raising capital through a share purchase plan?

MMJ believes that the adverse market and industry sentiment created in the past six months surrounding cannabis companies has created opportunities to invest in listed, and unlisted, Canadian cannabis businesses at attractive valuations.

MMJ is continually invited to invest funds into the global cannabis market in line with its investment mandate, and believes that it is in the best interests of shareholders to raise equity funds so that MMJ can have improved flexibility to participate in such investment opportunities.

Proceeds from the share purchase plan (SPP) have a primary intention to:

1. Provide the company with additional funds to invest in the attractive global medicinal and recreational cannabis and hemp market, with a particular focus on listed and unlisted Canadian Cannabis businesses. There is a favourable market backdrop with the majority of Canadian listed cannabis producers' valuations reducing last year, which now creates opportunities for additional investments for the MMJ portfolio.
2. Allow the company to increase its flexibility to make follow-on investments in current portfolio companies, it will also allow them to manage the timing of exit for its existing investments. MMJ has identified opportunities to invest additional funds into existing businesses eg, Sequoya Cannabis (based in Europe), Embark Health and Medipharm Labs through exercise of options to acquire more shares at attractive valuations.
3. In addition to opportunities to invest into new businesses in the global cannabis market in line with MMJ's investment mandate. MMJ also holds warrants (similar to 'options' in Australia) and contractual rights in a number of its existing listed and unlisted investments, which provide opportunities for MMJ to make follow-on investments in businesses at a discount to current valuations, and where MMJ is well placed to understand their potential returns.
4. We believe that an SPP is the fairest and most efficient means of raising equity, where our eligible shareholders will be offered the first opportunity to invest up to \$30,000 in the company, at a 50% discount to the the book value of our investments at no brokerage cost. These investment valuations are recent and already reflect the downturn in Canadian cannabis investment market.



3. What does your current investment portfolio consist of?

MMJ has created a significant number of investment opportunities across the international private cannabis investment market. These opportunities have been sourced on the following criteria that MMJ believes will determine who will be the successful cannabis companies:

1. Well Capitalised
2. Possess Low Cost Production or Process
3. Focus on high value/high margin (Extraction, Branded retail, etc)

MMJ has invested AUD \$74 million in cannabis business investments since 2015, for a total return of 1.3 times capital invested (MOIC).

Some of MMJ's biggest investments to date are:

1. Building the largest cannabis oil extraction business in Canada, with facilities in British Columbia and Ontario
2. Currently planning to go public by end of Q2/2020
3. To date MMJ has generated a return of 2 times its investment in Embark Health
MMJ's investment in Embark Health has generated a return of 2 times on current valuation with a prospective listing on CSE anticipated to occur in the first half of 2020.

MMJ has executed Canadian asset sales which have generated significant returns on investment:

1. Dosecann - 2.3 times MOIC
2. Medipharm LABS - 4.3 times MOIC (MMJ retains residual investment)
3. Fire and Flower - 1.6 times MOIC

The key investments in the MMJ portfolio are:

1. **WeedMD**

- Acquired in September 2019 - well capitalised name with recent CAD25 million investment from major Canadian pension fund
- Very low cost of production with outdoor grow and expansion space with a cannabis oil extraction facility

2. **Sequoia Cannabis**

- Poland based extraction company which has built a facility in record time since our initial investment in July 2019
- Sequoia has also achieved EU GMP certification for their facility which is based in Krakow, Poland
- Now focusing on processing biomass and selling CBD isolate and extracts Europe wide

3. **Harvest One**

- MMJ has held an interest in HVT businesses as a result of vending businesses owned by MMJ to HVT in 2017
- Exceptionally well-regarded branded products such as Royal High and vast distribution network through Shoppers Drug Mart, Holland & Barrett and Dreamwater, etc.
- MMJ has a strong position secured against HVT's assets:
 - o 26% equity ownership
 - o Secured first ranking charge over all HVT's physical assets through CAD2m secured loan
- In February 2020, HVT advised that it is undertaking a strategic review of the business to ensure that all available alternatives for the company are being evaluated to maximize value for its shareholders
- HVT confirmed in March 2020 that it is achieving its cost reduction targets, sold surplus assets and expects strong growth in operating cashflows in current quarter
- The return from Harvest One (HVT) has been MMJ's only materially unsatisfactory return - unrealised loss of 50% of investment (included in current NAV)

4. **Bespoke (BCAC)**

- Seeking to become global branded cannabis and CBD business in Europe and North America
- Global brand strategy focussed on low cost cultivation and extraction in federally legal frameworks
- BCAC team led by Paul Walsh, former CEO of Diageo pls, the world's largest spirits company, has strong track record in management of consumer products





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