Alternative Health Fund

August 2019 Commentary

Investment Team

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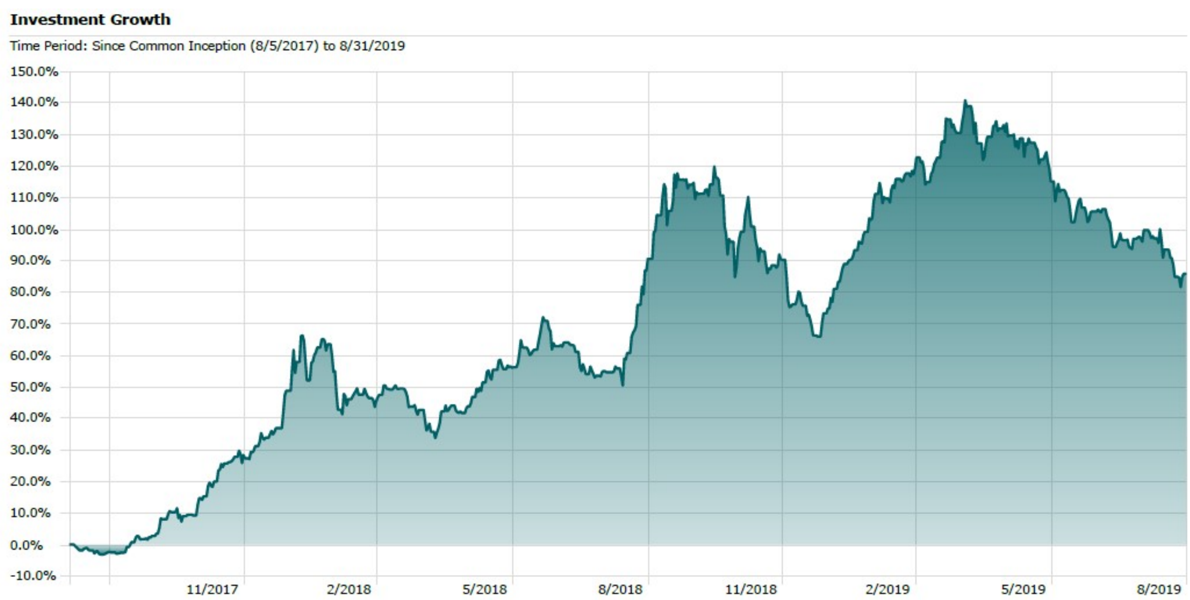
With a risk-off sentiment in the overall market during the summer months stock performance was particularly weak in the cannabis sector. In addition to the overall market cautious stance, the cannabis sector was weighed down by regulatory concerns and senior management shake ups at two of Canada's larger Licensed Producers. These periods of weakness demonstrate that having an actively managed approach can help investors proactively avoid some of the downside. During the month of August the Fund was down -5.19% relative to the HMMJ that was -12.75% for the month. These weak periods are challenging but should be viewed in relation to the longer term growth of capital that has been achieved in the Fund and the incredible investment opportunity unfolding as the cannabis industry grows and matures.. Relative to the passive strategy of HMMJ, we are holding on to gains, reducing volatility, with better risk adjusted returns.



Source: Morningstar

It's important to note as many clients have asked us about **Canntrust** - we sold **TRST** in April after disappointing quarterly results, selling the majority of our position in the $10/share range, long before the July 8 announcements about Health Canada discovering illegal grow rooms. The stock now trades in the $2 range. Another preventative measure was how we treated our **Canopy Growth (WEED/CGC)** position early in July after the departure of CEO Bruce Linton. We thought that further downside with disappointing quarterly results were on the way. We were well ahead of the carnage that affected the broader market. WEED dropped approximately 40 percent from early July to August end. Those are just some of the benefits of active management.

With our awareness that the equity markets were not positive on cannabis companies, rather than re-deploy some previous large positions, we increased our cash weighting, as well as adding to non cannabis names. One health and fitness company that catches investors' attention is **Planet Fitness (PLNT)**. Traded on NYSE, with fitness centres providing a variety of training services across North America has had 8 quarters of double digit earnings growth, with the stock practically doubling since we established our position in the Spring of 2018.

We have also "shortened our bench" in terms of the leading US and Cdn cannabis names we own, ones that are achieving bottom line results rather than growing just for growth sake. In terms of weighting, 60% of our cannabis weighting in the Fund are US based operations (listed on the CSE). We will discuss our key names below in the Financials Section.

Outlook for the Remainder of the Year

We continue to believe that the fall will bring stronger stock performance in the sector, particularly for the US MSO's. Resolution of the HSR Reviews (US Anti-Trust Legislation) should act as an important catalyst as positive resolution to one or two of the earlier M&A transactions will signal that the remaining gridlocked deals would be able to close. Passage of legislation such as the SAFE Act should also benefit the sector as it would reduce compliance costs and help the companies reduce their cost of capital due to better banking access.

On the Canadian side, we believe that there will be greater interest in the sector as the second phase of legalization gets closer and the market focuses more on the opportunity for Cannabis 2.0 products. We believe our key Canadian names are positioned well to compete in this evolving marketplace.

US Regulatory:

With the passing of the Farm Bill, clarity for better access to markets is also happening with the Drug Enforcement Administration (DEA) announcing that hemp (including hemp plants and CBD with less than 0.3% THC) are no longer a controlled substance and a DEA registration is not required to grow or research it. The Farm Bill of 2018 had taken a major step forward for CBD having it excluded from the Controlled Substances Act, however, the DEA previously did not affirm the legality of hemp, therefore resulting in some confusion about the plant's legal status

The SAFE Act – We see short term catalysts for US Multi-State Operators (MSO's) as legislators on Capital Hill consider hemp and cannabis legislation with respect to some type of combined federal legislation on banking with the approval of the Republican controlled Senate. Keeping in mind that Republican Majority Leader Mitch McConnell is the Senior Senator from Kentucky and that state is at the centre of hemp cultivation in the US, it is not surprising there is a desire to make access to banking and finance easier for hemp farmers. The Farm Bill was intended to allow hemp farmers to operate nationally, yet operations are being constrained by a lack of understanding on how to deal with hemp as there is no effective road map for hemp farmers to deal with FDIC financial institutions. Without a roadmap, the current lack of clarity may force Republicans in Congress to pass legislation. Going into an election year, we believe that with 33 states already operating legal medical markets, there is popular support for this type of legislation.

Cdn Company Financial Results:

The month of August had several Top Ten Fund holdings reporting quarterly results. Our team was pleased with our key holdings as all company results surprised to the upside. We would highlight

Village Farms (VFF) and **MediPharm (LABS).**

Village Farms (VFF) reported strong Q2/19 results as overall produce sales including both its traditional vegetable business as well as its cannabis business lines totalled US$41.3 million while earnings per share improved to US$0.20. EBITDA improved to US$4.6 million overall for VFF, including the strong contribution from its cannabis business in Canada, the Pure Sunfarms JV generating CAD$12.6 million for VFF.

The Pure SunFarms JV which is the 1.3 million sq ft cultivation facility in Delta BC (VFF owns 50%) generated revenue of CAD$32.4 million, up from CAD$14 million in the previous quarter. The PSF JV generated the 3rd highest quarterly net revenue among all Canadian LPs only behind **WEED** and **Aurora Cannabis (ACB).** Gross margin was 84%, COGS/gram decreased by roughly half QoQ to C$0.65/gram. EBITDA margin was 78% resulting in PSF generated $25.2 million of EBITDA (VFF gets 50% of that).

The majority of revenue during the quarter consisted of wholesale cannabis oil through the company's private label program. 95% of revenue generated during the quarter was derived from five external customers with each customer representing more than 10% of total revenue.

MediPharm Labs (LABS) released strong Q2 financial results, the fourth highest reported quarterly revenue amongst Canadian cannabis companies. Q2/19 revenue was $31.5 million, up 43% QoQ and above consensus of $27 million. Cannabis oil and bulk concentrate sales accounted for 98.6% of revenue in the quarter, with the balance coming from tolling and other sources. The company's Q2/19 gross margin was36%, up from 31% in the prior quarter while adjusted EBITDA was $7.7 million, up from $4.3 million in Q1, beating consensus estimates of $4.5 million.

As many investors are aware, there are very few Cdn producers in the cannabis industry that are producing bottom line positive results. In choppy markets, we believe that owning the most profitable names will weather the storm.

US Company Financial Results

The quarterly financial results from many of the US MSO's was markedly different than that of the majority of Canadian LP's that struggle for positive cash flow. With the lack of profitability seen from most Cdn LP's we continue to orient our cannabis allocation to US names as the path to profitability, the larger addressable market, the ability to brand and market products allow the MSO's to build value and build market share in a profitable manner. We focus our report on two of our largest holdings, that are generating strong growth and positive cash flow as they increase their footprint across the US.

Curaleaf (CURA) Q2/19 net sales for Q2/19 came in at $48.5m, up 38% QoQ, and in line with consensus of $49m. EBITDA of $3.3m, well ahead of consensus of $0.4m, and a Q1 loss of –$3.7m. Q2 proforma revenues including revenues from pending M&A transactions is approx. $440 million annualized, ~40% higher than its next closest MSO peer.

CURA's Q2 EBITDA gain was driven by sales growth in FL where we estimate it maintains the #2 mkt position after TRUL; NJ where it continues as the market leader; and AZ where it is in #2 position after HARV. Important in generating its cash flow is improving operating leverage with SG&A up 4% QoQ while revenues were up 38%. The operating platform for the national roll-out of this company is beginning to generate scale efficiencies, without major additional capital to sustain growth going forward, which could generate solid future margin potential. If we include the stores from announced M&A deals pending, Curaleaf has ~70 retail locations open today in ~19 states with the ability to expand its retail presence to 131 dispensaries nationwide.

The company initiated 2020 proforma guidance, with revenues of $1b–1.2b, representing the highest revenue outlook issued to date, which we note excludes REC contributions from IL where Grassroots is headquartered and will be opening 5 additional locations ahead of new competition as per the adult use laws which favour incumbents. Revenue guidance is bolstered by CURA's pending acquisitions (GR and Select) with significant capacity expansion, increasing production from 1.3m sq.ft. in 2019 to 2.3m sq.ft. in 2020. CURA's guidance for proforma EBITDA margin above 30% in 2020.

Green Thumb Industries (GTII) also announced Q2 results that beat analyst estimates driving higher net revenues and stronger cash flows as the company continues to grow through effective license application management, select acquisitions and focussed retail expansion. Revenues in Q2 came in at $44.7 million easily beating analyst estimates of $39 million while adjusted operating EBITDA was $5.0M also beating analyst estimates of $0.2 million. Increased capacity utilization and stronger pricing for premium product lines brought gross margins up to 54.6%. Retail revenue from its RISE brand of stores improved 60% QoQ relative to Q1/19 while revenues from wholesale distribution grew 70% QoQ supporting growth of its business in MA, ILL and PA. Same stores sales improved 50% for stores open during Q2/18 and improved 27% for newer stores that were open during Q1/19. For near term growth, in its conference call reiterated its goal with respect to its retail buildout target finishing 2019 with 35-40 stores across its platform. The company now has 31 stores open including those from its recently completed license acquired in New York, with total licenses across the GTII platform allowing for an aggregate of 95 dispensaries.

Option Strategy:

During August the Fund continued using its option strategy to enhance risk adjusted returns. With the above average volatility in the cannabis sector, we are able to generate significant option premium, while lowering the overall volatility of the Fund relative to its underlying benchmark.

Since inception of the option writing program in September 2018, the Fund has generated significant income from option premium of over $2 million. We will continue to utilize our option program to look for attractive opportunities given the above average volatility in the sector as we strongly believe that option writing can continue to add incremental value going forward.

During the month we used our option strategy to assist in rebalancing the portfolio in favor of names we prefer while generating approximately $145,000 in option income. During the month, we were able to write cash secured puts out of the money at strike prices that offered opportunities to increase our exposure, (at more attractive prices), to names already in the Fund including **GW Pharma (GWPH), Procter and Gamble (PG)** and VFF. We continue to write covered calls and strangles on names we feel are range bound near term and from which we could receive above average premiums. Examples of such trades include **PLNT** and **Aphria (APHA)** with covered calls on APHA having been especially rewarding.

We currently have a range bound view on **APHA.** On August 13th APHA was trading at USD $6.92 and we wrote a 10 day covered call by selling an aggressive August 23rd expiry at the volatility level of 69% with strike price USD$7.00 and earning USD$0.25. That equates to a strike yield of 3.57% for 10 days outstanding or the equivalent of 131% for a year. The breakeven for being assigned would be USD$7.25 or 4.78% higher than the reference point when the trade was placed. APHA had reported its Q2 results on August 1st and had appreciated nicely on the news. We took this opportunity to capture some additional upside by selling some high priced calls. On August 23rd APHA ended trading out of the money at USD $6.56 whereby we were able to roll the contract forward and sell additional calls capturing further upside potential.

Charles Taerk & Douglas Waterson
Portfolio Team
Ninepoint Alternative Health Fund

Compounded Returns[1]

	1MTH	YTD	3MTH	6MTH	1YR	INCEPTION
FUND	-5.7	6.3	-13.6	-15.2	-2.5	34.9
INDEX	-8.1	1.9	-13.3	-19.5	-19.1	14.5

Statistical Analysis

	FUND	INDEX
Cumulative Returns	85.9%	32.1%
Standard Deviation	31.5	33.9
Sharpe Ratio	1.1	0.4

[1] All returns and fund details are a) based on Series F units; b) net of fees; c) annualized if period is greater than one year; d) as at August 31, 2019. The index is 70% Thomson Reuters Canada Health Care Total Return Index and 30% Thomson Reuters United States Healthcare Total Return Index and is computed by Ninepoint Partners LP based on publicly available index information.

The Fund is generally exposed to the following risks. See the prospectus of the Fund for a description of these risks: Cannabis sector risk • Currency risk • Cybersecurity risk • Derivatives risk • Exchange traded fund risk • Foreign investment risk • Inflation risk • Market risk • Regulatory risk • Securities lending, repurchase and reverse repurchase transactions risk • Series risk • Specific issuer risk • Sub-adviser risk • Tax risk

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