Ninepoint-UIT Alternative Health Fund

July 2018 Commentary

Investment Team

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The month of July witnessed continued enthusiasm in the cannabis sector as investors realized profits in names that have done well since the early Spring. Some investors may perceive challenges with some of the larger provinces and the pace of the roll out of the Recreational market in certain cities and regions. The concern for some is that the roll out may not go as planned and could have a near term impact on revenues in H2/18 and perhaps H1/19. Uncertainty in the Province of Ontario has increased with speculation surrounding the upcoming decision by Premier Ford as he may announce changes to the proposed provincial distribution model. Allowing the private sector to operate independent licensed cannabis stores while the government controls distribution and manages online sales, would mirror the Alberta model, which will allow for privately run cannabis stores to sell marijuana with licences granted by its liquor and gaming commission. If adopted in Ontario, that model will accelerate the number of locations and reach the Federal Government's goal of creating convenience and regulated supply in order to reduce the reliance on the illicit market over time.

During the month, two of the larger provinces announced supply agreements for the non-medical market. In early July, the Alberta Gaming, Liquor & Cannabis Commission announced that it had agreements with 13 cannabis producers for supply for an initial six month period. On July 13th, British Columbia announced supply arrangements through its Liquor Distribution Branch (LDB) with 31 licensed producers of non-medical cannabis to offer a variety of products. Both provinces have adopted a mix of policy framework allowing independent stores with centralized government distribution. Still the questions on the minds of many investors are, will the stores be ready; will there be products available, and will the pricing be competitive.

In the early months of the recreational roll out it is anticipated that given current production capacity there will likely be a near-term shortage of cannabis and related extract in Canada that should support the per-gram price. Over time, the question is whether Canada will face oversupply as has been seen in certain US states? We note a key difference between our federal legislation and the early states that adopted legalization such as Washington and Oregon. In the US, supply is captive to individual state markets, where one cannot cross state lines nor distribute internationally. Canadian producers have both an ability to ship between provinces as well as the opportunity for global medical distribution, finding new markets for products beyond our borders reducing the reliance on domestic demand. In addition as more innovative products are developed the amount of plants required to produce extracts and oils leads to further demand for dried flower, resulting in continued buoyancy in the market for raw materials. At a point in time, we will reach equilibrium pricing and that is where the most efficient producers will stand out. Our focus is on selecting those companies that operate most efficiently, to be able to withstand the pricing pressure that may occur.

Two of our top ten holdings announced quarterly results during July, Aphria (TSX:APH) and Ogranigram (TSXV:OGI) . APH reported Q4FY18 revenues of $12 million, which were higher than consensus estimates of $11 million driven mainly from higher selling prices per gram at $9.16. In addition, cash costs of production that include cultivation costs and excludes packaging and amortization costs came in at $0.95, consistent with last quarter. Despite higher revenues and cost controls that are among Canadian industry leaders, APH reported negative EBITDA for the first time in 10 quarters due to investments in international operations which generated a negative adjusted EBITDA of $2.8m. As APH continues to expand its operations in legal markets, there are additional costs to operations that will be earned back in future quarters. Despite challenges with establishing international operations, APH was able to generate positive cash flow from domestic operations with adjusted EBITDA of $2.2m. Management of APH believes that the potential for international revenue growth is significant, an assessment we agree with. However, a period of investment will be required to capitalize on the opportunity. We continue to hold APH and accumulate on significant weakness maintaining our preferred weighting in the portfolio.

OGI announced its fiscal Q3 FY18 financial report with record net sales for both the three-months and nine-months ended May 31, 2018 of $3.7 million and $10.1 million. Of note for OGI was record sale volume of cannabis oil for the three-months ended May 31, 2018 (768,400 milliliters) up 39% from Q2/18 (552,250) and up 452% from Q3/17 (139,200milliliters). In addition, OGI came in with an industry leading low cost of cultivation per gram of dried flower of $0.80 per gram “all-in” which includes direct labour and depreciation. The company also reported net income of $2.8 million in the quarter, an increase of 162% compared to $1.1 million in Q2-2018 and a loss of $2.3 million in Q3-2017. Operational milestones supporting OGI’s growth in the quarter includes; current annual production capacity of 36,000kg; becoming a Licensed Dealer and obtaining a permit to export cannabis for global medical markets, with its first shipment to Australia completed subsequent to quarter end. We continue to accumulate OGI in our portfolio.

It is important that as investors consider the upcoming domestic recreational market that they also consider the longer term global medical opportunities that are open to leading Canadian producers. The global market is emerging with many countries legalizing for medical purposes. A recent study by Energias Market Research that analyzed global demand for medical marijuana was released mid-month that suggests the global medical marijuana market is expected to increase from US $8.3 billion in 2017, to US $28 billion by 2024, growing at a CAGR of 19.1% from 2018 to 2024. The global medical marijuana market is growing through innovative dosage formats, and unique formulations, not smokables, focussed in the treatment of various ailments. The study suggests that key factors assisting the global market are growing awareness of the benefits of alternative treatments and the growing number of clinical trials underway across institutions around the world.

Given the various views on both the domestic recreational market and global medical market, the cannabis sector continues to maintain a higher than average volatility rating, symbolic of an early stage sector where there isn’t wide research coverage. This is where we believe that our Fund stands out. We offer an actively managed approach that also offers a wider portfolio allocation than merely focussing only in the cannabis sector. With different segments in the global alternative health market, our strategy also allows the Fund to build periodic cash weightings when there are periods of weakness, enabling our team to adjust our positions and wait for a better opportunity. In addition, we offer the opportunity to invest in select private companies in the alternative health

space that are poised to go public in the near term.

For the month, the Canadian cannabis index represented by HMMJ, provided a negative return to investors of (9.91%), relative to the actively managed Ninepoint-UIT Alternative Health Fund that returned (2.86%) for the month. Year to date to the end of July, HMMJ has returned (14.58%) vs the Ninepoint-UIT Alternative Health Fund that is +4.00%, outperformance of +18.34% in favour of Ninepoint-UIT Alternative Health Fund.

In a tougher month for the cannabis sector, we are able to draw on our wider portfolio allocation to provide growth while reducing volatility. Although some of our leading cannabis names were down during the month; such as OGI -6.7%, APH -3%, Canopy Growth (TSX:WEED) (NYSE:CGC) -11% and CannTrust (TSX:TRST) -13%; we gained performance from our pharma sector weights with names such as Celgene (NASD:CELG) +13% for the month; Pfizer (NYSE:PFE) +10%, Johnson & Johnson (NYSE:JNJ)at +9%, Merck (NYSE:MRK) at +9%. In addition, the Fund had positive contributions from Enwave Corporation (TSXV:ENW)+3.2% and Pinnacle Foods (NYSE:PF) +2.1% for the month.

Since inception in March of 2017, we offer better risk adjusted returns than the passive strategy, with a standard deviation of 22 relative to the passive index strategy that has a standard deviation at 54.

Temporary market weakness allow the Fund to build a cash position and enter new names that offer attractive valuation opportunities. Many catalysts are on the horizon and we continue to see solid returns for the alternative health space in the coming months and years.

Until next month,

The Alternative Health Fund Team

Compounded Returns[1]

	1MTH	YTD	3MTH	6MTH	1YR	INCEPTION
FUND	-5.11	3.78	7.77	-0.36	52.9	32.50
INDEX	-4.5	2.7	10.1	1.3	36.8	29.48

[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 July 31, 2018. 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

investing in the Funds. Please read the prospectus carefully before investing. The indicated rate of return for series F shares of the Fund for the period ended July 31, 2018 is based on the historical annual compounded total return including changes in share value and reinvestment of all distributions and does not take into account sales, redemption, distribution or optional charges or income taxes payable by any unitholder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. The information contained herein does not constitute an offer or solicitation by anyone in the United States or in any other jurisdiction in which such an offer or solicitation is not authorized or to any person to whom it is unlawful to make such an offer or solicitation. Prospective investors who are not resident in Canada should contact their financial advisor to determine whether securities of the Fund may be lawfully sold in their jurisdiction.

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