Ninepoint Alternative Health Fund

2019 Outlook

As we look back on the performance of the North American cannabis sector in 2018, we see many periods of abrupt market change. During the year, there were four periods of more than 25% growth while there were also three periods of more than 25% declines. The sector has weakened considerably into year end (to Dec 21) down 39% from its most recent peak November 7th. That weakness has been driven by a number of industry specific factors as well as macro-economic and geo-political factors that have affected global equity markets.

Investment Team

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However, this weak ending to the year should not cause investors to lose sight of the remarkable developments in the sector over the past year. We believe that 2018 will be looked back upon as a turning point for the global cannabis industry. It was a year that saw more than 20 countries legalize medical marijuana (bringing the total to 40); a NASDAQ IPO for a Canadian cannabis company; passage of the Farm Bill legalizing hemp federally in the U.S, with 10 U.S. states and the District of Columbia establishing cannabis legalization for adult recreational usage.

Leading companies within industries affected by the growth of cannabis usage became more active during the year. Constellation Brands (STZ), with its $5 billion investment into Canopy Growth (WEED) demonstrated the interest of big alcohol, while tobacco giant Altria Group (MO) made a $2.4 billion investment into Cronos Group (CRON), and global pharma company Sandoz signed a global JV with Tilray (TLRY) for the development of non-smokable cannabis based medications.

Our thematic view for 2019 is that these trends continue. We believe that more countries will move to legalize medical marijuana, additional U.S. states will legalize adult use, and there will be additional strategic investments and joint ventures from alcohol, tobacco, and pharmaceutical companies. We also believe that scientific development including formulation, genetics, dosage, delivery, and alternatives to traditional cultivation will become more important.

As the new year begins, our Canadian cannabis weighting has been reduced, particularly our exposure to pure cultivation. We have greater focus on those companies that offer value added products, oils, extracts, gel caps and other dosage formats generate higher margins.

The logistical challenges faced in the early days of the recreational roll out are going to remain an overhang for some Canadian LP's for at least the next two quarters as the roll out of stores, SKU's and customer traffic have all been affected. Many investors did not anticipate the challenges faced between LPs and the provinces, and that has led to reduced market sentiment in the final weeks of the year. It will be interesting to see how LP's address the Supply/Demand imbalance; the store rollout, the ramp up of supply and the build out of their brands in Canada.

Health Canada released draft guidelines for the production, distribution and sale of vaping products

and edibles in late December. Edibles and vaping products are scheduled for release in October of 2019 so the government has provided these guidelines well in advance which should allow for a smoother roll-out. As edibles continue to grow in variety and demand, the category will become a significant component of the adult recreational market, and progress towards their introduction into the Canadian market is an important step for the overall success of the cannabis market. U.S. states with adult use legislation have seen significant demand for vape pens, edibles, topical creams and beverages. We believe that it will be important for the Federal government to bring these products into the market in 2019. It will be important from a revenue generation standpoint both for government tax revenue as well as for LP revenue and earnings as these products are all higher value added and higher margin SKU's. It will also be important from the standpoint of reducing reliance on the black market as products that are in demand, in convenient locations and offered without supply limits will mean a flourishing industry.

There are some challenges ahead for Canadian LPs including managing a successful ramp up in production while containing operating costs. We continue to prefer Canadian names such as Organigram Holidngs (OGI), Hexo Corp (HEXO), CannTrust Holdings (TRST) that have lower cost operations and continue to ramp up production on schedule. OGI has supply contracts with 9 of the 10 provinces, Quebec being the only exclusion. It also continues to be the lowest cost producer in the country and continues to add more indoor cultivation (36,000kg of current annual capacity building to 62,000kg by April /19). HEXO has the strongest presence in Quebec with a long term 5-year contract, the only LP to have such an agreement. HEXO is expected to have 100,000 kgs of annual capacity in early Q1/19. Given that the Quebec population is roughly 34% of the country, it is estimated that HEXO will have 9% of the national market. TRST, a pharmaceutically focussed LP continues to be the Canadian industry leader in patient growth, and percentage of revenues generated from extracts at 61% of overall revenues, positioning it well as a value added producer with higher margins.

Getting facilities up to full capacity will be important to deal with supply shortages currently hampering the industry. We believe that increasingly, LP's will be judged by their ability to meet previously announced projections, revenue growth expectations and increased cash flows. As we saw in November with calendar Q3 results, investors are losing patience with those companies that continue to disappoint.

Branding is important and will be a focus in 2019 as more stores and more SKUs are rolled out in the recreational market. The first weeks of the Rec market witnessed people buying without awareness of brand, more for the experiment of purchasing in the legal market. As time goes on, consumers will be influenced by brands and benefits. The winning LP's will be those that can communicate effectively in this highly regulated Canadian market.

Although the causes for supply shortfalls have been shared between LP's and provincial governments, another key challenge for the Canadian Rec roll out will be how provinces work together to create a more uniform set of policies and procedures that the LP's can work within. Having a national framework means having one set of overall rules and we would prefer to see a stronger central government take a leadership role in defining how the Rec market grows from this point forward. Having one set of rules will lead to more efficient operations, better product readiness and more SKU's available throughout the country.

A key theme from foreign markets in 2019 will be the opening of new medical markets. Over the last 24 months, the world has gone from 10 countries to 40 countries, representing an addressable

market of over 1.2 billion people, that now have some form of cannabis medical legalization. We believe that as more research is undertaken, more countries will legalize for medical purposes. That is a significant opportunity for leading Canadian companies to continue to expand their global footprint.

As mentioned above, there were significant strategic investments from 2018 that are important for global expansion of Canadian LP's in 2019 and beyond. The $5 billion strategic investment from Constellation Brands (STZ) into Canopy Growth WEED in August gives WEED a war-chest for growth and product development as the company looks to expand into new markets with new products around the world. In early December Altria (MO), one of America's largest tobacco producers announced a $2.4 billion strategic investment into Cronos Group (CRON) that will assist CRON in its global expansion plans. Later in December MO then acquired a 35% interest in Juul for $12 billion US. Juul is one of the largest e-cigarette (vape) companies in the world and can have significant implications for CRON as it develops vaporizers and other effective delivery methods for its products. MO is becoming a major player in the global cannabis industry through these investments.

Also in December, Tilray (TLRY) entered into two major collaborative agreements. First, the LP signed an extension to its existing agreement to collaborate with Sandoz AG, a global leader in generic pharmaceuticals (part of Novartis AG), developing non-smokable/non-combustible medical cannabis products for global distribution. This was followed by another announcement by TLRY, this time with AB InBev (BUD), one of the world's largest brewers to research non-alcohol beverages containing tetrahydrocannabinol (THC) and cannabidiol (CBD). We believe the TLRY/BUD partnership is also noteworthy in that it validates the opportunity launched last summer by HEXO-V with Molson Coors (TAP-N). It also confirms our previously communicated view that these partnerships with pharmaceutical, alcohol and tobacco companies represent major catalysts for the global cannabis industry. With WEED, CRON, TLRY and HEXO with established global players, companies like TRST, OGI could be next in line as candidates for global strategic arrangements. Overall we anticipate more global expansion plans being announced by Cdn LP's in order maintain their leadership in the global cannabis industry. Early expansion in the global market when US competition is still precluded from operating, allows Canadian LP's to establish a solid global footprint well ahead of future competition.

We believe in the global medical market and the long-term growth of that segment of the cannabis industry. Part of the global growth is the progressive legalization that is taking place in the United States. We have increased our weighting in the portfolio of US Multi-Sate Operators (MSO's) in legal medical states. There are now 32 states that are legal for medical and 10 States plus Washington DC that are legal for Rec. All together that represents approximately 70% of the US population. Despite limitations at the federal level, these markets are operating effectively with leading operators generating significant revenues and growing cash flows.

In 2019, we believe there will be further regulatory enhancements that will benefit investors in U.S. MSO's. At the national level, the 2018 Farm Bill, passed by Congress on December 12, 2018, and signed into law by President Trump on December 20, 2018, includes Section 10113 titled "Hemp Production," which removes hemp from the Controlled Substances Act, placing federal regulatory authority of hemp with the USDA, and allows state departments of agriculture to file hemp programs plans and regulate hemp cultivation per their state specific programs. Already, many legal dispensaries market CBD creams, oils, beverages and medicines. National legalization further opens CBD to more markets allowing MSO's to cultivate, brand and distribute more diverse product offerings. We believe Stanley Brothers (CWEB) one of the largest hemp producers in the US

and a top ten fund holding, famous for its Charlotte's Web line of CBD products will take advantage of these regulatory changes. Canadian LP's that have advantages in legalized US hemp cultivation include Village Farms (VFF) with its 5.5 million sq ft Texas vegetable greenhouse facility that can be converted to hemp in less than 9 months and WEED, that recently purchased Ebbu, a Colorado based hemp research and cultivation company.

Another interesting dynamic taking place in the US is the changing landscape of those states that are legal for medical purposes adding recreational legalization. State governments and Governors have watched the significant tax revenue collection in early adoption states such as Colorado, Nevada and Oregon where tax revenues have reached hundreds of millions of dollars in annual tax revenue collection from cannabis retail sales. Increasingly we believe that more states will adopt recreational laws as neighbouring states offer recreational access, potentially taking tax revenues away from their coffers. By example, a review of the northeast sees Massachusetts , Vermont, and Maine all recreational, forcing neighbouring states to adjust or lose potential tax revenue gains. If current trends continue, it is likely that sometime in the next 2 years, a majority of the U.S. population will live in states that have legalized recreational use of cannabis.

Given these state level trends, we also believe that The STATEs Act has the potential to be another major catalyst. The focus of the Act is to allow federally regulated banks to provide services to legal cannabis businesses, while also normalizing the tax treatment of certain expenses on cannabis business income statements. Also important is a goal to make legal state-run cannabis retailers exempt from federal prosecution.

We see that NY Governor Cuomo has stated he intends to legalize for recreational purposes with NJ, PA and other north east states joining. In the mid-west, MI has voted to legalize for recreational adult usage and we anticipate that IL will move forward with newly elected Governor Pritzker publicly stating his preference for recreational legalization. These changes offer larger opportunities for incumbent US MSO's operating in various medical state markets, with early brand recognition and dispensary locations established. Larger MSO's that are of interest include Curaleaf (CURA), Harvest Health & Recreation (HARV), and Green Thumb Industries (GTII).

Overall, we believe that 2019 will be a positive year for the industry. However, companies in the sector are going to need to execute and show improved financial performance. We believe that there will be significant differences in stock performance based on important metrics like sales price, market share, EBITDA, and for those pursuing it, results from international sales.

The cannabis sector continues to maintain a higher than average level of volatility, 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 that are poised to go public in the near term.

Our long-term view has not changed. This industry continues to have the potential to create major disruption in the beverage, pharmaceutical as well as health and wellness categories. Active and agile portfolio positioning will be key to successfully navigating these challenges while benefitting from this longer term industry opportunity.

Charles Taerk & Douglas Waterson
Portfolio Team
Ninepoint Alternative Health Fund

Compounded Returns[1]

	1MTH	YTD	3MTH	6MTH	1YR	INCEPTION
FUND	-1.9	27.9	-0.2	21.9	48.2	62.6
INDEX	-1.2	11.8	-8.8	8.5	27.3	37.5

[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 November 30, 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.

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