Ninepoint Alternative Health Fund

January 2019 Commentary

Investment Team

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The first month of the year was strong across most equity market sectors and cannabis sector names witnessed significant turnarounds from Q418. Top holdings in the fund erased Q4 weakness with names such as Canopy Growth (WEED)+74% in the month erasing its Q4 performance -37.5%; Hexo (HEXO) +53% vs Q4 of -42%; and Organigram Holdings (OGI) +52% in Jan vs -28% in Q4 while Village Farms International (VFF) +65.8% in Jan. Our US focused names also saw rebounds with Green Thumb Industries (GTII) 37%; Curaleaf (CURA) up 31% and Stanley Brothers (CWEB) +42.6%. The fund also saw strong performance from non-cannabis entries such as UnitedHealth Group Inc (UNH) rising 8.4%.

Our positioning in the cannabis sector favours US exposure at this time, with various Canadian LP's facing production ramp up uncertainties and developing regulations on edibles and other recreational products for October of this year. In addition, given the limited number of physical dispensaries, the first half of this year will see subdued revenue and earnings generation as many LP's are still working on cost efficiencies without distribution strong enough to generate meaningful bottom line results.

Despite the challenges faced by many of the country's LP's, one of our top ten holdings, Organigram Holdings Inc (OGI), announced very strong quarterly results that surpassed expectations. OGI is the first LP to generate positive EBITDA following the onset of the recreational market. Q1FY19 results for the period up to and including November 30, 2018, noteworthy as it included the impact of revenue from adult-use recreational cannabis for part of the quarter. Q1FY19 revenues came-in at $14.5m, up 350% QoQ, above consensus estimates of $13.9m, with $11.1 million of revenues coming from the recreational market. Most importantly, OGI continues to have the lowest cash costs from cultivation of all publicly listed LP's at $0.56/g resulting in OGI gross margin rising to 71%, with EBITDA margin of 40% or $5.0 million in Q1, well above consensus estimates of $0.2million. The difference vs consensus comes from healthier gross margins and continued discipline on SG&A expenses. With more than $90mmillion of inventory at quarter end, the company anticipates that its top line for Q2FY19 will be at least twice as high as its Q1FY19. During the month of January, our position in OGI was up 52%.

A review of January announcements from two of the larger Canadian LP's, quarterly results are challenged by some near term realities. On Jan 8th, Aurora Cannabis (ACB) issued guidance for Q2FY19 that includes financial results for the period up to November 30 2018, with revenues of $50m-$55 million, lower than consensus estimates of $75 million. In addition, ACB expects that the road to positive EBITDA will only occur in Q4FY19, later than originally expected. Two primary areas that are requiring ACB management to reduce expectations on the company's ability to reach positive EBITDA this fiscal year. First the logistics challenges faced by all LP's working with provincial

regulators that have slowed down the number of physical dispensaries. Second, slower than anticipated production ramp-up to its stated run-rate of 150,000 kg's of annual capacity reduces ACB's ability to fulfil provincial supply agreements from internally grown cannabis supply.

Similar weak results were also announced when Aphria Inc. (APHA) reported Q2FY19 results (up to and including November 30, 2018). Revenues in the quarter amounted to $25 million, up 85% QoQ but below consensus estimates of $29 million. As this is the first quarterly period to include sales from the Recreational market, it was instructive to see how the major LP's were able to operate. The EBITDA loss for the quarter was -$9.5M, including a -$6.1M loss from Canadian operations. The market was anticipating EBITDA consensus of approximately $1.2 million. Despite the quarterly results it is important to note two positive aspects to the company's operations. First, APHA exited the quarter with cash on its Balance Sheet of $185 million. Important in the near term is the expansions of Aphria One (Leamington) that is complete and awaiting Health Canada approval. Annualized capacity will be increasing from current capacity of 35,000kg to over 100,000kg anticipated during the next quarter while expanding to over 255,000 kgs by the end of calendar 2019.

Overshadowing the financial results was the announcement that CEO Vic Neufeld and Co-Founder Cole Cacciavillani will be stepping down from their operational roles at the company, working with the new Chairman of the Board, Irwin Simon on a smooth transition from the company. This can be seen as a result of the issues arising from the short sellers report that was released in early December involving the company's LATAM acquisitions. Announced changes to the Management team and Board of Directors serves to help stabilize the company's share value as minority shareholders would see improved governance. While we believe that more needs to be done on the governance side, we welcome these first steps.

An area that is becoming a significant part of the global medical market is the cannabidiol (CBD) market. CBD can be extracted from cannabis plants as well as from hemp plants. In the United States, hemp has been de-regulated, removed from the Controlled Substances Act with the passing of the 2018 Farm Bill in December. Hemp is legal federally in the US, however cultivation and production licenses rest with individual States. Passage of the Farm Bill allows Canadian LP's to enter the US market through hemp cultivation and distribution producing CBD, establishing their brands in the large US health and wellness market. First mover into the US was Canopy Growth (WEED) that was granted a licence by New York State to process and produce hemp. WEED intends to invest between $100 million USD and $150 million USD in its New York operations, capable of producing tons of hemp extract on an annual basis. For the month, WEED had a significant run, with its share price appreciating significantly after that announcement.

Another major announcement related to the burgeoning CBD market was from Tilray (TLRY) signing a global revenue sharing agreement with Authentic Brands Group to develop and market consumer CBD brands. Authentic Brands Group (ABG), is an owner of a portfolio of global lifestyle and entertainment brands, such as Tapout, Judith Leiber, Juicy Couture, Airwalk, Aéropostale, Nine West, Marilyn Monroe, Muhammad Ali and Elvis Presley. The two companies announced that they have signed a long-term revenue sharing agreement to market and distribute a portfolio of consumer cannabis products within ABG's portfolio in jurisdictions where regulations permit. Under the terms of the agreement. Tilray will initially pay ABG US$100 million and up to US$250 million in cash and securities, subject to the achievement of certain commercial and/or regulatory milestones. In return, TLRY will have the right to receive up to 49% of the net revenue from CBD products bearing ABG brands.

At the close of 2018, the U.S. Surgeon General Jerome Adams made a bold move, and called on the U.S. government to rethink marijuana's classification as a Schedule I substance. While the Surgeon General did not go so far as to condone legalization for recreational use, he did say that medically, marijuana should be studied like any other pain relief drug and that both health and criminal justice policies need to be re-examined as they pertain to cannabis drug classification. While the Surgeon General is right in his position on medical research, the move would serve other purposes as well. The change he proposed could be significant for US economic reasons as well. The current U.S. classification of marijuana inhibits research for medical advancements that include cannabis and cannabinoids. As a result, the U.S. is falling behind in both its knowledge base and its ability to finance new global opportunities. Not only are countries such as Israel leading in medical innovations and research, but Canada has become the leader in capital markets activities financing these global medical opportunities. In the latter six months of 2018, Canada's capital markets became the home for many US multi-state cannabis operations flocking to Canadian exchanges, as they have been unable to secure a public listing in the United States.

Progressive legislative changes continue to happen in the US with President Trump's nominee for Attorney General. William Barr, made headlines early in January during his Senate confirmation hearing with his pledge not to interfere with legal marijuana companies that comply with state laws. This is in stark contrast to the previous Attorney General Jeff Sessions who last January stated his disagreement with legislative changes vowing to shut down legal state run cannabis companies.

Finally in international developments, the Israeli government has approved exports of medical cannabis. Licenses will be granted by the Health Ministry and will require police approval. It estimated that the country could earn approximately $1.09 billion per year from such exports. There are currently eight companies cultivating cannabis for medical purposes in Israel, and many more have applied for approval to commence work in the sector.

During January, the Fund continued using its option strategy to generate option premium while lowering the overall volatility of the Fund. We are writing cash secured puts on specific names we would like to own to increase our exposure to such names in the Fund, while writing covered calls on names we feel have stretched valuations; and we are writing short straddles (puts and calls written on the same name with similar strike prices) and short strangles (puts and calls written on the same name but with different strike prices) on names we feel will trade range bound. Depending on the strike price chosen, all these strategies are neutral to bullish strategies that allow us to generate option premium or enter and exit positions at more attractive prices during periods of elevated volatility.

The final month of 2018 saw continued market weakness in the cannabis sector whereby many large cap names were under selling pressure. Investors began re-examining the multiples upon which many companies were trading at given the opening of the recreational market in Canada and a supply shortage that was not anticipated. However, in January, sentiment improved as investors returned to the sector, buoyed by hopes of further strategic investments or M&A activity in the sector.

Taking advantage of the continued volatility in the sector, we used our option strategy in January to assist in rebalancing the portfolio in favor of names we prefer while generating approximately $209,000 in option income. We were able to write cash secured puts out of the money at strike prices that we would like to own to increase our exposure to such names in the Fund. Examples of

such trades included Canopy Growth, Planet Fitness, Savaria, Hexo Corp., and Cronos to name a few. We also wrote covered call options out of the money at strike prices that we believe are closer to values that better represent our belief in the companies while still maintaining a cautious but bullish market sentiment. Examples of such trades included Vocera Communications. We continue to write covered strangles on names such as Canopy Growth, GW Pharma and HEXO Corp. we felt would trade range bound and from which we could receive above average premiums.

We continue to see unique opportunities for investment in the global cannabis sector as well as the broader alternative health care space, with the rapidly evolving global medical, health and wellness markets continuing to open new markets and new delivery methods offering compelling investment opportunities for growth oriented investors. Our actively managed approach allows the Fund to invest in a broad universe of companies that include both public companies and select private companies that are focussed on go public transactions.

The Ninepoint Alternative Health Fund, launched in March of 2017 is Canada's first actively managed mutual fund with a focus in the cannabis sector and remains open to new investors, available for purchase on a daily basis. Utilizing our actively managed approach we are able to invest when we see new opportunities arise. Many catalysts are on the horizon and we continue to see solid returns for the alternative health space in the coming months and years.

Charles Taerk & Douglas Waterson
Portfolio Team
Ninepoint Alternative Health Fund

Compounded Returns[1]

	1MTH	YTD	3MTH	6MTH	1YR	INCEPTION
FUND	19.4	19.4	7.6	35.0	34.8	63.74
INDEX	24.6	24.6	7.3	18.1	19.7	40.12

[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 January 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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