Canadian Cannabis Sector Report

Higher Sales in The Cannabis Industry

The Cannabis industry is in its infancy; with legalization having been approved in October 2018. Despite the industry's newness, the cannabis market has seen many ups and downs. In the past two years, Cannabis has made a large impact on the Canadian economy and has changed the way the world views the variety of uses for marijuana.

The Cannabis industry is distinguished by its unique attributes. The handful of market leading participants, rapid technological and product development, and the one of a kind impact COVID-19 has had on the Cannabis industry makes it an exciting prospect for future growth within the Canadian economy.

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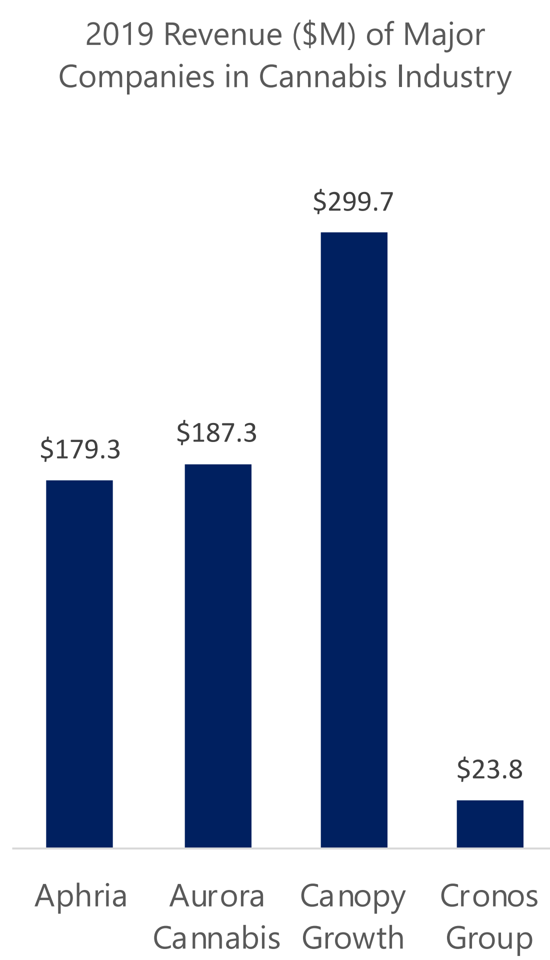
Introduction to Industry

Industry Description

The Canadian Cannabis industry has seen substantial growth since the legalization of marijuana in October 2018. Cannabis products are sold in brick and mortar stores, and through regulated online provincial sales channels. The cannabis industry has various federal jurisdictions, but provinces are ultimately in charge of the selling structure, whether it be public, private, or a hybrid of both channels. Ontario cannabis retailers led sales at the provincial level, contributing $217 million from October 2018 to September 2019, while the total sales across the nation amounted to $907 million. Between 2019 and 2024, the legal adult-use market will grow at a 22.5% compound annual growth rate (CAGR), reaching over $5.2 billion. The cannabis sector not only involves marijuana, but the introduction of cannabis 2.0 products, that include marijuana-infused chocolates, teas, drinks, and distillate based vaporizers. The Canadian Cannabis industry has seen varying sales metrics between regions and per capita store sales. A variety of factors may influence the ease of access to cannabis in a given area, including the administrative and operational steps required to establish a cannabis retail store. Some factors that may affect the industry as a whole are the immediate or staggered entry of retail operations, competition from illegal markets, and the density and distribution of the population of stores in a given region. Demographic and income factors, along with disruptions in the supply chain, can also make it a challenge to introduce this new product to Canadians all across the country. Cannabis is available through online retailers in every province and territory, with Manitoba and Saskatchewan allowing online sales via a private retail model. The majority of private and hybrid models are in Western Canada, while Nunavut is the only jurisdiction without a physical retail store. The Cannabis industry has many potentials, but seeing as it is so new, the sector is still figuring out how to make it as efficient as possible for Canadians to get high quality, safe products.

Market Share Concentration

Being relatively new, the Cannabis industry is categorized as having a low to moderate degree of market share concentration; however, as the industry rapidly grows, the market is estimated to become fragmented through an increase in companies entering the market. A large part of this fragmentation results from the market shifting from a focus on medical marijuana to recreational cannabis. The key players in the Medical Cannabis industry did have an advantage in making this transition due to their already effective and efficient internal infrastructure. Despite the predictions for a fragmented market, as current major competitors receive more funding, they may begin to acquire their competition to further expand their market share, then creating a concentrated market.



Sources: CIBC Capital Markets, Ontario Cannabis Store, Stats Canada

Major Players

Canopy Growth Corporation

Headquartered in Smith Falls, Ontario, Canopy Growth Corp. (Canopy Growth) was one of the first companies to operate in the industry in Canada when they obtained their license to cultivate, produce, and sell medical marijuana in November 2013. With an early start, Canopy Growth has separated itself from the competition through a unique branding strategy. The company sells a wide array of products, including Leafs By Snoop, a cannabis product produced by music artist Snoop Dogg. Through a $4 billion investment by Constellation brands in 2018, the company has begun to position itself in the Recreational Cannabis industry as medical marijuana decreased to 20% of its total revenue. As the company grows within Canada, its high market cap has allowed them to raise enough capital to target the U.S. market by the end of the 2020 fiscal year.

Aurora Cannabis Inc.

Aurora Cannabis Inc. (Aurora) is a wholly-owned subsidiary of Aurora Cannabis Enterprises Inc., that has been licensed to cultivate, produce, and sell medical marijuana products as of 2015. Based in Edmonton, Alberta, Aurora develops its cannabis plants in 11 production facilities throughout the world, leading to 500,000 kilograms produced per year. While the company has only recently been founded, their adoption of an acquisition-focused strategy has allowed them to become a leading marijuana company in the Canadian market. To date, Aurora has acquired 17 companies that are in all different fields of the Cannabis industry. In addition to its acquisitions, the company has positioned itself to expand overseas. Presently, they are a crucial player in the European market's medical marijuana industry and are equipped to take over the entire market if recreational cannabis becomes legalized.

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Aphria Inc.

Headquartered in Leamington, Ontario, Aphria Inc. (Aphria) joined the industry when it first received its license to produce and sell medical marijuana in November 2014. Aphria has three different revenue streams, with online sales being the highest. All of Aphria's products come from a greenhouse that acts as one of their primary value propositions. Aphria has been able to position themselves as an industry leader through their distribution agreements. In 2017, Aphria partnered with Shoppers Drug Mart, a leader in the pharmacy industry. Further, in 2018, they allied with Southern Glazer's Wine and Spirits LLC to spread their recreational products throughout Canada. Through online means and effective partnerships, Aphria has set itself to be the most profitable and cost-efficient company in the industry in the past six years.

AURORA®

aphria™

CANOPY GROWTH
CORPORATION

Sources: IBISWorld

Cost Structure and Sales Data

Wages

The majority of dispensaries are local businesses whose revenues are highly dependent on their employee's ability to sell their products, resulting in labour costs being a high share of revenue. Even for larger companies, the production of cannabis is labour intensive, as corporations tend to hire highly paid researchers to further develop the quality of their products. However, as the industry begins to mature, wages as a share of revenue will decline as companies begin to optimize their production operations, and as revenue surpasses their operational expenditures through their investment in research and development as well as cheaper cultivation processes. Overall, wages were predicted to be 39.6% of industry revenue in 2019.

Depreciation

While less common in most retail operations, depreciation plays a key role in cultivation facilities due to the heavy spending on capital expenditures. Cannabis production requires extensive irrigation systems, processing machinery, hydroponic systems, and temperature-controlled spaces for curing and drying. Altogether, depreciation related to the aforementioned assets were predicted to make up 17.2% of industry revenue in 2019. However, as the industry matures, capital expenditures will decrease leading to depreciation accounting for less of the industry's costs.

Other Costs

Other costs include legal fees, government taxes, research and development expenses, and other administrative costs. Research and development is a primary driver for this section, as many companies have boxed themselves into negative profit margins as they significantly invest in product development. These costs tend to be higher for medicinal marijuana businesses. Overall, other expenses were predicted to account for 20.4% of the industry revenue in 2019.

Purchases

Purchases amount for a significant portion of the cost structure in two manners: facilities and store maintenance. Besides large initial facility costs, there are added costs such as soil, fertilizer, and seeds. In the retail stores, retailers need to ensure they have the proper lighting, air conditioning, sealed containers and cases, and other equipment in order to store marijuana. Through these costly expenses, purchases were predicted to be 20.2% of industry revenue in 2019.

Pre COVID-19 Sales

The cannabis market in Canada has seen steady growth since the legalization of the substance in 2018. Sales for the period of October 2018 to September 2019 have been $907 million across the nation. Sales in Ontario from April 2019 to March 2020 are $385 million in the province alone, with $71 million coming through online sales, and $313 million coming from retail stores. The OCS has had a hard time converting the illegal market in the past, but Q4 of 2019 captured 19% of illegal market share, a growth of nearly 15% compared to Q4 of 2018. The OCS had a hard time capturing the illegal market due to the costs associated with purchasing marijuana. The OCS did not offer bulk pricing as many illegal marketplaces did and are also not providing their consumers with fresh products. Many of the items sold in Q4 2018, had already been prepackaged for close to a year, making the product very dry and unappealing to the mass market. Sales before COVID-19 have had a steady increase, with over 600 new products being available online and through retailers. Cumulative sales of the provinces have also grown exponentially. The sales were positively affected by COVID-19, where an increase was seen in Q1 2020, as consumers looked to stock up.

Sales during COVID-19

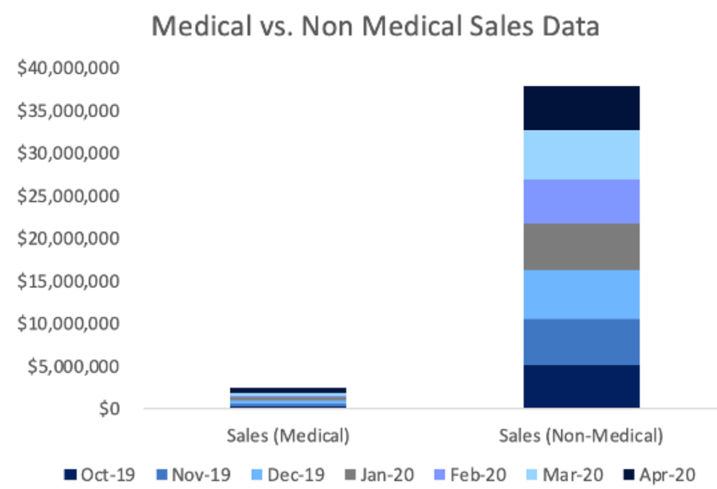
With COVID-19 forcing federal and provincial governments to put forth lockdown measures in the middle of March, Canadians responded with excessive purchasing habits.

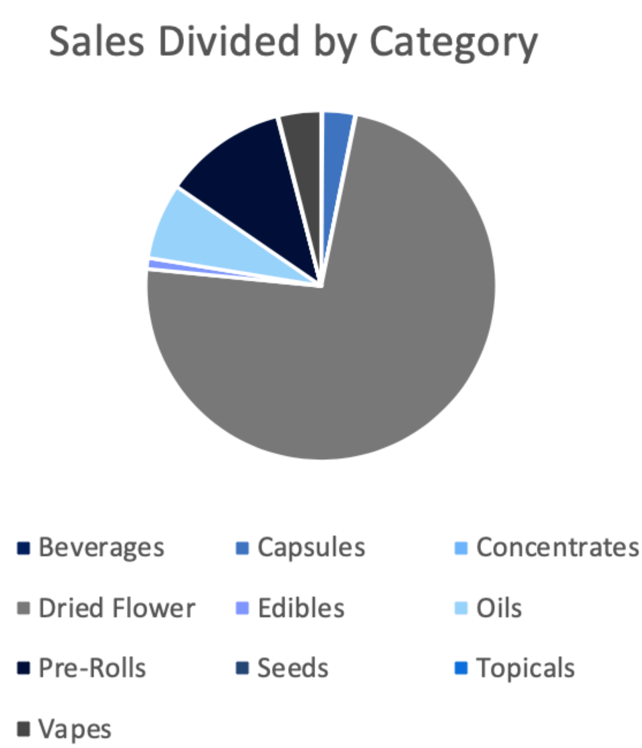
Sources: CBC News, CIBC Capital Markets, IBISWorld, Ontario Cannabis Store, Yahoo Finance

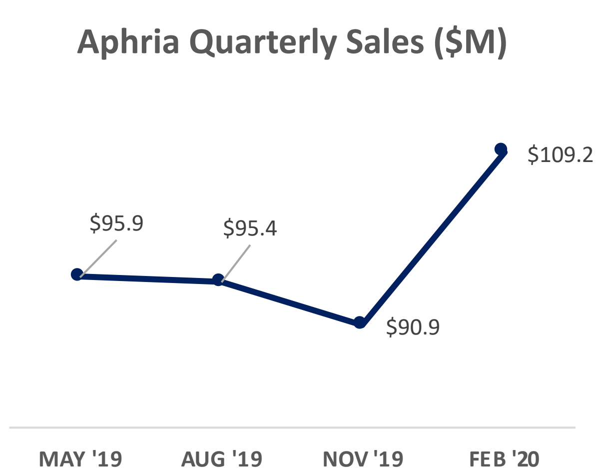
Sales Data (Continued)

Sales during COVID-19

Many Canadians immediately worried that stores were going to be temporarily shut down, thus restricting their access to purchase cannabis. Unlike most retail stores, many provincial governments deemed cannabis retailers to be an essential business, due to its connection to medical marijuana. However, because of the fear of cannabis retailers possibly closing, cannabis sales spiked in March, leading to $181 million being sold, an increase of 19.2% from February. This jump in sales has been the largest one-month gain Canada has seen since recreational pot was legalized. Sales continued to maintain in April, with a small decline of 0.6% from the previous month. Despite the increase, there were major discrepancies in how consumers reacted in each province. While having the largest total addressable market, Ontario's sales fell by 9.6% likely due to retailers being forced to close in order to establish curbside pickup and home delivery. On the contrary, Quebec faced a 9% increase in sales, an approximate increase of $41 million. Although the industry showed a positive trend in the first quarter, CIBC Capital Markets altered its original 2020 forecast for cannabis sales by a decrease in nearly a billion dollars. This is mainly rooted in the concern of Ontario being unable to issue its new store rollout plan because of the pandemic. They have, however, projected total cannabis sales to reach $2.5 billion, which will still be a $1 billion + increase from the previous year.







Sources: CBC News, CIBC Capital Markets, IBISWorld, Ontario Cannabis Store, Yahoo Finance

Development and Trends

Innovative Technology of Production

Technology continues to evolve across various sectors of the Canadian macroeconomy, more potently in the Cannabis Sector. Technological advancements in both the seed-to-sale process and the consumption of cannabis are radically reshaping the industry. A prime example of technology facilitating the seed to sale process is the US based company Akerna (Nasdaq: KERN). Akerna is the result of a merger between MJ Freeway and MTech Acquisitions Corp, both of which revolve around process management in the Cannabis industry.

Akerna consolidates cannabis technology companies to connect data points in the global supply chain, thus creating the world's most transparent and trusted consumer packaged goods supply chain on a global scale. Akerna is also highly specialized in cannabis software engineering. The parent company MJ Freeway is the very company that created seed-to-sale tracking software and the industry's first cannabis ERP (Enterprise Resource planning). To this day, they've tracked upwards of $18 billion in legal cannabis sales globally.

The technology provided by Akerna consists of tracking software that includes inventory control and growth management applications, which all facilitate workflow and efficiency. MJ Freeway's specialized Leaf Data Systems also enable governments to track cannabis plants from seed to sale, which ensures patient, public, and product safety in the respective countries.

Akerna also continues to secure funding, exemplified in the $17 million raised in early June 2020 from two institutional investors. Proceeds from the investments are diverted towards Akerna's growth initiatives in technology, infrastructure, and corporate purposes. Successful investing rounds indicate that Akerna and the Cannabis Industry are yet to reach their peak as an integral part of a nation's economy.

AKERNA CORP.

Consumption Side of Technology

Gene Editing from Canopy Growth

With a near 30% market share of the legal Cannabis industry, Canopy Growth has carried out scientific research that, with the use of gene editing, allows them to grow plants with no THC or CBD at all. These customized breeds could also carry different flavors and be a lot easier to grow. The plant also produces a rarer cannabinoid called the CBC, with powerful anti-inflammatory qualities. Canopy continues to research the possibility of extracting the gene from the chemicals and planting them in yeast or bacteria for industrial size production.

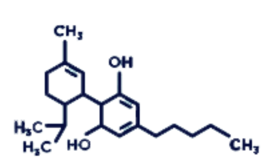
CannabisDNA

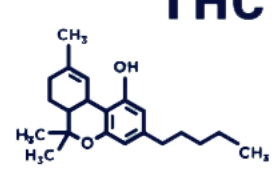
This new technology allows for personalized, one-off experiences with cannabis consumption. CannabisDNA administers a 130$ saliva swab test with more than 70 gene markers that outline your personal reaction to cannabinoids. They then produce a report that predicts your compatibility with different strains.

Nanoencapsulation

CBD is known for its insolubility and low bioavailability. A low bioavailability means that when consumed, only about 20% of the CBD ends up in your bloodstream. Nanoencapsulation technology turns CBD into smaller, more potent dosages. It also allows for smoother blending with water and beer, making it easier to consume.

THC





CBD

Developments of Cannabis

Alternative Uses of Cannabis

To some, the Cannabis industry is not a very large developmental space, but on the contrary, cannabis has gone from a drug that is primarily smoked to being available in virtually every form. Development is proven in the continuous and ever-advancing new forms of cannabis that continue to emerge in the market, further solidifying that the industry is only at the beginning of an expansion. Marijuana consumption can occur in many ways, with smoking being one of the most popular; dry herb made up over $274 million of total sales during the first full fiscal year of legal cannabis purchases. The OCS has explored alternative uses of cannabis, with its development of cannabis 2.0. This new category has opened up the market for beverages, capsules, concentrates, edibles, oils, seeds, topical, and vaporizers, allowing consumers to have some variety in their consumption choices.

Consumers can also choose between different levels of THC and CBD, THC being the psychoactive chemical that gets you "high", and CBD being the chemical that can treat muscle pain, as well being a natural aid in falling asleep and staying asleep. Cannabis producers have found a way to offer products with only CBD, which can be very useful for the medical uses of marijuana, and can also apply to a much more extensive audience, specifically appealing to nervous first-time users. Cannabis 2.0 has introduced many different ways to consume the same product, but the beer market has also seen expansion with THC's addition to beverages. THC beer has been on the market in Colorado. Usually, it accompanies about 5mg of THC per drink, resulting in a more laid-back experience when consuming marijuana, making it easier for consumers to pace themselves and enter this new category with ease. Cannabis has also seen a multitude of leaps and bounds in medical research. Studies have shown that CBD is helpful to PTSD patients, people dealing with anxiety, and even insomnia. These alternative applications provide goods to a broader market and are more appealing to first-time users.

Sources: Business Wire, Healthline, Ontario Cannabis Store

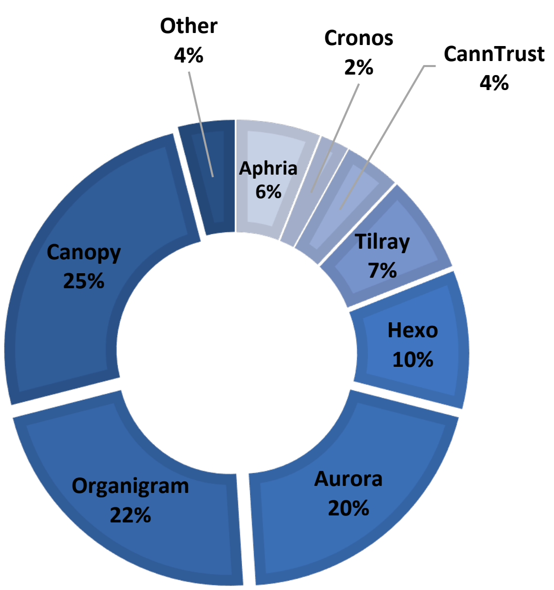
Developments and Trends (Continued)

The Legal Market

The largest performers in terms of market capitalization, volume and overall growth in the Canadian cannabis market are Canopy Growth, Aphria, Aurora, Cronos and Tilray, all of which are in both cultivation and retail. Canopy growth continues to dominate, having had a 34% market share in 2019.

Smith Falls, Ontario based Canopy Growth (CGC) continues to make several acquisitions in both the Canadian and US markets. Ever since the inception of legalization on October 17th, 2018, Canopy's stock price continued to rise from 38$ per share to a peak of 49$ per share in mid to early 2019. With competitors following a similar trend.

Canopy also continues to grow beyond the Canadian cannabis sector with collaboration in the US market through multibillion-dollar investment made by Constellation Brands Inc., the largest beer importer in the United States. Canopy reported total sales of nearly $226.3 million for the three months ended Dec 31, 2019. The annual revenue growth was an astounding 191% compared to the previous year. Of that 149.5 million was from the Canadian recreational channel and $78.9 million in global medical sales.

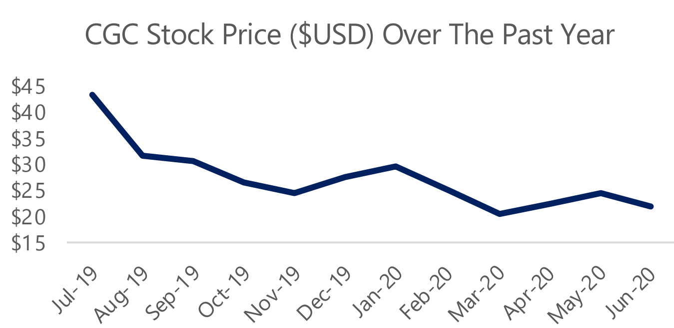


Impact of COVID-19

Sales all around the industry were down approximately 13% for the quarter ending March 31, 2020. Keeping our focus on Canopy, who's general experience with COVID can be mirrored to the rest of the industry. Sales were a weaker than expected $108 million compared to the targeted 128.8 million for Q1 2020, and Canopy booked an adjusted EBITDA loss of $102 million. Canadian recreational revenue plunged by 28% quarter over quarter (Q1 2020 to Q2 2020) to $49 million. The decline was caused by a surge in cannabis retail spending in late February and early March recorded by Statistics Canada. Sales sharply declined mid to late March as stay-at-home orders were put in place.

Although dominating the market with a 22% market share in February of 2020, Canopy Growth closed 23 corporately owned stores in mid March due to the pandemic. Moreover, Canopy and various other major companies in the Cannabis industry in Canada have reevaluated their net income and profitability target, citing the impacts of the COVID-19 pandemic. New performance targets and figures should be out by early Q3 2020.

Stock performances and prices also took a large hit due to the pandemic. Canopy Growth's (CGC) stock price was down approximately 60% for the first fiscal quarter of 2020, with far more devastating repercussions for smaller scale cannabis companies.



Sources: Canopy Growth, Crunchbase, PC Mag, Yahoo Finance

M&A and Capital Markets Activity

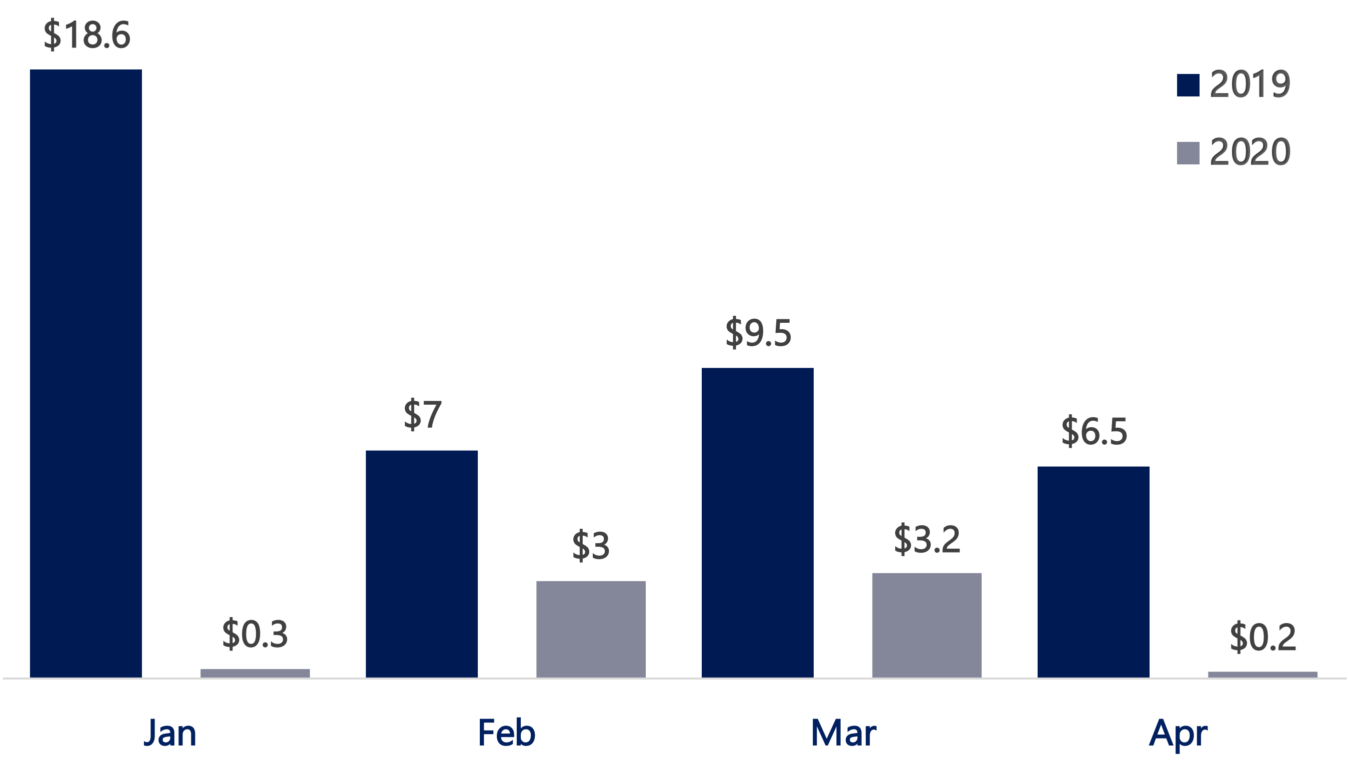
High capital markets activity has also been a strong suit for many cannabis companies in the Canadian economy pre COVID-19. Late 2019 saw large corporations in both the US and Canadian markets continue to raise funds through successful investment rounds. Recent corporations including Mississauga based Terrascene raised more than $30 million USD to fund expansion in Toronto and New York. Greenbits has also secured $23 million in capital that will be used towards further expansion. Venture capital funds also continue to create a pertinent effect on the Cannabis industry in both the US and Canadian markets.

The Canadian Cannabis Industry was also eligible for funds issued to businesses as part of the COVID-19 relief efforts, in hopes of offsetting the lack in revenue, sales and employment throughout the broader economy.

M&A activity and deal making in the cannabis sector has halted as a result of COVID-19. Bloomberg reports that the number of cannabis M&A deals in the four weeks ended March 31 came to only 3, compared to 36 from a year ago. Bloomberg also reported that the slowdown is linked to a mix of a sharp decline in share prices and a muted capital financing environment during the pandemic. The only significant M&A deals continue to appear amongst the largest corporations. Akerna, for example, recently acquired Trellis, a cultivation compliance software company, for $2 million USD.

Overall, it becomes difficult to predict the direction of the current state of the market, however, the trends and developments continue to suggest that the COVID-19 pandemic is just a bump along the way in the cannabis sector's journey to becoming an integral part of both the Canadian and US economies.

Announced Canadian Public M&A Deals in C$ billions



Sources: BDO, Firmex, The Guardian, Yahoo Finance

Industry Drivers

Legalization

On October 17th, 2018 the *Cannabis Act* came into place implementing a new framework for controlling the sales, possession, distribution and production of marijuana (being the first G7 country to do so). The two main goals of the *Cannabis Act* are to prevent youth from accessing it and to displace the illegal cannabis market. Any Canadian over the age of 18 or 19 (depending on the province/territory) can posses and share up to 30 grams of legal cannabis and can grow 4 plants per residence (from legally bought seeds). Failure to comply with these regulations result in ticketing and or a penalty of up to 14 years in prison.

Identifying Legal Cannabis

Products must have the excise stamp sealing the package, (unless its 0.3% THC or less) they also must have the standardized cannabis logo on the package (on products that have a THC concentration of more than 10 micrograms).

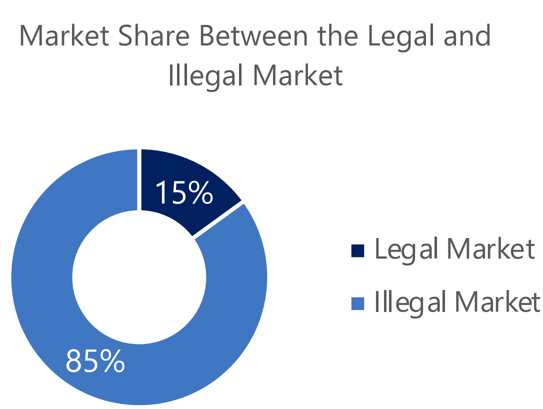
Excise Stamp

Standardized Cannabis Logo

Licensing for Supply Chains

To make sure laws are being followed there are many licenses needed in order to mass produce and sell Cannabis. These licenses are required and are the primary driver behind the industry's growth. The first class of licensing is the Cultivation License. These are required to sell to other cultivators, processors, and authorized researchers. These cultivation licenses vary in size and products between the Standard Cultivation, the Micro-Cultivation, the Nursery-Cultivation and the Industrial Hemp Licenses. The next category of licensing is the Processing License which allows for the same rights as the Cultivation License, with added features such as federal medical sales. These vary between large scale operations, with the Standard Processing License, and small-scale operations, with the Micro-Processing License. Finally there are sales to public licenses which allow permit holders to sell tested, labelled, and packaged marijuana to the public. These licenses include the Authorized Provincial and Territorial Sales License and the Federal Sales License which allows online sales.

Despite the hope for the black market to diminish with the legalization of pot, the government's actions did not properly brand legal cannabis in order to do so. While illegal weed sales have slowed down holistically, it is projected that the illegal market still controls 85% market share. This contradicts the predictions of many big corporations, such as Scotiabank's estimate of the black market only holding 72% of the post legalization market by the end of 2019.



Sources: Government of Canada

Government Analysis

Government's Middleman Role

Since legalization, the legal market and illegal market have shifted further and further away from each other. In the legal cannabis market, the average price increased from $9.69 per gram in 2018 to $10.30 per gram by the end of 2019. As that change occurred, the illegal cannabis price declined on average to $5.73 per gram by the end of 2019 from $6.44 per gram in the prior year. Despite some companies like Hexo Corp.'s decision to release a $4.49 per gram product in October 2019, larger corporations continue to hold their prices at a relatively steady number, meaning that anyone with inexpensive prices are a minority in the market. However the reason for major players being unwilling to lower their prices lies in the government's role as a middleman. As all consumers are purchasing through the government, profits are being minimized for producers due to excise and sales taxes. This then causes the production companies to raise their prices in order to maintain operations. Ultimately, as provincial governments move more towards privately owned cannabis stores, prices will decrease through direct transactions between the customer and producer.

Repercussions of The Licensing System

The main cause for this faulty start focuses on Ontario's lack of action in comparison to the rest of Canada. Upon the date of legalization, Ontario was worried that the federal supply would be unable to match the demand, and for that reason, they implemented a retail lottery system. The model placed a temporary cap on the number of private outlets to 25. With an already small number of openings for points of sale, applicants had to reach numerous requirements, including a bank letter confirming authorization to $250,000, and another confirming access to a $50,000 standby letter of credit. However, according to Cannabis License Experts, the cap caused reluctancy within investors. They quoted, "most banks aren't entertaining business loans for cannabis retailers (deeming it too high risk), and investment is getting more difficult to come by as the industry matures and those early stage investors have already committed themselves to other ventures." Ontario's barriers of entry caused great impacts for the market in the first year of legalization, in which it can be broken down into two sections: improperly targeting the market, and an increasing market surplus.

Improperly Targeted The Market

As 2019 ended, Ontario only had 24 stores open to the public, meaning that there was approximately less than 1 store per 500,000 people. With a population one-third the size, Alberta follows the same model of government-operated website and private licensed brick and mortar stores as Ontario but authorized 356 retail stores. In comparison to Alberta, there was more than 1 store per 10,000 people. This implies that Ontario finished 2019 with only 3% of Alberta's number of retail stores per capita. If Ontario had acted differently, there would have been a greater result for the market. Due to Ontario's retail lottery system, there was a 6-month wait time from the date of legalization until retail stores were available to the public. However, once the product hit the market, sales rose from $8 million to $19.6 million over the course of one month. Provided that Ontario matched Alberta's ratio of stores to the population, there could have been an additional 700 points of sale for consumers. If revenues followed Alberta's rate in proportion to the population, Canada's legal market would have surpassed Scotiabank's 28% market share prediction, leading to much higher profit margins for the industry's key players. Even if Ontario had increased its retail store count to 75, sales could have increased by $950 million, nearly doubling the total market's revenue in 2019. In addition to a surge in revenue, an increase in store locations would have undermined the black market. Even when Ontario finally authorized private outlets to sell, they were mostly all concentrated in Toronto. This was also the case for most provinces as well. Hence, those who were not in an appropriate driving distance had no choice but to purchase from the black market if they wished to buy cannabis.

Increasing Market Surplus

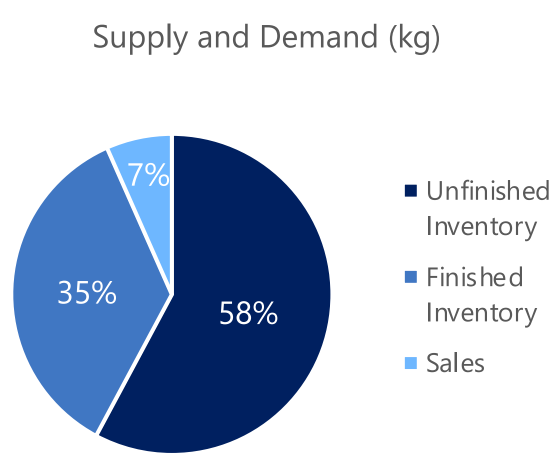
Ontario's retail lottery system also played an influential role in the market's surplus of inventory. With a limited number of stores available to sell and a growing number of cultivation spaces, companies began to stock up on their inventory. However, the growth in unfinished inventory grew exponentially while finished inventory and sales maintained a relatively steady trend. 10-months after legalization, Health Canada reported that as of August 2019 the industry's inventory was 30 times the size of sales. This played an immediate impact on the market's pricing system.

Sources: Cannabis License Experts, CBC News, Health Canada

Government Analysis (Continued)

Increasing Market Surplus (continued)

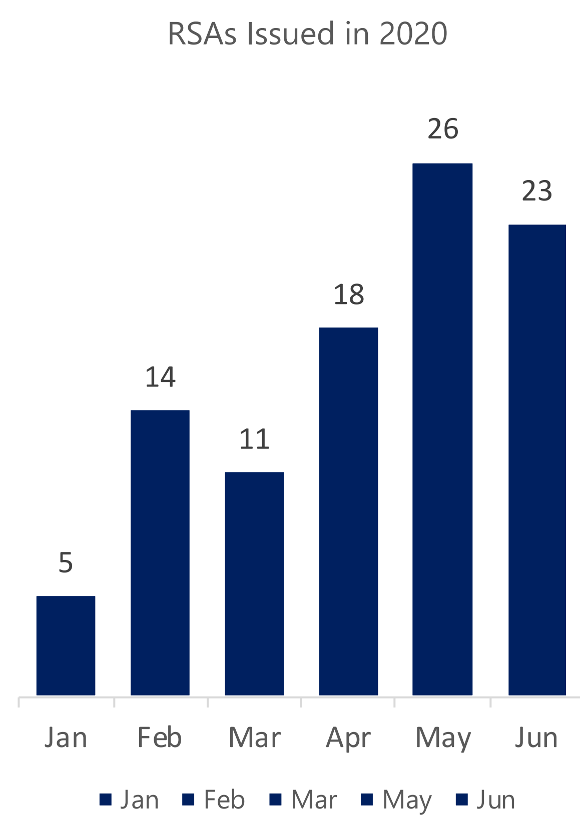
This played an immediate impact on the market's pricing system. In Q1 of 2019, the average price per gram was $9.48 pre-tax, whereas in Q4, the average was $7.48 per gram. Because of the slower than expected store rollout plan leading to an intense surplus, all key players reported missing their 2019 revenue and profit projections. An exemplar of this is Hexo Corp.'s struggle in finding a way to balance out its oversupplied inventory with demand, leading to them withdrawing their 2020 financial outlook near the end of 2019. However, the repercussions of oversupply did not end in 2019. In the second quarter of 2020, Hexo Corp. announced a $16.1 million write down on inventory with $14.9 million of it being caused by an oversupply of unfinished inventory. The reasoning for this results from the unfinished inventory's value depreciating as the quality of the cannabis decreases over time.



Government's Response

While Ontario missed the opportunity to maximize revenue in the first year of sales, they recognized the problem and began addressing it early 2020 through the following actions: end the retail lottery system, increase the cap on the number of private retailers, and cancel some of the pre-qualification requirements. To acquire the ability to sell cannabis, applicants need to obtain two certifications: a Retail Operator License (ROL), and a Retail Store Authorization (RSA).

As of February 2020, there have been 800 applications sent for an ROL in the hopes of being able to then apply for the RSA on March 2nd. From March 2nd until September, licensed operators can have a maximum of 10 stores; then increasing to 30 until September 2021; and finally being capped at 75 thereafter. After earning a ROL, one can then apply for the RSA. The government has announced its commitment to issuing up to 20 RSAs per month beginning in April 2020; however, there is still the concern that they will not reach this quota. So far, the Alcohol and Gaming Commission of Ontario has been working at an efficient rate as we begin to see an explosion of stores opening across the province. While COVID-19 has restricted access for consumers to purchase in-store, an increasing number of issued private outlets is a significant sign for the market to begin growing at a much higher rate post-pandemic.



Sources: AGCO, CBC News, CTV News, Health Canada, Stats Canada

Industry Outlook

Short-Term

COVID-19 and Unemployment

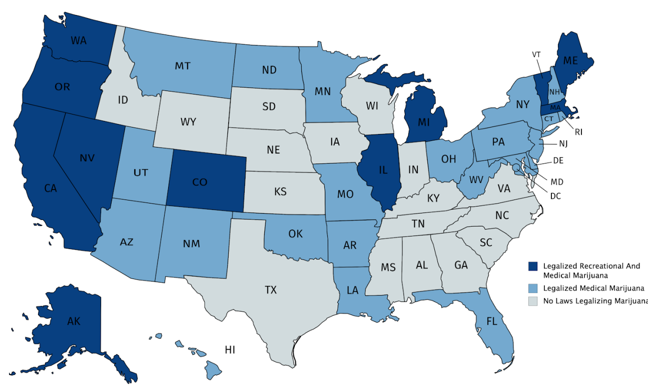
Due to COVID-19, unemployment rates are at a record high, with 13.5% of the workforce affected. In total, this includes 5.5 million Canadians. In May of this year, Stats Canada reported that this is the highest recorded unemployment rate since comparable data became available in 1976. The loss of over 13% of the workplace has had a dramatic impact on the economy, making it very difficult to sustain profitability and continue with business as usual. Concerning these statistics, the Cannabis industry has been dramatically affected in the short-term.

Although cannabis sales have grown in the recent past, and consuming cannabis has become more socially accepted in society, the current situation has boosted the industry with short-term gains. CIBC Capital Markets forecasted recreational cannabis sales hitting $2.5 billion this year – much lower than its previous $3.4 billion estimates. So why the difference? The main reason is that COVID-19 has put savings on the top of Canadian's minds in these uncertain times. On the other hand, the Ontario Cannabis Store has seen spikes in sales for the last month of data available in March compared to January and February, respectfully gaining 50-60% in that period. This sales increase was caused by cannabis consumers buying more than usual in anticipation of store closures further into provincial lockdown. The data available from the OCS shows that the first quarter of 2020 has had strong evident sales growth. However, due to Canadians concerns about savings during this global pandemic, it will hurt companies in the medium term. This short-term increase in sales is not representative of how the industry will evolve for the rest of the year, even though the government did name the Cannabis industry as "essential business." Looking at the short-term analysis of the Cannabis industry shows that consumers are more likely to purchase cannabis in anticipation of COVID-19 and that this impact has been positive on the sales of marijuana in Ontario and Canada for Q1. These sales further prove that the legal cannabis market has a strong presence in Canadians' minds when they are looking to purchase these products.

Long-Term Outlook

New Markets

Already established Canadian companies such as Aurora Cannabis and Canopy Growth will further benefit from the legalization of marijuana in the seventeen states where it is currently outlawed. Cannabis is still a schedule one drug on the DEAs Illegal Substance List; however legalization is showing no signs of stopping. Whether it be for recreational use or medicinal use, as more states become accepting of this substance, the market will undoubtedly grow and create more opportunities for larger customer bases, mergers, and acquisitions. US states where cannabis is legal have also been conducting more research on the medical benefits of marijuana and have even contracted and hired specialists from Israel, the country that is leading the world in cannabis research, to help with their studies.



Another more specific market that is showing signs of a promising future is the use of CBD oils in sports therapy. In 2018, CBD was removed from the World Anti-Doping Agency's list of prohibited substances and is no longer tested for in major league sports. Many former and current athletes have started endorsing these products and backing its health benefits that fight joint pain, inflammation and muscle soreness. The American CBD oil market is expected to grow from $813.2 million in sales to $1,812 million in sales by 2022.

Sources: CIBC Capital Markets, DEA, Forbes, Healthline, Ontario Cannabis Store, Statista, Stats Canada

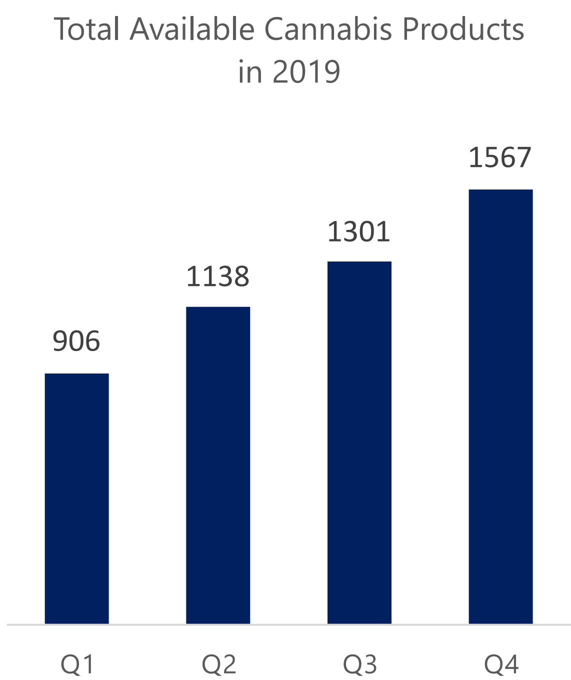
Long Term Outlook

Product growth

Over the course of 2019 there were 35,100,000 grams of marijuana sold in Ontario alone and these sales are divided into ten different product categories. From the most popular category "dried flower" to the least popular product category "topical", over $385 million in revenue was generated. The product catalogue grew 70% in just one year (906 to 1567).

Potential Growth

Many of the product categories are in the early stages and show the potential for growth. The beverage category previously accounted for only 1% of the market but has been growing in recent years and is estimated to grow 19% over the next four years. Many regulations pose an obstacle for this category and in response, the Cannabis Beverage Association (CBA) was formed and plans on further educating policy makers and establishing new laws surrounding this form of cannabis consumption.



Valuation and Financial Performance

Company Name	Ticker (TSE:)	Market Cap ($M)	Enterprise Value ($M)	Revenue ($M)	EBITDA ($M)	EV/Sales TTMx	Rev/Employee TTMx	Interest Coverage TTMx
Aphria	APHA	$1,180.40	$1,563.64	$179.31	-$67.73	8.9x	382.4x	-14.5x
Aurora Cannabis	ACB	$1,371.32	$8,194.98	$187.32	-$230.65	43.2x	89.2x	-5.9x
Canopy Growth	WEED	$6,273.40	$4,243.61	$299.65	-$676.18	15.2x	89.9x	-152.6x
Cronos Group	CRON	$2,244.99	$1,135.91	$23.75	-$112.24	46.7x	49.8x	-3.6x
Mean		$2,767.53	$3,784.54	$172.51	-$271.70	28.5x	152.8x	-44.2x
Median		$1,808.16	$2,903.63	$183.32	-$171.45	29.2x	89.6x	-10.2x

Conclusion

Despite being so relatively new, the Cannabis industry presents a variety of promising channels by which the general public, investors, and stakeholders can expect to see strong growth in. Industry leader's heavy investments in product development, paired with the government's continuous efforts to find their footing within the industry will lead the way to a brighter, stronger future for the Canadian Cannabis industry.

Cannabis companies benefitted from the initial uncertainty behind COVID-19 in Q1 2020. Despite this, we believe the industry should brace for softer sales in the coming quarters because of higher household savings. In the long run, we've identified promising catalysts within the industry that should drive strong growth for years to come.

Sources: Crunchbase, DEA, Forbes, Healthline, Statista, Yahoo Finance