

Equity Research: Healthcare - Cannabis
Patrick Smith | Analyst | patrick@ubikaresearch.com | (647) 444-5506
Christopher Bednarz, MBA | Associate | chris.b@ubikaresearch.com | (416) 558-5548

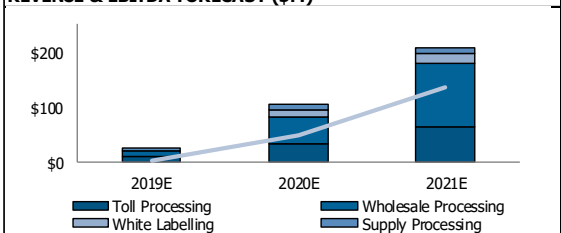
NEXTLEAF SOLUTIONS LTD. CSE:OILS
(Currency is CAD\$, unless noted otherwise)
(Fiscal year-end is as of Sept. 30)

Last Price	\$0.60
Target Price	\$1.75
Potential Return	192%
Net Asset Value Per Share	\$2.37
52 Week Low / High	\$0.30 / \$0.83
Average Daily Volume (30-Day)	398K

CAPITALIZATION	Basic	Diluted
Shares Outstanding (M)	107.8	147.3
Market Capitalization (\$M)	\$64.7	\$64.7
Enterprise Value (\$M)	\$61.1	\$61.1
Last Reported Cash (\$M)	\$3.6	\$3.6
Last Reported Debt Balance (\$M)	\$0.0	\$0.0

OILS OPERATIONS	F2020E	F2021E	F2022E
Biomass Processing Volume (kg)	6,720	24,900	52,600
Crude Produced (kg)	560	1,890	3,420
Distillate Produced (kg)	240	1,000	2,520
Total Revenue (\$M)	\$35.8	\$119.4	\$232.1
EBITDA (\$M)	\$1.5	\$49.4	\$134.9
FCF (\$M)	-\$6.0	\$28.6	\$86.4
Total CAPEX (\$M)	\$6.0	\$4.0	\$3.0
CFPS	\$0.00	\$0.23	\$0.58
EPS	-\$0.02	\$0.20	\$0.56
Cash At Year End (\$M)	\$1.4	\$50.2	\$136.6
Debt At Year End (\$M)	\$0.0	\$0.0	\$0.0

RELATIVE VALUATION	EV/EBITDA		EV/SALES	
	2020E	2021E	2020E	2021E
Nextleaf Solutions	39.8x	1.2x	1.7x	0.5x
Extraction Companies	15.1x	5.2x	4.1x	2.0x
CAN-Based Major Cultivators	23.3x	17.2x	6.2x	3.5x
US-Based Operations	9.3x	4.7x	2.5x	1.6x

REVENUE & EBITDA FORECAST (\$M)

MAJOR SHAREHOLDERS

Management and Insiders (17%)

Disclosure: 1, 3 (See back page for further details)

Source: Ubika, Capital IQ

Nextleaf 3-Month Share Price Performance


Source: www.stockcharts.com

NEXTLEAF RECEIVES A HEALTH CANADA PROCESSING LICENSE

Received Health Canada Processing License. On September 9, 2019, Nextleaf announced it had received its Standard Processing License from Health Canada on September 6, 2019. This was ahead of our expectations and we consider it a significant de-risking milestone as it transitions the Company from a start-up to an operator. Recall, on July 8, 2019, Nextleaf submitted its Affirmation of Readiness and Video Evidence Package to Health Canada, which suggested the Company received its license exactly 60 days from when it was submitted. We believe this is a strong sentiment to the strength of management to know how to submit a license without any further delay. Although still at an earlier stage compared to larger extraction players, in terms of market cap and the amount of time in operation, the Company can now be seriously discussed as a processing option in competition to MediPharm Labs (TSX:LABS), Valens GroWorks (TSXV:VGW), Neptune Wellness (TSX:NEPT), and Radiant Technologies (TSXV:RTI).

Next steps – tolling and supply agreements leading up to a sales license.

We anticipate the next few months to roll out similarly to MediPharm, the first company to receive an oil processing license without being a cultivator. After MediPharm received a process license on March 29, 2018, the Company began to build inventory, and subsequently announced that it had received its sales license on November 12, 2019. With the announcement, MediPharm also announced that it had processed 180 kg and had secured four tolling agreements with Emerald Therapeutics (TSX:EMH), INDIVA Limited (TSXV:NDVA), Bonify (Private), and James E. Wagner Cultivation (TSXV:JWCA). On January 12, 2019, LABS announced that its first shipments were sold for \$10M in December 2018. Of note, it took MediPharm ~8 months to receive its sales license after receiving its processing license and to book first revenues. Following a similar pattern, we believe Nextleaf should be able to book revenues by FQ2/20 (ending March 31, 2020) and, in the meantime, should begin to start announcing supply/tolling agreements. As a benchmark example, MediPharm ramped up quickly and surpassed many cultivators in terms of reported revenue and profitability. MediPharm reported Q2/19 revenue of \$31.5M on August 12, 2019, and is currently the third-highest revenue generating Canadian cannabis company behind Aurora Cannabis and Canopy Growth. In our view, Nextleaf could ramp up even faster than MediPharm.

VALUATION
Licensing milestone significantly reduces risk – raising target to \$1.75.

Receipt of the Standard Processing License on time attests to the strength of the management team and increases our confidence in the Company. We expect more institutional interest to occur, which should lead to more financing opportunity, coverage and liquidity. As such, we reduced our discount rate to 8% (was 10%), which was the main driver for our increase in NAV to \$2.37/share (was \$2.16/share). As a result, our blended one-year target price increased to \$1.75 (was \$1.65). Of note, our target F2021E EBITDA multiple remains at 4.0x, which we believe is reasonable, given the weakness of the cannabis space in general of late (Canopy is down 17% in the last 30 days and 37% in the last 90 days) and that MediPharm, the leader in the extraction space by market cap, currently trades at a similar F2021E EBITDA multiple of 4.1x.

Nextleaf's Comps Table

Company Name	Last Price (\$CAD)	Mrkt Cap (\$CAD)	EV (\$CAD)	Cash (\$CAD)	Debt (\$CAD)	EV/Revenues			EV/EBITDA		
						2019E	2020E	2021E	2019E	2020E	2021E
Nextleaf	\$0.60	\$64.7	\$61.1	\$3.6	\$0.0	n/a	1.7x	0.5x	n/m	39.8x	1.2x
Pure Play Cannabis Extraction Companies											
MediPharm Labs Corp.	\$4.95	\$645.6	\$566.9	\$72.7	\$6.0	3.9x	2.3x	1.4x	15.3x	7.2x	4.1x
Neptune Wellness Solutions Inc.	\$5.61	\$518.8	\$507.6	\$5.3	\$5.8	20.8x	7.8x	2.8x	n/m	33.1x	8.0x
Valens GroWorks Corp.	\$3.46	\$426.3	\$369.3	\$57.0	\$0.0	7.3x	2.3x	1.7x	22.1x	5.0x	3.6x
Radiant Technologies Inc.	\$0.71	\$192.5	\$161.7	\$23.5	\$7.3	n/a	n/a	n/a	n/m	n/m	n/m
Mean Cannabis Extraction						10.7x	4.1x	2.0x	18.7x	15.1x	5.2x
Canadian Majors											
Canopy Growth Corporation	\$35.70	\$12,418.8	\$8,405.7	\$1,816.6	\$2,196.4	37.1x	13.5x	7.0x	n/m	n/m	n/m
Aurora Cannabis Inc.	\$7.91	\$8,071.2	\$7,085.4	\$346.7	\$639.1	28.1x	10.3x	6.0x	n/m	91.0x	20.9x
Cronos Group Inc.	\$14.89	\$5,005.3	\$3,422.5	\$1,579.2	\$3.5	n/a	15.7x	8.2x	n/m	n/m	44.0x
Tilray, Inc.	\$39.65	\$3,871.9	\$3,061.9	\$241.4	\$568.6	12.8x	6.8x	4.0x	n/m	n/m	38.3x
Aphria Inc.	\$8.91	\$2,244.8	\$1,205.4	\$550.8	\$488.6	5.1x	1.8x	1.3x	n/m	16.0x	7.0x
HEXO Corp.	\$5.84	\$1,500.8	\$1,293.9	\$173.1	\$33.7	21.7x	3.8x	2.4x	n/m	21.7x	8.9x
OrganiGram Holdings Inc.	\$6.17	\$963.6	\$867.0	\$47.2	\$49.5	8.7x	4.2x	2.9x	22.8x	11.2x	7.8x
The Green Organic Dutchman Holdings Ltd.	\$2.76	\$760.4	\$689.3	\$68.7	\$2.4	18.9x	3.1x	1.3x	n/m	11.2x	6.5x
Village Farms International, Inc.	\$15.48	\$762.7	\$690.7	\$15.3	\$56.7	2.5x	1.9x	1.3x	12.7x	6.7x	4.0x
CannTrust Holdings Inc.	\$2.19	\$309.8	\$291.0	\$3.2	\$15.6	2.6x	1.3x	0.8x	n/m	5.4x	n/m
Mean Canadian Majors						15.3x	6.2x	3.5x	17.8x	23.3x	17.2x
US Based Operations											
Curaleaf Holdings, Inc.	\$9.93	\$4,622.0	\$4,279.7	\$140.4	\$201.9	12.5x	3.6x	n/a	86.4x	11.6x	n/m
Green Thumb Industries Inc.	\$12.88	\$2,797.5	\$2,458.9	\$177.6	\$161.1	8.8x	3.9x	2.6x	64.1x	12.9x	7.3x
Charlotte's Web Holdings, Inc.	\$21.37	\$2,082.8	\$2,004.2	\$67.3	\$11.3	12.1x	5.0x	3.4x	48.4x	15.8x	9.7x
Cresco Labs Inc.	\$12.45	\$1,565.1	\$1,421.0	\$80.0	\$64.2	6.0x	1.5x	1.1x	53.1x	5.9x	3.3x
MedMen Enterprises Inc.	\$2.65	\$1,384.4	\$1,089.1	\$29.3	\$266.0	5.4x	2.3x	1.3x	n/m	8.1x	4.2x
Trulieve Cannabis Corp.	\$10.90	\$1,239.7	\$1,010.5	\$70.7	\$158.5	3.2x	2.0x	1.6x	7.3x	5.1x	3.9x
Acreage Holdings, Inc.	\$11.36	\$1,016.2	\$867.5	\$110.5	\$38.1	3.7x	1.5x	0.8x	n/m	8.6x	2.4x
iAnthus Capital Holdings, Inc.	\$3.15	\$546.9	\$365.7	\$39.9	\$141.3	2.7x	1.0x	0.7x	n/m	4.3x	2.5x
Origin House	\$8.15	\$592.1	\$555.9	\$14.8	\$21.4	4.0x	2.0x	n/a	39.7x	11.1x	n/m
Mean US Based Operations						6.5x	2.5x	1.6x	49.8x	9.3x	4.7x

Source: Capital IQ, Ubika

Discount to peers. As of yesterday's close, OILS trades at 0.5x F2021E sales and 1.2x F2021E EBITDA, a discount to extraction peers, which trade at 2.0x and 5.2x, respectively. Once supply agreements with other Canadian cultivators start and continue to be announced, the market should continue to pay more attention to Nextleaf stock, which we believe will gradually close this valuation gap and drive the stock higher and closer to our one-year target price of \$1.75/share.

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Buy: Recommendation: stock is expected to appreciate from its current price beyond 20% in the next 12 months.

Neutral: Recommendation: stock is expected to trade in a narrow range from its current price level in the next 12 months.

Sell: Recommendation: stock is expected to decline from its current price level below 20% in the next 12 months.

U/R: Under Review.

N/R: Not Rated.

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- | | |
|---|--------|
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