

Delta 9 Cannabis Inc.

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Delta 9 Cannabis joins short list of profitable cannabis companies by staying true to its model

Delta 9 Cannabis Inc (TSE:DN) (OTCQX:VRNDF) is a Canadian cannabis producer with a key advantage over its industry peers - it's turning a profit.

The Winnipeg-based company reported revenues of C\$11.8 million during its first quarter 2020, a 109% increase from the \$5.6 million from the same period a year ago, and positive net income of \$2.9 million or \$0.02 per share for the three-month period ended March 31.

At a time when so many cannabis companies are struggling even without the added burden of the coronavirus pandemic, these numbers are remarkable. With quarter-over-quarter growth and near-term catalysts that position the company to deliver results, Delta 9 is clearly on a roll.

WATCH: Delta 9 Cannabis leverages unique strategy to generate record earnings in Q1 2020

The numbers are a clear indicator of the strength of the firm's three individual business units, says CEO John Arbuthnot. Delta 9's diversified revenue streams include a chain of four retail storefronts (with an additional three pending license), wholesale cannabis sales and a B2B division that offers the modular cultivation equipment known as Grow Pods, consulting, and genetics sales. Retail sales lead the company's overall totals at \$5.7 million, while B2B and wholesale revenues both landed at \$3 million.

"What stands out to us from a revenue standpoint is the strength in our retail division," Arbuthnot said in a recent interview with Proactive. "Our B2B numbers continue to be strong, and we saw quite an uptick in our wholesale business both in number of grams sold and the average selling price."

The results led to Canaccord Genuity upping its price target from C\$0.60 to C\$0.75 and rating the stock as a Speculative Buy this week. "We believe a pipeline of Grow Pod projects will continue to boost revenues over the next couple of quarters while retail store growth should provide a conduit for wholesale distribution over the coming 24 months," analyst Kimberly Hedlin wrote.

Pattern of profits

In a sign of positive momentum, gross profit came in at \$4.9 million during the quarter, a 51% increase from the \$3.2 million it put up over 4Q 2019.

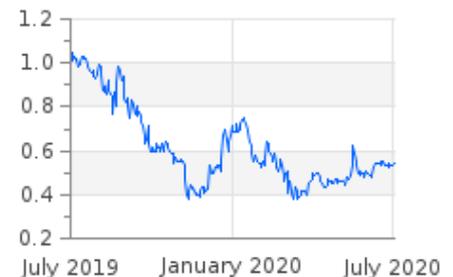
"It's a major inflection point for any business to reach profitability, particularly important in the cannabis space and obviously critical given the COVID-19 situation and capital markets volatility," Arbuthnot commented.

For a company that displays a pattern of positive growth and positive earnings, it may come as a surprise that Delta 9's market capitalization still sits at around \$42 million. That's largely a function of the wider dynamics at play in the

Price: 0.54

Market Cap: \$48.18 m

1 Year Share Price Graph



Share Information

Code: DN

Listing: TSX

52 week High Low
1.13 0.33

Sector: Cannabis

Website: www.delta9.ca

Company Synopsis:

Delta 9 Cannabis Inc. is a vertically integrated cannabis company focused on bringing the highest quality cannabis products to market. The company sells cannabis products through its wholesale and retail sales channels and sells its cannabis grow pods to other businesses. Delta 9's wholly-owned subsidiary, Delta 9 Bio-Tech Inc.

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cannabis sector, according to Arbuthnot. Investor sentiment towards the space has soured considerably as companies routinely fell short of expectations during the first year of legalization. Capital allocation is going towards the big players that provide a sense of security, rightly or wrongly, in the stock.

The recent results, however, may change that perception, according to Arbuthnot. "I think we've weathered the past few months a little bit better than our competitors. Posting positive results like we have puts the company in a very different light. I've always thought that cannabis companies will start to trade based on metrics like revenue, earnings and EBIDTA, similar to all other sectors. Right now we're only trading at around four times earnings, but as we start to see a rebound in global equities, a name like Delta 9 could see a significant increase in our share price once the market starts to gain recognition of these results."

Diversified revenue model

What's driving the success of Delta 9 is its diversified revenue model that allows the company to be nimbler than their peers. The firm is an industry leader in the province of Manitoba with a 30% market share and boasts an ample strain library with 350 seeds available for cultivation, including 75 commercial and 12 core strains. It is also pioneering a unique method of cultivation using Grow Pods, or modular shipping container-esque units that ensure consistency and quality in production.

"The best way to de-risk our business model was to vertically integrate and capture as much margin as possible along the value chain," Arbuthnot said.

The firm positioned its business to become a low cost producer who can take product right to the end consumer, which helps to protect it against any supply and demand uncertainties. "It's very important in terms of the company's strength, and certainly unique from an investor standpoint to have the opportunity to have exposure to many different business segments."

Delta 9 is currently licensed to produce around 8,500 kilograms per year. Health Canada recently approved a purpose-built processing centre that will allow the firm to bottle, package and distribute up to 25,000 kilograms annually. As a result, the firm is ramping up its production capacity and should be able to nearly double its current first quarter output of 1.2 million grams.

Arbuthnot also sees an opportunity for the company to become a net buyer of cannabis from other producers and distribute branded Delta 9 product in a consumer packaged format. "We work with a lot of different partners in our B2B segment and provided our grow pods or other infrastructure with genetics, and now we can work with these groups to bring that product into our facility for distribution across Canada," Arbuthnot said. "It gives us a great opportunity to not only leverage our business assets but also our existing partnerships with other licensed cultivators to increase our overall revenue and capacity from our wholesale business."

Essential service

Unlike most small businesses around the world, Delta 9 is deemed an essential service amid the coronavirus pandemic. Its retail segment saw a notable uptick in foot traffic to physical locations and a huge increase in online orders since a pandemic was declared in March. In addition to making the required adjustments such as heightened cleaning procedures and Plexiglas shields, Arbuthnot and the team boosted the salaries of front-line employees by \$2 per hour. What's more, the company has hired an extra 76 staff members since March 26.

Delta 9's strong balance sheet gives the company a solid basis to grow. Its cash position increased from the end of last year to the end of the first quarter and the company is now producing positive operating cash. It ended the quarter with C\$23.9 million in working capital and has excess capacity under its existing credit facility - an important differentiator in an uncertain post-COVID global economy.

"We have a good amount of working capital and access to additional capital where we need it," Arbuthnot said. "There's a strong underlying foundation here that gives us real safety."

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