

GTEC Holdings Ltd. (GTEC:TSX)

RECOMMENDATION: Buy

1 YR-TARGET PRICE: \$2.00

RISK RATING: HIGH

Grey Bruce License a Step Towards Unlocking Value

SHARE DATA

Price (5/17/19)	\$0.45
Shares outstanding (basic)	140M
Shares outstanding (diuted)	184M
Market cap (basic)	\$63M
Market cap (diluted)	\$83M
Net Cash (debt) 2019E	\$5M
Enterprise Value (Diluted)	\$88M

FINANCIALS	2018A	2019E	2020E
Revenue (\$M)	\$0.1	\$13.1	\$62.2
EBITDA (\$M)	-\$10.4	-\$3.0	\$29.3
EPS (FD) (\$)	\$ (0.10)	\$ (0.02)	\$ 0.11

RATIOS	2018A	2019E	2020E
EV/Sales	1519x	6.7x	1.4x
EV/EBITDA	n/a	n/a	3.0x
P/E	n/a	n/a	4.0x

VALUATION:

Recommendation:	Buy
One Year Price Target:	\$2.00
Valuation:	12.5x 2020E EV/EBITDA



Grey Bruce Facility Granted Cultivation License by Health Canada

We view the Grey Bruce (GB) approval as positive for GTEC and see it as another step towards unlocking the value of the company's underappreciated assets and team. Our estimates and target price, which already included a mid-year approval for GB, are unchanged post the announcement. However, we see the news garnering a positive reaction from the market as investors accord a lower risk profile to the buildout of GTEC's cultivation footprint. **In brief, we see three main takeaways from the news:**

- The approval of Grey Bruce adds an annualized ~1,700 kg of capacity and ~\$8.5M of revenue.** Our current forecast includes GB delivering 743 kg and revenue of \$3.7M in 2019, before growing to 1,698 kg and \$8.5M in 2020. While we have not changed our estimates on the back of the announcement, we believe the market may grant a higher degree of certainty to GTEC's growth profile on the back of the news.
- The license gives both ACC and GB access to high end cultivars.** With GB now approved, GTEC is able to transfer in new premium genetics and ultimately move those cultivars to its other facilities. Given the company's growing expertise and unique genetic strains, we believe that GTEC's new genetics could garner premium wholesale pricing once established.
- Last, we see the approval de-risking the completion of the company's additional facilities (Tumbleweed, GBP and F20).** GTEC's team has now gone through the approval process at multiple facilities which showcases their ability to build and license cultivation facilities under Health Canada's regulatory requirements. We see this experience de-risking the completion process of GTEC's additional three facilities.

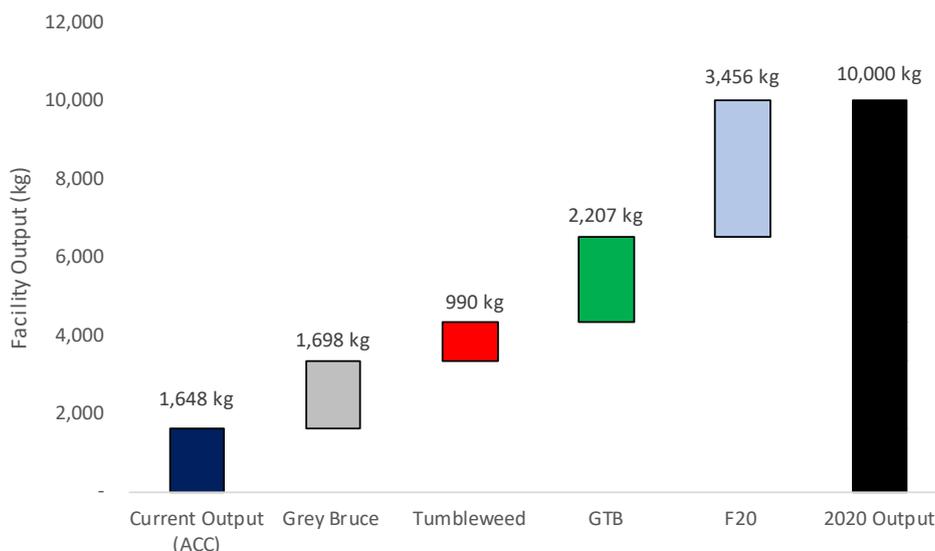
Stock Undervalued Relative to Peers with Catalysts Coming

As highlighted in more detail below, GTEC continues to trade at a discounted valuation of 3.0x our 2020E EBITDA vs. the group at 9.3x. Given the company's growth profile and additional short term catalysts, we believe that this gap will close. Potential catalysts include Tumbleweed obtaining its cultivation license and ACC obtaining a sales license, both of which should occur in the near term. We see these as major checkpoints along the buildout of GTEC's operations, and would expect shares to appreciate following the news flow.

Market Continues to Undervalue Production Potential Output

With the addition of Grey Bruce, GTEC now operates two indoor facilities, ACC and Grey Bruce, which will be able to produce an estimated 3,346kg of ultra-premium craft cannabis annually. In addition to these facilities, GTEC is awaiting approval of its third facility, Tumbleweed Farms, and is building two additional facilities, GBP and F20. In total, we expect these facilities to boost total annualized production capacity from 3,346 kg/annum to over 10,000 kg/annum (Note: We only include GTEC's 49% share of production at F20) (Figure 1).

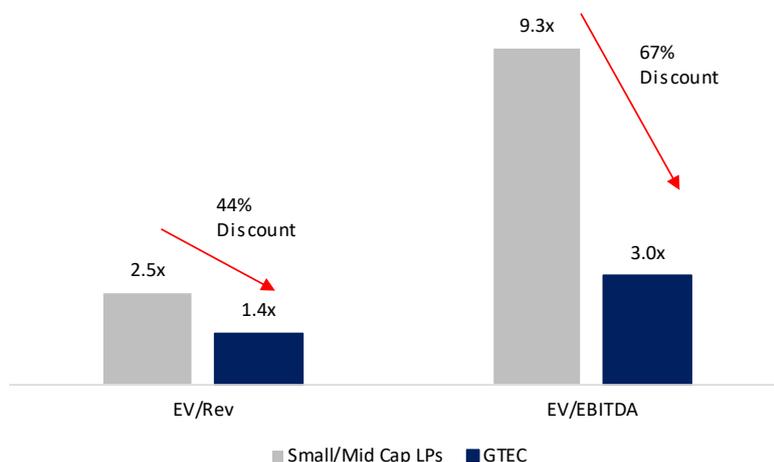
Figure 1: Incremental Flower Output from New Facilities



Source: SCP research

Despite this potential increase in output, GTEC shares continue to trade at a discount to other mid/small cap cannabis LPs at 3.0x versus the group at 9.3x 2020 EBITDA estimates (Figure 2). We believe that as GTEC's additional facilities come online, this multiple gap will close, leading to strong returns for patient shareholders. Additionally, we note that similar high end cultivators like Whistler Medical Marijuana Corp, have sold for as high as 17x forward EBITDA estimates. While we agree that the market dynamics have changed since this sale, we believe that in the long term the market will continue to pay a premium for premium indoor cultivation.

Figure 2: Trading at a discount to 2020 estimates



Source: SCP research

Why We Like GTEC

- I. Top quality management team with a track record of producing ultra-premium flower at scale
- II. Value of near term production increase is not reflected in current valuation
- III. Retail assets could provide upside to our forecast
- IV. Ultimately, we see GTEC as a takeout candidate

Income Statement

Income Statement (C\$000)	2018A	2019E	2020E	2021E
Revenue	58	13,084	62,192	62,192
Cost of sales	42	4,110	21,658	21,658
Gross margin	16	8,974	40,533	40,533
Unrealized gain on changes in FV of biological assets	160	520	-	-
	176	9,495	40,533	40,533
Operating expenses		68.6%	65.2%	65.2%
Amortization	195	848	1,174	1,165
SG&A	10,859	12,301	11,194	11,194
	11,054	13,149	12,368	12,359
Net loss from operations	(10,879)	(3,654)	28,165	28,174
Adjusted EBITDA	(10,406)	(3,014)	29,339	29,339
EBITDA Margin %	-18017%	-23%	47%	47%
Other income (expense)	(2,072)	(143)	-	-
Net Loss before income taxes	(12,950)	(3,797)	28,165	28,174
Income tax expense/recovery	2,414	(212)	7,605	7,607
Net loss and comprehensive loss	(10,537)	(3,585)	20,561	20,567
Earnings (loss) per share (Basic)	\$ (0.14)	\$ (0.03)	\$ 0.15	\$ 0.15
Earnings (loss) per share (Diluted)	\$ (0.10)	\$ (0.02)	\$ 0.11	\$ 0.11
Weighted basic shares outstanding	76,349	122,798	139,953	139,953
Weighted diluted shares outstanding	110,543	165,952	184,126	184,126

Source: SCP research

Disclosures & Disclaimers

This research report (as defined in IIROC Rule 3400) is issued and approved for distribution in Canada by Sprott Capital Partners LP (“SCP”), an investment dealer who is a member of the Investment Industry Regulatory Organization of Canada (“IIROC”) and the Canadian Investor Protection Fund (“CIPF”). The general partner of SCP is Sprott Capital Partners GP Inc. and SCP is a wholly-owned subsidiary of Sprott Inc., which is a publicly listed company on the Toronto Stock Exchange under the symbol “SII”. Sprott Asset Management LP (“SAM”), a registered investment manager to the Sprott Funds and is an affiliate of SCP.

This research report is provided to retail clients and institutional investors for information purposes only. The opinions expressed in this report are the opinions of the author and readers should not assume they reflect the opinions or recommendations of SCP’s research department. The information in this report is drawn from sources believed to be reliable but the accuracy or completeness of the information is not guaranteed, nor in providing it does SCP and/or affiliated companies or persons assume any responsibility or liability whatsoever. This report is not to be construed as an offer to sell or a solicitation of an offer to buy any securities. SCP accepts no liability whatsoever for any loss arising from any use or reliance on this research report or the information contained herein.

Past performance is not a guarantee of future results, and no representation or warranty, expressed or implied, is made regarding future performance of any security mentioned in this research report. The price of the securities mentioned in this research report and the income they generate may fluctuate and/or be adversely affected by market factors or exchange rates, and investors may realize losses on investments in such securities, including the loss of investment principal. Furthermore, the securities discussed in this research report may not be liquid investments, may have a high level of volatility or may be subject to additional and special risks associated with securities and investments in emerging markets and/or foreign countries that may give rise to substantial risk and are not suitable for all investors.

SCP may participate in an underwriting of, have a position in, or make a market in, the securities mentioned herein, including options, futures or other derivatives instruments thereon, and may, as a principal or agent, buy or sell such products.

Dissemination of Research:

SCP’s research is distributed electronically through email or available in hard copy upon request. Research is disseminated concurrently to a pre-determined list of clients provided by SCP’s Institutional Sales Representative and retail Investment Advisors. Should you wish to no longer receive electronic communications from us, please contact unsubscribe@sprott.com and indicate in the subject line your full name and/or corporate entity name and that you wish to unsubscribe from receiving research.

Research Analyst Certification:

Each Research Analyst and/or Associate who is involved in the preparation of this research report hereby certifies that:

- The views and recommendations expressed herein accurately reflect his/her personal views about any and all of the securities or issuers that are the subject matter of this research report;
- His/her compensation is not and will not be directly related to the specific recommendations or view expressed by the Research analyst in this research report;
- They have not affected a trade in a security of any class of the issuer within the 30-day period prior to the publication of this research report;
- They have not distributed or discussed this Research Report to/with the issuer, investment banking group or any other third party except for the sole purpose of verifying factual information; and
- They are unaware of any other potential conflicts of interest.

UK Residents:

Sprott Partners UK Limited is an appointed representative of PillarFour Securities LLP which is authorized and regulated by the Financial Conduct Authority. This document has been approved under section 21(1) of the FMSA 2000 by PillarFour Securities LLP (“PillarFour”) for communication only to eligible counterparties and professional clients as those terms are defined by the rules of the Financial Conduct Authority. Its contents are not directed at UK retail clients. PillarFour does not provide investment services to retail clients.

PillarFour publishes this document as non-independent research which is a marketing communication under the Conduct of Business rules. It has not been prepared in accordance with the regulatory rules relating to independent research, nor is it subject to the prohibition on dealing ahead of the dissemination of investment research. It does not constitute a personal recommendation and does not constitute an offer or a solicitation to buy or sell any security. Neither Sprott nor PillarFour nor any of its directors, officers, employees or agents shall have any liability, howsoever arising, for any error or incompleteness of fact or opinion in it or lack of care in its preparation or publication; provided that this shall not exclude liability to the extent that this is impermissible under the law relating to financial services. All statements and opinions are made as of the date on the face of this document and are not held out as applicable thereafter. This document is intended for distribution only in those jurisdictions where PillarFour is permitted to distribute its research.

Equity Research

Sprott Capital Partners Explanation of Recommendations:

Should SCP issue research with recommendations, the research rating guidelines will be based on the following recommendations:

BUY: The stocks total returns are expected to be materially better than the overall market with higher return expectations needed for more risky securities markets

NEUTRAL: The stock's total returns are expected to be in line with the overall market

SELL: The stocks total returns are expected to be materially lower than the overall market

TENDER: The analyst recommends tendering shares to a formal tender offering

UNDER REVIEW: The stock will be placed under review when there is a significant material event with further information pending; and/or when the research analyst determines it is necessary to await adequate information that could potentially lead to a re-evaluation of the rating, target price or forecast; and/or when coverage of a particular security is transferred from one analyst to another to give the new analyst time to reconfirm the rating, target price or forecast.

NOT RATED (N/R): The stock is not currently rated

Research Disclosure		Response
1	SCP and its affiliates collectively beneficially owns 1% or more of any class of the issuer's equity securities ¹	NO
2	The analyst or any associate of the analyst responsible for the report or recommendation or any individual directly involved in the preparation of the report holds or is short any of the issuer's securities directly or through derivatives	NO
3	An SCP partner, director, officer or analyst involved in the preparation of a report on the issuer, has during the preceding 12 months provided services to the issuer for remuneration other than normal course investment advisory or trading execution services	NO
4	SCP has provided investment banking services for the issuer during the 12 months preceding the date of issuance of the research report or recommendation	YES
5	Name of any director, officer, employee or agent of SCP who is an officer, director or employee of the issuer, or who serves in an advisory capacity to the issuer	NO
6	SCP is making a market in an equity or equity related security of the issuer	NO
7	The analyst preparing this report received compensation based upon SCP's investment banking revenue for the issuer	NO
8	The analyst has conducted a site visit and has viewed a major facility or operation of the issuer	YES
9	The analyst has been reimbursed for travel expenses for a site visit by the issuer	NO

Sprott Capital Partners Equity Research Ratings:

Summary of Recommendations as of June 2019	
BUY:	14
HOLD:	1
SELL:	0
UNDER REVIEW:	1
NOT RATED:	1
TOTAL	100%

