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Fundamental Research Corp.

*Investment Analysis for Intelligent Investors*

April 24, 2019

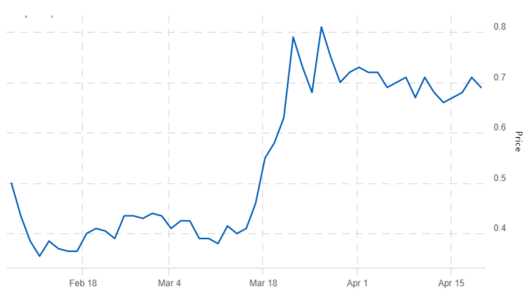
# Blueberries Medical Corp. (CSE: BBM / OTC: BBRRF / FRA: 1OA) – Latin American Producer with Enormous Footprint and Low Production Costs – Introductory Note

**Sector/Industry: Cannabis** **www.blueberriesmed.com**

**Market Data (as of April 24, 2019)**

| | |
|---|---|
| **Current Price** | **$0.69** |
| **Fair Value** | **N/A** |
| **Rating*** | **N/A** |
| **Risk*** | **N/A** |
| 52 Week Range | $0.36 - $0.72 |
| Shares O/S | 107,287,772 |
| Market Cap | $74.03 M |
| Current Yield | N/A |
| P/E (forward) | N/A |
| P/B | 8.23x |
| YoY Return | N/A |
| YoY CSE | -6.08% |

*see back of report for rating and risk definitions




## Highlights

- Blueberries Medical Corp. (“Blueberries”, “company”) is a leading Latin American producer of premium medical-grade cannabis products, with operations in Colombia and Argentina.
- **Huge Cultivation Operations:** Blueberries estimates that company-wide, dried flower equivalent production may hit 2.21 million kg by 2025, multiples of the proposed production capacity of even Canada’s largest producers.
- **Low Production and Operating Costs:** Due to ideal climate conditions and low labor costs, the company expects a long-term cost per gram of US$0.15. This is exceedingly low relative to the average cost per gram of Canadian producers.
- **Explosive Growth in Latin America’s Legal Cannabis Market Expected:** According to a report by Prohibition Partners, legal Latin American cannabis sales of US$125 million in 2018 are expected to grow at a CAGR of 58.41% to US$12.70 billion by 2028.
- **Undervalued Relative to Peers:** Based on the valuation multiples at which various comparable cannabis companies are trading, the company could have significant upside.
- **We will be initiating coverage on Blueberries shortly.**

## Risks

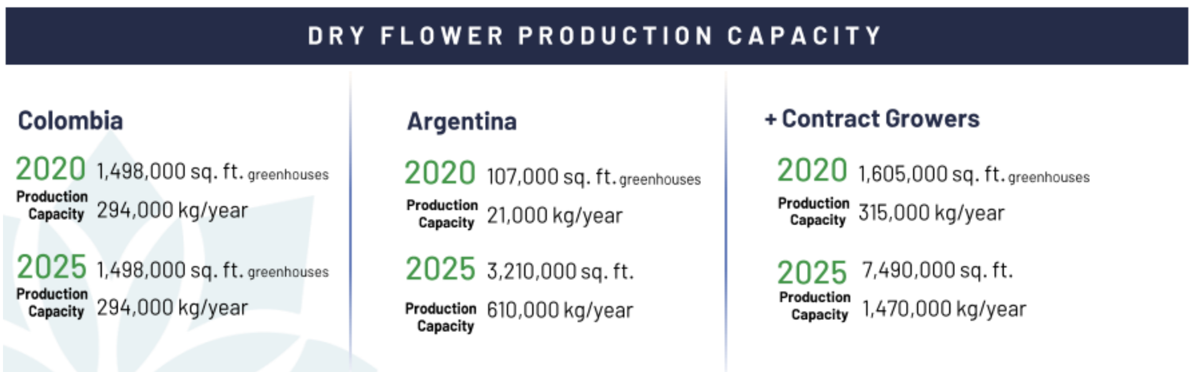
- Highly regulated industry.
- Licensing/ production delay risks.
- Biological contamination risks.
- Access to capital and share dilution.
- Liquidity risks.

| (in C$) - YE Dec 31st | | |
|---|---|---|
| **Liquidity & Capital Structure** | | **Q3-2018** |
| Cash | $ | 7,776,290 |
| Working Capital | $ | 7,548,160 |
| Current Ratio | | 33.09 |
| LT Debt | $ | - |
| Total Debt | $ | - |
| LT Debt / Capital | | - |
| Total Debt / Capital | | - |
| Total Invested Capital | $ | 1,213,698 |

## *Company Overview*

Blueberries is one of only a few public cannabis companies with core operations located in South America. Blueberries began trading on the Canadian Securities Exchange ("CSE") on February 6, 2019, becoming the first cannabis company with operations in Colombia to do so. Fully licensed for the production, extraction and export of cannabis in Colombia, Blueberries has recently initiated a push into Argentina via definitive agreements to enter into a joint venture ("JV") with Cannava Avatara, S.E. ("Cannava"). The JV with Cannava, an Argentinian state-owned cannabis company, will provide Blueberries with all the licensing and authorization required to set up production in Argentina, and will make Blueberries one of only three companies with Argentinian cannabis production, extraction and export rights.

**As a result of the above operational initiatives, the company will have a total production capacity of 2.21 million kg of dried cannabis equivalent by 2025.**




*Source: Company*

The production is expected to be derived from both internal cultivation operations as well as the cultivation from contract growers in the Latin American region. **This production capacity is multiples higher than the total announced production capacity of even Canada's largest LPs.** Furthermore, Blueberries' expected production foot print, apart from being massive, is also expected to be low-cost. According to the company, the long-term production cost per gram is forecasted at US$0.15, a fraction of the average cost per gram of Canadian LPs. With significant growth drivers to fuel a large pipeline of catalysts, we believe investors should begin monitoring Blueberries, as we expect to initiate on the company shortly.

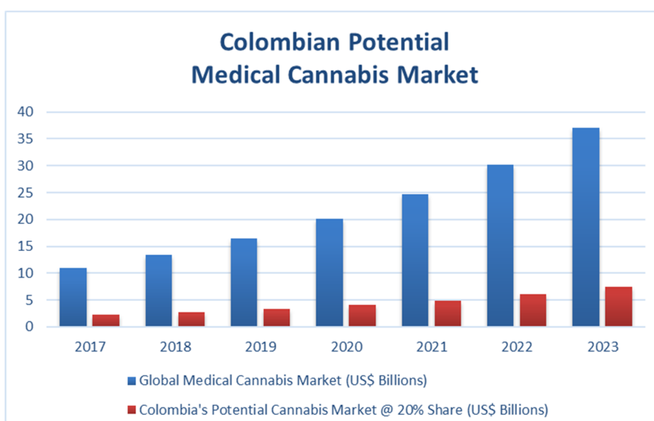
## *Strong Management with Brand Name Track Record*

When dealing with companies with operations in emerging markets, we expect that many investors view these companies with an emphasis on potential risk factors. This is especially true for young industries such as cannabis, where a lack of an established status quo, and constant change, create a need for deeper analysis and strong awareness for sources of risk. A mitigating factor that can help reduce a cannabis company's risk profile is a strong management team, ideally with a track record at established companies that are leaders in their respective industry. We believe that given these criteria, Blueberries management tick many of the prerequisites, complementing strong operations, and heady growth prospects, with competent leadership. The below gives an overview of the company's management. **We note that Blueberries' CEO, Dr. Stocker, combines experience with a large-cap company with experience in the Latin American cannabis space, having served as CEO of Colombian cannabis company Pharmacielo Ltd. (TSXV: PCLO) between 2015 and 2018.**


*Source: Company*

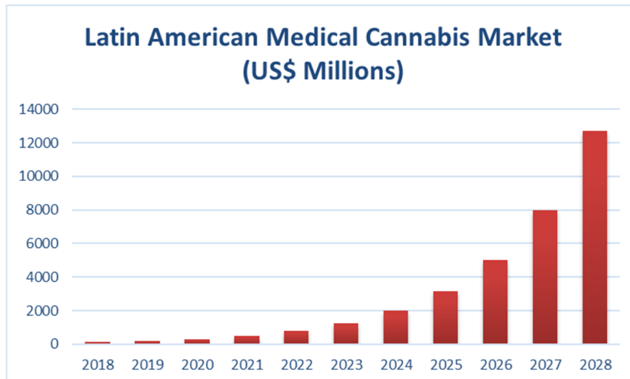
***Cannabis in Latin America***

Steering clear of the heavily competitive Canadian cannabis industry, Blueberries have set up shop in Colombia and Argentina, two Latin American countries with a combined population of 93.34 million. In both Colombia and Argentina, the recreational consumption of cannabis, whilst illegal, is decriminalized, and medical usage is federally legal. Decriminalization implies that whilst illegal, personal possession of cannabis is not prosecuted. Despite the domestic recreational market technically being off limits, this has not stopped significant foreign investment pouring into these countries, with Colombia alone having received over $100 million in CAPEX funding during 2018, largely from Canadian LPs. Indeed, a report by Reuters in 2018 indicated that Colombian growers believed that they could eventually capture 20% of the global medical cannabis market. For reference, Research and Markets predicts that the global medical cannabis market could grow at a CAGR of 22.41% from 2017, to reach US$37 billion by 2023. That indicates that Colombia's medical cannabis market could hit a US$7.40 billion valuation by 2023, assuming that Colombia captures a 20% market share. However, to assume that 20% of global cannabis supply will come from a single country may be a stretch.




*Source: Reuters, Research and Markets, FRC*

Looking at the entire Latin American region as a whole demonstrates the lucrative opportunity open to Blueberries. According to the LATAM Cannabis Report published by Prohibition Partners, legal sales in Latin America, despite being only an expected US$125 million in 2018, could grow to US$12.70 billion by 2028, reflecting a CAGR of 58.41% during the period.




*Source: Prohibition Partners, FRC*

Looking at Colombia, the total legal cannabis market is expected to reach US$664 million in sales by 2028, representing 5.23% of Latin America's forecasted cannabis market in 2028. According to Prohibition Partners, and a survey done by the United Nation Office on Drugs and Crime ("UNODC"), the average price of cannabis in Colombia is US$1.60 per gram. As an additional anecdote, Bogota was the second cheapest city for purchasing cannabis in 2018, according to the UNODC.

**Colombia Forecasted Cannabis Market**

| | Forecast Medical Cannabis Market Value 2028 (US$m) | Forecast Recreational Cannabis Market Value 2028 (US$m) | Forecast Industrial Cannabis Market Value 2028 (US$m) | Total 2028 (US$m) |
|---|---|---|---|---|
| Primary Market | 280.0 | 137.9 | 0.41 | 418.3 |
| Secondary Market | 164.4 | 81.0 | 0.24 | 245.7 |
| Total | 444.4 | 218.9 | 0.66 | 664.0 |

- primary market refers to sales of base cannabis goods, whereas secondary market refers to ancillary services.

*Source: Prohibition Partners*

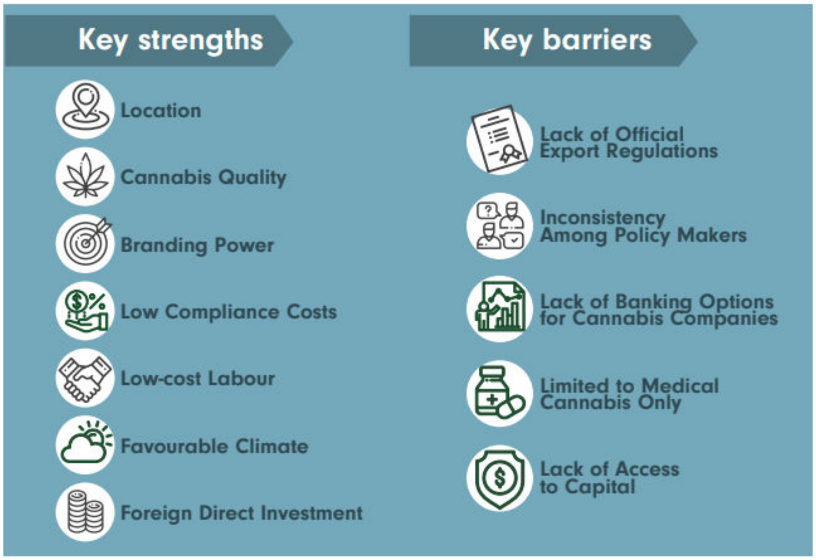
With regards to Argentina, the total legal cannabis market is expected to reach US$1.13 billion in sales by 2028, representing 8.90% of Latin America's forecasted cannabis market in 2028. According to Prohibition Partners and the UNODC, the average price of cannabis in Argentina is US$1.30 per gram.

**Argentina Forecasted Cannabis Market**

| | Forecast Medical Cannabis Market Value 2028 (US$m) | Forecast Recreational Cannabis Market Value 2028 (US$m) | Forecast Industrial Cannabis Market Value 2028 (US$m) | Total 2028 (US$m) |
|---|---|---|---|---|
| Primary Market | 474.6 | 233.8 | 0.7 | 709.1 |
| Secondary Market | 278.7 | 137.3 | 0.4 | 416.5 |
| Total | 753.4 | 371.1 | 1.1 | 1,125.6 |

*Source: Prohibition Partners*

Though interest in cannabis commerce was previously concentrated in the Canadian market, as international markets have opened, we have seen a shift in market sentiment in favor of non-domestic players. In the case of Latin American producers such as Blueberries, investors may benefit from exposure to region-specific advantages that these companies enjoy. Amongst these benefits are low costs associated with cheaper labor, and favorable climate, that makes cultivation for these companies significantly less costly than for Canadian LPs.




*Source: Prohibition Partners*

***Enormous Production Footprint: Colombia and Argentina***

As we mentioned earlier in this note, Blueberries has a tremendous proposed production footprint divided between their operations in Colombia and their recently initiated JV with Cannava in Argentina.

In Colombia, the company own 18 hectares or 1.94 million square-feet worth of land, with three hectares (0.32 million square-feet) allocated to their Guatavita property, and 15 hectares (1.61 million square-feet) allocated to their Zipaquira property. The Guatavita property includes a currently operating nursery, propagation and production center, which came online in 2018, according to management. The Zipaquira property, which does not currently include any operating assets, has been acquired as an expansion property to provide scalability to the company's Colombian operations. Construction of the nursery, propagation, and production facilities on the Zipaquira property, is starting in late April 2019. In addition to their cultivation assets, the company also has an extraction and processing facility located in an industrial park approximately 17 kilometers away from the cultivation properties. This processing facility (size and processing capacity undisclosed) is expected to be commercially operational in Q4-2019. Furthermore, the company expects that they will receive the EU-GMP certification necessary to begin international exports from production at this facility in Q4-2019.

**Guatavita Property**

*Source: Company*

Moving forward, the company expects to expand their total greenhouse footprint in Colombia to 1.50 million square-feet by 2020. Expected production capacity from the greenhouse facilities is estimated at 294,000 kg per annum, suggesting a yield of 196.26 grams per square-foot. Though this is higher than our observation of an average yield of between 80 grams per square-foot and 120 grams per square-foot for Canadian cultivation operations, we estimate that the higher yield may be due to more ideal climate conditions than those faced by Canadian growers. As an example, the company reports that the regions in which their Colombian cultivation operations are located receive an average of 12 hours of sunlight year-round, with an average temperature of 21 degree Celsius and a humidity below 45%. These are conditions that are ideal for cannabis cultivation, and thus, provide yield-enhancing advantages to the company.

In Argentina, similar ideal growing conditions and access to an even larger growing property than their Colombian assets provide further upside. Through their JV with Cannava, the company has access to an initial property comprising 3.21 million square-feet. Whilst the build out of this property is expected to be slower, with only a 107,000 square-foot greenhouse facility producing 21,000 kg of cannabis per annum expected by 2020, Blueberries expects that by 2025, they will be jointly operating a 2.20 million square-foot greenhouse capable of producing 441,000 kg per annum. In addition, the company plans on establishing outdoor cultivation operations, leading to a total of 3.21 million square-feet in greenhouse and outdoor cultivation space, which is expected to produce 661,000 kg of cannabis per annum by 2025. The Jujuy province in which the JV facility will be located, is a province of Argentina that is famed for its production of tobacco, and given its history, it is likely that the land package can be easily converted into cannabis production.

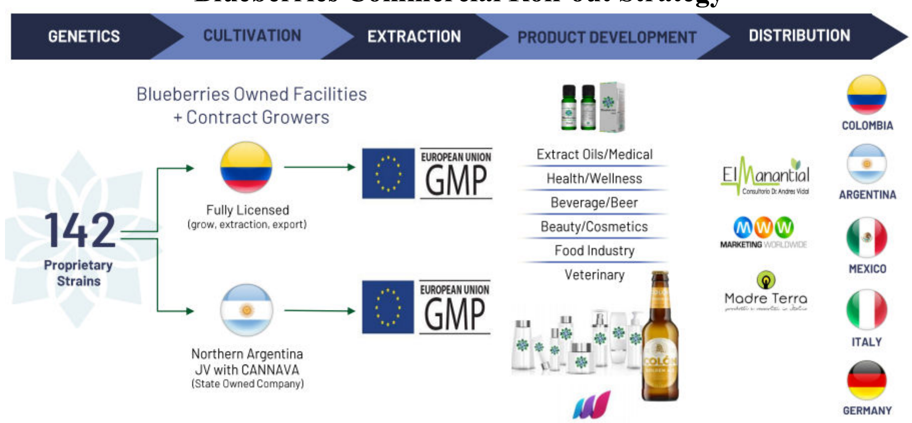
**Blueberries Argentina Production Capacity**


*Source: Company*

***Strategic Roll-Out***

With such a massive cultivation footprint, Blueberries has all the biomass required to set up a finished infused goods division that more specifically targets and disrupts various segments of the consumer-packaged goods industry. Utilizing various partnerships which we will outline in our initiating report, Blueberries intends to leverage future licensing and certification to distribute their production to international markets. The below image provides a flavor of the company's global ambitions, as well as the key targeted markets.

**Blueberries Commercial Roll-out Strategy**




*Source: Company*

***Valuations in the Sector***

With substantial expected production, increasing product development and wide commercial distribution, Blueberries has the growth drivers to suggest a powerful value proposition. Though the company's story should command investor's attention based on the merits of its own asset-base and planned operational initiatives, we believe that the company may be undervalued relative to its own peers. The table below outlines various valuation multiples at which Blueberries' peers are trading.

| Company | Ticker | Total Proposed Facility Area (SQ-FT) | Proposed Production Capacity (KG) | EV | MC | EV/ SQ-FT | EV/ KG | P/ SQ-FT | P/ KG |
|---|---|---|---|---|---|---|---|---|---|
| Blueberries Medical Corp. | CSE: BBM | 4,708,000 | 904,000 | $ 66,268,233 | $ 74,028,563 | $ 14 | $ 73 | $ 16 | $ 82 |
| Pharmacielo Ltd. | TSXV: PCLO | 15,000,000 | 5,600,000 | $ 789,755,000 | $ 797,390,000 | $ 53 | $ 141 | $ 53 | $ 142 |
| ICC Labs Inc.* | Acquired | 1,216,000 | 450,000 | $ 290,000,000 | $ 290,000,000 | $ 238 | $ 644 | $ 238 | $ 644 |
| Khiron Life Sciences Corp. | TSXV: KHRN | 2,400,000 | 220,000 | $ 270,726,000 | $ 285,425,000 | $ 113 | $ 1,231 | $ 119 | $ 1,297 |
| Avicanna Inc. | Private | 410,000 | 24,000 | $ 122,302,300 | $ 139,846,216 | $ 298 | $ 5,096 | $ 341 | $ 5,827 |
| Colombian Cannabis S.A.S | Acquired | 4,500,000 | | $ 152,000,000 | $ 152,000,000 | $ 34 | | $ 34 | |
| **Average** | | | | | | **$ 125** | **$ 1,437** | **$ 134** | **$ 1,599** |

*Source: FRC, Capital IQ*

We have omitted expected production from contractors for BBM. Also, as the funding status varies across companies listed above, the table is not meant to provide any type of valuation, but a preliminary perspective on the valuations in the sector.

## *Financials*

Whilst the Guatavita property is currently operating, it is not clear if sales have begun. It is possible that the initial facilities are still in the test harvest stage, and will initiate sales in the near future. The liquidity and capital position are outlined below:

| (in C$) - YE Dec 31st<br>Liquidity & Capital Structure | | Q3-2018 |
|---|---|---|
| Cash | $ | 7,776,290 |
| Working Capital | $ | 7,548,160 |
| Current Ratio | | 33.09 |
| LT Debt | $ | - |
| Total Debt | $ | - |
| LT Debt / Capital | | - |
| Total Debt / Capital | | - |
| Total Invested Capital | $ | 1,213,698 |

*Source: FRC, Financial Statements*

**We expect to initiate coverage on Blueberries shortly.**

**Fundamental Research Corp. Equity Rating Scale:**
**Buy** – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk
**Hold** – Annual expected rate of return is between 5% and 12%
**Sell** – Annual expected rate of return is below 5% or the expected return is not commensurate with risk
**Suspended or Rating N/A—** Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

**Fundamental Research Corp. Risk Rating Scale:**
**1 (Low Risk) -** The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

**2 (Below Average Risk) -** The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

**3 (Average Risk) -** The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

**4 (Speculative) -** The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

**5 (Highly Speculative) -** The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.

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