



THC Global Group
ACN 614 508 039

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THC GLOBAL

Initiation of coverage

24 January 2020

FY2020 – Transitioning to growth

With the first bottling of its medicinal cannabis oil in early December at its Southport Therapeutic Goods Administration (TGA) approved good manufacturing practice (GMP) pharmaceuticals biomanufacturing facility, THC Global (THC) has validated its locally grown “biomass to bottle” processing capability. THC is now able to accept feedstock from any licensed permitted cultivator, or its own cultivation operations, to produce cannabinoid oil to sell domestically or export globally.

All licensed up and ready to go

The TGA has granted THC a license for the commercial manufacture of therapeutic goods (GMP License) at the Southport facility. By the end of 1Q CY2020 we forecast THC will have met all the required product validation tests on the cannabidiol (CBD) oil being produced at Southport and will have received the final TGA approval allowing THC to sell that product into the market.

By mid CY2020 we forecast THC will receive its Office of Drug Control (ODC) license to cultivate at Eden Farms. We forecast limited production in CY2020 from Eden Farms with the site ramping up to 66,000 m² by the end of CY2024.

Flexible business model

THC has the potential to cultivate cannabis in over 100,000m² of hydroponic greenhouse facilities in Australia at its Bundy, Eden Farms and Ballina sites; i.e. “farm to pharma”.

Alternatively, it may look to source lower cost cannabis biomass and imported crude cannabis oil from other licensed permitted cultivators to put through its TGA GMP approved site. This follows on from the decision by the ODC to allow appropriately licensed and permitted organisations to import cannabis material, including extracts, for use in manufacture. This would allow THC to utilise the capacity at its Southport facility while cultivation at Eden Farms ramps up.

Given the Southport facility has clearance from the TGA as a GMP site, THC is capable of exporting lower cost cannabinoid product to globally approved markets that have reciprocal agreements with Australia.

Valuation

Our 12 month forward base case valuation is \$0.81 on an adjusted diluted basis. We have THC ramping up its hydroponic cultivation to ~67,200 m² by the end of CY2024 in line with how fast we believe THC can grow product sales.

Clearly if THC can ramp up production and sales faster than we are forecasting there is upside in our valuation. If THC was cultivating and selling 67,200 m² of hydroponic greenhouse cannabis by the end of CY2022, our valuation lifts to \$0.94.



THC operates under a ‘farm to pharma’ pharmaceutical model. It now holds all three required key cannabis licenses being the Cannabis Research License, Medicinal Cannabis Cultivation License and two Manufacturing Licenses allowing it to cultivate, produce and sell medicinal cannabis.

Having secured significant cannabis growing capacity, a good manufacturing practice (GMP) pharmaceuticals biomanufacturing facility, THC is in prime position to service both the domestic and the export markets.

THC also operates a hydroponics business in Canada, Crystal Mountain, that focuses on the manufacturing and distribution of hydroponics equipment and supplies for cannabis cultivation.

Stock	THC.ASX
Price	A\$0.41
Market cap	A\$56m

Company data	
Net cash (Sep 19)	A\$4.0m
Shares on issue	139.2m

Next steps	
End 1Q CY2020	First CBD sales
2H CY2020	Eden Farms cultivation



Financials

THC Global						THC-AU							
Year end 31 December													
MARKET DATA						12 month relative performance versus S&P/ASX Small Ordinaries							
Price	\$					0.41							
52 week high / low	\$					0.60 - 0.31							
Valuation	\$					0.81							
Market capitalisation	\$m					56.4							
Shares on issue (basic)	m					139.2							
Options / Performance shares	m					31.0							
Other equity	m					0.0							
Potential shares on issue (diluted)	m					170.2							
INVESTMENT FUNDAMENTALS						PROFIT AND LOSS							
		FY18A	FY19E	FY20E	FY21E	FY22E		FY18A	FY19E	FY20E	FY21E	FY22E	
Reported NPAT	\$m	(8.6)	(9.7)	(6.7)	(0.9)	4.8	Total Revenue	\$m	2.8	5.0	10.8	31.2	50.5
Underlying NPAT	\$m	(5.5)	(7.6)	(6.7)	(0.9)	4.8	Operating costs	\$m	(8.2)	(12.6)	(16.8)	(30.0)	(41.5)
EPS Reported (undiluted)	¢	(6.9)	(7.4)	(4.6)	(0.6)	3.2	EBITDA	\$m	(5.4)	(7.6)	(6.0)	1.2	9.0
EPS Underlying (undiluted)	¢	(4.4)	(5.8)	(4.6)	(0.6)	3.2	Depreciation & amortisation	\$m	(0.1)	(0.2)	(0.8)	(1.8)	(1.8)
Underlying EPS growth	%	n/m	n/m	n/m	n/m	n/m	EBIT	\$m	(5.5)	(7.8)	(6.8)	(0.6)	7.2
P/E Reported (undiluted)	x	n/m	n/m	n/m	n/m	12.7	Net interest	\$m	0.0	0.1	0.1	(0.3)	(0.3)
P/E Underlying (undiluted)	x	n/m	n/m	n/m	n/m	12.7	Non-operating income	\$m	0.0	0.0	0.0	0.0	0.0
Dividend	¢	0.0	0.0	0.0	0.0	0.0	Pretax Profit	\$m	(5.5)	(7.6)	(6.7)	(0.9)	6.9
Payout ratio	%	0%	0%	0%	0%	0%	Tax expense	\$m	0.0	0.0	0.0	0.0	(2.1)
Yield (Y/E/ spot)	%	0.0	0.0	0.0	0.0	0.0	Minorities	\$m	0.0	0.0	0.0	0.0	0.0
Franking	%	n/a	n/a	n/a	n/a	n/a	Underlying NPAT	\$m	(5.5)	(7.6)	(6.7)	(0.9)	4.8
Gross Yield (Y/E/ spot)	%	0.0	0.0	0.0	0.0	0.0	Adjustments & Significant items	\$m	(3.1)	(2.1)	0.0	0.0	0.0
Reported NPAT	\$m	(8.6)	(9.7)	(6.7)	(0.9)	4.8	BALANCE SHEET						
KEY RATIOS						BALANCE SHEET							
		FY18A	FY19E	FY20E	FY21E	FY22E		FY18A	FY19E	FY20E	FY21E	FY22E	
Year end shares	m	127.3	139.2	151.7	151.7	151.7	Cash	\$m	6.3	3.7	0.5	0.5	8.3
Market cap (Y/E / Spot)	\$m	59.8	56.4	61.4	61.4	61.4	Receivables	\$m	0.9	1.5	2.8	3.5	4.0
Net debt /(cash)	\$m	(6.3)	(3.7)	4.1	4.4	(3.4)	Inventory	\$m	1.3	1.6	3.0	3.7	4.2
Enterprise value	\$m	56.1	55.4	68.2	68.5	60.7	Other	\$m	0.0	0.4	0.4	0.4	0.4
EV/Sales	x	21.1	12.3	6.3	2.2	1.2	Current assets	\$m	8.5	7.1	6.6	8.1	16.9
EV/EBITDA	x	n/m	n/m	n/m	57.3	6.7	PPE	\$m	17.7	18.2	22.3	20.7	19.1
EV/EBIT	x	n/m	n/m	n/m	n/m	8.4	Intangibles	\$m	4.4	2.4	2.4	2.4	2.4
Net debt / Enterprise Value	x	(0.1)	(0.1)	0.1	0.1	(0.1)	Other	\$m	2.1	2.1	0.4	0.4	0.4
Gearing (net debt / EBITDA)	x	1.2	0.5	(0.7)	3.7	(0.4)	Non current assets	\$m	24.2	22.8	25.1	23.5	21.9
Operating cash flow per share	¢	(4.7)	(5.8)	(5.4)	(0.1)	5.3	Total Assets	\$m	32.7	29.9	31.7	31.5	38.8
Price to operating cash flow	x	n/m	n/m	n/m	n/m	7.7	Accounts Payable	\$m	0.4	1.1	1.8	2.3	2.6
Free cash flow (OCF-SIB capex)	\$m	(5.9)	(7.7)	(8.1)	(0.3)	7.8	Borrowings	\$m	0.0	0.0	0.0	0.0	0.0
Free cash flow per share	¢	(4.7)	(5.8)	(5.6)	(0.2)	5.1	Other	\$m	0.0	0.0	0.0	0.0	0.0
Price to free cash flow	x	n/m	n/m	n/m	n/m	7.9	Current liabilities	\$m	0.4	1.1	1.8	2.3	2.6
Free cash flow yield	%	n/m	n/m	n/m	n/m	12.7%	Borrowings	\$m	0.0	0.0	4.7	4.9	4.9
Book value / share	¢	22	18	13	12	16	Deferred tax liabilities	\$m	3.9	3.9	4.7	6.0	7.1
Price to book (NAV)	x	2.1	2.3	3.0	3.4	2.6	Other	\$m	0.4	0.4	0.4	0.4	0.4
NTA / share	¢	19	16	12	10	14	Non current liabilities	\$m	4.3	4.3	9.8	11.3	12.4
Price to NTA	x	2.5	2.6	3.5	3.9	2.9	Total Liabilities	\$m	4.7	5.4	11.5	13.5	14.9
EBITDA margin	%	n/m	n/m	n/m	4%	18%	Equity	\$m	23.0	27.6	32.6	32.6	32.6
ROE (Average Equity)	%	n/m	n/m	n/m	n/m	21%	Retained earnings	\$m	(11.0)	(20.7)	(27.4)	(28.3)	(23.4)
ROA (EBIT)	%	n/m	n/m	n/m	n/m	23%	Reserves / Other	\$m	16.1	17.6	15.0	13.7	14.6
Interest cover (EBIT / net interest)	x	125.3	54.0	58.5	(2.2)	22.8	Shareholder's equity	\$m	28.1	24.5	20.2	18.0	23.8
DIVISIONAL						CASH FLOW							
		FY18A	FY19E	FY20E	FY21E	FY22E		FY18A	FY19E	FY20E	FY21E	FY22E	
Average cannabis planted (m ²)	-	-	-	3,700	18,200	32,200	EBITDA	\$m	(5.4)	(7.6)	(6.0)	1.2	9.0
Plants / m ²	3.0	3.0	3.0	3.0	3.0	3.0	Change in working capital	\$m	0.0	(0.5)	(2.0)	(1.0)	(0.7)
Crops p.a.	4.0	4.0	4.0	4.0	4.0	4.0	Net interest	\$m	0.0	0.1	0.1	(0.3)	(0.3)
Plants p.a. (m)	-	-	-	0.0	0.2	0.4	Tax paid / Refund	\$m	0.0	0.3	0.0	0.0	0.0
Dried flower yield per plant	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	Other	\$m	(0.5)	0.0	0.0	0.0	0.0
Dried flower (kg)	-	-	-	3,863	19,001	33,617	Operating cash flow	\$m	(5.9)	(7.7)	(7.9)	(0.1)	8.0
Wastage	25%	25%	25%	25%	25%	25%	Stay in business capital expenditure	\$m	0.0	0.0	(0.2)	(0.2)	(0.2)
CBD active pharma ingredient (API)	0.9%	0.9%	0.9%	0.9%	0.9%	0.9%	Growth capex	\$m	(0.8)	(0.4)	(4.7)	0.0	0.0
Total CBD Oil Produced (kg)	-	-	-	25	124	219	Net investment / Other	\$m	(2.3)	0.8	0.0	0.0	0.0
Sale price / mg (\$)	-	-	-	0.20	0.20	0.20	Investing cash flow	\$m	(3.1)	0.4	(4.9)	(0.2)	(0.2)
Cannabinoid Revenue (A\$m)	-	-	-	5.0	24.8	43.9	Change in Equity	\$m	4.2	4.6	5.0	0.0	0.0
Canadian / Other Income (A\$m)	2.8	5.0	5.7	6.4	6.7	Increase / (decrease) in borrowings	\$m	0.0	0.0	4.7	0.2	0.0	
							Dividend / other	\$m	0.0	0.0	0.0	0.0	0.0
							Financing cash flow	\$m	4.2	4.6	9.7	0.2	0.0
							Change in Cash / FX	\$m	(4.7)	(2.7)	(3.1)	(0.1)	7.8
							Year end cash	\$m	6.3	3.7	0.5	0.5	8.3

Investment Thesis

THC Global (THC) aim to be the leading integrated supplier of cannabinoid products to the Australian and New Zealand medicinal cannabis market with a view to exporting excess production from its Southport manufacturing facility to markets in Europe and Asia through its global commercial partners. At the same time, it will look to leverage its retail and wholesale hydroponics business in Canada to expand into the provision of medicinal cannabis in that market.

With the first bottling of its medicinal cannabis oil in early December, THC Global (THC) has validated its locally grown “biomass to bottle” processing capability and is currently awaiting Therapeutic Goods Administration (TGA) approval and licensing allowing THC to manufacture at Southport. THC is now able to accept feedstock from any licensed permitted cultivator, or its own cultivation operations, and process up to 120,000 kg of cannabis biomass to produce cannabinoid active pharmaceutical ingredient (API) at its TGA approved good manufacturing practice (GMP) pharmaceuticals biomanufacturing facility.

Figure 1 – THC Global has bottled its first cannabidiol (CBD) with new products to be released in 2020



Source: THC Global

FY2020E is forecast to be a transition year.

The TGA has just granted THC a license (GMP License) for the commercial manufacture of therapeutic goods at the Southport facility. By the end of 1Q CY2020 we forecast THC will have met all the required product validation tests on the cannabidiol (CBD) oil being produced at Southport and will have received the final TGA approval allowing THC to sell that product into the market.

By mid CY2020 we forecast THC will receive its Office of Drug Control (ODC) license to cultivate at Eden Farms. We forecast limited production in CY2020 from Eden Farms with the site ramping up to 66,000 m² by the end of CY2024. We note here that both the Bundy and Southport sites have been granted Schedule 4 and Schedule 8 licenses from the TGA that enable the manufacture and supply of cannabis medicines and additionally allow THC to operate on-site analytical laboratory’s for product development.

Flexible business model

One of the things we really like about THC as at this stage is that it is the only player in Australia that we know of that owns its own manufacturing facility. Other potential players in the medicinal cannabis space rely on relationships with contract manufacturers to convert their biomass to end product. This of course is likely to change over time, but at this stage we see THC as having first mover advantage in Australia.

While THC has the potential to cultivate cannabis in over 100,000m² of hydroponic greenhouse facilities over time at its Bundy, Eden Farms and Ballina sites, it has the option to source lower cost biomass from other licensed permitted cultivators who do not have current offtake agreements if and when it becomes available to process at Southport.

This follows on from the decision by the ODC to allow appropriately licensed and permitted organisations to import cannabis material, including crude extracts, for use in manufacture. This would allow THC to utilise the capacity at its

Southport facility while cultivation at Eden Farms ramps up. Given the Southport facility has clearance from the TGA as a GMP site, THC is capable of exporting cannabinoid product to globally approved markets.

With demand for medicinal cannabis products growing in Europe and Australasia, we believe THC will look to start to export product to higher cost markets where its lower priced product will be attractive.

We believe there is a very real opportunity for THC to source lower cost biomass from other licensed permitted cultivators and process this feed at Southport which will have a significant level of free capacity, to then sell into the local and global markets given its GMP, TGA approved status.

If THC can source this biomass at a price lower than our assumed \$600/kg of flower cultivation cost at Eden Farm's then it is in the enviable position of producing higher margin product while it could slow the ramp up of cultivation at Eden Farms; thus pushing out near term capital expenditure.

We note that globally there are a number of companies already pursuing this approach; i.e. moving up the value chain by sourcing cheaper biomass to manufacture product to sell into growing demand including Medipharm Labs, (LABS-TSE) C\$530 market capitalisation) and Valens GroWorks, (VLNS-TSX C\$430m market capitalisation).

Recent significant events

We note below that since its formation in late 2016, THC has methodically ticked off all the requirements needed to become an integrated supplier of cannabinoid products; i.e. from "farm to pharma".

- February 2016: Federal parliament amendments to the Narcotics Drug Act legalise medicinal cannabis
- May 2017: The Hydroponics Company (THC) lists on the ASX.
- July 2017: Canndeo granted medicinal cannabis research license by the ODC
- October 2017: Canndeo granted a medicinal cannabis cultivation and growth license.
- January 2018: Australian Federal Government legislates to allow the export of medicinal cannabis
- April 2018: THC acquires the bio-pharmaceutical manufacturing facility at Southport for \$2.6m
- July 2018: Secures a USDA certified cannabis growing site at Ballina with off take agreement
- November 2018: Secures rights to import and sell Endoca product in New Zealand
- March 2019: Cannabis production site (~ 1.6 ha) acquired in Nova Scotia, Canada
- July 2019: Southport granted a Manufacture Licence to produce cannabis oil by the ODC
- October 2019: Southport and Bundaberg facilities granted Schedule 4 and Schedule 8 licenses
- November 2019: Southport manufacturing permit received from the ODC
- December 2019: First medicinal cannabis bottled at Southport facility
- January 2020: Southport granted a Manufacture Licence to produce cannabis oil by the TGA

Potential near-term catalysts

- Product validation tests on the cannabidiol (CBD) oil being produced at Southport successful allowing TGA approval
- Office of Drug Control (ODC) licenses THC to cultivate at Eden Farms
- THC looks to source appropriately licensed and permitted cannabis material, including extracts, for use in manufacture at Southport.

Financial outlook

Our base case modelling assumes THC ramps up production at its Eden Farms contracted cultivation site to 66,000 m² from mid-2020 by the end of CY2024 and selling that medicinal cannabis product into the Australian and global markets. Given the rate of growth, change and development of the global cannabis market we can safely say our forecasts have a reasonable degree of risk associated with them.

FY2020 is forecast to be a transition year with THC forecast to be EBITDA positive in FY2021.

In FY2020, THC's Canadian business is forecast to continue to report strong growth, while at the same time THC's medicinal cannabis oil manufacturing is forecast to ramp up with first product being sold from the Southport facility from 1Q2020 onwards.

Given THC has a very low capital intensity; i.e. cultivation of its biomass will be from contracted sources (Eden Farms will largely be a variable cost operation based on kg of flower cultivated) and its manufacturing facility is 100% owned we see THC generating a free cash flow (operating cash flow less stay in business capital) yield of over 10% in FY2021.

Sensitivities and Risks

We believe THC has minimised the majority of the initial “start-up” risks given it has obtained all of the required licenses, permits and regulatory approvals allowing it to grow feedstock at Bundaberg and produce cannabinoid oil at its Southport site.

Near term risks that we believe are unlikely to impact THC, but we note here are

- Failure to achieve validation of cannabidiol currently under production at Southport by the end of 1Q CY2020 thus delaying first sales.
- THC via Candeo does not gain approval from the Australian Office of Drug Control (ODC) to cultivate cannabis at Eden Farms. We believe the application for an additional cultivation site at Eden Farms, given THC’s manufacturing capacity at Southport, is unlikely to be denied.

Longer term, the key risks we note are

- A continuation of pressure on cannabinoid product pricing given competition from other medicinal cannabis suppliers and their aggressive pricing aimed at growing market share in the early development of the market.
- THC currently has access to high cannabidiol (CBD) cannabis strains. It will need to identify and source new cannabis tissue strains with high tetrahydrocannabinol (THC) to allow it to produce a full range of cannabinoid products. Key to sourcing new strains will be whether the strains can acclimatise to Australian growing conditions.
- Slower ramp up of cultivation at Eden Farms impacting production of cannabinoid oil.
- Higher costs of cultivation and manufacture than forecast.
- Lower dried flower yield per plant than forecast.
- Lower active pharmaceutical ingredient per kg of biomass sourced either from THC owned production or from other licensed permitted cultivators.
- Slower ramp up in market demand.
- Changes in the regulatory framework.

On the financial front we believe THC will need to fund ~\$10m of capital expenditure and working capital demands in FY2020E through a mixture of debt and equity.

We have assumed in our forecasts that \$5m of equity is raised at \$0.40 lifting the number of shares on issue by year end FY2020E.

We have also assumed the balanced of the funding requirements is sourced from a debt facility. If debt funding cannot be arranged the size of the equity piece may be bigger than currently forecast.

Valuation

We have derived a 12 month forward base case valuation of \$0.81 on an adjusted diluted basis, using discounted cash flow (DCF) valuation. The key drivers are THC ramping up its hydroponic cultivation to ~67,200m² by the end of CY2024 and a CBD oil pricing of \$0.20/mg.

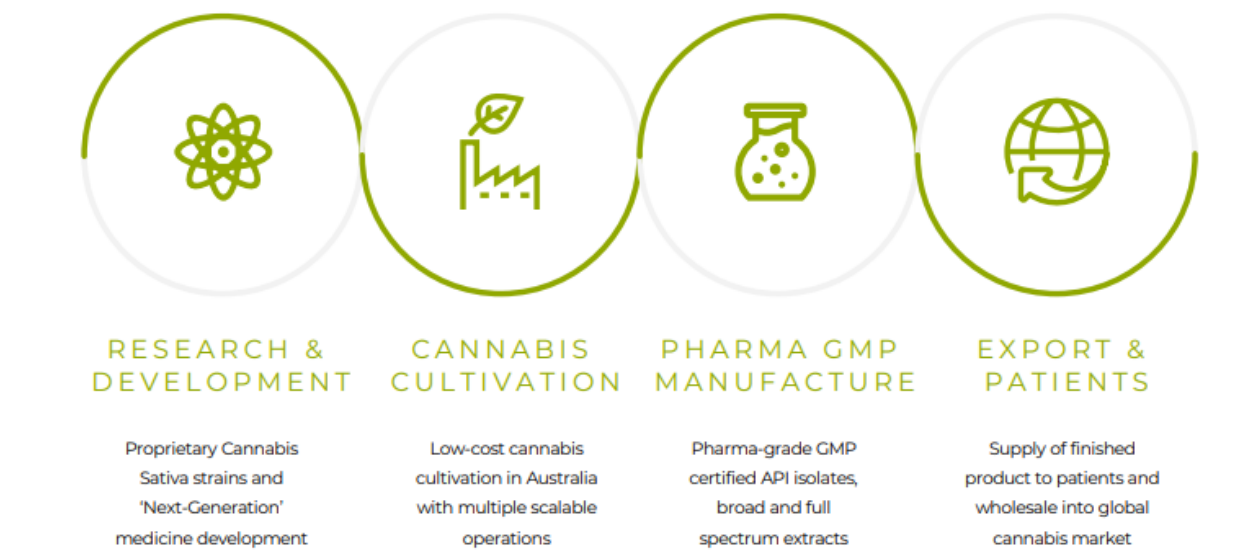
Upside risk to our valuation results if product sales ramp up faster than we are forecasting. If THC was cultivating 67,200 m² of hydroponic greenhouse cannabis by the end of CY2022, our valuation lifts to \$0.94.

Additionally, as manufacturing and product sales ramp up, we will de-risk our discount rate. We are currently using an equity beta of 1.50 in line with the current FactSet beta of 1.47. We note if we lower our equity beta from 1.5 to 1.25, our valuation lifts from \$0.81 to \$0.98.

Company Description

THC Global (THC) operates under the “farm to pharma” pharmaceutical model, now holding all three of the key cannabis licences required to research, grow, manufacture and sell medicinal cannabis.

Figure 2 – THC Global operates a fully integrated model



Source: THC Global

THC has built a domestic medicinal cannabis production and supply capability. This has been achieved through the licensing program established under the Narcotic Drugs Act 1967.

THC holds a Cannabis Research Licence, a Medicinal Cannabis Licence (Cultivation), and two Manufacturing Licences through its domestic medicinal cannabis subsidiaries THC Pharma and Canndeo.

THC’s Southport Manufacturing Facility, a pharmaceutical bio-floral extraction plant, is licenced and permitted, including the required TGA GMP manufacturing license and the Schedule 8 controlled substances and Schedule 4 pharmacy medicines licences required to import and or export feedstock and product. The Bundy operation is similarly licensed with both also being able to operate on-site analytical laboratory’s for product development under the respective licenses.

THC has three grow sites in Australia at Bundaberg, Eden Farms and Ballina. With the potential for over 100,000m² of large-scale hydroponic cannabis cultivation.

In addition to its core Australian medicinal cannabis assets, THC has a significant Canadian presence. THC’s hydroponics equipment division, Crystal Mountain, is a revenue generating manufacturer, wholesaler, and retailer of hydroponics equipment and supplies for cannabis cultivation. THC also owns Canndeo Canada, a holder of property in Nova Scotia, Canada which can be developed into a large-scale cannabis production site.

THC’s global commercial partners operate across four continents, supporting THC’s future international growth. THC also operates a revenue generating global hydroponics business in Canada, focusing on the manufacturing and distribution of hydroponics equipment, materials, and nutrients.

THC has built a domestic medicinal cannabis production and supply capability. This has been achieved through the licensing program established under the Narcotic Drugs Act 1967. There are three relevant licences issued by the Office of Drug Control i.e. A cannabis research licence allowing the production of cannabis strains for research into medicinal use, a medicinal cannabis licence allowing either cultivation or production or both of medicinal cannabis plants and a manufacturing licence allowing the manufacture of cannabis and cannabis extract into medicinal cannabis.

Australian operations

Bundaberg aka Bundy

THC own and operate a facility in Bundaberg (Bundy), Queensland that has access to a large plant breeder's rights (PBR) repository of registered cannabis sativa strains. This allows THC exclusive perpetual access to six high quality cannabis PBR's for research and development and commercialisation purposes.

Figure 3 – Cannabis has been harvested at “Bundy” and sent for CBD extraction at Southport



Source: THC Global

We note that genetic traceability of the cannabinoid being sold is a major selling attribute in Asian markets where strict pharmaceutical regulations are applied i.e. customers want to know where the biomass was cultivated, and that the product was produced in a GMP facility and not sourced from out the back of Griffith.

Bundy has ~1,200m² of cannabis already cultivating and has recently harvested a crop for the first manufacturing of CBD at Southport.

Bundy, through Canndeo, has been granted a medicinal cannabis research license by the Office of Drug Control (ODC), a medicinal cannabis cultivation and growth license through the ODC and has been granted Schedule 4 and Schedule 8 licenses.

As with the Southport facility THC is now approved to carry out on site tissue culturing and other analytical work to bring on new strains to build out THC's product offering going forward.

Eden Farms

THC has an agreement where the owner of Eden Farms will cultivate cannabis effectively on a per kg of biomass, so is largely a variable cost structure with a small fixed rental component.

Eden Farms has 60,000 m² of operational hydroponic greenhouses (currently producing cucumbers) with an additional 180,000 m² of open field agricultural land. We anticipate there will be a small amount of capital expenditure (\$3m-\$4m) to be expensed over 2020 to ramp up cultivation at Eden Farms.

Figure 4 – Eden Farms forecast to be cultivating by mid-2020.



Source: THC Global

Ballina

THC has entered into an agreement for the exclusive leasing rights of 73,500 m² of United States Department of Agriculture (USDA) certified organic land in northern New South Wales which THC proposes to use for the growing of medicinal cannabis subject to necessary statutory and regulatory approvals and demand. Initial options include up to 40,000 m² of greenhouses for the cultivation of cannabis biomass.

THC has agreed an off-take agreement for the use of THC’s medicinal cannabis in Meluka honey products. Meluka Health being owned by EVE Investments (EVE).

Under the agreement, EVE will be provided with access to THC’s medicinal cannabis for use in product development by Meluka Honey of novel cannabis blended products including incorporation of Melaleuca tea tree extract from EVE’s tea tree plantations. We have not included Ballina production in our forecasts so is just a free option at this stage.

Southport manufacturing

THC acquired the production facilities of international pharmaceutical company, LEO Pharma in April 2018 which was previously manufacturing a product for the treatment of a skin disease. Given the product did not make it through Phase 3 trials, keeping the facilities in Southport did not match with its future strategy so the asset was sold. THC separately acquired the freehold land and buildings housing the facilities.

Figure 5 – Southport manufacturing facility up and running



Source: THC Global

The facility acquired by THC is one of the largest pharmaceutical bio-floral extraction and refinement plants in the southern hemisphere with the capacity to process up to 120,000 kg of biomass. The acquisition has enabled THC to become a globally significant manufacturer of medicinal cannabis products for the Australian domestic and future export markets. The facility provides THC with a fully functioning biomanufacturing plant with extraction technology to fractionate and crystallise during the manufacturing process, and a high-quality purification system that will enable THC to produce a broad range of high quality, pure cannabinoids as Active Pharmaceutical Ingredients (API) products including API isolates, broad spectrum and full spectrum extracts with additional finished product capacity to be established for creams, tablets, powders, sublinguals and other medicines.

Total consideration paid for the land and facility was ~\$2.6m. At the same time THC secured the workforce with expertise in operating the Queensland bio-manufacturing operation which they have retained to today. An independent market valuation (AON Valuation Services) valued the facilities at ~\$15m. THC has estimated a replacement cost at ~\$35m and has insured it on that basis.

Canadian operations

THC owns 100% of Crystal Mountain Manufacturing (CMP) which is a Canadian-based hydroponic equipment wholesale supplier to the North American market.

Over 600 products and proprietary trademarked products including lighting and power supplies, lighting relays and climate controls, ventilation and trimming, extraction bags, plant rotation systems, eyewear, nutrients and accessories etc.

Crystal Mountain provides guidance, service and support to home growers and Micro LP in legal Canadian recreational cannabis marketplace. It has strong distribution networks for hydroponic equipment and nutrients across Canada, UK, Europe and USA. With 9 established trademarks across a range of product categories and many products in their catalogue, it is diverse with the added strength of being nimble and scalable.

Proprietary Trademarked Products include lighting and power supplies, lighting relays and climate control, ventilation and trimming, extraction bags, plant rotation systems, eyewear and nutrients and accessories.

Figure 6 – Crystal Mountain product examples



Source: THC Global

Nova Scotia

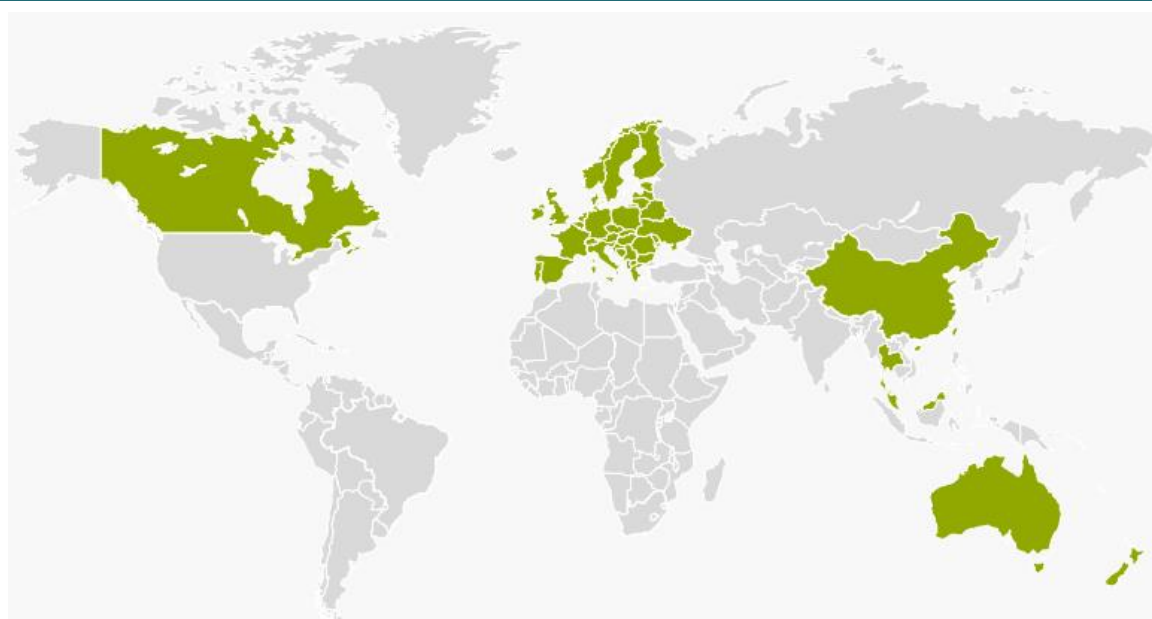
THC has secured a 4.5 ha property in Nova Scotia, Canada with a letter of readiness from Health Canada for development of a cannabis production site. THC is targeting to supply Australian products to Canada's 300,000+ patients accessing medicinal cannabis. THC is targeting to start distributing THC's Australian medicinal cannabis products into Canada in late 2020 with Therapeutic Goods Order (TGO) 93 and European Union (EU) GMP certification.

Potential market

Depending on who you listen to and where you source your data the global market for medicinal cannabis related products is potentially material. Combine that with the global attention being brought to bear on the growth in opioid related deaths, consumption and addiction, we believe the growth in cannabinoid medicine will remain strong for the medium to long term as long as regulatory approvals and public concerns can be met.

Over time as more cannabis related clinical trials conclude and more real-world data and evidence is collected that allow quicker approvals for additional health indications for different cannabinoid strains, we believe market concerns re cannabis related products will ease and the market will be further stimulated.

Figure 7 – THC’s initial global target markets



Source: THC Global

We have tabled below a recent estimate of the global medicinal cannabis market size in 2024. Clearly, if this is anywhere near correct, the global opportunity for THC is material.

Figure 8 – Potential medicinal cannabis market size (US\$b) in 2024

Region	US\$b
Africa	1.3
Asia	10.7
Europe	22.3
Latin America	6.6
North America	20.2
Oceania	1.5
Total	62.6

Source: Prohibition Partners, November 2019.

We note other market participants have estimates for the potential medium term global medical cannabis demand of US\$44b (Zion Market Research), US\$48.5b (Fortune Business Insights), and US\$53b (Aurora Cannabis).

Australian opportunity

In Australia, the federal government amended the Narcotics Drugs Act 1967 in February 2016, allowing the cultivation of cannabis for medicinal or scientific purposes. Australia has a TGA produced classification system that controls how medicines and poisons are made available to the public. The medicines and poisons are classified into schedules dependent on the level of regulatory control and are published in the Standard for the Uniform Scheduling of Medicines and Poisons (SUSMP). The SUSMP is referred to as the Poisons Standard and provides a legal framework for the States

and Territories to adopt a uniform approach to control the availability, accessibility, and safety of poisons in Australia. CBD products sit in Schedule 4 while THC products in Schedule 8.

In November 2016, the TGA implemented a new Schedule 8 entry for medicinal cannabis products. Approval to prescribe medicinal cannabis to a patient can be sought from an authorised medical practitioner through an application to the TGA under the SAS. In addition to TGA approval, various states and territories impose additional approval steps before allowing a patient to receive medicinal cannabis. In July 2018, an online system was introduced by the TGA to support SAS application lodgement and notifications. The online SAS system allows prescribers in certain States and Territories to submit an application to both the TGA and the relevant State/Territory Health Department simultaneously.

Thus, in Australia patients can access cannabis products via the pathways below:

Authorised Prescriber:

A medical practitioner applies to the TGA to become an Authorised Prescriber of a medicinal cannabis product to a particular group of patients for a specific indication. An Authorised Prescriber does not need to notify the TGA when they are prescribing the medicinal cannabis product, however they must report on a six-monthly basis. Medical practitioners seeking to become Authorised Prescribers need to have their application approved by a Human Research Ethics Committee (HREC) or endorsed by a specialist college.

Special Access Scheme Category B (SAS-B):

SAS-B applications are submitted on a per patient basis and must be submitted by a medical practitioner. The applications need to include the patient diagnosis and clinical justification for the proposed prescription, including commentary regarding the seriousness of the relevant condition, justifying the supply of medicinal cannabis products and the way in which the medical practitioner will monitor the safety and efficacy of that product. The application also must identify the proposed medicinal cannabis product and any safety and efficacy data relevant to the proposed product.

Clinical trials:

These applications as per the standard pathway of using therapeutic goods supplied for clinical trials in Australia need to follow the TGA clinical trial notification scheme or the clinical trial exemption scheme.

Potential Australian market revenue opportunity assuming 100,000 patients

There has been a rapid growth in SAS-B patient approval numbers in Australia (see Appendix 6) with accumulative approvals for CY2019 exceeding 25,000. Noting that this forecast does not include patients engaged in clinical trials (small number) and those patients receiving product from an authorised prescriber.

We estimate the current patient numbers are probably less than half the accumulated approval numbers given patients change medicine due to cost and product shortage (thus need a new approval), approvals expire, patients change product due to ineffectiveness and thus a new approval etc etc. Thus, we estimate current active patient numbers at circa 10,000 -12,500 or about 35,000 – 40,000 prescriptions per annum.

We note that it is estimated that in Australia over 100,000 patients are self-medicating with illegal cannabis. We also note that Pain Australia estimated that 3.2m Australians were living with chronic pain in 2018 (over 65% of a working age). If a small percentage of those chronic pain sufferers become medicinal cannabis patients, we believe in the next two to three years we could see growth in medicinal cannabis patient numbers exceed 100,000.

If we assume 100,000 patients consume an average cannabinoid API dosage per day of ~50mg (Fresh Leaf Analytics Q3 2019 study found average dosage levels were 54 mg /day in the Australian market) and pricing of \$0.20/mg (so ~\$10/day), we estimate the **Australian market alone could be worth \$365m p.a. within the next three years.**

We are forecasting cannabinoid revenue in FY2023E for THC of \$63m implying a 17% market share. Not too heroic given THC should have a pricing advantage given THC product will be locally sourced and produced. However, we note there is already significant competition in the market from imported products and ultimately locally produced product will also come to market.

Given THC's potential production capacity at Southport, we expect it will become a significant global exporter in the medium term.

Financial forecasts

We have tabled our forecast assumptions below for the ramp up in cultivation at the three sites and the levels of API oil production. We have assumed for cultivation forecasting that the plants/m², crops p.a., dried flower yield and API yield are in line with the modelling carried out by Deloitte Access Economics for the Australian Department of Health in 2016. (Reference: *Modelling the cost of medicinal cannabis; Department of Health – Office of Drug control; 23 September 2016*).

Figure 9 – THC cultivation and production forecasts

A\$m	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E
Bundaberg								
Hydroponic greenhouse (m ²)	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Average planted (m ²)			1,200	1,200	1,200	1,200	1,200	1,200
Plants per m ²	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Plants			3,600	3,600	3,600	3,600	3,600	3,600
Crop rotations p.a.	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Plants p.a.			14,400	14,400	14,400	14,400	14,400	14,400
Dried flower yield per plant	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%
Dried flower (kg)			1,253	1,253	1,253	1,253	1,253	1,253
Wastage	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Active pharmaceutical ingredient (API)	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%
Cannabinoid oil (kg)			8.2	8.2	8.2	8.2	8.2	8.2
Eden Farms								
Hydroponic greenhouse (m ²)	66,000	66,000	66,000	66,000	66,000	66,000	66,000	66,000
Year end planted (m ²)			10,000	24,000	38,000	52,000	66,000	66,000
Average planted (m ²)			2,500	17,000	31,000	45,000	59,000	66,000
Plants per m ²	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Plants			7,500	51,000	93,000	135,000	177,000	198,000
Crop rotations p.a.	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Plants p.a.			30,000	204,000	372,000	540,000	708,000	792,000
Dried flower yield per plant	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%
Dried flower (kg)			2,610	17,748	32,364	46,980	61,596	68,904
Wastage	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Active pharmaceutical ingredient (API)	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%
Cannabinoid oil (kg)			17.0	115.8	211.2	306.5	401.9	449.6
Ballina								
Hydroponic greenhouse (m ²)	40,000	40,000	40,000	40,000	40,000	40,000	40,000	40,000
Year end planted (m ²)			-	-	-	-	-	-
Total THC Global CBD Sales								
Hydroponic greenhouse (m ²)	107,200	107,200	107,200	107,200	107,200	107,200	107,200	107,200
Year end planted (m²)	1,200	1,200	11,200	25,200	39,200	53,200	67,200	67,200
Average planted (m ²)	-	-	3,700	18,200	32,200	46,200	60,200	67,200
Plants / m ²	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Crops p.a.	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Plants p.a.	-	-	44,400	218,400	386,400	554,400	722,400	806,400
Dried flower yield per plant	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%
Dried flower (kg)	-	-	3,863	19,001	33,617	48,233	62,849	70,157
Wastage	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
API	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%	0.87%
API Oil Produced (kg)			25	124	219	315	410	458

Source: THC Global, MST Access

We have assumed full cultivation at Bundy from day 1 with cultivation to ramp up to 66,000 m² at Eden Farms by the end of CY2024 from mid-2020. We have assumed no cultivation at Ballina in our modelling and leave this as a free option in our forecasts and valuation.

NB: We have conservatively assumed fully ramped up production of ~69,000 kg of dried flower from 66,000 m² at Eden Farms versus THC's assumed 80,000kg. Additionally, our assumed fully ramped up plant numbers for Eden Farms is ~800,000 versus THC's stated assumption of over 1,000,000.

Profit and loss

Key assumptions in our profit and loss include:

- Sale price of cannabinoid of \$0.20/mg. We note that products with higher levels of tetrahydrocannabinol (THC) (Schedule 8) are currently pricing at a premium to CBD (Schedule 4), so as THC expands its product mix average price points may move upwards. Freshleaf Analytics note in Q1 2019 the cheapest THC products priced at a 60% premium to the cheapest CBD products.
- Cost to cultivate and manufacture is a mix of essentially fixed costs (primarily Eden Farms rental and compliance fees), variable cultivation cost per kg of dried flower (payable to the Eden Farms owner) and a variable manufacturing cost (Southport cost per kg flower). We are forecasting the total variable cost at ~\$650/kg (\$600/kg of flower for cultivation and \$50/kg of flower for manufacturing at Southport) in the initial years dropping down to ~\$600/kg as the benefits of scale step up. We note this is lower than modelling carried out for the Australian Department of Health in 2016 given we have assumed the attractive cultivation cost agreement agreed with the Eden Farms owner and operator will be lower than the aforementioned study.
- Canadian operations continue to maintain a gross margin of ~30% with sales growing from \$4.5m in FY2019E to \$5.7m in FY2020E

Figure 10 – THC Global forecast profit and loss

A\$m	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E
API Oil Produced (kg)			25	124	219	315	410	458
Sale price / mg (\$)			0.200	0.200	0.200	0.200	0.200	0.200
Cannabinoid API Revenue			5.0	24.8	43.9	62.9	82.0	91.6
Rent, fees and compliance			(2.3)	(5.0)	(7.0)	(7.2)	(7.4)	(7.5)
Variable cultivation costs per kg flower			(2.3)	(11.2)	(19.3)	(27.1)	(34.6)	(38.6)
Variable manufacturing costs per kg flower			(0.2)	(1.0)	(1.7)	(2.4)	(3.1)	(3.5)
Variable cultivation costs per kg flower			600.0	587.5	575.0	562.5	550.0	550.0
Variable manufacturing costs per kg flower			50.0	50.0	50.0	50.0	50.0	50.0
Implied total costs per kg flower			1,232.5	900.6	833.2	761.3	717.0	707.4
COGS			(4.8)	(17.1)	(28.0)	(36.7)	(45.1)	(49.6)
Gross Profit			0.3	7.7	15.9	26.2	37.0	41.9
Gross margin			6%	31%	36%	42%	45%	46%
Crystal Mountain Revenue	2.7	4.5	5.7	6.4	6.7	6.9	7.1	7.4
Growth	44%	69%	27.6%	11.0%	4.4%	3.5%	3.5%	3.5%
Gross profit	0.8	1.4	1.7	1.9	2.0	2.1	2.1	2.2
Gross margin	29%	32%	30%	30%	30%	30%	30%	30%
TCH Group Revenue	2.7	4.5	10.8	31.2	50.5	69.8	89.1	98.9
COGS	(1.9)	(3.1)	(8.8)	(21.6)	(32.7)	(41.5)	(50.1)	(54.8)
Gross Profit	0.8	1.4	2.0	9.6	17.9	28.3	39.1	44.1
Other income	0.1	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Pre SG&A Profit	0.9	1.9	2.0	9.6	17.9	28.3	39.1	44.1
SG&A costs	(6.3)	(9.5)	(8.0)	(8.4)	(8.8)	(9.3)	(9.7)	(10.2)
EBITDA	(5.4)	(7.6)	(6.0)	1.2	9.0	19.0	29.4	33.9
D&A	(0.1)	(0.2)	(0.8)	(1.8)	(1.8)	(1.8)	(1.8)	(1.8)
EBIT	(5.5)	(7.8)	(6.8)	(0.6)	7.2	17.2	27.6	32.1
Net interest	0.0	0.1	0.1	(0.3)	(0.3)	(0.2)	0.0	0.4
PBT	(5.5)	(7.6)	(6.7)	(0.9)	6.9	17.0	27.6	32.5
Accounting tax	0.0	0.0	0.0	0.0	(2.1)	(5.1)	(8.3)	(9.8)
Underlying Profit	(5.5)	(7.6)	(6.7)	(0.9)	4.8	11.9	19.3	22.8
Underlying EPS (¢)	(4.4)	(5.8)	(4.6)	(0.6)	3.2	7.8	12.7	15.0
Underlying P/E (x)	n/m	n/m	n/m	n/m	13.5	5.5	3.4	2.9

Source: THC Global, MST Access

Forecast Cash flow

We table below our forecast cash flow resulting from our base case profit and loss above.

Key points to note are:

- Forecast capital expenditure in FY2020 of ~\$5.0m primarily for the ramp up of operations at Eden Farms.
- Negative accounting free cash flow in FY2020 of \$12.8m necessitating debt and equity funding of ~\$5.0m and ~\$5.0m respectively.
- Free cash flow (as defined as operating cash flow less stay in business capital expenditure) to grow strongly from FY2021 onwards.
- We have assumed no dividends are declared at this stage but if the free cash flow occurs as we are forecasting, we would expect THC to put in place a dividend policy to return retained earnings to shareholders.

Figure 11 – THC Global forecast cash flow statement

A\$m	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E
EBITDA	(5.4)	(7.6)	(6.0)	1.2	9.0	19.0	29.4	33.9
Change in working capital / Other	(0.5)	(0.5)	(2.0)	(1.0)	(0.7)	0.0	(1.6)	(0.8)
OCF - pre interest & tax	(5.9)	(8.1)	(8.0)	0.2	8.4	19.0	27.8	33.1
Cash interest earned	0.1	0.1	0.1	0.0	0.0	0.1	0.4	0.7
Cash interest paid	(0.1)	0.0	0.0	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Tax Paid	0.0	0.3	0.0	0.0	0.0	(0.3)	(8.3)	(9.8)
Operating cash flow (OCF)	(5.9)	(7.7)	(7.9)	(0.1)	8.0	18.4	19.5	23.8
Maintenance capex	0.0	0.0	(0.2)	(0.2)	(0.2)	(0.3)	(0.4)	(0.5)
Free Cash Flow (OCF-SIB capex)	(5.9)	(7.7)	(8.1)	(0.3)	7.8	18.2	19.2	23.3
Capital expenditure	(0.8)	(0.4)	(4.7)	0.0	0.0	0.0	0.0	0.0
Acquisitions / Investments	(2.3)	(0.3)	0.0	0.0	0.0	0.0	0.0	0.0
Divestments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investing cash flow	0.0	1.1	0.0	0.0	0.0	0.0	0.0	0.0
Net investing	(3.1)	0.4	(4.9)	(0.2)	(0.2)	(0.3)	(0.4)	(0.5)
Net movement in equity	4.2	4.6	5.0	0.0	0.0	0.0	0.0	0.0
Cash dividends paid	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt draw down	0.0	0.0	4.7	0.2	0.0	0.0	0.0	0.0
Debt repayments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other financing cash flow	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net financing	4.2	4.6	9.7	0.2	0.0	0.0	0.0	0.0
Change in cash	(4.7)	(2.7)	(3.1)	(0.1)	7.8	18.2	19.2	23.3
Cash beginning	11.0	6.3	3.7	0.5	0.5	8.3	26.4	45.6
FX Impact	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash end	6.3	3.7	0.5	0.5	8.3	26.4	45.6	68.9

Source: THC Global, MST Access

Risks to our financial forecasts

We believe THC has nullified the majority of the initial “start-up” risks given it has obtained all of the required licenses, permits and regulatory approvals allowing it to grow feedstock at Bundaberg and produce cannabinoid oil at its Southport site.

Near term risks that we believe are unlikely to impact THC, but we note here are:

- Failure to achieve validation of cannabidiol currently under production at Southport by the end of 1Q2020 thus delaying first sales.
- THC via Canneo does not gain approval from the Australian Office of Drug Control (ODC) to cultivate cannabis at Eden Farms. We believe the application for an additional cultivation site at Eden Farms, given THC’s manufacturing capacity at Southport, will not be refused.

Longer term, the key risks we note are:

Slower ramp up in market demand with lower product pricing given competition from other medicinal cannabis suppliers. We note that in the 3Q 2019 Freshleaf Analytics (FA) “Patient, Product and Pricing Analysis”, the average prices of cannabis medicine was \$0.23/mg (MST base case forecast for THC is \$0.20/mg) and oral product pricing had remained unchanged for the previous six months.

FA pointed to a number of oral products that were pricing down to \$0.10/mg.

- THC currently has access to high cannabidiol (CBD) cannabis strains. It will need to identify and source new cannabis tissue strains with high tetrahydrocannabinol (THC) to allow it to produce a full range of cannabinoid products. Key to sourcing new strains will be whether the strains can acclimatise to Australian conditions.
- Slower ramp up of cultivation at Eden Farms impacting production of cannabinoid oil.
- Higher costs of cultivation and manufacture than forecast.
- Lower dried flower yield per plant than forecast.
- Lower active pharmaceutical ingredient per kg of biomass sourced either from THC owned production or from other licensed permitted cultivators.
- Changes in the regulatory framework. We note that cannabis medicines are not subsidised by the Australian Federal Government (via the Pharmaceutical Benefit Scheme [PBS]). If this happens at some stage, we would expect to see a material step up in demand.

On the financial front we believe THC will need to fund ~\$10m of capital expenditure and working capital demands in FY2020E through a mixture of debt and equity.

We have assumed in our forecasts that \$5m of equity is raised at \$0.40 lifting the number of shares on issue by year end FY2020E.

We have also assumed the balanced of the funding requirements is sourced from a debt facility. If debt funding cannot be arranged the size of the equity piece may be bigger than currently forecast.

On the contrary we see some positive risks to our forecasts including:

- Local medicinal cannabis demand is greater than 100,000 patients and THC achieve a higher market share given its early mover advantage.
- THC ramps up cultivation at Eden Farms to 66,000 m² by the end of CY2022E.
- Local and global demand is such that cultivation at Ballina is brought forward. Local and global demand allows THC to bring on cultivation at Nova Scotia.
- Average product pricing is higher than \$0.20/mg going forward given the potential to produce high specification product designed to meet specific patient demands at the Southport facility going forward.
- Fully ramped up cost of cultivation is lower than our assumed \$750/kg of dried flower.

Capital structure has simplified

Post the 31 December 2019 option exercise, THC has 139.2m ordinary shares on issue with 31.0m options and performance shares outstanding resulting in a potential diluted share count of 170.2m.

Of the remaining 31.0m options and performance shares, we estimate only 0.7m would vest given our view on THC meeting the performance hurdle requirements and the current spot share price.

At our valuation price we estimate 4.8m new shares will issue with the options raising \$2.6m over various vesting periods.

Figure 12 – THC Global capital structure

	No(m)	Exercise Price	Comment
Current Shares on issue	139.2		
Option Expiry			
31-Dec-20	0.7	\$0.40	
31-Dec-20	2.0	\$0.50	
31-Jul-21	1.5	\$0.75	
31-Jul-21	2.5	\$1.20	
31-Jul-21	0.4	\$0.50	
01-Jan-22	0.2	\$0.80	
01-Jan-22	0.3	\$0.90	
01-Jan-22	0.6	\$1.05	
01-Jan-22	1.1	\$1.20	
Options	9.2		
31-Dec-19	12.0		Unlikely to vest in our view given Canndeo unlikely to report \$2m profit in FY19
31-Dec-20	6.0		Unlikely to vest given Epigenetics unlikely to report \$1m profit in FY20 or FY21
31-Dec-20	0.3	\$0.60	Share price above \$0.60
30-Jun-21	0.5	\$0.85	Share price above \$0.85
31-Dec-21	0.7	\$1.10	Share price above \$1.10
31-Dec-21	2.5		Unlikely to vest given unlikely to verify a stable polyploidy within cannabis by 2021
Performance Shares	21.9		
Potential diluted shares on issue	170.2		

Source: THC Global, MST Access

Valuation

Our FY20E base case valuation for THC is \$0.81 on an adjusted diluted basis, based on THC ramping up its hydroponic greenhouse planted cultivation to ~67,200m² by the end of CY2024.

Key assumptions in our valuation are:

- Our base case model financial forecasts with cash tax to be paid in FY2022 given the ~\$15.3m of carried forward tax losses we forecast at FY2019.
- Equity beta of 1.50 (FactSet 2-year beta 1.47)
- THC to raise ~\$10m funding in FY2020 [debt (~\$5m) and equity (~\$5m at \$0.40 equating to additional 12.5m shares)] for working capital, to fund first production from Eden Farms and to do minor capital works at Southport and Bundaberg for tissue culturing and repurposing work.

Figure 13 – THC Global discounted cash flow assumptions

Sum of discounted forecast cash flows	61.7	Target Debt / Enterprise Value Ratio	10.0%
Nominal long run growth rate	2.0%	Statutory Tax Rate	30.0%
Discounted terminal value	66.3	Risk Free Rate	4.0%
Enterprise Value	128.0	Equity Beta	1.50
Less: Net debt	(4.1)	Equity Market Risk Premium	6.0%
Assumed option exercise at valuation price	2.7	Cost of Equity	13.0%
Total Equity value	126.6	Debt Premium	4.0%
FY20E diluted shares on issue	156.7	Cost of Debt	8.0%
FY20E Value per share	0.81	WACC	12.3%

Source: THC Global, MST Access

Sensitivities

We have run two sensitivities to our base case model to demonstrate below the leverage to product pricing.

Based on our forecast production and cost assumptions we note the current share price is factoring in a forecast cannabinoid oil sale price of ~\$0.17/mg from going forward.

Figure 14 – THC sensitivity analysis

Year ending December A\$m	FY19E	FY20E	FY21E	FY22E	FY23E		
	Forecast	Forecast	Forecast	Forecast	Bear	Base	Bull
Assumed API pricing \$/mg	n/a	0.20	0.20	0.20	0.170	0.200	0.230
Southport biomass throughput (kg)	n/a	3,863	19,001	33,617	48,233	48,233	48,233
Revenue	5.0	10.8	31.2	50.5	60.4	69.8	79.3
EBITDA	(7.6)	(6.0)	1.2	9.0	9.6	19.0	28.5
EBIT	(7.8)	(6.8)	(0.6)	7.2	7.8	17.2	26.7
Net interest	0.1	0.1	(0.3)	(0.3)	(0.6)	(0.2)	(0.0)
Underlying Profit	(7.6)	(6.7)	(0.9)	4.8	5.1	11.9	18.6
Underlying EPS (¢ps)	(5.8)	(4.6)	(0.6)	3.2	3.3	7.8	12.3
P/E (x)	n/m	n/m	n/m	13.5	12.9	5.5	3.5
Operating cash flow	(7.7)	(7.9)	(0.1)	8.0	9.0	18.4	21.8
Free cash flow (OCF- SIB capex)	(7.7)	(8.1)	(0.3)	7.8	8.7	18.2	21.5
Free cash flow yield	n/m	n/m	n/m	11.9%	13.4%	27.8%	33.0%
Market Capitalisation	59.8	65.2	65.2	65.2	65.2	65.2	65.2
Net Debt / (Cash)	(3.7)	4.1	4.4	(3.4)	(0.8)	(21.6)	(36.1)
Enterprise Value	58.8	72.0	72.3	64.5	67.1	46.3	31.7
EV/EBITDA (x)	n/m	n/m	60.5	7.1	7.0	2.4	1.1
December 2020 Valuation		0.81			0.38	0.81	1.21

Source: THC Global, MST Access

As noted in the Financials section, there are some key drivers that have a material impact on the financial forecasts for THC including:

- Biomass area planted
- Plant density
- Number of crops p.a.
- Dried flower yield per plant
- Wastage
- Active pharmaceutical ingredient (API)
- Crop management and cultivation costs
- Product pricing

Appendix 1 – Board

Steven Xu; Non- Executive Chairman.

Steven is a Chartered Accountant (CA ANZ) with over 15 years' experience working in Price Waterhouse Coopers and listed companies in Australia and China. He specialises in financing, IPO and M&A activities in a broad range of sectors including technology, agriculture, smart manufacturing and healthcare.

Steven is the head of the MY INP Venture Capital Fund with global investments in Medicinal Cannabis and related industry companies. He has strong international connections, especially in North America, Israel and China, and continues to analyse and seek out investment opportunities in these industry sectors.

Alan Beasley; Deputy Chairman; Non-Executive Director.

Alan has worked in the Investment Banking and Investment Management industries for over 30 years, with Bankers Trust Australia, Goldman Sachs Asset Management, and BNP Paribas Asset Management Ltd - the last two positions as Managing Director and Australian Country Head. Alan is a director and former director of several listed and unlisted public and private companies.

Alan graduated with a Bachelor of Economics, (UNE) and completed an Advanced Management Program in International Investment Management, from the Graduate Business School, Stanford University, USA. Alan is a Certified Practising Accountant, (CPA) Fellow of the Governance Institute of Australia, (FGIA) and Fellow of the Australian Institute of Company Directors (FAICD).

Lou Cattelan; Non-Executive Director

Lou has over 30 years' experience in Pharmaceutical, Nutraceutical, Complementary Healthcare and allied industry sectors. He specialises in Project Management, Operations, Quality Assurance, Supply Chain, Strategic Planning, New Product Development, Regulatory Compliance (TGA & FDA), Sales & Marketing, Business Development and Special Projects. Lou sat on the ASMI (Australian Self Medication Industry – which is the peak industry Body for Australian Pharmaceuticals) Committee for Complementary Medicines to act as a liaison between TGA and key industry stakeholders.

Lou is currently a Director of Contract Pharmaceutical Services of Australia (CPSA) as well as their Sales & Marketing Director. During his 17 years at CPSA he has consulted with all major Pharma companies including Pfizer, MSD, Mylan and GSK to take innovative concepts through to compliant finished products. He has also worked in senior hands-on positions with Ella Bache, Milpharma, Sunspot Products, Bayer Pharma and Blackmores.

Gary Radcliff; Non-Executive Director

Gary is a practicing Barrister, having been called to the Bar in 1984 and is the President of the Gold Coast Bar Association. Gary is also a specialist adjudicator in relation to Dispute Resolution recognised by the Office of the Commissioner for Body Corporate and Community Management (Queensland, Australia).

Gary provides a wealth of experience in corporate governance and compliance matters in both Australia and internationally. In addition to his legal practice, Gary has significant experience in project management, corporate advisory and company directorship in a wide range of sectors, most notably; pharmaceuticals, financial services and technology.

Henry Kinstlinger; Company Secretary

Henry Kinstlinger has in the past thirty years been actively involved in the financial and corporate management of several public companies and non-governmental organisations. He is a professional company secretary and corporate consultant with broad experience in investor and community relations and corporate and statutory compliance.

Appendix 2 – Senior Management

Ken Charteris; Group Chief Executive Officer.

Ken is a veteran of multiple biotech and pharmaceutical companies over the past three decades as CEO, Managing Director and Chairman. In previous Executive roles Ken has had full profit and loss and balance sheet responsibility including legal and financial compliance in listed and international structures, leading businesses with revenue exceeding \$200m and asset bases within \$100m - \$500m. Ken has a proven track record in hands on roles within major listed international companies improving profit growth and effecting share price increase.

Ken was involved in various senior levels within THC since prior to listing on the ASX, Ken has been instrumental in the execution of the Company's strategic plan, including the acquisition of THC's manufacturing facility and the securing of commercial partnerships with Endoca (Europe). Ken has a specific mandate to drive future acquisitions and alliances for THC Global.

Jarrod White; Chief Financial Officer.

Jarrod is a Chartered Accountant and founding Director of Traverse Accountants Pty Ltd, a Corporate Advisory and Chartered Accounting Firm based in Sydney. Jarrod has been appointed Company Secretary and Chief Financial Officer of several other listed entities that operate on the Australian Stock Exchange and London Stock Exchange.

He has a sound knowledge of corporate governance and compliance. Jarrod has also been an advisor to a wide range of capital raisings, IPO's and reverse takeover transactions.

Angela Macquire; Chief Operating Officer, THC Pharma.

Angela has over 30 years' experience in the pharmaceutical industry including managerial and directorial roles at PCI Clinical Services, LEO Pharma and IDT Australia as well as technical roles at GlaxoSmithKline and Pfizer.

Her experience includes managing the development and commercial manufacture of various pharmaceutical formulations, both sterile and non-sterile and including nasal sprays, ointments, capsules, and tablets for Australian and North American clients to current good manufacturing practice (cGMP) standards.

Angela will lead the scale-up of THC's commercial production of Australian medicinal cannabis for Australian patients and the global export market.

Dr Andrew Beehag; Lead, Medicinal Cannabis Division.

Andrew led the establishment of this business at its inception in 2016 including its successful licensing and partnership alliancing with Endoca and BOL Pharma and will continue to build THC's successful investment and partnership strategy gearing up THC to supply to domestic patients and the export market in the near to medium term. Andrew's key skills include creation and execution of strategic plans, operations and personnel management, intellectual property management and commercialisation, budgeting and financial forecasting, stakeholder negotiation and management, project management, public speaking and development of high performing teams.

Laura Harvey; Chief Operating Officer (Canada).

Laura has over 25 years managerial experience in the construction/service industry with a varied skillset including operations, sales, marketing and finance with key roles at Slide Clear, Phoenix Restorations, the Beck Group of Companies and Broco Glass.

Appendix 3–Register

	Shareholder	Shares ('000)	Percentage of Ordinary Shares
1	BNP Paribas Nominees	9,801	7.0%
2	0971224 BC Ltd	9,700	7.0%
3	Agri Fibre Industries	4,000	2.9%
4	MMR Corporate Services Pty Ltd.	2,500	1.8%
5	Pegasus Agriculture Pty Ltd	2,500	1.8%
6	Mrs Katja Gordon	1,898	1.4%
7	Une Innovation Consulting Pty Ltd	1,587	1.1%
8	Citicorp Nominees	1,578	1.1%
9	Pears Daisley Pty Ltd.	1,500	1.1%
10	Mr Nicholas Pownall	1,375	1.0%
11	Mr Sid Bainy	1,200	0.9%
12	Ruchnius Pty Ltd	1,090	0.8%
13	Madonna Andrews	1,024	0.7%
14	Mr George Dababoul	1,000	0.7%
15	Ganja Capital Pty Ltd	1,000	0.7%
16	Hamsar Pty	1,000	0.7%
17	Mishtalem Pty Ltd	1,000	0.7%
18	Mr Nicholas Pownall	998	0.7%
19	Blackies super Holdings Pty Ltd	900	0.6%
20	Sawfam Pty Ltd	800	0.6%
	Sub total	46,451	33.4%
	Other	92,714	66.6%

Source: THC Global 2019 Annual Report

Appendix 4 – Global Commercial Relationships

Endoca

A recognised leader in the supply of quality CBD products worldwide.

European pioneers in extraction and purification, sales exceeding €50 m p.a.

Focus on distributing world's best medicinal cannabis products in Australia.

CBD oil, CBD capsules and a unique CBD+CBDA oil.

BOL Pharma

One of Israel's leading suppliers of medicinal cannabis solutions with an extensive portfolio of products targeted for specific clinical applications.

Pioneering creation of medicinal cannabis industry in Israel since 2007.

Partnership to develop Australian market through THC.

Supplying products for Clinical Trials.

Sinapse and Pharma Programs

Sinapse has extensive experience working for, and with, global pharmaceutical companies. It offers broad experience and deep expertise in key areas such as strategy formulation, business transformation, systems selection and implementation.

Pharma Programs works closely with doctors, pharmacists and industry to provide bespoke solutions to support optimal medication usage, adherence and ultimately health outcomes. Their solutions improve access to pharmaceutical treatments and programs for all stakeholders.

Together, Sinapse and Pharma Programs administer the Medicinal Cannabis Medicines Portal (MCMP)

<http://mcmp.com.au/>

The MCMP is a collaborative approach between Prescribers, Pharmacists and Suppliers to help patients get timely access to appropriate Medicinal Cannabis treatment.

ANSPEC

For 25 years, Anspec has been a major supplier of medical and pharmaceutical products to the Pacific region and has maintained long close relations with Government and private health care centres, together with retail pharmacy clients. Endoca products will be distributed in Australia by Anspec, which will offer accounts to participating pharmacies

MCIA

MCIA represents licensed companies undertaking medicinal cannabis research, cultivation and manufacturing in Australia. The association seeks to operate with high standards of quality, delivered within appropriate nationally-harmonised, policy and regulatory frameworks. MCIA seeks to be an industry expert with a strong export focus, producing trusted products for a global market

Appendix 5 – Office of Drug Control (ODC) licensing

Cultivators

A cultivator will need to hold either a medicinal cannabis licence or a cannabis research licence granted by the Office of Drug Control (ODC) under the Narcotic Drugs Act 1967 (the ND Act) to cultivate cannabis for medicinal or related research purposes. A medicinal cannabis licence authorises either cultivation (the growing of cannabis plants) or production (the separation of cannabis and cannabis resin), or both.

There is no restriction on the number of licences that can be granted; however, under international conventions, the overall quantities produced must not exceed domestic requirements. Therefore, the number of cultivators that will be licensed to grow and supply cannabis to licensed manufacturers will depend on the demand from prescribers and the patient groups they treat.

ODC will not be able to grant a medicinal cannabis licence unless it is satisfied that the cultivation and production of cannabis is for supply either to a person licensed to produce cannabis or a person licensed to manufacture medicinal cannabis products. In practice, this may mean the applicant demonstrating that they are known to the producer/manufacturer and that producer/manufacturer is willing to enter into contracts for the supply of cannabis raw material.

Mixed use crops (i.e. separating cannabis from the plant for medicinal/research purposes and using the remainder for industrial purposes) are not permitted under both Australian domestic legislation and international drug conventions. Therefore, cannabis grown for medicinal purposes will need to be grown and used solely for that purpose. A person may hold a medicinal cannabis licence from ODC and an industrial hemp licence from the relevant state/territory, but will have to maintain strict separation between the two crops and comply with the applicable security requirements. Regular site inspections will be undertaken to ensure compliance.

Manufacturers

A person may apply for a licence to manufacture narcotic drugs involving cannabis under the Narcotic Drugs Act 1967 (ND Act). You must hold both a ND Act licence and a permit before manufacture can occur.

Medicinal cannabis products must be manufactured to Good Manufacturing Practice (GMP). The Therapeutic Goods Administration (TGA) is responsible for licensing GMP.

Supply of medicinal cannabis products is limited to clinical trials, Special Access Scheme and Authorised Prescribers (AP). State and territory governments may also have additional requirements for supply, such as patient cohorts or specific indications. Manufacturing licences will be refused if the applicant cannot demonstrate that supply will be in accordance with all pre-requisites.

It is not a prerequisite to hold a state/territory licence authorising activities related to Schedule 8 (Controlled Drugs) before applying for a Commonwealth Manufacturing Licence. However, you must provide evidence that you hold the necessary licences/approvals (if required by the State or Territory where the manufacturing site is located) when applying for a manufacturing permit.

The export of medicinal cannabis (extracts and preparations) is not permitted unless the product is listed as export-only or registered on the Australian Register of Therapeutic Goods (ARTG) and the exporter holds a licence and permit to export drugs from the Office of Drug Control.

Import of cannabis material is permitted for manufacture of medicinal cannabis products.

A person holding a Commonwealth licence to manufacture narcotic drugs involving cannabis and a Commonwealth licence and permit to import drugs, may import cannabis material, including extracts, for use in manufacture.

However, the importer must:

- hold a state/territory licence allowing possession of cannabis material before import approval may be granted.
- only import from countries where cannabis for medicinal use is approved at the federal level.

Appendix 6 – Cannabis

What is cannabinoid oil?

Cannabis oils may contain various concentrations of cannabidiol (CBD), tetrahydrocannabinol (THC), and other minor cannabinoids, mainly depending on the cannabis variety used for extraction.

Oil has become a favourite mode of administration for many medical users of cannabis and cannabinoids for multiple reasons. Firstly, concentrated extracts allow the consumption of a large dose of cannabinoids in an easily ingestible form. With CBD oil, there is no risk of intoxication (getting high), so much larger doses can be consumed than would be possible for THC-rich products.

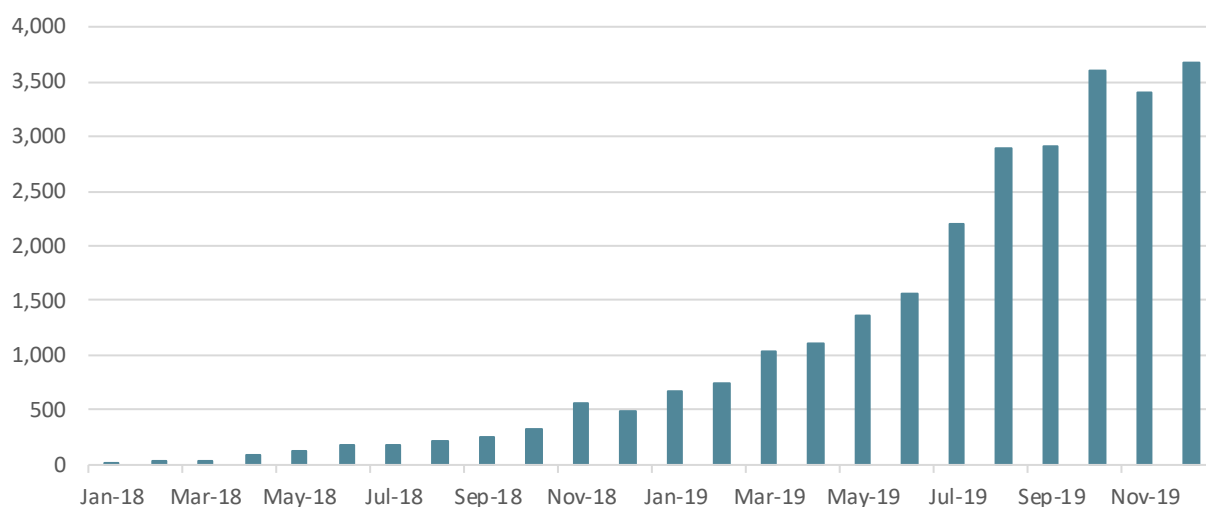
Cannabidiol (CBD) oil is essentially a concentrated solvent extract made from cannabis flowers or leaves that is dissolved in an edible oil such as sunflower, hemp, or olive oil. Solvents used can vary from relatively innocuous organic solvents (ethanol, isopropyl alcohol). THC extract at the Southport manufacturing facility with ethanol.

Currently, the market is developing more sophisticated products, including oral gel caps, sublingual sprays, skin creams, and bottled CBD chewing gums containing CBD.

Therapeutic effects of cannabinoids

Today, cannabinoids are proposed to treat a wide range of medical conditions and to date the TGA has approved circa 25,000 Special Access Scheme (SAS) applications in 2019 with 3,682 in December 2019.

Figure 15 – Special Access Scheme Category B approvals for medicinal cannabis



Source: Therapeutic Goods Administration, MST Access

As can be noted above the growth in SAS medical cannabis approvals has grown materially over the last two years and we would expect the cumulative number of approvals to be around 25,000 in CY2019, up from ~2,500 in CY2018. Noting these figures represent SAS Category B approvals only and it does not represent the number of patients given repeat prescriptions due to expiry and multiple applications by the same patient.

Key medical conditions being targeted but not limited to are epilepsy, multiple sclerosis, chronic neuropathic pain, palliative care and chemo induced nausea.

Research into the therapeutic effects of cannabinoids is rapidly increasing but most current uses are not yet supported by clinical data. With the exception of Nabiximols, marketed as Sativex, for the treatment of severe spasticity, medicinal cannabis products are not registered medicines in Australia, and none are subsidised through the Pharmaceutical Benefits Scheme (PBS), so they can only be accessed through special pathways available for unapproved medicines.

Appendix 7 – Australian Cannabis Stocks

There are 19 Australian cannabis related stocks that we have identified.

The sector has currently got a market capitalisation of ~\$1bn.

Figure 16 – Australian cannabis stock performance

Ticker	Security Name	Last price	YTD Change	Market Cap.(A\$m)
AGH	Althea Group Holdings Ltd.	0.45	61%	105
BOT	Botanix Pharmaceuticals Limited	0.09	22%	90
EVE	EVE Investments Limited	0.01	17%	26
CP1	CannPal Animal Therapeutics Ltd.	0.15	15%	14
ZLD	Zelira Therapeutics Ltd.	0.06	12%	56
IDT	IDT Australia Limited	0.16	10%	38
MXC	MGC Pharmaceuticals Ltd.	0.04	(8%)	51
MDC	Medlab Clinical Ltd	0.34	(15%)	79
THC	THC Global Group Limited	0.41	(15%)	58
RNO	Rhinomed Limited	0.18	(18%)	30
BDA	Bod Australia Ltd	0.34	(32%)	31
CAN	Cann Group Ltd.	1.37	(39%)	194
MMJ	MMJ Group Holdings Ltd.	0.14	(44%)	33
SUD	SUDA Pharmaceuticals Ltd	0.06	(49%)	9
ESE	eSense-Lab Ltd	0.01	(50%)	3
AC8	AusCann Group Holdings Ltd	0.34	(52%)	106
CGB	Cann Global Limited	0.02	(57%)	52
EXL	Elixinol Global Ltd.	1.09	(61%)	150
RGI	Roto-Gro International Ltd.	0.13	(62%)	19
CPH	Creso Pharma Ltd	0.18	(68%)	30
Total				1,174

Source: FactSet; 22 January 2020

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