



Is This Pure-Play Cannabis Extractor Set to Double?

Description

MediPharm Labs Corp ([TSX:LABS](#)) is a pure-play cannabis [extraction company](#) focusing on wholesale (private and white label) solutions of CO2 extracted cannabis oil concentrates for existing licensed producers (LPs). As a pure-play extractor, Labs does not grow its own cannabis, but purchases its dried throughput from existing producers and sells the extracted oil on a wholesale B2B basis.

The company also operates tolling agreements with various LPs in which the LPs deliver dried flower to Labs, who then extracts the oil for a fee, then delivers the finished product back to the LPs without taking ownership of the source or refined product. As of writing, Labs currently has a \$554 million diluted market cap, which I believe presents a value proposition given the prospects of the cannabis sector, Lab's first mover advantage and stable business model, and its proposition as a takeover candidate.

Edibles arrival will be a game changer

A recent study by Deloitte estimates the market for cannabis edibles to be worth roughly \$2.7 billion per year. Furthermore, the report also highlighted that \$1.6 billion will be spent annually on edibles, while \$529 million will be spend on cannabis-infused drinks, while topicals, concentrates, tinctures and capsules will account for more than \$400 million sales.

This next phase of the cannabis cycle means that demand for extraction capabilities will be high, especially as consumer preferences are shifting toward concentrates as opposed to dry flower; concentrate sales in the U.S. have grown by two-fold since 2015, while flower sales as a portion of cannabis sales have decreased by 15% over the same time span.

First-mover advantage and sound business model

As I mentioned earlier, Labs has first mover advantage and a footprint that will allow for 250k kilograms of GMP-certified extraction capabilities later this year. Internationally, the company is also poised for

growth with a 10,000 square foot facility under construction in Australia that will offer 75k kilograms of capacity once approval is reached in the second half of 2019.

Labs' business model also provides a turn-key solution to virtually every small scale LP without the resources to be vertically integrated in the value chain or non-cannabis players (such as legacy beverage companies) to pursue key verticals in the space, without a need for in house extraction or expertise. The pure-play nature of Lab's business also means the company can focus solely on extraction, and will not have to worry about any cultivation issues.

This wholesale B2B model has led Labs to come roaring out of the gate, with \$10 million in revenues after the first month of operations and \$22 million in revenues for Q1 of 2019. More important, Labs is already profitable on an adjusted EBITDA basis (\$4.3 million in Q1)- a rarity in this sector. Furthermore, as Labs ramps up its operational footprint, we can expect the company to benefit from economies of scale and its margins to expand going forward.

Labs' strong growth momentum, footprint and productivity through economies of scale means that the company could be taken out in the near future by one of the larger LPs. This is theory is by no means implausible, as **Canopy Growth Corp** ([TSX:WEED](#))(NYSE:WEED) has already bought out Saskatchewan based extractor **KeyLife Sciences** earlier this year.

Based on deal flows in this space, I would expect a potential buyer to pay 2 to 3 times the current market cap of the company, and the takeout premium to be a key driver of this stock as [edibles become legalized](#).

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