Marijuana Stock Report

October 2016

Table of Contents

Disclaimer

This publication's sole intended purpose is to provide investment-related information and opinions to subscribers The recommendations and analysis presented is for the exclusive use of subscribers. Copying or disseminating any information published is strictly prohibited. Members should be aware that investment markets have inherent risks and there can be no guarantee of future profits. Likewise, past performance does not assure future results. This report does not represent the exact prices at which you should buy or sell. This report is purely for informational purposes and should not be used as a resource own it's own to invest in the marijuana market.

Marijuana, Pot, Weed, Cannabis, Mary Jane, Grass, Herb, Reefer - Money Maker?

Marijuana Stock Report - October 2016

Before we start, I want to address several things:

1. *Marijuana is a very controversial topic, which I am not here to debate. You are are either for it or against it, and in this report I'm not going to convince either way.*

2. *The marijuana plant produces THC (tetrahydrocannabinol) and CBD (cannabidiol). THC has psychoactive effects and gets you 'high.' CBDs do not get you high, but have been proven in many studies to treat everything from cancer to pediatric epilepsy.*

3. *There are numerous legal issues surrounding marijuana and its uses. I believe that the majority of reasons why marijuana is illegal is due to various corporate interests and unfounded bad reputations the plant has carried. I also believe that within the next several years there will be a huge change of heart both in the public's eye and in the government's eye; leading to a much more open market.*

With that said, this report is not to convince you about the benefits of marijuana and what types of ailments it can treat - there is a ton of information online that you can research for yourself.

So, let's assume that you have done all of your homework and are convinced that marijuana is going to be an extremely profitable market to get into... but how do you get "into it?"

The easiest way is to buy stocks that are publicly traded. If you're confused, don't worry. Most people don't realize that there are hundreds of marijuana companies out there that are legally making money and running their operations just like any other business.

Some of these businesses are listed on public stock exchanges (some of these businesses are complete scams too, so we'll watch out for those).

It's also important to note that not all marijuana companies grow cannabis. In fact, most of the companies provide services and supplies for the industry. This is very important to understand because this means that these companies don't have to comply with marijuana laws - they only have to comply with whatever laws apply to the specific product they are producing.

I released a report on marijuana stocks about a year ago where I analyzed the top companies based on market capitalization. Many of those stocks have skyrocketed in price since I released that report. Some of those companies also completely crashed.

I have since trashed that report because the market has changed so much in the past year. The actual list of companies based on market cap is completely different from last year - which shows the volatility and immaturity of this market.

Of course, as investors, we know that when there is massive change there is massive opportunity - and that's why this industry is so exciting.

While I usually provide my opinion of stocks and investing, I have not done so for this report. Instead the analysis in this report has been done by Layton Cox, who chose to share this information exclusively with us.

Layton is an independent equities researcher and holds multiple financial certifications and licenses. He has worked at several different financial firms and has done research on a variety of different industries. Layton is currently not accepting clients, but please reach him HERE if you'd like to connect or follow his writings HERE.

Although I agree with the majority of Layton's analysis, there are areas where my opinion differs - I'll share those differences in future articles where I will talk about specific companies.

Now I'll turn it over to Layton:

By the end of 2016, there could be five more states joining Colorado, Washington, Oregon, and Alaska by legalizing recreational marijuana. There could also be four more states joining the 25 that have legalized medical cannabis.

That's nine out of 50 states, and I didn't even mention the multiple other states discussing future legislation. This is bringing marijuana, and the profits that could be involved, to the forefront of the investing public's conscious.

While there is no guarantee that all of these states will pass their respective marijuana laws, I believe at least some will. Based on the most recent polls, Arizona, North Dakota, and Massachusetts do not look likely to pass their marijuana bills. However, Maine, Florida, Nevada, and more importantly, California do look likely to approve recreational marijuana.

California represents the sixth-largest economy in the world as of 2016. While medical marijuana has been legal for two decades, the vote of recreational marijuana could be HUGE for all marijuana based businesses.

Which is why we are here today, how can we take advantage of this "green gold rush" most effectively?

It is possible to start your own marijuana based business, but this will take a significant amount of startup capital, risk, and work. Since marijuana is still federally banned, it may not be a good idea to sink the mortgage into a weed venture quite yet.

The easiest way to profit from the upcoming voting cycle is to buy cannabis stocks that are publicly traded.

I dug through more than 50 publicly traded marijuana stocks, and I'll be reporting on 19. These stocks have enough average daily volume where a few thousand shares won't move the needle either way, are large enough to demand some legitimacy, have passed my fraud review, and haven't already blown up from the last election cycle (2012).

Average volume had to be more than 25,000 shares. Market cap had to be between $2 Million and $900 Million. Float per shares outstanding had to be greater than 25%, anything under may be a pump and dump scam.

Before we dive into these stocks, let's look at how the majority of these companies make money in the marijuana industry.

Growing & Distributing Marijuana

You can grow marijuana and then sell it to people for medical or recreational use. However, most companies that fall into this category grow their marijuana in Canada, due to the U.S.'s restrictive federal laws.

These companies have more sales if more people can buy their product. If more medical marijuana prescriptions are written or if recreational laws are passed, these companies will see a growth in sales.

Growers & distributors can grow their margins, and make more profit, if they perfect their supply chain. As of now, it is rare that a company ONLY grows or ONLY distributes, because the margins are not as high this way.

Most growers & distributors will grow the weed in Canada, package and ship it to their "retail" locations, and then sell to their target customer.

Consulting & Supplying Marijuana Growers & Distributors

A marijuana farm is a big operation. You need thousands of marijuana plants to grow enough weed to sell. This demands a lot of space, supplies, and people.

As many know, during the gold rush many of the supply store owners made more money than actual gold prospectors. By supplying picks, shovels, wheelbarrows, housing, and legal services, these people were able to create huge companies off the backs of the actual miners. Under this same thought, enter the marijuana consulting and supply companies.

Consulting on supply chain, real estate, security, and marketing needs; or supplying greenhouses, growing technology, or packaging materials, these companies will see a significant bump in gross sales and net profits as more growers and distributors enter the market (or grow in size). Two likely scenarios from marijuana legalization.

Cannabis & Marijuana Pharmaceutical Research & Sales

As many know, Marijuana is “just a plant”. With the recent trend of all natural and organic foods, medicines, and treatments, it only makes sense that marijuana becomes a large ingredient in drugs.

Marijuana can be used in a variety of ways in the medical profession. From a tobacco substitute to a painkiller, the industry is just now starting to experiment with the idea of marijuana as a true medical drug.

Pharmaceutical companies have popped up to try and be the first to prove to the FDA that their product is legitimate, so that they can later spike the price 500x. While the legalization of marijuana may help expedite these companies products to market, it does not mean an immediate boost in their gross sales or net profit.

Now, let’s dive into these companies…

Growers & Distributors

The five growers and distributors I am looking at are Kaya Holdings Inc (KAYS), OrganicGram Holdings Inc (OGRMF), Canopy Growth Corp (TWMJF), Aurora Cannabis Inc (ACBFF), and Terra Tech Corp (TRTC).

Kaya Holdings Inc (KAYS)

http://www.kayaholdings.com/

Business Model

KAYA Holdings owns and operates brands that produce, distribute and sell weed. Touted as the first fully reporting U.S. public company to actually own and operate a vertically integrated seed-to-sale legal marijuana enterprise in the United States, their operations include medical marijuana dispensaries ("MMDs"), medical marijuana grow operations ("Grows"), the manufacturing of proprietary cannabis products, and the research and development of medical grade cannabis strains and extracts for pain relief and treatment of serious illnesses. They opened their first KAYA Shack™ MMD in Portland, Oregon in July 2014. Immediately, the press dubbed them the "Starbucks of Medical Marijuana." While the comparison is a stretch, they have opened another MMD in South Salem, Oregon.

They grow their own weed and then sell it at their locations. A clean business model. Their board has two independent members on it, a hedge fund manager and an investment banker. Their senior management seems qualified and engaged. No need to assume they are lacking leaders or vision.

Financials

The first way to look at a growing and distributing company is to see how much of their inventory are they selling each period. KAYA sells 784% of their inventory each quarter. That means they grow and sell almost 8x their inventory capacity. However, in order to sell this much they are borrowing a good amount each year. Their quick ratio (current assets divided by current liabilities) is only .1. Meaning for each $1 of bills due this year, they can only pay $0.10 now. The long term debt issue looks bad too. They have the highest total debt to assets that I looked at with a 2.2 ratio. Meaning every $1 of assets they own, they owe $2.20. Not good.

Their profitability doesn't look much better. Net income is -$400k and their cash from operations is a -$365k. They are losing money, and have used debt to fuel it. Not a good combination.

Luckily, investors seem to understand this. Their valuations are low for the industry. Price-to-sales is our #1 valuation ratio because so many marijuana companies have a negative net income. Price-to-sales for KAYA is only 21.96, the lowest out of the growers. However, they have a negative book value because of their immense leverage (which creates negative shareholder's equity).

Financially, they don't look like a long-term solvent company. They have lost their current shareholders money and with only two retail locations, it looks unlikely they will make a quick turnaround.

Sentiment

Three-month price is flat at 0%. Year to date, the stock has gone down 19.5%.

Summary

This isn't a company you want to invest into for the short or long term.

OrganiGram Holdings Inc. (OGRMF)

https://www.organigram.ca/

Business Model

OrganiGram is actually a Canadian company. They grow the marijuana and ship it to you. It's the 1-800-Contacts of the medical marijuana world.

However, they only ship to Canadians (and you have to have your medical prescription). I bet they would be more than happy to ship to US citizens once pot is legal (and they could confirm your birth date).

The business model is a great one. It works in many different industries, reduces retail costs, and increases margins. However, the biggest risk to this company is the fact that they may or may not distribute to Americans - something that we won't know for a while, as US federal laws currently prohibit this.

Financials

With a positive working capital and an inventory turnover greater than 1, OrganiGram's operations seem to be working. They don't have many bills due in the next year and a high amount of inventory. There is little doubt that they will be around in a year. They can cover nearly 2x more debt than they are currently holding. They can also cover 10x their annual interest expense.

They aren't going bankrupt this year or anytime in the near future. Actually, OrganiGram has a positive net income, rare in this industry, and a positive cash flow from operations; also rare. OrganiGram is the most profitable grower and distributor I evaluated.

Weirdly, investors don't seem to be paying attention to this. With a price-to-sales of only 41.21, OrganiGram has the second lowest valuation for the growers and distributors. They also have the second highest book-value to share at $0.21, meaning only $1.11 of their share price is speculative on the future growth prospects.

Sentiment

In the last three months, OrganiGram went up 63.8%. In 2016 so far, OrganiGram is up 95.5%. People are buying, but it is still undervalued.

It seems investors believe it will see growth from this US election cycle.

Summary

OrganiGram is a solvent, profitable, and safe company. With a smart business model and the financials to back it up, OrganiGram is a good play in the marijuana growing and distribution business.

However, it may not be the best play for the 2016 US election cycle. Since it is a Canadian company, bringing marijuana over the border is currently not an option. As an investment play, OrganiGram looks interesting.

Canopy Growth Corp (TWMJF)

http://canopygrowth.com/

Business Model

Canopy Growth Corp is a grower-only company. They sell their product wholesale to other distributors. However, they grow A LOT of cannabis. Through Canopy Growth's three wholly-owned subsidiaries, Bedrocan Canada, Tweed, and Tweed Farms, they operate more than half-a-million square feet. Using a data-driven, automated and lean operation, housing an R&D facility, oil extraction infrastructure, and in-house lab, Canopy Growth is an impressive growing operation. They have precise climate controlled spaces for each stage of cannabis production, from clone to cured bud, which allows for the highest quality and widest variety of product in the sector.

They also partner with Snoop Dogg and have four independent stock analysts, which is rare for any marijuana company.

However, they are another Canadian company. Facing the same issue of getting marijuana over the border. They are focusing on exporting to other countries, like Germany, though.

Financials

Due to the difficulty of moving their product and the large amount of marijuana they produce, they only sell about 30% of it each period. That's not much. If they could sell closer to 75% of their crop each period, I would feel better. This doesn't stop them from having a huge amount of working capital, $42 Million.

They also have little to no debt. Their current ratio is 2.85, the highest out of any company I looked at. Their debt-to-assets is also only .07, and they have no interest expense.

Problem lies in profitability. They have a net loss of nearly $4 Million and a loss from operations of $3.7 Million. That's a big hole to dig yourself out of.

They don't have much debt, so they have little to no bankruptcy risk. They have a lot of inventory, but it is moving. They are losing money, and I'm not sure if the few states legalizing Marijuana in the US will help their overall revenue.

Sentiment

In the last three months, the stock is up 46.7%. For 2016, the stock is up 41.6%. This indicates that all the growth in stock price is based on the upcoming US elections.

Summary

The biggest benefit Canopy Growth Corporation has on its side is the fact that it has so much assets and so little debt. The book value per share is $1.26. The stock price is $3.07. Nearly half of the stock price is actual assets of the company. This leaves a high floor, but the ceiling is low too.

With sales depending on legalization and moving the product over multiple borders, it may not see a huge sales growth from the 2016 election cycle.

Aurora Cannbis Inc (ACBFF)

https://auroramj.com/

Business Model

Another Canadian grower company that ships their product to the customer. Think Amazon but for weed. They currently have six different strains of weed with different THC and CBD amounts.

What makes them interesting is that they work directly with Physicians. They allow physicians to register patients and prescribe them through Aurora. Aurora seems to have a significant hold on the medical marijuana industry. They face the same risk of Canada to America exports as everyone else.

Financials

They have a positive working capital, but they only turn over around 10% of their inventory each year. That's not much. A big part of their profitability is that they have $4.8 Million in biological assets unrealized gain. They have a lot of inventory, but it isn't selling. They claim it is going up in value, but that's not actual cash money.

They have negative $5 Million in cash from operations. That's really bad.

If you exclude inventory, their quick ratio is only .06. Debt-to-assets, with inventory, is 0.49. Inventory plays a huge part of their financials from their solvency to their profitability.

Worst case, they have super high valuations. Price-to-sales is at 654. That means for every $1 in sales, investors expect to gain $654 in shareholder wealth. That's way too high for a company that is only profitable because it says its marijuana is worth more today than yesterday.

Sentiment

Over the last three months, Aurora is up 188.9%. For 2016, it is up 147.9%. All growth is speculation for the election cycle.

Summary

This isn’t a good company for the long-term and only looks like a good company now because of the unrealized gains on inventory. With unrealistically high valuations and massive 3-month stock growth, growth is 100% speculative.

Overall, I don’t like the company for the long-term and I think only uninformed investors are buying into the recent growth. When it falls, it will fall big and hard.

Terra Tech Corp (TRTC)

http://www.terratechcorp.com/

Business Model

TRTC is an American company that: “Through multiple subsidiaries…. are committed to cultivating and providing the highest quality medical cannabis consistently delivered to qualified, registered medical marijuana establishments in the safest and most secure manner. Our commitment to advancing research within the medical cannabis industry will lead our approach in cultivating and cross-breeding strains of medical cannabis that treat a variety of ailments.” They are a grow, package, and deliver company. They grow through their MediFarm brand. They package their brands as either IVXX or EDIBLE GARDEN. They have multiple weed shops through their brand called Blüm (in CA & NV). I’m sure they would be happy to open their doors to non-medical patients if it was legal. Special because of their multiple brands and locations in CA & NV.

Financials

Terra Tech has an interesting problem: they sell a lot of product but have a negative cash flow from operations. They don’t have any solvency issues with a fair quick ratio and a low debt-to-assets, so bankruptcy isn’t logical even though they have a negative net income of $4.9 Million, the biggest loss I evaluated.

Even though they aren’t profitable, they have a positive gross margin. So what’s making them lose so much money? I’m not sure, but I do know that they have $51 Million in intangibles and goodwill assets. That is WAY too much. Which is a red flag.

Unrealistic assets, unprofitable business, and high inventory turnover makes me think that the actual business of growing and selling weed isn’t working for Terra Tech.

Sentiment

Up 13.4% in the last three months and up 308% so far in 2016, this stock has a lot of positive sentiment.

Summary

Terra Tech has some big red flags, and some of the highest sales with a low price-to-sales, so I’m torn. Half of me thinks it could be a good buy and can grow more, but the other half thinks it may never actually be profitable and stock price growth is from speculation.

It's business model would go up if marijuana was legalized, especially given its Nevada distributors. All this growth in sales may help make it profitable, but they already sell a lot and aren't profitable, so who knows.

Suppliers & Consultants

The companies I am evaluating that are suppliers and consultants are Surna Inc (SRNA), Kush Bottles Inc (KSHB), MCIG Inc (MCIG), and GrowBLOX Sciences Inc (GBLX).

Surna Inc (SRNA)

http://surna.com/

Business Model

Surna Inc engineers and manufactures products that address the energy and resource intensive nature of indoor cultivation. They make indoor greenhouses for marijuana. This is an industry that will grow exponentially when marijuana is legalized. Growing weed outside is cheaper, but also harder to secure and control. While weed may one day be an outdoor cash crop like cotton, it has started indoors. They are unique because they use water-chilled climate control systems. Instead of having huge electric bills to run the AC in these greenhouses, they use water. This technology may have the potential to be used in any commercial buildings.

It's a niche, but it may be a profitable niche if more growers decide to sprout up - no pun intended.

Financials

Nothing is good or bad with regards to inventory turnover, quick ratio, or working capital. They have more debt than they do assets, which is never good… even if you include $650k in intangible assets. That's not a good indication of Surna's long-term health.

While they have a negative net income, they do have a positive cash flow from operations. Surna also has low valuations. A price-to-sales of only 9.26 is a good buy in almost any industry. It is an especially good valuation in the marijuana industry.

High amounts of debt with unreliable assets can lead to bankruptcy. However, with valuations so low, it seems like most investors believe it will go bad.

Sentiment

In the last three months Surna has only gone up 11.1%. For 2016, Surna is up 52.8%. It doesn't look like investors are buying out of speculation for the election cycle, which is odd because Surna could see a significant growth in sales if more growers pop up.

Summary

Surna may not be the strongest company financially, but they have a unique niche and business model. I believe they will see growth in sales from more growers entering the marketplace. Investors are ignoring this company though. Which can lead to a big value buy.

Buying Surna is a good idea for the short-term, but you will need to watch the company in the long-run to make sure its debts don't corrupt the entire business.

Kush Bottles, Inc. (KSHB)

https://www.kushbottles.com/

Business Model

Kush Bottles creates packaging to store, ship, and safely secure marijuana. They also sell marijuana smoking devices and accessories. It's an interesting play because it can be used by both legal/illegal distributors, users, and other suppliers. They have a huge following and are featured on CNBC and INC. With locations in CA, CO, and WA these guys are legit. They are special because they were the first ones to start this and it's proven to be big.

Financials

Financially, Kush Bottles looks good. Hence they are a normal retailer of goods, they have good turnover and a solid amount of working capital. However, what makes Kush Bottles special is that their current ratio is 2.76. For every $1 of bills due this year, they have $2.76 waiting to pay. Their overall debt-to-assets is only 0.12 as well. Debt wise, Kush Bottles is good which is where most retailers of packaging struggle.

However, Kush Bottles cash from operations is NEGATIVE $690k, even though their net income is a positive $23k.

This isn't what I would expect. Given the high turnover and low debt, I wouldn't think they have a negative cash from operations. They also have a higher than normal price-to-sales at 57.7. That is really high for a retailer.

Sentiment

Last three months, up 67.8%. For 2016, up 38.5%. Investing based on election.

Summary

I'm not a big Kush Bottles fan. Why do you need packaging specifically made for pot? Why not buy a normal jar or baggie off of Amazon. While Kush Bottles does have a "consulting" and marketing business, it's not the main profit driver for them.

Kush Bottles negative cash from operations and high price-to-sales doesn't make me feel good about investing in them either.

MCIG Inc. (MCIG)

http://mcig.org/

Business Model

MCIG makes electronic marijuana cigarettes. They also help create buildings made specifically for marijuana. Do those two go together? No.

I could see the electronic marijuana cigarettes being a big growth opportunity, but at the same time, why the are they making greenhouses? It's obviously not a big part of their business and they only do it for online stock marketing purposes.

Overall, the main driver of revenue is selling marijuana electronic cigarettes.

Financials

They sell a ton of these things too. They have an inventory turnover of 72x. That's a lot. They use a Chinese plant to manufacture all of their cigarettes, so they can make a ton of these things for cheap. They also have a high current ratio and low debt-to-assets. All good signs.

Surprise, they aren't profitable. A $1.4 Million net loss and a negative $46k in cash from operations. That's a big difference, why so large? They paid out $1.3 Million in stock based compensation last year, and $4 Million the year before.

That's a huge red flag.

Sentiment

Investors seem to be paying attention to this high of a stock compensation, a -14.6% for the last three months. Year to date, -20%. Investors aren't into this thing.

Summary

What could be a fine company seems to be happier to line its pockets than your pockets. With no buyers, stay away from this one.

GrowBLOX Sciences Inc (GBLX)

http://growblox.com/

Business Model

GrowBLOX makes high-tech “grow boxes” to grow marijuana in. This stuff looks like it’s from Star Trek. They have amassed a huge amount of information on how to grow the best pot (starting at the seed Cultivation Science and moving to the end-user phase intellectual Property & Regulatory). These guys are smart and have a lot of ways to distribute their products for revenue.

Problem is, they haven’t sold anything yet.

Financials

They have no sales. That’s usually not good, but given their massive amount of research it somewhat makes sense.

They have a low quick ratio and a high debt-to-assets. They have used debt to fuel their business so far, which is necessary because they don’t have any sales. Obviously, they aren’t going to be profitable either.

Sentiment

-10% in the last three months but up 129% for 2016. There doesn’t seem to be much speculative buying, which is odd because GrowBLOX may be one of the best companies to buy before legalization. No sales but still standing means they have strong backers on the debt side, which every company needs. If they can start making some sales, it may be the perfect time to capitalize on a bunch of new potential growers.

Summary

Good product, no sales.

If they can start making sales, they will have a good company on their hands. This is a longer marijuana play than any of the others we’ve evaluated.

Pharmaceutical & Biotechnology

In the pharmaceutical and biotechnology area of the Marijuana market, I am looking at Abattis Bioceuticals (ATTBF), InMed Pharmaceuticals Inc (IMLFF), CV Sciences Inc. (CVSI), and Digipath Inc (DIGP).

Abattis Bioceuticals (ATTBF)

http://www.abattis.com/

Business Model

Abattis does a few things. They test marijuana for potency, and they create some pharmaceutical products they sell. Specifically, they are focusing on pain caused by inflammation and mental ailments common to our modern lifestyle. However, out of all of their products (http://www.abattis.com/vergence-sales) I can't seem to find any that have marijuana or cannabis as an ingredient. This makes me think that their only involvement in marijuana is testing it.

Testing marijuana can be profitable, if they sign some big contracts. However, it seems they do spend a lot of time and resources on their "natural" pharmaceutical products.

Financials

No sales.

Unprofitable. -$360k net income. -$673k in cash from operations.

All signs are looking bad.

Sentiment

41.5% up in last three months. -2.9% in 2016. Pure speculative buying.

Summary

Abattis isn't a huge marijuana player. With their only involvement in the industry regarding testing marijuana, they seem to be valued more like a pharmaceutical research company than an actual marijuana tester (which we will see later). With no revenue and speculative buying, I wouldn't invest in this at all.

InMed Pharmaceuticals Inc (IMLFF)

http://www.inmedpharma.com/s/home.asp

Business Model

InMed is a legitimate pharmaceutical company with a drug pipeline and R&D testing. They are using cannabis as the key ingredient in two drugs aimed at Epidermolysis Bullosa and Glaucoma. As of now, both drugs are in the pre-clinical stage (a good way away from showing up on your local pharmacy's shelves). They believe cannabis can help treat Arthritis, Psoriasis, Epilepsy, Anti-anxiety, Diabetes, Obesity, and Asthma. If they can pull that off, then they will make tons and tons of money… in 50 years.

InMed does have an independent board and scientific board as well. This boosts their legitimacy.

Financials

No revenue, but that is normal for a legitimate research pharmaceutical company. Not a big red flag in my mind.

Negative working capital, normal for R&D again.

Low quick ratio of only .05 and higher than I like debt to assets of .58. Obviously, they have to pay their scientists somehow. They seem to be turning to debt in order to do so. As long as they can move their drugs through the pipeline on schedule, this shouldn't be an issue. They do have $1.4 Million in intangible assets, which I'm never a big fan of.

Negative net income and cash from operations (expected).

Any pharmaceutical research company is going to have questionable financials, so this doesn't tell us much. Neither good or bad.

Sentiment

Last three months: up 25.5%

For 2016: down 23.5%

Speculative buying based on 2016 election.

Summary

InMed is a pharmaceutical research company. They will pop because they use cannabis, but it is unlikely they will see a significant amount of revenue flow if California or any other state legalizes recreational marijuana. It really doesn't make much sense to invest into at this point in time.

CV Sciences, Inc (CVSI)

http://cvsciences.com/

Business Model

CV Sciences has two divisions: pharmaceuticals and consumer products. Pharmaceutical Division is developing synthetically-formulated cannabid oil-based medicine, pursuing the approval of the U.S. Food and Drug Administration (FDA). Consumer Division is engaged in the development, manufacturing, marketing and distribution of consumer products containing plant-based cannabidiol (CBD), which is refined into its portfolio brands: PlusCBD Oil and Purified Liquid (vape eliquids). Their pharmaceutical is a chewing gum that is cannabis based. They could be the Nicorette of Marijuana and with the growth of e-cigs, they could be big there too.

With a legitimate pharmaceutical product in the preclinical stage and an e-cigarette for marijuana, they are greatly involved in marijuana and could see a boost in revenue upon its legalization.

Financials

This company's financial statements are almost too pretty. It scares me. With a huge amount of working capital (nearly $14 Million) their assets easily dominate their liabilities. A quick ratio of .88 means that they are not in trouble of financial stress for this year. A low debt to assets of .19 means that they aren't in bankruptcy risk anytime soon.

While they do still have a negative net income and cash from operations, which can somewhat be expected given their pharmaceutical research and lack of legalization of their e-cigarette, their valuations are unreal. Actually, if it wasn't for their extremely high SG&A expense, of nearly $44 Million, they would've turned a profit.

With a price-to-sales of only 6.9 they have the second lowest valuation, second only to MCIG another e-cigarette maker. Their book value per share is $0.42. Their share price is only $0.33. You are buying $0.42 of assets for only $0.33.

Sentiment

Last three months -20%. For 2016, up 33%. It doesn't seem to have much speculative investing, which is good for investors now.

Summary

CV Sciences has the valuation of a crappy e-cigarette company, but it has the potential to be a huge pharmaceutical player in the cannabis space. While they are still a few years from having a marketable product, few are looking into making marijuana gum.

I think CV Sciences is a buy low. The extremely great valuations are just a boost to your portfolio.

Digipath Inc. (DIGP)

http://digipath.com/

Business Model

Digipath tests marijuana. Just like any drug, food, beverage, or anything, weed must be tested to ensure it is not harmful. DIGP is doing that and from what I've found, they are the only one. If weed becomes legal, FDA and other government entities will need standards. Then they will need a way to measure these standards. DIGP and its equipment will be the answer. Dr. Cindy Orser, Ph.D., a 20-year biotech and diagnostic industry veteran, leads these efforts on behalf of Digipath, serving as Chief Science Officer and assists cannabis providers and regulatory agencies, as well as working in academia in several key roles. In addition to her work, she holds 18 patents and authored 41 peer-reviewed publications.

It is very likely that they will see a pop in revenue if marijuana is legalized. More buyers = more product. More product = greater risk of danger. Greater risk of danger = more legislation and rules. More rules = more requirements. More requirements = more testing. Digipath will see a significant jump in revenue in 2017.

Financials

Positive working capital and an inventory turnover of 2.74. That's good. They have assets to work with and are making sales every day. Their quick ratio tells you more. A quick ratio of 2.05. They have twice the assets than liabilities due in the next year. That's a great sign.

They also have low long-term debt as well. Debt to assets is only .07. A very clean running company all the way around.

All of these assets haven't quite made a profit yet. Negitive net income of $1 Million and negative cash from operations of $800k make Digipath still unprofitable. However, I think this will change in 2017. They actually only have a negative net income because of professional fees of +$1M. Professional fees increased primarily due to increased stock based compensation of $770,676 during the three months ended June 30, 2016, consisting of the amortization of $737,936 of options expense and $32,740 of amortized stock based compensation on previously awarded shares of common stock issued for services. Those aren't ridiculous levels of stock based compensation, but it is something to keep your eye on.

Valuations are low for the marijuana industry. Price to sales of 16.71 is the 5th lowest I saw. Positive book value, but only of $0.03 per share.

Sentiment

3 months: 2.88%

For 2016: 42.14%

It doesn't seem to have a lot of speculative buying.

Summary

This is a great buy. Digipath has set itself up as THE marijuana testing firm and will see big spikes in revenue when marijuana is legalized. With relatively low valuations and the lack of speculative buying, I like this company and it's future.

Keep in mind that the election is November 8th and the results may determine much of these stocks prices.

Fraud Alerts

In an attempt to help investors maximize returns and minimize risk, I am going to identify three stocks that I believe are at a high risk for fraud in the marijuana industry.

The over-the-counter (OTC) market for securities, often referred to the microcap market or pink sheet, is made up of companies with small assets and low stock prices (usually less than $1, hence the name penny stocks). While companies that trade their stocks on major exchanges (like the NASDAQ or NYSE) undergo a formal application process and meet minimum listing standards, companies quoted on the OTCBB or the OTC Markets do not have to apply for listing or meet any minimum financial standards. This creates a significant amount of potential for fraud.

To make situations ever blurrier, there are numerous legal and political issues surrounding publicly traded marijuana companies. Nonetheless, there has been a growing demand for marijuana stocks in the last few months leading up to the November election cycle. This demand and “hype” further increases the incentives to run a fraudulent marijuana penny stock.

Given the growing demand and interest in marijuana and the lack of regulation in the penny stock market, fraud will occur. Several companies can already be claimed as being fraudulent, but that doesn’t help us now.

The following is by no means the “be-all-end-all” of fraudulent marijuana companies. These three are just the ones that stick out to me, given their business model, financial statements, and price changes.

Cannabis Sativa Inc (CBDS)

http://cannabissativainc.com/

Business Model

Best known for its former CEO, and 2016 Libertarian Party Presidential Candidate, Gary Johnson, this company has an extremely odd business model. It owns five subsidiaries: three "pharmaceuticals," a customer rewards card, and a website (CBDS.com: All Things CBD).

The pharmaceuticals are facial creams, balms, and water (yes drinkable water) that is infused with cannabis. The water sounds interesting: CBD Water by Wild Earth Naturals but most of this is more of a "natural products" play than a "marijuana is legal" play.

They also offer a "benefits card" that helps with prescription products somehow. The website isn't really live and it's trying to be the Wikipedia of pot… which doesn't seem like a good business idea since Wikipedia is already in existence.

Corporate Governance

Overall, it seems like they are trying to become a franchise distribution company. They have a business model for selling weed and they sell it to franchisers. If they truly had an edge in the market (like cheaper growing wholesale prices, scientifically better equipment, or even anyone with a significant business background), it may work. However, they don't. Their board of directors consists of a senator (talk about corruption in an organization), a guy who used to work at NUMEROUS marijuana fraud companies (HEMP), a judge, and an ex-patrol officer from the LAPD.

Also, Financial Industry Regulatory Authority, Inc. (FINRA) denied the CBDS application for a 1.5 share dividend for each share of common stock outstanding, record date November 16, 2015, as previously approved by the company. That doesn't happen often.

Financials

The first thing that sticks out is that they have $60,000 in "digital currencies" (consisting of HEMPCOINS and GARYCOINS). That's weird, since I can't find anything on Garycoins via Google. Hempcoins are valued where 10 coins = 1 share of stock in RMTN. Not reliable.

They also have $545,256 in prepaid expenses. Given that their total working capital is only $384,767, that prepaid expense number makes it look like their assets are significantly larger than they really are. Prepaid expenses are not a "real" asset. They are an “accounting” asset. You can’t invest prepaid expenses, it just means you paid for something you haven’t used yet (like a gym membership). This is a massive red flag.

They are neither liquid or solvent. With a 0.33 quick ratio, they would not be able to pay their bills tomorrow if they needed to. With a negative interest coverage ratio, it doesn’t look like they will ever be able to pay off their debts, so how are they generating “shareholder equity?”

They have $2,891,297 of intangible assets on the balance sheet. That’s make belief assets. I could say I have a great idea that’s going to turn Gatorade into marijuana water and say it’s a $1 Million idea and that becomes an intangible asset. They have done that 2.8 times.

They have little to no real assets. They have significant debt. They are creating shareholder wealth with intangible ideas and “assets”.

They also have a net loss of -$58,563 from operations. However, they were positive before you come to administration costs. Administration costs, things like salaries and rent, was $101,238. They had a gross profit of $43,985 before that hit. What that sounds like to me is instead of living on the little they do make, they borrow more to pay themselves higher salaries. Fraud.

Trading & Sentiment

There are nearly 18 Million shares outstanding, but they only allow a little over 2 million to be traded. Why? Because it creates an artificial demand. Less trades available for trade means larger spikes up and down. This has worked because on average, almost 3% of their tradable shares trade each day. That’s a lot. It also shows that there could be a lot of day traders in this position, which is never a good indication of a long-term wealth building company.

Despite all of this, over the last three months their stock has gone up 61.18%. So far for 2016, they are up 291.43%. Making their price/sales grow to 1068.23. Meaning for every $1 of sales, you believe the stock will go up by $1068.23.

Don’t line these guys pockets.

Cannabics Pharmaceuticals Inc. (CNBX)

http://www.cannabics.com/

Business Model

Their goal is to create a cancer product using marijuana. The Company's principal product is Cannabics SR'. It's an oil capsule composed solely from food grade materials that delivers a steady level of effects for 4–8 hours. It's a pot pill.

The most common oral administration of cannabinoids is through eating edibles. Edibles usually contain high dosages of cannabinoids which may cause side effects like dizziness, anxiety and dissociation. The oral administration route has the longest beneficial effect and lacks the undesirable effects of smoking.

Sounds like a good idea right?

Problem is Cannabics Pharmaceuticals Inc. does not manufacture, distribute, dispense or possess any controlled substances, including cannabis or cannabis based preparations.

So how do they make money? They don't.

Corporate Governance

They are clean from what I can find. Cannabics Pharmaceuticals Inc. was founded in 2012 by Israeli researchers from the fields of molecular biology and cancer. The Company's R&D is based in Israel, where it is licensed by The Ministry of Health.

I don't find any information about a board of directors or anything.

Financials

No inventory (because they don't sell anything). This means they really have no activity at all.

The lack of assets just kills their quick ratio and debt/assets. Quick ratio is only 0.18 (meaning they can only pay $0.18 of each $1 of debt they owe) and their debt to assets is 4.75 (meaning they have nearly 5x as much debt as they have assets).

Somehow they have $50k in revenue. Not sure where that came from, but it's still not much. They have a net loss of $26,480 and have -$50,727 in cash from operating activities. That's not a good long term business model.

Trading & Sentiment

The stock may be dead. It hasn't traded much in the last three months. THIS ISN'T A GOOD SIGN. For 2016, it is still up around 10%.

Once again, they are restricting how many shares you can trade. More than 100 Million shares are outstanding, but only 13 Million are traded. That's not good. It increases volatility.

Price to sales is 121.80. Meaning for every $1 increase in sales, you expect them to turn that into $121.80 in earnings for the shareholder. For a comparison, Apple's is 2.87

The business model is a reach and their financials aren't much better. It may already be dead, but if you are in it, get out. If you aren't, stay out.

United Cannabis Corp. (CNAB)

http://www.unitedcannabis.us/

Business Model

They actually have a legitimate business model (on the website at least). They create a pharmaceutical drug that is an oil (with Cannabinoid as the main ingredient). This drug is supposed to be more potent.

Their research looks legitimate and I think it's probably a real drug.

Corporate Governance

They have a great board of directors as well. Legitimate businessmen who have been in the industry since 2009 operating a growing farm & distribution center.

Their doctors are legitimate and have studied things other than just marijuana. If a doctor is just a pot doctor, they could be a whack job. These guys aren't.

They also have a pr/investor relations group who seems knowledgeable (rare for penny stocks).

Financials

This is where it gets ugly.

They are $2.5 Million dollars in debt.

They only own $168k of stuff (they just acquired with a 50% interest in Cannabinoid Research & Development Company Limited ("CRD"), a Jamaican company, in exchange 40,000 shares of common stock valued at $88,000. That makes up about half of their assets).

One customer makes up 92% of their revenue. They only made $197k in total revenue. If they lose that one customer, they are dead in the water. They have been selling their consulting services for future royalty payments and stock options, which isn't usually a good idea.

That could just be bad management, but this is where the fraud comes in: "On January 12, 2016, we awarded 1,050,000 stock options to each of Messrs. Blackmon, Verzura and 980,000 stock potions to Mr. Ruby under our 2014 Stock Incentive Plan. The options were fully vested at the time of grant and give the option holder the right to purchase shares of our common stock at $0.20 per share during the ten year term of the option."

This occurred in 2015 too: “On January 9, 2015, we awarded 200,000 stock options to each of Messrs. Blackmon, Verzura and Ruby under our 2014 Stock Incentive Plan. The options were fully vested at the time of grant and give the option holder the right to purchase shares of our common stock at $0.70 per share during the ten year term of the option.”

Over the last two years, they gave away $1,036,000 in combined stock options for Blackmon, Verzura, and Ruby.

If your company is losing $128,079 each quarter, would you give your managers a million-dollar bonus?

This seems like another company that is looking to line its management’s pocket with the money from the shareholders.

Pricing & Sentiment

With somewhat more reasonable valuation of 56.38 price/sales, it isn’t horrible, but it is nowhere close to good. Their 3-month price trend is -17.86%, but for 2016 they are up almost 5%.

Once again we see the trick of limiting tradable shares. Only 14% of total shares are tradable. 2% of those tradable shares trade each day on average. This can spell a lot of volatility and risk. Which is what happened earlier this year. Within 6 months they had a swing from $0.40 to near $0.01. That’s not normal even with penny stocks.

While the business might be legit, the managers are misusing assets and not dedicated to creating shareholder value. Don’t invest.

Risky Strategy

With new laws, come eager buyers looking for a quick buck.

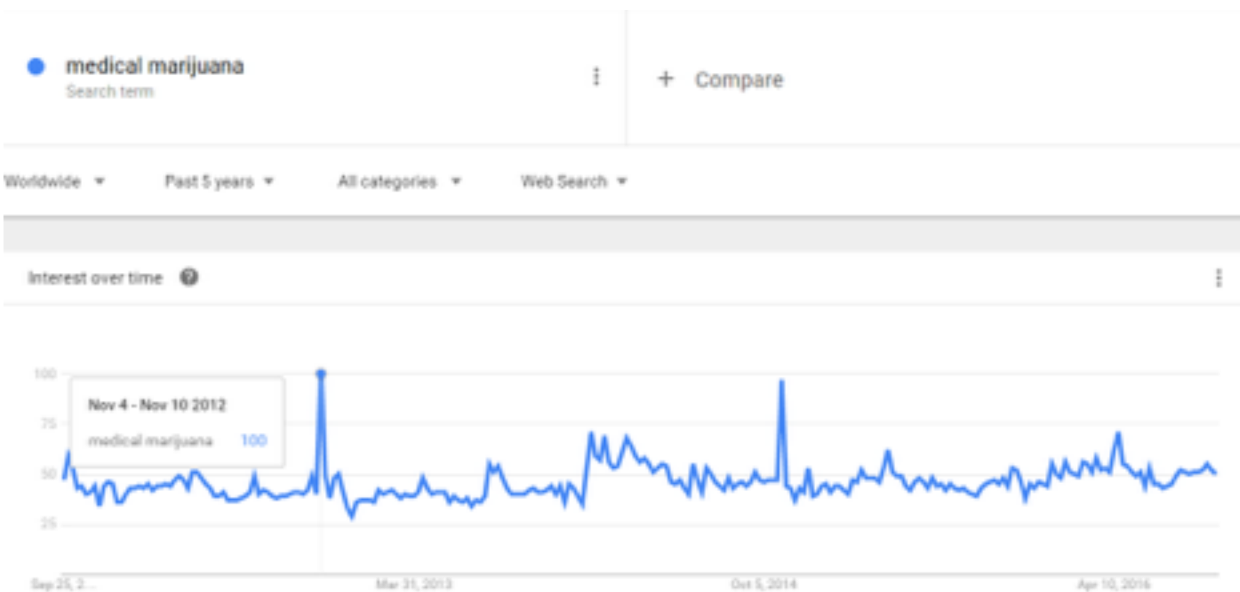
Mark my words, CNBC will have a few headlines with marijuana stocks in the title if California passes legalization. This will drive the average, uninformed, investor to the marijuana stock market. This is called a bubble.

You want to make a play off of the emotions of these investors. These investors aren't looking at the actual company - they're just reading the ticker symbols and piling in money on a bet. Hell, I did it four years ago into HEMP (turned out to be a fraud).

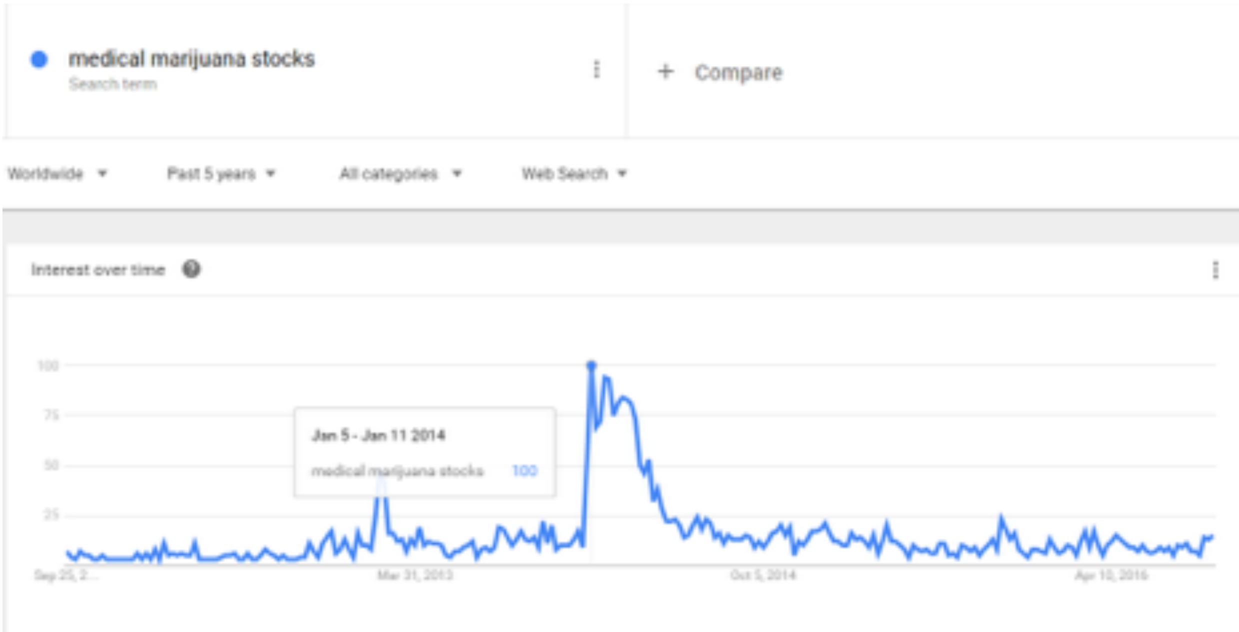
This strategy is essentially the same as the ones making the bet, with one big difference: price. We can enter the market way before those gamblers and buy up shares for a fraction of the price that they will be buying at. This is a RISKY STRATEGY and not a long-term investment. This is a bet.

Timing The Buy-In & Sell-Out

The search term "medical marijuana" spikes the first week of November every election year. I believe this will continue for 2016 as well.



Funny enough, the search term "medical marijuana stocks" doesn't peak until January.



This means AT A MAXIMUM, you will want to get into these stocks before November and exit before the end of January, if you are trading as a speculation.

Recommended Tickers

There are three tickers that blatantly shout “WE DO BUSINESS WITH WEED”. Those tickers are: MJNA, CANN, and AMMJ.

Medical Marijuana Inc (MJNA)

http://www.medicalmarijuanainc.com/

Business Model

They are a grower and distributor of medical marijuana in many forms. The Company is CURRENTLY not in the business of selling or dispensing either recreational or medical marijuana, directly or indirectly, but they are poised and for eventual cannabis legalization. They have seven subsidies, that do everything from research their hemp-oils to makes cannabis chewing gum. Overall, not a bad company at all. Business model makes sense, but they won't make it big until marijuana is legalized.

Financials

They are an active company. They sell about 83% of their inventory each quarter and have positive working capital (meaning they have more inventory/cash than they owe this year). They are liquid and can pay all of their yearly debts off if they have to (good sign if you are afraid of bankruptcy).

Big red flag when you look at their debt, they have a +$3 Million interest expense. That's a big amount of cash to shell out each and every year. Especially when their sales were only $1,725,681. Long-term solvency, bad. Short-term liquidity, good. Luckily, we aren't in this for the long-term.

That's really the only thing that surprises me on their financials though. They aren't profitable (because they aren't supposed to be yet). Their stock is going for 51.72 price to sales (meaning for every $1 in sales, investors think they will get $51.72 back in shareholder wealth). A "crazy" multiple for many industries, but not really marijuana.

Sentiment

Three-month price is up 22.89%. For 2016, it is up 37.84%. Both solid positives regarding investor sentiment. They have more than 1.75 BILLION shares outstanding and most of those are tradable, which is good. Their average trading volume is 5.5 million shares. Making them the most liquid marijuana stock we are looking into.

These are all good signs for someone who is trying to exercise this strategy. You want a market that is liquid enough for you to buy in and sell out without moving the stock price.

Summary

MJNA is a risky long-term bet because of their high interest expense, lack of profitability, and negative cash flow from operations (negative $3,923,241.00). However, they can pay their debts for this year. Which is all we care about.

With a name like Medical Marijuana Inc., they will get plenty of action this November.

They had more than double their average volume and HUGE spikes in price the last two times legalization of Marijuana went to vote. Expect this to continue.

My target price would be $0.30 based on past historical price jumps (not financial models). At the current price of $0.05, that is a 6x return. $10,000 turns into $60,000. However, if the price is not there by January 6th, exit. Gains are gains.

General Cannabis Corp (CANN)

http://generalcann.com/

Business Model

They help new and established growers and sellers stream-line their business through their various products. They have a greenhouse consultant, security firm, brand development, and apparel line. The only one that seems unique to me is the greenhouse consultant.

Financials

Currently they have negative working capital, which isn't always what you want to see. However, in a service driven business (instead of a product driven business), it somewhat makes sense. The majority of their assets are their people, not their plants or equipment. The little inventory they do have they sell all of it each quarter with an inventory turnover ratio greater than 100%.

They are neither liquid or solvent. The would not be able to pay for this year's debt and they have almost as much debt as they have assets. None of this is good for the long-term. It isn't pretty for the short-term either. What scares me the most though is that they have $1,354,712 in intangible assets and $187,000 in goodwill. I can somewhat justify the $1.3 Million in intangible assets because of their service model. I hate goodwill and $187k is significant to them.

While their underlying balance sheet and income statement aren't pretty, they have a net loss of $1,336,471.00 and their cash flow from operations is a negative $434,095.00, they are valued pretty nicely. With a price to sales of only 38.42, they are considered low when compared to most other marijuana companies.

Sentiment

Their sentiment is through the roof though, which makes their valuation even prettier.

Over the last three months, CANN is up 50.9%. For 2016, CANN is up 176.9%. If their price to sales was valued the same as MJNA, their stock price would be worth $2.34….it is at $1.74 now. While historically "marijuana stocks" has done better than "cannabis stocks" in terms of search results, this stock is blowing up. Average volume of shares traded is ~50,000. Lately it's been closer to 1 Million. IT'S A HOT STOCK.

Summary

Its financials aren't pretty, but the valuation allows us to see significant upside WITHOUT LEGALIZATION. If legalization does occur, we imagine this could have a 6x to 8x upside.

Another big plus for CANN is that it is a large constituent in the Marijuana Index (http://marijuanaindex.com/stock-quotes/marijuana-index-global-composite/). We imagine this will be the place A LOT of investors turn to in order to get information on Marijuana stocks.

Price target is $10.00 before January. Anything above that is heaven sent gold.

American Cannabis Co Inc (AMMJ)

http://www.americancannabisconsulting.com/

Business Model

AMMJ provides end-to-end consulting and product solutions for the medical, adult use and low-THC regulated cannabis markets both nationally and internationally. They tell people who actually work in the marijuana industry how to start, grow, protect, and sell their product. They sell everything from soil to retail marketing. With some big name clients (like OrganiGram), they seem legitimate.

The business model is fine, but I'm not in love with the people running the business (they just seem like a bunch of ex-ski instructor hippies that were good at growing weed in college and somehow have turned it into a business).

Financials

This company turns over product like your dad flipping burgers on Memorial Day weekend. They turn over 3x their inventory each quarter. They only have around $70,000 in inventory, but turning it over helps that number grow fast. They also have positive working capital, which is the first step to profitability.

They are liquid as well. They are a small company, but they can cover all of their debts for this year and still have some money left. More than 40% of their assets are held in cash. That's not optimal (because cash doesn't make you money), but it makes you feel good about their short-term bankruptcy issues.

The have a positive gross margin…. which is rare in the marijuana industry. However, they still end up with a negative net income of $84,775. However, if they can sell more, they will eventually become profitable. This is a company that will truly go profitable once legalization occurs.

The real kicker though is that their valuation is only 17.88 price to sales. That is the lowest we have seen between these three companies.

Sentiment

Investors don't like them that much. Average volume of 215,000 shares traded out of 46 million total shares isn't super inspiring for a "bubble" play. Their performance has also lagged. They are only up 18.9% over the last three months and 16.74% for 2016. Investors don't seem to like them that much (hence the low valuation).

Summary

Overall, not the best sentiment play with low volume and poor recent performance. However, if an investor checks their financials, they may think this is a good stock. I wouldn't argue with them.

In my mind, you buy this if you think they will turn profitable fast and believe investors will look for profitability over price changes.

I would enter in October and wait until after 2Q results are posted to sell. If they can turn profitable in the 1Q of 2017, that would be huge and their stock would jump. That's a big if though.

Short recap for speculative buyers…

CANN is driven by pure speculative buying….which is exactly what I am looking for in this situation. The hardest part is going to be timing when to sell. My price target is $10 in December. Don't hold past January. It's not a sound company.

AMMJ isn't currently in the hot seat. Performance and volume have been lagging, which isn't what I'm looking for. However, with a name like "American Cannabis Co" and an "A" ticker symbol, it is possible that it will see significant volume after legalization. Its financials are solid, so it may get more investments from more experience and savvy investors. Price target is too hard to guess. Maybe $0.50?

MJNA is a mix of these two. Financials are fine for right now, but look bad in the long-run. Sentiment is good, but nothing amazing. However, it has the best name, "Medical Marijuana inc", and will get plenty of action if marijuana is legalized (because it has in the past election cycles). Possible 6x investment (or more).

Conclusion

Cody:

As you can see, there is much to research. Although cannabis has been used for thousands of years, the ‘formal marijuana industry’ is only now taking shape. There is tremendous uncertainty and opportunity - it’s a matter of finding the right needle in the haystack.

As stated in the beginning, this is the second marijuana stock report that I have released. The first report is only a year old, but completely outdated and so I disposed of it’s contents. This report may well see the same fate as the first report in an even faster time frame.

I will be sure to release a new report when there has been significant movement within the industry. This will probably be sooner, rather than later.

In addition, I will provide updates on any notable movements in the market through the Explorer Report.

We are living in exciting times where the world is changing and advancing at speeds that we struggle to comprehend. Whether it’s healthcare, technology, space travel, or even the marijuana industry, we have the opportunity to get involved now.

Cody

"California will switch soon. Once that happens, I think the floodgates will open and I will be one of the first investors when it gets a federal mandate."

- Kevin O'Leary

"I'm not going into the marijuana business -- I am already in it, as an investor."

- Rose McGowan

"Pot's a big business. People know what the profits are going to be, so I think hitting it fast and early is the number-one prize.

- Barbara Corcoran