

30-Mar-2023

Verano Holdings Corp. (VRNO.CA)

Q4 2022 Earnings Call

CORPORATE PARTICIPANTS

Julianna Florence Paterra

Director-Investor Relations, Verano Holdings Corp.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Aaron Miles

Chief Investment Officer, Verano Holdings Corp.

OTHER PARTICIPANTS

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Aaron Grey

Analyst, Alliance Global Partners

Kenric Tyghe

Analyst, ATB Capital Markets, Inc.

Scott Fortune

Analyst, ROTH Capital Partners LLC

Russell Stanley

Analyst, Beacon Securities Ltd.

Andrew Semple

Analyst, Echelon Capital Markets

Matt Bottomley

Analyst, Canaccord Genuity Corp.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Audra, and I will be your conference operator today. At this time, I would like to welcome everyone to the Verano Holdings Corp. Fourth Quarter 2022 Earnings Conference Call. Today's conference is being recorded. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

At this time, I would like to turn the conference over to Julianna Paterra, Vice President of Investor Relations. Please go ahead.

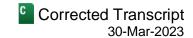
Julianna Florence Paterra

Director-Investor Relations, Verano Holdings Corp.

Thank you, and good morning, everyone. Welcome to Verano's fourth quarter and full-year 2022 earnings conference call. I am joined today by George Archos, Chief Executive Officer and Founder; Brett Summerer, Chief Financial Officer; Darren Weiss, Chief Operating Officer; and Aaron Miles, Chief Investment Officer.

During this call, we will discuss our business outlook and make forward-looking statements within the meaning of applicable US and Canadian securities laws, which are based on management's current assumptions and expectations. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance and achievements of the business or developments in the company's industry to differ materially from those implied by such forward-looking statements. Actual events or results could differ considerably due to risks and uncertainties mentioned in our filings on EDGAR and SEDAR, including our financial statements and MD&A for the quarter and year-ended December 31, 2022.

Q4 2022 Earnings Call



In addition, throughout today's discussion, we will refer to non-GAAP financial measures that do not have any standardized meaning prescribed by GAAP, such as EBITDA, adjusted EBITDA and free cash flow. Management believes non-GAAP results are useful to enhance the understanding of the company's ongoing performance, but these are supplemental to and should not be considered in isolation from or as a substitute for GAAP financial measures. These non-GAAP measures are defined in our earnings press release and available on our website at investors.verano.com, which also includes the reconciliation of these measures to the most comparable GAAP financial measures. Lastly, all currency is in US dollars, unless otherwise noted.

I will now turn the call over to George. Please go ahead.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Good morning and thank you for joining us. I'll begin today's call by highlighting at our strong fourth quarter and full-year 2022 performance, after which, I will give Brett the floor to review the financials in further detail. I will then provide my thoughts in 2023 and speak to the exciting path we see ahead of us here at Verano. I will then close with a discussion regarding our capital allocation plans, including providing guidance around certain financial metrics.

I am extremely pleased with what we were able to accomplish in 2022. Throughout the year, we maintained agility in navigating our industry's evolving environment, managing the business by diversifying our portfolio and improving efficiencies while aiming to protect the bottom line. Our strategy since inception has been to build a self-sustaining business set up to thrive, even under extreme market uncertainty, making no assumptions about changes to federal law. To-date, the net result of these efforts has been the creation of what we feel is one of the strongest cannabis companies in the industry, with the belief that it is positioned to endure difficult macroeconomic conditions while generating cash flow and building long-term value.

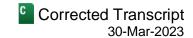
Turning to the results, I am proud to report that in 2022, we generated over \$879 million in revenue, representing 19% growth year-over-year; and \$324 million in adjusted EBITDA, representing a 37% margin. New Jersey and Florida were the largest contributors to our growth in 2022, which Brett will speak to in more detail later.

Looking at the fourth quarter 2022, results were in line with our guidance, with revenue of \$226 million and adjusted EBITDA of \$79 million, representing a 35% margin. Fourth quarter, retail sales were up 1.7%, driven by strength in our New Jersey operations as our final adult use location contributed a full quarter of sales, offsetting softness in Pennsylvania. We also had another quarter of improved vertical sell-through in our retail channels, increasing over 100 basis points sequentially to 47%, demonstrating the strength and breadth of our brand portfolio and SKU mix.

Gross wholesale revenue for the quarter was down 6% sequentially, largely due to increased supply coming to the New Jersey market, which we anticipated, in addition to some price compression in Illinois. Notably, the Verano product line was the number one brand in New Jersey for 2022 based on sales data according to BDSA. So, we are optimistic regarding future wholesale growth once additional dispensaries in the state open.

We have always looked to appropriately supply each market in which we operate. So, in Illinois and Massachusetts, we have scaled back total output and optimized head count, as we've seen some recent oversupply in these states. Please note, we maintain the ability to ramp up production once we see the opportunity to put additional supply on shelves.

Q4 2022 Earnings Call



Throughout 2022 and to-date in 2023, we took decisive actions and made numerous investments to fortify our business, portfolio, organization and value chain. We continued to thoughtfully pace growth by adding 29 dispensaries during the year, a 32% increase in our retail footprint versus 2021, adding 21 in Florida, 2 in Nevada, 2 in Pennsylvania and 4 in West Virginia. Subsequently, we added five dispensaries across Florida and Pennsylvania. Similarly, we continued to increase our cultivation capacity, mainly in New Jersey and on the launch of its adult use program and in Florida to support additional store count.

In October 2022, we also strengthened our balance sheet by refinancing our debt in a rising rate environment, which included significant optionality by allowing us to prepay the first \$100 million with only \$1 million prepayment fee. We expect to be able to decrease our blended cost of capital by leveraging our unencumbered real estate.

In addition, we continued to enhance and expand our portfolio of strong brands. First, by launching Savvy valuetier brand which was quickly embraced by consumers, with the brand representing 15% of Verano flower sales in the fourth quarter on a unit basis. On that note, we are very proud of how our brands have performed, for some even, with only a short time on shelves. According to BDSA, Savvy is now the number one top-selling, large-format flower brand in Maryland after launching in the fall. Savvy holds a top 5 spot in Massachusetts and Pennsylvania and a top 10 spot in Arizona and Illinois. As we expand this product line, we anticipate Savvy's popularity to continue to grow.

We also launched BITS midway through the fourth quarter, which is a lower-dose edible line paired with a range of adaptogens. This is now the top 10 best-selling edible brand in number of our key markets. Lastly, our Verano brand continues to perform well. For BDSA, Verano's ranked as a top five brand nationally. Of note, Verano's brand performance is particularly compelling, given that we only produce in 7 of the 13 states included in this data set.

In addition we continue R&D as we explore new brands and form factors. Specifically, we've seen success with our new line of solventless extracts and have plans for launches in additional select markets over the coming months. Relatedly, we also successfully launched a niche line of specialized, infused pre-rolls at a premium price point in Illinois. We anticipate rolling this out in other markets throughout the year.

In an effort to provide deeper insight into our business, we want to highlight a few efficiency metrics that management utilizes to monitor and evaluate our business. For example, we closely track dollars per labor hour, which helps us determine how efficiently our retail outlets operate. I am pleased to report that this measure increased over 26% quarter-over-quarter. Similarly, we look at transactions per head at retail, which also went up 14% quarter-over-quarter. At our CPG facilities, units produced per head increased 6%, while cost per gram decreased 9%, sequentially. These metrics demonstrate our continued operational improvement. I am very pleased with what we accomplished, even while navigating a complex and challenging inflationary environment.

And now, I will turn it over to Brett to cover the financial results before I provide a more detailed outlook for 2023.

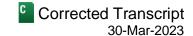
Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Thanks, George. I'm pleased to deliver our solid financial results today. I'll begin by covering full-year results before drilling down into the fourth quarter results. Revenue for the full year increased 19% versus 2021 to \$879 million, driven by the adult use New Jersey sales and increased contribution from Florida as we expanded our footprint.



Q4 2022 Earnings Call



On a gross revenue basis, excluding intersegment eliminations, 72% of sales were derived from the retail business, with the largest contributions from Florida, Illinois and New Jersey. The remaining 28% of sales were derived from the wholesale side of the business, with the largest contributions being from Illinois, New Jersey and Connecticut.

Gross profit for the year was \$423 million or 48% of revenue versus \$331 million or 45% of revenue in prior year. On an adjusted basis, this was \$517 million or 59%, in line with what was previously communicated. SG&A expenses were \$357 million for the year, or 41% of revenue, versus \$271 million in the prior year, or 37% of revenue, due to increased costs associated with the 29 dispensary openings, which can take up to 6 months to fully ramp up. On an adjusted basis, SG&A was \$249 million or 28%.

We continue to optimize head count and expenses in our retail operations to strike a balance between prudent expense management and enabling continued growth. We have seen a decline, over time, from our Q2 peak in this cost as a percent of sales. We had a net loss for the year of \$269 million driven by impairments to an Arizona cultivation license and to Pennsylvania and Arizona goodwill. Notably, impairments were the biggest driver of our deferred tax liability decrease of approximately \$50 million. Adjusted EBITDA for the year was \$324 million or 37% of revenue.

Moving on to the financials for the fourth quarter of 2022. Revenue was \$226 million, up 7% year-over-year, driven by adult use sales in New Jersey and increased retail contribution from Florida store openings. Gross profit for the quarter was \$103 million or 46% of revenue, versus \$109 million or 52% of revenue in the prior year, driven by increased discounting and cost increases associated with expansion activities. On an adjusted basis, this is \$125 million or 55%, driven by the inventory reduction we spoke about on the last earnings call. Ultimately, we reduced inventory days by 17% quarter-over-quarter. And while this was a drag on adjusted EBITDA, it has made us leaner and faster to pivot, as well as freeing up some cash and helping us continue to build a stronger balance sheet.

SG&A expenses were \$81 million for the quarter or 36% of revenue versus \$82 million in the prior year or 39% of revenue, driven by lower stock-based compensation and decreased M&A activities, offsetting increased costs associated with additional stores. On an adjusted basis, this was \$62 million or 27%, in line with the lower target we previously communicated. We had a net loss for the fourth quarter of \$216 million driven primarily by the onetime impairments previously discussed. Adjusted EBITDA was \$79 million or 35% of revenue.

This quarter, Verano filed for a tax rebate known as the Employee Retention Credit. This credit is worth \$11 million net. And we qualified given that we met certain criteria for operations during the COVID cycle. This credit is an offset to payroll tax, which is included in our adjusted EBITDA. So, this credit is also included even though it is onetime in nature. Also, if this credit was excluded, our adjusted EBITDA margin would have remained above 30% for the fourth quarter and above 36% for the full year, even with the inventory drag we previously discussed.

Turning to the balance sheet and cash flows, we ended the year with \$85 million in cash and cash equivalents. Cash flow from operations for the year was \$94 million. George will speak to our cash flow expectations in more detail later.

CapEx spend for the fourth quarter and full year was \$9 million and \$119 million, respectively. Net of PP&E disposals, this was \$9 million and \$113 million, respectively. Spend for the fourth quarter was slightly lower than our guidance of \$20 million, as some projects carried over into the first quarter. We still expect \$25 million to \$50 million in CapEx spending for 2023, spent largely on Florida and Pennsylvania retail expansion, Connecticut JV retail partnerships and minor cultivation projects.

Q4 2022 Earnings Call



In addition to the deferred tax liability decrease discussed, other significant changes on the balance sheet include the reduction of acquisition consideration payable to \$18 million, a decrease of about \$35 million. The remaining balance will be materially paid out this year. We continue to approach 2023 with a cost focus and will continue to opportunistically manage our cost of capital as we evaluate uses for excess cash. Overall, I'm very optimistic about 2023 and look forward to the year ahead.

And now, I'll hand it back to George to wrap up.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Thanks, Brett. As we look ahead to 2023, we are confident that our business will build in the momentum and strength from 2022. We anticipate that our brands will continue to deliver value to patients and consumers across our strategically curated geographic footprint. This includes two states converting to adult use in 2023: Connecticut, which launched in January; and Maryland, which we anticipate to launch in the second half of the year.

So far, we have seen a strong start with the adult use Program in Connecticut, in line with our expectations. In the first four weeks at our Zen Leaf Meriden location versus the same period in the prior year, sales more than doubled, while sales of our in-house brands at Zen Leaf Meriden nearly quadrupled. This speaks for a leading wholesale position of brand power, resulting from the quality of our CT farm operations and products in the state.

We continued to work with the local municipality for other medical store to gain formal approval to convert to adult use. Additionally, we are making progress with our six social equity joint ventures, each of which plans to open a hybrid retail location. We are supporting each venture through the entire retail launch process from zoning to opening day and expect our first joint venture to open its doors to adult use and medical consumers as soon as next month.

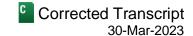
As mentioned, Maryland is another state slated for a 2023 adult use program launch. We are heartened by the progress the state is making as recently as this week in advancing the adult use initiative, getting us closer to adult use sales. Maryland's medical program has presented challenges to vertical operators, including steep pricing reductions. Despite that, we worked to increase Verano's sell-through by 30% to nearly 44% in the fourth quarter, sequentially.

And on the wholesale side, despite a difficult pricing environment, we increased revenue sequentially by nearly 6%. We have held a legacy presence since the early days of Maryland's medical program, and we are well-positioned ahead of the anticipated increased demand. With nearly 40,000 square feet of cultivation and four dispensaries in the state, we look forward to serving adult use consumers soon.

The Pennsylvania, Florida, and Ohio markets provide our portfolio with additional adult use upside, as we are optimistic these states could legalize adult use sales within the next two years. Taking a look more broadly, the industry continues to face challenges from a tax and banking perspective. While we are encouraged by the momentum surrounding a passable safe banking passage, we were disappointed this was not passed in 2022.

However, this has not impacted our business. We have built the business to be self-sustaining and have never run the company relying on contingencies related to federal legalization. However, we will be ready to swiftly capitalize on any federal changes if and when they occur. And the impasse at the federal level has not prevented

Q4 2022 Earnings Call



states from advancing state-level reform, including, for example, New Jersey's recent legislation around 280E and Illinoi's progress on the same issue.

Overall, we expect 2023 to be an inflection point for the industry and believe that it will be particularly difficult for smaller operators, as it struggle to stay afloat in the absence of banking or tax release and continued pricing pressure. However, this is a potential opportunity for Verano to acquire operators in attractive markets at favorable valuations.

Since the founding of the company, we have said, we would be painstakingly strategic about growing our footprint. That is precisely what we have done and what we will continue to do. And now, we believe we are in even stronger position as we evaluate developing opportunities at attractive prices. Though we anticipate an appetite for M&A in 2023, we will also remain disciplined, patient and highly selective.

Looking ahead, the number one priority in 2023 will be to continue to strengthen the balance sheet and focus on generating as much cash flow as possible. We understand that preserving cash is more important now than ever before, given the burdensome tax structure our industry faces and a difficult capital markets environment. We have always sought to employ a thoughtful approach in deploying capital with discipline and balance, and we will continue to do so.

Regarding CapEx, we have sought to appropriately build our footprint to maintain strong market position. While we spent \$119 million in 2022 we made the decision late last year to significantly decrease our spend for 2023 based on internal assumptions of market growth and adult use activations. We are reiterating guidance of \$25 million to \$50 million of CapEx for the year and await further state-level legislative movement that would justify additional spend ahead of growth.

I want to clarify that we will not step back CapEx at the expense of growth. So, if we see opportunity, we will invest ahead of it appropriately. But in the meantime, we are able to fully supply our markets with our current footprint. Given our significantly lower CapEx expectations and then continued focus on efficiencies within the business, we anticipate generating between \$50 million to \$75 million of free cash flow for 2023. In addition, we plan on evaluating the best use of excess cash from the ROI perspective, with an eye towards our cost of capital.

Regarding our expectations for the first quarter of 2023, we anticipate flat top line performance versus the fourth quarter. We also expect continued margin unfavorability from inventory rightsizing. However, as mentioned earlier, our focus is on the cash flow production of the company and we're anticipating generating positive free cash flow and increasing our cash balance sequentially. We look forward to sharing our results on our next earnings call, which is scheduled for May 10, 2023. The official announcement will be distributed subsequent to this call.

With decades of experience building businesses for longevity, downturns are not new to me. And even with market conditions deteriorating in certain states, I believe the strength of our strategy is more apparent than ever. We do not need to exit any unattractive fragmented markets as we have had the wherewithal to avoid them from the start. We have methodically built today's footprint, and we see the opportunity in the horizon to strategically build off this space. I want to thank the incredible Verano team for their efforts last year. We are re-energized, and we are excited.

With that operator, please open up to Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We'll go first to Matt McGinley at Needham.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Thank you. So, my first question is on the gross margin. And the stat, that was about 9-point quarter-over-quarter drop. Was that mostly the aging inventory reduction that you noted and maybe more of a onetime pressure in the fourth quarter or the first quarter; or is that 55% now the new run rate given what you noted with the price decline in New Jersey and Illinois?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Hey. Good morning, Matt. I'll pass it off to Brett.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Hey, Matt. Yeah. So, that decline is driven almost entirely by the inventory reduction that we had kind of messaged on the call last quarter. In terms of what does that mean for the future, we're going to continue to manage our inventory and kind of dial it in to make sure that we're supplying the right level of product to the market.

Over the last few years, we've had our new openings, and we started to understand the markets better. It was more focused on making sure we had the right supply, so we didn't shorthand anyone, but now it's more dialing in. So, you're going to continue to see us manage the inventory level. And there will be some impacts from that. Obviously, we can't talk about what that will be. But you would expect we're going to see some more of that over the course of the year.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Okay. And then, the cash flow from ops, how much of the \$94 million in operating cash flow that you generated this year was an increase in your income taxes paid in balance? And we don't have the full balance sheet yet, but it looks like you did have a step up in inventory in the fourth quarter. Is that the case? And if so, I guess, what drove that if you're reducing that inventory, which is pressure on gross margin?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

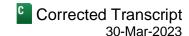
Yeah. So, inventory did step down. You'll see it when the 10-K comes out after this call. In terms of the taxes, it's hard to say specifically because obviously we're accruing at different levels this year than we did last year because our profits are different and our revenue is different as well. So, there is some benefit to that, but of that operating cash flow, about half.

Matthew Robert McGinley

Analyst, Needham & Co. LLC



Q4 2022 Earnings Call



Great. Thank you.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Yes.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

А

Thanks, Matt.

Operator: We'll move next to Aaron Grey at Alliance Global Partners.

Aaron Grey

Analyst, Alliance Global Partners

Hi. Good morning, and thank you for the questions. So, just want to continue on with the gross margin. I certainly understand the inventory step-downs inventory and how that might have an impact. But just talking about in terms of the brand portfolio, can you just remind us in terms of obviously the increase you've had in terms of the value brands with Savvy having its success outside of this inventory rightsizing? And how do you think the brand portfolio evolves in the near term [indiscernible] (00:22:53) you expect Savvy to continue to increase outperformance and impact on margin outside of the inventory impact that you're having? Thank you.

George Archos
Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

A

Hey. Good morning, Aaron. I'll pass off to Brett again on the margins.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Yeah. So, other than the inventory movement, I don't think our margins are all that different than what we would have expected them to be. We've talked in the past about having an adjusted gross margin in that kind of 59% to 61% range. And that's kind of the same place that we feel that we're at when you don't think about the inventory piece.

In terms of the brands and the differentiation there, the fact that we're going to some more value prop, value-oriented branding, that allows us to sell more and allows us to sell – to reach other customers and to help offset as people get more price-conscious. And we're still making it ourselves, valuing it ourselves, so we're getting good margins from that as well. So, even though it is slightly dilutive on the lower side, it's being offset with volume. And I think overall, we're still pretty happy with where our margins are.

Aaron Grey

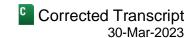
Analyst, Alliance Global Partners



Oh, good. Great. Thank you. And then, you guys did speak to M&A opportunities kind of coming up. Obviously, we talked in the past a disconnect between the public and private markets, a lot has changed in the last couple of months, particularly with states not passing. So, talk about [indiscernible] (00:24:16) those opportunities are actively coming available now, or you think they will be in the next couple of months? What type of markets you might want to be going into, new markets, even expanding deeper into existing markets? Any color in terms of how you're seeing those potential M&A opportunities evolving? Thanks.

Q4 2022 Earnings Call

Analyst, ATB Capital Markets, Inc.



George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

A combination of both. I mean, we want to continue to go deeper in some of the markets that we're in, and we're also looking at expanding in other markets. But we're being, like we said on the call, highly selective. There are opportunities currently that we are evaluating, and we believe there will be much more opportunities between now and the next couple years. By then, it's – there's no rush for us to do anything. We have a fantastic base. We have good organic growth. We have adult use ahead of us, preparing for certain markets. So, we'll continue to evaluate and we'll make that decisions as we see fit.

As far as valuations, when the public valuations come down, so do the private ones. Maybe not as [ph] seeply (00:25:11) as some of the public valuations have, but in order to make a deal, they still have to be highly accretive for Verano in order for us to transact. So, we'll be selective and we anticipate some deals in the in the next 24 months.

Aaron Grey Analyst, Alliance Global Partners	Q
Okay. Great. Thanks very much. I'll jump back in the queue.	
George Archos Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.	A
Thanks, Aaron.	
Operator: We'll go next to Kenric Tyghe at ATB CM.	
Kenric Tyghe	

Thank you, and good morning. George, you spoke to a strong performance in New Jersey. You also highlighted that as increased capacity has come online we've seen some constraints at wholesale. Could you speak to how orderly do you expect the evolution of that market to be, just given some of the capital constraints, given some of the real estate availability and the like? How should we think about that, the evolution this year, as we get into the first full year of New Jersey?

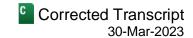
George Archos Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Co-Founder, Chairman & Chief Executive Unicer, Verano Holdings Corp.

Good morning, Kenric. Great question. Obviously, we love New Jersey. Legacy state for us. Adult-use has been fantastic for the company and for other operators there. What I generally see happening is, we think, dispensaries will continue to open throughout the year, albeit slowly because zoning is very difficult to the Northeast, particularly, the New Jersey. But I don't see much cultivation capacity coming online.

And we're not hearing of projects being built out. Obviously, there's not much cash available to the cannabis companies currently, especially new operators. So, we see it as a strong opportunity for us for many years to come. So, we think, although we might see some decline in some of our retail outlets, as the municipalities allow stores closer to us, I think, we'll be in a very strong position to be able to supply the wholesale market. We built a large-scale facility there, high-quality, one of the best facilities that we have in the company. So, we really like what we see in the future for New Jersey.

Q4 2022 Earnings Call



Kenric Tyghe

Analyst, ATB Capital Markets, Inc.

Thanks. So, that's a great color. And if I could, just on the balance sheet, a commentary with respect to preservation of cash and strengthening the balance sheet. Could you sort of speak to that in the context of the deferred tax liability? How are you thinking about your priorities as uses of cash. And also perhaps, just philosophically, how you think about, let's call them, some of the levers in the discussion?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

I'll pass off the Brett, and I'll add any additional comment. Go ahead, Brett.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Sure. So, in terms of the deferred tax liability, I just want to remind, the deferred tax liability is an artifact of the M&A transactions that we do from equity and it's a disconnect between the IRS taxes and the US GAAP tax calculation. So, it's just the time delay in terms of how the taxes come through.

The income tax payable, I think, is what you're referring to in terms of similar to the question that we were asked a few minutes ago. We think about that the same way we have in the past, and we've stuck to that. Twelve to 18 months past the filing date is when we intend to take care of those taxes. And we are fully on that plan right now. We haven't deviated. In terms of what we plan this year, it's very similar. So, the obligations that we incurred in 2021 are going to be paid off here in 2023 and then – Yeah. And you'll see that tax balance kind of maintained at the level that it's at or maybe slightly below.

The deferred taxes liability and our liabilities is a part of the balance sheet. you will see that, that is reduced. It's reduced by about \$50 million. The biggest movement in that is related to the impairment. So when we impair it, we no longer have that gap between the IRS and between US GAAP taxes and it will be reduced on the balance sheet. But there's no actual cash tax impact on that.

Kenric Tyghe

Analyst, ATB Capital Markets, Inc.

Thanks, Brett. Appreciate that. I'll get back in queue.

Operator: We'll take our next question from Scott Fortune at ROTH MKM.

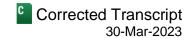
Scott Fortune

Analyst, ROTH Capital Partners LLC

Yeah, good morning. Thanks for the questions. Obviously, a challenging environment out there with margins in mind here. You've been able to hold SG&A flat and becoming more and more efficient from that standpoint. Are there additional cost savings or opportunities that can move levers to drive margins there? Just a little color on – just specifics of return, kind of speak to your margin levels that you want.

And then, follow-on to that, are you seeing the pricing stabilization with the tight capital markets, and obviously, the cut back in CapEx; or are we seeing some pricing stipulation in key states and need to call that out, with respect to kind of March and March easing, picks up in seasonality? Kind of, your sense there.

Q4 2022 Earnings Call



George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Good morning. All good questions. We have seen some price stabilization. I think Q4 was kind of a dip, and we're starting to see things stabilize here in Q1 and moving forward, and we feel pretty comfortable with that. Seasonality, it's a thing, so we're coming out of that. March usually starts to pick up here, so a lot of the markets in the Northeast, the closed markets, we're starting to see the pick-up, and we're excited about it. Overall, I can pass off to Brett in anything else, but that's kind of how we see things here.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Sure. On margin, I'll address in two different aspects, because it's not just the SG&A, but the GM as well. And I know that hasn't been a question here so far, and I want to make sure that, that's – we drive that point home. But in terms of the SG&A, on an adjusted basis, we're in about 27% in Q4, but that's actually stepped down. So, it's not going to maintain, we're actually continuing to step down.

How's that going to look next year? I think we have cost control in that space. If you think about what generally drives increased SG&A in our business, it's more stores. We are adding a few more stores, but we're adding revenue at the same time. From a margin perspective, I wouldn't expect significant swings, unless we announce some investments or that sort of thing.

And then, on the gross margin, again, we've communicated in the past here, between 59% and 61% on an adjusted basis. And other than inventory here in Q4, and then also favorable impact of inventory in Q3, that continues to remain at that level. So, if you think about it, just natural level of gross margin on adjusted basis is right around that 59% to 61% sort of percentage.

Scott Fortune

Analyst, ROTH Capital Partners LLC

Appreciate the color. Thanks. And then, real quick, one last one for me. Can you provide a little more overall growth from a transaction volume standpoint versus pricing? And then, kind of the opportunity from a wholesale standpoint, obviously, New Jersey went with more stores coming on board and held them on cash. Are there drivers on the wholesale growth side in 2023?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

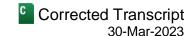
The drivers in the wholesale side will continue in Illinois and New Jersey as stores open, where we have to supply Illinois. Unfortunately, we believe, there's some more to supply in the state. So, to manage that, we will continue to slowly ramp down the facility and keep enough inventory in place to be able to fully supply what happened, because these stores are opening slowly than anticipated. Brett, you can comment the rest. And that's good thing with New Jersey, as we mentioned earlier.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Yeah. I would just say, we don't give out necessarily our gross revenue growth quarter-over-quarter because discounts are very real in this industry and the gross pricing isn't necessarily something that we talk too much about. But what we can tell you that, yes, we are transacting higher volumes, we are transacting higher gross revenues. So, we are seeing an increase period-over-period-over-period.

Q4 2022 Earnings Call



Scott Fortune

Analyst, ROTH Capital Partners LLC

Appreciate that. I'll jump back in the queue.

Operator: We'll go next to Russell Stanley at Beacon Securities.

Russell Stanley

Analyst, Beacon Securities Ltd.

Good morning, and thank you for taking my question. Just wanted to follow up, George, on your comments around Illinois and stores opening I think a little slower than expected. I guess, what's your latest view on how many new doors you might see in that market? I think in November, you were thinking we might see a-third of 192 licenses get opened. Just wondering what your latest thinking is ,given we're almost a quarter of the way through the year.

Aaron Miles

Chief Investment Officer, Verano Holdings Corp.

Hey, Russ. This is Aaron. Could you repeat that? Our phone...

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Oh, Russ, my phone cut out. I got you. I was speaking to myself there. So, store openings in Illinois. I think we see about 35 to 45 stores this year with some pretty slow start. Again, zoning is very difficult in all these municipalities, but we are helping a handful of groups that are opening their stores. And I think there's a couple other groups that are helping as well. So, I think that store counts probably pretty right on point for the year. I think 35 to 45 stores from what we're seeing and who we're talking to, that's kind of what happens for the year in Illinois.

Russell Stanley

Analyst, Beacon Securities Ltd.

Got it. Thanks for that. And maybe if I could, on the CapEx guidance. You came in under what you were expecting in Q4 and you've reiterated the range for 2023. I guess, in real terms, it looks like maybe you're actually reducing CapEx in that sense, given some spillover from Q4 into 2023. So, just wondering what you may have pushed out or eliminated from your 2023 plan there.

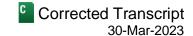
George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

So, I mean, at the end of 2020 we made our plans and nothing has changed. We feel very confident with what we're about to open, and we're just looking at optionality in the future in PA, Florida, Ohio and some of those adult use markets, so we're ready to jump. PA facility, we have a second facility built. It's ready to turn on pretty quickly with some additional construction. Florida, the second facility's built, we'll continue site work and adding space as we see fit. And in Ohio, we just added the capacity there, so we're watching adult use markets. So, we feel very confident with what we said.

As far as, your push comment, we didn't really push. We left the range at \$25 million to \$50 million. Some of it spilled over into Q1. So, we still feel pretty confident in that range. And we'll adjust throughout the year, if we see any opportunities that come up.

Q4 2022 Earnings Call



Russell Stanley

Analyst, Beacon Securities Ltd.

Great. Thanks for the color. I'll get back in the queue.

Operator: We'll move to our next question from Andrew Semple at Echelon Capital Markets.

Andrew Semple

Analyst, Echelon Capital Markets

Hi, there. Good morning, and thanks for taking my question. Just want to go back to the comment made earlier about using maybe the real estate that you own to lower your average cost of capital. Just wondering how you would potentially use those proceeds from a possible debt financing. Would you use those to pick away at tuck-in M&A opportunities, or would your first priority be to reduce some of the existing debt outstanding? I know you're able to pay back \$100 million of that with de minimis penalties. So, how are you thinking about potential uses of the proceeds, if you were to lower your cost of debt capital?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Depending on what M&A opportunities arise, it could be a combination of both. If we don't have any real M&A opportunities that need cash, then most likely we'll be paying those out regarding debt. I mean, that was obviously why we structured the deal that way. Our goal is to knock on that debt and it's something we want to do. That being said, if the cost of – if our capital is very well spent in M&A deals, then we'll do that. But right now, that opportunity is continue to build the balance sheet and knock down the debt to put us in a strong position.

Andrew Semple

Analyst, Echelon Capital Markets

And in terms of the M&A opportunities you're seeing across the US landscape, are you focusing more on, potentially, markets that are mature with some operators that may be struggling or may not be growing as fast as they might otherwise be without stronger balance sheets; or are you looking to lay groundwork in new and emerging markets as they unfold?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

It's both. It's whatever we think is a great opportunity. If it's a state with limited licenses that's new or we get an opportunity to be first to market, then obviously we would definitely look at that. It's something we're good at. If it's a mature operator in a mature market, where we feel we can add brands, optimization, automation, et cetera, and make it a better deal for us, then we'll also do that as well. I mean, we've done them both and we'll continue to look at every opportunity comes across our desk, and we'll transact if and when it makes sense for Verano.

Andrew Semple

Analyst, Echelon Capital Markets

Great. That's helpful. And congrats on Q4 results, and I'll get back into queue. Thank you.

George Archos

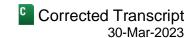
Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Thank you. Have a great day.

А



Q4 2022 Earnings Call



Operator: Next, we'll move to Matt Bottomley at Canaccord Genuity.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Q

Yeah. Good morning, everyone. Just wanted to go back to some of your commentary around one of the questions in New Jersey. And just if you could provide any more insights on where you currently are in terms of your own internal capacity to service that market? Do you have more CapEx dollars allocated there? We've had some of your peers kind of mentioned they're kind of capped out right now with respect to their ability to increase overall production. So, just wondering kind of where you are in that landscape in your own facility.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.



Hey. Good morning, Matt. So our facility is fully built out, no real additional CapEx, other than some maintenance CapEx and maybe some additional equipment here and there as things change in the automation side. We do have additional capacity to add to the wholesale market. We'll have some rooms that are available to turn on some different tiers, et cetera. So, as the a store count ramps up in the state, we can continue throughout that process. But the store openings are going to be slow. So right now, we're focused on the current wholesale market [indiscernible] (00:38:59) as well as our stores, and we're in good shape.

Matt Bottomley

Analyst, Canaccord Genuity Corp.



Got it. And then just one other for me just in – and this may be a Florida-related question, but you had mentioned in some of the prepared remarks about promotional activities and discounting. Is that more specifically related to what's happening in Florida? I get a lot of inbounds on the dynamic there, given that we're still seeing a pretty wide dispersion between the overall growth and volume versus some of the sample data, everyone looks at, whether it's BDSA. So, I'm just wondering what your experience is in Florida or if that commentary was more broadly related to markets in general?

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.



It's more broadly related. I mean, it's just kind of something that happens everywhere as markets mature, different discounts are put in place, et cetera. So, it's something that we evaluate by market. Florida is also one of them. Some pretty highly promotional activity in Q4 towards the holidays. We've seen that balance out now, but that's an ebb and flow. We watch every single market, and we pivot when it makes sense.

Matt Bottomley

Analyst, Canaccord Genuity Corp.



And is there anything specific in Florida that's notable with respect to the dynamic, just given that it seems to be, over the last two or three quarters, a trend that a lot of MSOs have talked about on these calls with respect to the need to discount in-store?

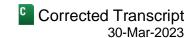
George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.



It just depends what's going on the market. Even within Florida, it's not like the entire state's discounting. It's by region, different stores. You have people that open new stores. They do have the discounting. You get in new

Q4 2022 Earnings Call



customers. So, it's just – again, it's an ebb and flow. Right now, we feel like it's kind of balanced out a little bit. It hasn't been as aggressive as it was in Q4. And we'll continue to watch throughout the year what happens.

I think the last couple years, a lot of supply came online in Florida. I think that's going to balance out as well, with cash being a priority for MSOs and other operators to continue to building their balance sheet. I'm not sure how much is going to be deployed in Florida in cultivation until this adult use news comes out, so we'll see how it balances off of the year.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Got it. Okay, thanks. Appreciate all that.

Operator: And there are no further questions at this time. I would like to turn the call back over to George for closing remarks.

George Archos

Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.

Thank you, everyone, for joining us today, and we'll see you in the next call.

Operator: And that does conclude today's conference. Thank you for your participation. You may now disconnect.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet Calistreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2023 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.