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Verano Holdings Corp. (VRNO.CA)

Q1 2022 Earnings Call

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George Archos

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Camilo Lyon

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and thank you for standing by. Welcome to the Verano Holdings Corporation First Quarter 2022 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised, today's conference is being recorded. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Julianna Paterra. Please go ahead.

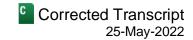
Julianna Paterra

Director-Investor Relations, Verano Holdings Corp.

Thank you and good morning, everyone. Welcome to Verano's first quarter 2022 earnings conference call. I'm joined today by George Archos, Chief Executive Officer and Founder; Brett Summerer, Chief Financial 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 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.

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Actual events or results could differ considerably due to risks and uncertainties mentioned in our filings on EDGAR, including our financial statements and MD&A for the quarter-ended March 31, 2022. In addition, throughout today's discussion, Verano will refer to non-GAAP 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 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 issued earlier today and available 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'll now turn the call over to George. Please go ahead.

George Archos

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

Thank you, Julianna, and thank you, everyone, for joining us today. This was another important quarter for Verano as we continue to work diligently to position the company ahead of anticipated growth. I am proud of the team as we were able to deliver first quarter adjusted EBITDA margins of 40% despite some industry-wide pressures. Today, I'll provide some updates on the business before passing off to Aaron Miles, our Chief Investment Officer, to discuss some capital markets update, which will be followed by a detailed overview of our financials from Brett Summerer, our Chief Financial Officer.

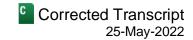
I'd like to kick things off with an update on the progress we are making in New Jersey. We are off to an extremely strong start in the state with performance exceeding our early expectations. This is highlighted by foot traffic during the first week of adult-use sales up more than 13 times versus the prior week of medical-only sales. We anticipate continued momentum in the coming months as New Jersey's adult-use program continues to develop and with the anticipated approval of adult-use sales at our existing Neptune dispensary.

Zen Leaf Neptune is only two miles from the Jersey Shore, and other popular landmarks such as the Asbury Park Boardwalk. With the coming summer season, we anticipate this will be our strongest location in the state. We also continue to have ample supply to meet demand in New Jersey and are currently wholesaling select products throughout the state. We expect an increased contribution from wholesaling towards the end of the year. We will provide more visibility into the New Jersey market once our third location opens to recreational consumers and the market is further developed.

Now, on to some financial highlights. As we guided to on our last call, the quarter came in at a mid-single-digit decline at \$202 million in revenue. This was driven by seasonality effects with lighter sales in January and February, while we saw a pickup in March that we think will carry through 2Q. The first quarter also grappled with a sweeping Omicron variant in addition to the industry-wide vape recall in Pennsylvania, which halted our vape sales for six weeks. And of course, inflation was a headwind during Q1 as we fought for wallet share alongside other industries. Strikingly, cannabis is perhaps one of the few industries, if not the only industry, to experience pricing pressures alongside inflation. We do not believe this is a time to substantially lower prices, and we'll be avoiding deflationary actions to the best of our abilities.

What I want to focus on today is our extremely strong positioning in markets that we foresee legalizing recreational use in the near future. These are areas in which we have prioritized our CapEx spend so that we are best prepared to meet increased demand. As discussed, New Jersey is already performing well, and we are strongly positioned on wholesale side with ample supply to meet demand. We've ramped up operations to full

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swing once adult-use sales were given the green light and we expect to expand our wholesale efforts in the state throughout the year.

With expectations of our Neptune locations to be our top performing location given its adjacency to the Jersey Shore, we anticipate this opening alongside increased wholesaling in the second half to drive significant growth for the company. We also expect Connecticut to begin the adult-use sales towards the end of this year. In preparation, we are in the process of an internal cultivation expansion. We already hold very strong market share positioning in the state, thanks to the members of the CTPharma team, which have proven themselves excellent operators and partners. We expect to build off a strong foundation once we welcome adult-use customers.

Additionally, Pennsylvania is poised for legalization. We are seeing promising progress in the state and believe an adult-use framework could be put forth in the near-term. We are investing in cultivation ahead of any legalization with the first phase of our second cultivation site planned at 75,000 square feet of cultivation and manufacturing space, which would put us at a total of over 135,000 square feet of production. Our Verano strains are now growing in the [indiscernible] (00:06:00) and we expect to begin wholesaling our namesake brand in the third quarter.

We are also hearing positive things out of Maryland and now believe we could see an adult-use program as soon as next year. We don't talk about Maryland often enough, but it is a strong and steady state within our portfolio. Our market share has been increasing year-to-date, so news of an adult-use program in the state come at a good time.

In our pending acquisition of Goodness Growth, our partners there are in the process of expanding their New York and Minnesota facilities. In New York, they are building out the interior of a 320,000 square foot indoor facility, which we built out to Verano level specs and quality. And in Minnesota, their team is building out a new indoor facility which we built out in phases alongside market growth. We also continue to build out our second Florida facility. Phase 1 of this expansion is complete at 40,000 square feet. We have plans in the ground. And at first harvest, we will be prepared to service new locations brought on-line to support our medical patients. We believe Florida has the potential to pass adult-use legislation in the next few years, so we will build the facility out in phases as we gain visibility into program structure.

Lastly in Illinois, as you may recall, we took proactive measures to enhance capabilities ahead of the additional 185 dispensaries that will ultimately come on-line. We are reaping the benefits of efforts we've made in our flower market share increase throughout Q1. Positioning is of the utmost importance for us, so we are prioritizing CapEx for our dollar spent. We see tremendous value in reinvesting into the business. And this is a critical time as we prepare for these aforementioned growth markets and position ourselves ahead of anticipated increased demand.

Now, I'll turn it over to Aaron, our Chief Investment Officer, who will speak to the actions we are taking to benefit our capital market positioning.

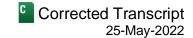
Aaron Miles

Chief Investment Officer, Verano Holdings Corp.

Thanks, George. I'd like to take a few moments to touch on our capital markets initiatives, especially given the persistent pressure across the industry. Unfortunately, given the extreme limitations for many institutions to enter the space, we feel that we do not yet trade on fundamentals and instead generally trade [ph] on volatile with health sentiment (00:08:07) surrounding federal legislation.



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There are, however, actions we are taking to position Verano to be any place to take advantage of US capital market opportunities as they develop. This includes taking steps to be prepared for a potential uplifting through US exchange. We remain actively engaged with both of the major exchanges in the US and given their prior experience at the NYSE, unable to leverage relationships from both to continue the dialogue.

We're also having proactive discussions with blue chip asset managers, and while many may not be able to invest just yet, we are taking time to educate these groups on the US cannabis industry and Verano. While there are no guarantee, we will continue to devote as much time and effort necessary to ensure that these participants will be fully educated on the Verano story as soon as the federal regulatory landscape permits potential investment.

Safe banking is also critical to this discussion. Verano recently joined ATACH or the American Trade Association of Cannabis and Hemp to help advance efforts to get a form of legislation passed. Verano joined with the goal of leveraging key experiences and relationships in the capital markets including [indiscernible] (00:09:18) for the advancement of our industry.

Lastly, as George touched on earlier, we have a multitude of high ROI CapEx projects in the pipeline. While we have discussed the option of share buybacks internally, we believe there is still enormous value in investing into the Verano footprint. Once these numerous CapEx projects near completion, nothing is off the table. We want to drive value and returns for our investors and are always evaluating ways to do so, which ranges from further areas of investment, including M&A and CapEx to share buybacks.

I want to end by acknowledging that we are not naive to the levels that what we're trading at, but we can't run the business based on non-fundamental dislocations in the equity market. We're building the company for long-term growth and success, while building relationships now that will benefit us in the future.

And now, I'll turn it over to Brett.

Brett Summerer

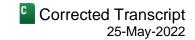
Chief Financial Officer, Verano Holdings Corp.

Thanks, Aaron. Today I'll review the financial highlights from the first quarter of 2022. As a reminder, all financials are now reported in US GAAP. First quarter 2022 revenue was \$202 million, up 67% compared to the first quarter of 2021, and down 4% sequentially. As George mentioned, we experienced softness due to seasonality in January and February. Across our footprint, Illinois and Pennsylvania were the largest drivers versus the prior quarter.

Gross profit for the first quarter of 2022 was \$100 million or 49% of revenue, compared to \$54 million or 45% of revenue for the same period last year. SG&A expenses inclusive of depreciation and amortization were \$80 million for the 2022 first quarter or 40% of revenue. However, we typically exclude depreciation and amortization and earn-outs, which would be 27% versus 25% on the same basis during the prior quarter. Sequentially, SG&A expenses increased 2%, primarily due to costs associated with our conversion from IFRS to US GAAP and M&A deal costs. We had a net loss for the quarter of \$7 million versus a loss of \$2 million in Q1 of 2021. Adjusted EBITDA was \$80 million or 40% of revenue for the first quarter and \$60 million or 50% of revenue in the same period of last year.

Turning to the balance sheet and cash flows, we ended the quarter with \$140 million of cash and cash equivalents. Cash flow from operations for the first quarter was \$53 million and free cash flow was \$6 million. CapEx spent for the quarter is \$47 million, on track for the full year of \$185 million to \$250 million we projected earlier this year. As both George and Aaron discussed, we have no shortage of attractive projects. The main

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areas for current investment are Pennsylvania, Illinois, Connecticut, and Florida cultivation expansion projects. Though we have numerous CapEx projects slated for the year, we also expect to remain selectively acquisitive as we look to round out our portfolio in attractive markets. Ultimately, I am extremely confident that our strong financial standing will continue to allow for further reinvestment into the company and support future growth. When thinking about our debt capacity, it's worth noting that we are underlevered versus our peers on a debt-to-EBITDA basis. If we were to be in line with our peer set, our debt could be substantially higher than it is today.

With that, I'll pass it back to George for some closing remarks.

George Archos

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

Thank you, Brett. To close, this was another foundational quarter for Verano. And as I discussed, we have many reasons to be extremely excited about what the remainder of 2022 will bring. Looking ahead, we are expecting a slow progress of margins throughout the year, likely with some volatility, but still expect for the full year to end with 40-plus-percent margins. We expect solid growth in the second quarter, and we anticipate giving more formal guidance by the second quarter call once we get more clarity into New Jersey and other moving pieces.

Operator, please open it up for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] We have our first question comes from the line of Camilo Lyon from BTIG. Your line is open.

Camilo Lyon

Analyst, BTIG LLC

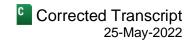
Thank you. Good morning, everyone. I wonder just on New Jersey, George and Brett, clearly, this has been a market that has been a drag on EBITDA margins for you given the delay in adult-use sales. You've got two stores open now. You're talking about the third coming online in the summer. And obviously, you've had a really strong early start to sales and the success you're seeing in the market has been very, very noticeable. So, the question is, could you help us understand how we should think about this market becoming EBITDA accretive given the drag that it's been thus far pre-adult-use sales? How do we think about when this market can actually be an accretive market to the overall enterprise?

George Archos

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

Good morning, Camilo. George here. So, the markets – I mean, it was accretive for us before. Obviously, it's more accretive now. There's quite a bit of vertical integration within our two stores. And with the third, that will be great for us. We're also starting to wholesale. So, we're seeing the benefit of a 120,000-foot facility finally coming to full use, right? It's full of plants now and we expect the market to continue to expand. So, I think you're seeing a little bit of a margin pickup in Q2. We're getting call it half the quarter and that will continue into Q3 when that – hopefully that third store will be open by then and probably get stronger throughout the end of the year as we continue wholesale pickup. So, I think it will be a gradual increase from Q2 on.

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Camilo Lyon

Analyst, BTIG LLC

Great. It's perfect. And then shifting to Illinois, you talked about progressive market share gains after the reset in that market. Maybe if you could just shed some more color on that? And are you beginning the second quarter — did you begin the second quarter from the perspective of really operating at full capacity and full speed? And then if you could just give any sort of insights, George, there's been some news over the last day or two that the — under the legislation and judge overseeing the social equity litigation could actually remove the roadblocks and issue those licenses as early as later this week. Any insights into that would be very interesting.

George Archos

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

So, on the licenses, we're hearing that that could happen, very viable and, obviously, that's what we're hoping for. But market share pickup will be significantly easier with 185 new stores opening versus trying to get all that back within the current environment. It's not easy to just take that shelf space back after it's gone. I mean, that's just the reality of it. So, yes, we are going to pick-up some market share, [indiscernible] (00:16:12) very slow move up with the current environment. If these new 185 stores get released this week or within the next few weeks and they start opening at the end of the year, great for us. Right opportunity to get new market share and new markets that'll have new stores and that's really what we're anticipating. It's not a matter of if, it's just a matter of when. And it sounds like everything we're hearing that this is going to happen in pretty short order. So, fingers crossed.

Camilo Lyon

Analyst, BTIG LLC

And then just as you stand with the reset that you did on your cultivation, irrespective of the licenses just where you are with, kind of, the resetting of your existing facilities and the product that's coming out of those facilities?

George Archos

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

Yeah. We saw some favorable pickup on the gross margin side. But again, that's going to – the facility is back to where it used to be, legacy product, everything is fantastic from that front. But again, gaining that market share back is going to be a slow write up. You know, I don't want to say that it's a flip of a light switch. There's a lot of work to be done to get that market share back and it's obviously, significantly easier. We have 185 new shelves versus trying to get it from the current one time, right? I mean that's just – that's the way we look at it. But we're ready for it, the product is there, which for us is the most important piece. Customer feedback is phenomenal and everyone is excited for the reset. So, that's – that was step one. And now step two is slowly getting the market share back.

Camilo Lyon

Analyst, BTIG LLC

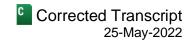
Great. And if I can just throw one more in there. We talked last quarter about a value brand rollout. Any sort of thoughts you can share on the timing of that rollout and what markets might see that first?

George Archos

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

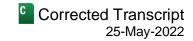
Yeah.

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Camilo Lyon Analyst, BTIG LLC	Q
And if you're actually seeing consumer demand for a lower-priced product?	
George Archos Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp.	A
We do. I mean, the lower-priced product demand has always been there. It's just something that we hat played in. So, we anticipate rolling it out in Illinois first over the next few months, that'll be the first priori we have enough supply to be able to do it. And then, slowly we'll roll it out into other markets where it is sense. But for right now, Illinois is the first target for the value brand.	ty where
Camilo Lyon Analyst, BTIG LLC	Q
Great. I'll turn it over. Thanks a lot, George.	
George Archos Co-Founder, Chairman & Chief Executive Officer, Verano Holdings Corp. Theories Cossilla Llave a great day.	A
Thanks, Camilo. Have a great day.	
Camilo Lyon Analyst, BTIG LLC	Q
Yeah.	
Operator: Our next question comes from the line of Matt McGinley from Needham. Your line is open.	
Matthew Robert McGinley Analyst, Needham & Co. LLC	Q
Great. Thank you. On the liquidity outlook, Verano had about \$149 million in cash exiting the quarter. A much in cash outflow do you expect to have in the second quarter related to the deferred consideration and cash tax payments?	
Brett Summerer Chief Financial Officer, Verano Holdings Corp.	A
Well, I would say that we manage that depending on other demands that we have from a capital perspectange expansion, M&A, all that stuff. So, it always moves around that. But you should expect Q2 to be a little than Q1 in that regard. Most of our payouts were weighted towards the first half of the year and within towards Q1. So, it'll be probably in \$30 million, \$40 million range, but less than Q1.	bit lower
Matthew Robert McGinley Analyst, Needham & Co. LLC	Q
And that's for deferred consideration CapEx and cash tax payments altogether or that's just cash back	things?
Brett Summerer Chief Financial Officer Vergne Holdings Com	А
Chief Financial Officer, Verano Holdings Corp. That's just deferred payments.	<i>"</i>

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Matthew Robert McGinley

Analyst, Needham & Co. LLC

Okay. Okay. And on the adjusted EBITDA, the way you bucket all the add-backs in EBITDA doesn't really give us a good sense of what's actually in that number. I think you added back about \$10 million or so related to M&A you're announcing. There's probably another, I think \$4 million or so related to inventory step-ups. But can you help us understand what's actually in that \$17 million bucket in your adjusted EBITDA?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Yeah. So, it's – the \$17 million specifically is the gain that we had on the equity for one of the transactions that we did. We didn't feel that was an appropriate number to include in our results, so we excluded it. The rest of the stuff is kind of to the point that you already made, right? It's this – it's the earnouts. It's the inventory step-up and it's the amount of money that we had for the flip to US GAAP from IFRS and also really it's the M&A deals like the fees that we paid to lawyers and that sort of thing.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Okay. Thank you.

Operator: Our next question comes from the line of Scott Fortune from ROTH Capital Partners. Your line is open.

Scott Fortune

Analyst, ROTH Capital Partners LLC

Good morning, and thanks for the question. Just came back on New Jersey real quick, you know, you had a real tough time rolling out new product sets [indiscernible] (00:20:34) after the approval was started. Where are you as far as offering full product set and/or are you still limited on the product availability for New Jersey [ph] kind of (00:20:44) little color on that?

George Archos

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

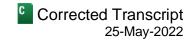
Hey. Good morning, Russ (sic) [Scott] (00:20:47). So, we have been [indiscernible] (00:20:48). We added mints, we added tinctures, botanicals. We have new flower strains. So, every week we're adding new things. So, the menu is becoming pretty full, and we're excited about that. We're actually just going through inventory right before this call and we continue to add supply at the cultivation facility which will not only add more supply into our stores, but will give us the ability to wholesale more throughout the state. So, you know, the state approved quite a few things the week of the launch, so it just takes time to ramp up, and add all the concentrates, et cetera. But those are all coming out and very exciting for the market, right, and having variety for the consumers there is key to basket size and sell through of all the products at the facility.

Scott Fortune

Analyst, ROTH Capital Partners LLC

Okay. And then one follow up for me. Kind of looking at the key markets where we see price inflation and promotions due to competition there. Can you provide a little color in the second quarter here, how are you seeing pricing? Is there some sort of stabilization? And kind of what you're seeing from a traffic versus average basket size in the States of Florida, Pennsylvania? We know Massachusetts is [indiscernible] (00:21:55). Those key

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states [indiscernible] (00:21:57) shape up the consumer and kind of the trend you're seeing in second quarter here would be great.

George Archos

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

Yeah. Great question and we've answered this all the time. So, for us, our pricing is pretty stabilized in the premiere side of the market. The only difference for us is we've introduced that mid-tier line and we're looking forward to introducing a value red line. So, that stabilization for Verano is there. We're just attacking different peers in the pricing category. As far as basket size, we've seen about 2% decline overall throughout the country and that is what it is, right? If you look at the macro environment and what's going on, it makes sense. So, adding these different price points now for us is an opportunity. I'm looking forward to seeing the results.

Scott Fortune

Analyst, ROTH Capital Partners LLC

Appreciate the color. I'll jump back in the queue. Thanks.

Operator: Our next question comes from the line of Russell Stanley from Beacon Securities. Your line is open.

Russell Stanley

Analyst, Beacon Securities Ltd.

Good morning and thank you for taking my question. First around Florida. George, you indicate some optimism around adult-use there. Just wondering what kind of path you expect that to take. I assume you mean something voter-driven or do you have hopes on – you see some sort of legislative action there.

George Archos

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

[ph] That was values on which state (00:23:16). I didn't catch that.

Russell Stanley

Analyst, Beacon Securities Ltd.

That was Florida.

George Archos

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

Florida, I think that's going to be more of a 2024 voter referendum issue. I mean, it would make sense for it to be approved via legislation. I just don't know if that's going to happen, right? I don't know we're going to make that push. I don't think they want all those voters go into the polls, and you see there's more Democratic voters and it's a Republican state for the most part. But we'll see if we can push that across the finish line next year. But we're more anticipating at 2024 vote. So, that's what we're looking at for Florida.

Russell Stanley

Analyst, Beacon Securities Ltd.

And staying on Florida, I guess the City of Miami is now expected to finally – or has been kind of cracked open, I guess, for dispensaries. Just wondering how much of an opportunity that is from a retail build-out perspective and what you might be doing on that front?

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Aaron Miles Chief Investment Officer, Verano Holdings Corp. So, I mean, we do have some stores we're looking at in that area. We're adding some to the portfolio. Historically, it's not a great medical market in the Miami area. I think it's more of an adult-use opportunity. So, as we get closer to 2024, we'll look at different sites and locations there and make sure that we have enough access for the consumers, but it's not something that we've been focusing on [indiscernible] (00:24:27). Russell Stanley Analyst, Beacon Securities Ltd. Okay. And just one more, if I could. Just on the cash from operations, \$53 million. Another strong quarter there. Just wondering if you can break down, I guess, how much the working capital you simply have made or benefited from in the quarter? **Brett Summerer** Chief Financial Officer, Verano Holdings Corp. No. Actually, our working capital is up as we increased our inventories relative to building out [ph] for Fort Wayne (00:24:50). So, it was actually a drag from a working capital perspective. Russell Stanley Analyst, Beacon Securities Ltd. How much - that's great. How much of a drag was it? **Brett Summerer** Chief Financial Officer, Verano Holdings Corp. Sorry? Russell Stanley Analyst, Beacon Securities Ltd. How much of a drag was it? Brett Summerer Chief Financial Officer, Verano Holdings Corp. Mid-double digits. Not mid-double digit, mid-teens. **Russell Stanley** Analyst, Beacon Securities Ltd. Okay. That's great. Thank you very much. I'll get back in the queue. **Brett Summerer** Chief Financial Officer, Verano Holdings Corp. Thank you.

Operator: Our next question comes from the line of Andrew Semple from Echelon Capital Markets. Your line is

open.

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Andrew Semple

Analyst, Echelon Wealth Partners, Inc.

Hi there. Good morning and congrats on the first quarter results. First question here is just on New Jersey, just want to get your sense on when you would anticipate seeing new first stores opening that aren't affiliated with the existing alternative treatment centers in the states. I'm not going to pin you down there on an exact timeline, but what I'm trying to get at is to get a sense of when the wholesale opportunity from the state might expand with new stores opening?

George Archos

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

Hey, good morning, Andrew. Good question, I think, if they hold on to the real estate because [indiscernible] (00:25:58) stores opening probably around eight months from now, and then continue throughout the next 18 months. That's probably the earliest, this timeframe. If they didn't hold on to their stores, it's difficult. New Jersey is, you know, not easy to find a location and go through zone and get open. So, it could take longer. But I would anticipate a few of those licenses, they hold on to the locations. So, I think by, you know, Q1 next year you'll see some start popping open.

Andrew Semple

Analyst, Echelon Wealth Partners, Inc.

Great. And my next question, I just want to go back to the gross margins which improved quarter-over-quarter. I mean just really want to home in on what were the big drivers behind that? It sounds like Illinois and the improved cultivation facility there was a step in the right direction. You know, besides that and across other markets, did you allocate more product internally or did you fair better in the face of some of the pricing competition that we've seen many of your peers discuss? What really drove that margin improvement?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Sure. So, margins were largely flat, but they were up slightly on an operational basis, which is to say excluding our depreciation, our step up. And with the two drivers behind that are the Illinois improvements that we talked about. And also in the market, we've been able to dial back discounts relative to, you know, some – where they had been, you know, historically. So, I think both of those things helped us get a lift on that, on our gross margin this quarter.

Andrew Semple

Analyst, Echelon Wealth Partners, Inc.

Great. Thanks for taking my questions.

George Archos

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

Thank you.

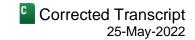
Operator: Our next question comes from the line of Matt Bottomley from Canaccord Genuity. Your line is open.

Matt Bottomley

Analyst, Canaccord Genuity Corp.



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Yeah. Good morning, everyone. Just wanted to go back to the cash flow profile. So, one of those limited number of MSOs that has free cash flow from operations. But just looking at that \$6 million contribution this quarter, just going back to some of your comments on cash outflows, I think you touched a little bit on some of the deferred compensation about \$30 million, \$40 million on the acquisitions. Can you just talk a little bit more of the tax specifically because obviously, every MSO has a pretty large tax payable for Q1? And I'm just curious, of the \$200 million or so on the balance sheet, how much of that is cash? What's the timing? Just kind of get a refresh on that, please.

George Archos

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

Sure. So, I think we certainly answered this question, [indiscernible] (00:28:20) to answer again. The total deferred taxes on our balance sheet represents – we target about a year right now, I think we're about a year-and-a-half. So, if you think about the total amount that we have out there, it's essentially debt at a very low cost. It makes sense for our shareholders to have that as opposed to market-based debt. So, we keep managing that, you know, intelligently to make sure that we're providing the right cost of funding. So, having said – again, we do have an internal target of about a year. Right now, we're a little over that. We actually have made a recent

payment here in Q2, so you'll see that fall in Q2.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Got it. Appreciate that. And just on the M&A side, you know, look, you mentioned you're going to be sort of selectively acquisitive going forward. Is there any meaningful take that you think are needed in your portfolio? Or are these more sort of tack on like you've done in the past in markets like Pennsylvania and other ones that have good regulatory programs?

Aaron Miles

Chief Investment Officer, Verano Holdings Corp.

Listen, we look at every market. There's nothing that we necessarily need. We're very happy with the footprint that we have. That being said, you know, there are tuck-in opportunities for us in a few states that we already operate in and we're vertical in. And there are some new states that could be attractive, just the price point makes sense and if the operations, you know, fit the Verano culture. So, we look at everything. We don't transact on everything, but [ph] we're not afraid to do (00:29:32) something that makes sense for us.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Okay. Thank you.

George Archos

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

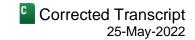
Thanks, Matt. Have a great day.

Operator: Our next question comes from the line of Kenric from ATB Capital Markets. Your line is open.

Kenric Tyghe

Analyst, ATB Capital Markets, Inc.

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Thank you and good morning. George, just on New Jersey, and I'd like to pivot to PA quickly. But on New Jersey, first line sales of \$24 million. We've all seen the announcements on six additional stores coming on-line soon, just in line with potential planned openings from some of the other major operators. Those new stores obviously provided some short-term oxygen to the market. But how confident are you in your ability sort of an absolute relative basis to capitalize on that near-term store expansion? And also, just more broadly on any impact you provide on the pace of the ramp or the acceleration that those new stores give to New Jersey in the short-term outside of anything else later in the year on additional OpEx?

George Archos

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

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Good morning, Kenric. So, another good question. I mean, the market needs more stores, plain and simple, right? I mean, the velocity of the market has been great. But we're going to see further growth with additional capabilities to serve the consumers, right? There's only so long people want to wait in line and people want to travel far distances to get their product. So, the more stores that open, it takes away from the black market and provides an opportunity for us, licensees. We plan on wholesaling to all the stores in the state when they open. We're also excited to get our third store open as well in the Shore. So again, what we talked about earlier, yes, the market's been great so far, but there's a lot of room for growth and expansion. So, this is just another step in that direction, and we view it as a positive one.

Kenric Tyghe

Analyst, ATB Capital Markets, Inc.



Thank you, George. And then, just on Pennsylvania, and then you did call out, you know, the weakness in Illinois and PA, but can you speak to Pennsylvania? How much of that would be the broader market weakness? How much of that was – and, sorry, the broader market weakness on the vape recall? How much of that may or may not have been other factors impacting the Pennsylvania performance, any insight on Pennsylvania will be appreciated?

George Archos



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

Well, the vape ban was significant, right, six weeks of no vape sales was – it hurt quite a few operators there and it hurt the market. Obviously, Pennsylvania was not an outlier and as far as the weakness in January and in February, the market was, it was weaker there. So, it's come back a little bit in March and, you know, hopefully, it continues to ramp throughout the year. We have some additional store openings as well that we're very excited about in the Philadelphia region and some in the Pittsburgh region. So, that'll provide some additional growth for us throughout the year, and we're looking forward to launching our Verano products, right?

I mean we've been, you know, we had to sell through everything that the former facility had. It wasn't of the quality that we like to be able to sell Verano. So, we're very much so excited for that in Q3. And, we think, Pennsylvania is still one of the best markets in country and we think that adult-use is on the horizon there. So, we're preparing and anticipating that over the next 12 months to 18 months, and that's really what we're focused on.

Kenric Tyghe

Analyst, ATB Capital Markets, Inc.

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Great. Thanks, George. I will pass the line.

George Archos

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

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Thank you.

Our next question comes from the line of Neil Gilmer from Haywood Securities. Your line is open.

Neal Gilmer

Analyst, Haywood Securities, Inc.

Yeah. Thanks very much. Many of the questions have been answered. But maybe just an update on the Goodness Growth divestitures. You know, is that going to be towards the closing that you're expecting at the end of this year? Is that just still going to happen throughout the year as you sort of complete the [ph] RFP (00:33:05) process?

George Archos

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

The goal would be to have a - more of a - almost a simultaneous closing. So, that will push first through towards the end of the year. Obviously, we have to work with the regulators to make sure that we follow all their guidelines, but it would be more towards the end of the year.

Neal Gilmer

Analyst, Haywood Securities, Inc.

Yeah. Okay. And then, just maybe a small one, you know, about 10 days ago, you announced the launch of the mobile applications, you know, across a number of the different states you're in. I'm just wondering whether – how the initial uptake has been and adoption of that has been?

George Archos

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

We've been pleasantly surprised. When you have a loyal following, it shows when you do things like that and we have quite a few sign-ups and it gives us an opportunity to reach our customers on an easier basis. So, we're excited about the opportunity there. And it's kind of – it was a good launch. The sign-ups are tremendous. The app is good, but it's only going to get better. There's a lot of things that we need to improve upon there, but we're looking forward to expanding on that side of the tech front.

Neal Gilmer

Analyst, Haywood Securities, Inc.

Great. Okay. Thanks very much.

George Archos

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

Thank you.

Operator: [Operator Instructions] We have a question from Spencer Hanus from Wolfe Research. Your line is open.

Spencer Hanus

Analyst, Wolfe Research

Great. Thank you. So, getting back to New Jersey sales. Could you just talk a bit about how your stores performed versus the \$2 million average AUV that the industry saw in the first month? And then are you seeing

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any issues with inventory and your peers that maybe have less cultivation capacity than you guys [indiscernible] (00:34:35)?

George Archos

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

I'm sorry. I didn't catch the first part of that question.

Spencer Hanus

Analyst, Wolfe Research

Can you just talk about how your stores performed versus the industry average volume [indiscernible] (00:34:45) \$2 million level and then any issues are you seeing with inventory in the state?

George Archos

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

Is this the New Jersey? We didn't catch which state you're talking.

Spencer Hanus

Analyst, Wolfe Research

New Jersey. In New Jersey.

George Archos

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

So, we don't comment on specific sales on the stores. Obviously, they are doing tremendously well. We would rather wait for the program to play out a little bit, get our third store opened, see some of new store openings before we comment on specific sales. That being said, we have great operations on the cultivation front, ample supply across all categories. So, you're seeing our menu increase week-over-week. Basket size is increasing due to expanded variety in the menu side and I think Jersey is going to be a very strong market for us for years to come.

Spencer Hanus

Analyst, Wolfe Research

Got it. That's helpful. I'll stay tune there. And then, I guess, just in terms of Q2, I don't know if you commented on sort of how sales are trending quarter to-date, if you could just quantify that. And then you comment about 2% decline in basket. Are you expecting or expecting that decline to accelerate going forward? How are you thinking about – be about that as inflation [indiscernible] (00:35:47)?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Yeah. So, from a Q2 perspective, you know, we will provide some guidance here in the upcoming future. And all I can say right now is that, you know, if you expect Q2 to be up above Q1, which I think that we've talked about before. So, I don't think we share anything new there, but we'll provide something more specific in the near future. In terms of basket size, you know, I would think that the trend is the trend, it's pretty consistent and I would think that that will follow up for a while.

Spencer Hanus

Analyst, Wolfe Research



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Got it. Thank you.

Operator: We have no further questions at this time. Now, I'll turn the call over to George.

George Archos

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

All right. Thank you, everyone, for joining today and look forward to talking soon.

Operator: This concludes today's conference call. Thank you for participating. You may now disconnect.

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