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Verano Holdings Corp. (VRNO.CA)

Q1 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Julianne and I will be your conference operator today. At this time, I would like to welcome everyone to Verano Holdings Corp. First Quarter 2024 Earnings Conference Call. 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] Thank you.

I would now like to turn the call over to Julianna Paterra, Vice President of Investor Relations. Please go ahead.

Julianna Florence Paterra

Vice President-Investor Relations, Verano Holdings Corp.

Thank you; and good morning, everyone. Welcome to Verano's first quarter 2024 earnings conference call. I am joined today by George Archos, Chief Executive Officer and Founder; Brett Summerer, Chief Financial Officer; Darren Weiss, President; 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 for the quarter ended March 31, 2024.

In addition, throughout today's discussion, we will refer to non-GAAP financial measures that do not have any standardized meaning prescribed by GAAP. 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 their respective most directly comparable GAAP financial measures. Lastly, all currency is in US dollars unless otherwise noted.

I'll now pass it to George.

George Archos

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

Good morning, and thank you for joining our first quarter 2024 earnings call. We have a lot of great news to get through this morning, but first let me provide a roadmap.

I'll begin today by providing an overview of the quarter followed by commentary on the groundbreaking news regarding the DEA's acceptance of the recommendation to reschedule cannabis, another significant domino to fall in the fight to legalize cannabis and unlock the cannabis industry's full potential. We are obviously thrilled about the news, but I want to reiterate, as I have been saying for the last several years, we never built Verano's business based on assumptions of federal, regulatory or legislative movements, and the company is positioned to continue achieving strong results, independent of federal changes, as evidenced by our first quarter results.

After Brett reviews the numbers in detail, I'll close with thoughts on our unique position for growth in 2024 in addition to our updated outlook for the year.

We had a much stronger start to the year than originally anticipated, with \$221 million in revenue and 30% adjusted EBITDA margins for the first quarter, providing a strong launchpad for the remainder of the year as we have and will continue to take action to position the company ahead of a number of really exciting potential catalysts.

We have been able to consistently get ahead of adult use transition opportunities, which has given us what we believe is one of the strongest portfolio positions in the industry. This includes Illinois, New Jersey, Connecticut and Maryland, all states in which Verano has a leading presence. Ohio's upcoming adult use program further accelerates this momentum as we can leverage our five dispensaries, the maximum currently allowable in the state, and our high-quality indoor cultivation facility. Pennsylvania, also primed to approve adult use in the near term, is another state where we have built a leading footprint ahead of this possible transition with 18 affiliated dispensaries and high-quality indoor cultivation. However, and most notably, Florida, which will have adult use on the ballot in November, is a monumental opportunity for us as we look to strategically grow our already deep footprint of 74 dispensaries and counting, all of which are supplied by our high-quality indoor cultivation facilities.

And Floridians, roughly 1 million of whom joined the signature campaign to put the issue on the ballot, have been voicing their undeniable support for legal and safe cannabis. With the state's Supreme Court affirmative ruling confirming their right to vote on the issue this November, they will finally have the opportunity to say yes to legal adult use cannabis.

As soon as we heard news of the ruling, we stepped up our support of the Smart & Safe Florida campaign with over a \$2 million contribution. This program unites operators to educate the voter base on the countless economic, health and wellness benefits this incredible plant provides millions of Americans, and more than 800,000 Florida medical patients, every day. We're thrilled to join Smart & Safe Florida alongside our peers and a large veteran coalition as we campaign together for lasting change for the residents and visitors of Florida.

We are incredibly excited about the opportunity in Florida, and I'll let the numbers speak to why. In 2023, we generated \$222 million in revenue in Florida. Given our experience in other states that have transitioned to adult use, if you assume a similar pattern of a 2.5 to 3 times increase in revenue, that would translate to between \$300 million and \$450 million in incremental annual revenue. And we think this estimate is conservative given the state's large tourism influx of over 135 million people annually. As a reminder, we have the second largest footprint in this 100% vertical, high-margin market.

Our expansion plans are already underway in Florida to significantly increase our high-quality indoor cultivation capacity. We temporarily shut down some rooms in our cultivation facility in the first quarter as we built them out to increase capacity, and we have since ramped those rooms back up and expect to significantly increase output by this summer. Looking ahead, we will continue to focus on growing the highest quality flower in Florida for what we see as the largest overnight growth this industry has ever experienced.

Additionally, we anticipate adding new MÜV-branded dispensaries this year across Florida to further prepare for the anticipated increase in demand. Given our deep experience in adult use transitions, we are also bullish on our ability to grow our market share both ahead of and during adult use. We look forward to November, but in the meantime, we are focused on supporting the Smart & Safe Florida campaign alongside our industry peers.

Moving on, last quarter, we discussed the positive growth trajectory of the wholesale side of our business, and we were extremely pleased with its performance in the first quarter, which helped offset some of the anticipated softness on the retail front. In fact, the strength of our brands and wholesale platform helped us outperform our initial expectations and add nearly 50 new dispensary customers, largely across New Jersey and Illinois. And we continue to see wholesale growth, with our dispensary partners consistently demanding that the Verano house brands holds a meaningful presence on their shelves.

In New Jersey, retail performed as expected, given seasonal softness combined with the continuation of new dispensary openings. But as I previously mentioned, we saw our business grow, with net wholesale revenue up 130% and the number of net wholesale orders up over 300% versus the prior year period. The strength of our wholesale platform nearly offset the normalization in retail sales in absolute dollars for the quarter. New doors are showing strong interest in carrying our products, evidenced by the 21 new accounts gained in the quarter, and we were still above a 90% penetration rate for the state. This positive momentum has continued into the second quarter as we are seeing continued strength in net wholesale revenue

We're similarly excited about our Illinois wholesale market, which saw sequential net wholesale growth each month in the quarter paired with 45 basis points of market share gains, according to BDSA. Verano entered 15 new doors in the quarter, keeping up with new dispensary openings in the state. As we look forward, we continue to see third-party dispensaries as a growing wholesale opportunity as the number of retail doors grow in both New Jersey and Illinois. We believe a growth in dispensary count is directly correlated to organic consumer growth as new customers and patients find and engage with cannabis, and we look forward to serving a growing and passionate consumer base.

And in Ohio, our team is working hard to prepare for adult use by increasing our output in advance of the anticipated growth in demand. With an expected fall launch date, we are exploring the addition of our sixth dispensary per current regulatory proposals. In the interim, we feel very prepared with today's five dispensaries and look forward to serving a large consumer base in the near future.

Our mission here at Verano is to cultivate progress. And we are doing that by focusing on differentiation, innovation and disruption. To that end, we launched Cabbage Club, a first-of-its-kind US cannabis membership club, and it is off to a great start, with our enrollment after initial launch exceeding our internal goals. By offering an annual paid membership, we can provide our most passionate consumers with a trove of benefits including an enrollment gift, monthly credits for retail purchases, early access to limited edition strains, priority pickup lines, and even warm cookies when visiting their favorite Zen Leaf. And we have more great stuff coming. We view the Cabbage Club as a symbiotic relationship with our most prized patrons, who clearly recognize the value in the program as membership continues to grow. As planned, we rolled out Cabbage Club in New Jersey and Illinois to start, and we anticipate rolling out the green carpet in additional states in 2024.

Turning to rescheduling. The news suggesting we will see the DEA reschedule cannabis from Schedule I to III in the near future only affirms what we've always known – cannabis is an incredible plant that provides numerous health and wellness benefits, contributes billions of dollars to local economies, and supports close to 0.5 million careers across a growing number of states. We have been preparing for months for possible opportunities that may result from this announcement, so when we heard the news, not only did we feel thrilled, we felt prepared.

Beginning with capital market preparedness, we are an SEC filer, completing our first SOX audit for the year ended 2023, and continue to build out our financial reporting capabilities. We migrated our listing to Cboe Canada last fall, where we achieved senior exchange status which we believe gives us a first-mover advantage should US exchanges permit cannabis listings. Additionally, we currently remain eligible for both the MSCI and FTSE

indices. We are proud to provide what we view as the deepest level of transparency in our industry in financial reporting, offering state-by-state revenue per segment.

While our credit facility is over two years from the term expiration, as prudent stewards of capital, we are already exploring options, including refinancing, and have paid off \$50 million this year, bringing the facility down to \$300 million in principal, retaining optionality to pay down an additional \$50 million in the future, without any additional prepayment premium. In connection with the prepayment, our lender has agreed to release certain real estate assets valued over \$50 million, providing us more opportunity to lower our overall cost of capital with lower interest rate mortgages.

As a reminder, a DEA rescheduling decision is an important step towards operating as a normal business. We may have the opportunity to significantly improve our credit terms, resulting in lower cost of capital. Our consumers might be able to use credit cards, which we estimate would modestly increase basket sizes. Further, we could have a much less burdensome cash management system, allowing us to earn interests on our significant cash balance. And more importantly, our employees would be safer as we'd anticipate a decrease in break-ins industrywide, with dispensaries holding less cash on premises. Our vendor pool could also greatly widen. And lastly, we could expect incremental institutional investor comfort.

Although we don't think a Schedule III designation alone would be enough for a US listing, we think there's a chance that a Schedule III decision would continue momentum for certain exchanges. So, as usual, we remain proactive in that arena. And perhaps most tangibly, should the DEA's rescheduling proposal take effect, we would benefit greatly from operating under a fair tax regime. We estimate we would have saved over \$80 million in taxes in 2023 alone.

Cannabis acceptance continues to gain momentum. And while I know everyone, including me, is anxiously awaiting an announcement, it is still a major win that the highest levels of the government continue to discuss normalization of cannabis at the federal level.

I will now turn it over to Brett before providing some final thoughts.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Thanks, George. Revenue for the quarter decreased 3% versus the prior year period to \$221 million, driven by pressures in New Jersey retail, as expected, as dispensaries continue to open across the state.

On a gross revenue basis, excluding intersegment eliminations, 66% of sales were derived from the retail business, with the largest contributions from Florida, Illinois and New Jersey. The remaining 34% of sales were derived from the wholesale side of the business, with the largest contributions from New Jersey, Illinois and Connecticut.

We welcome the steady increase in proportion of the wholesale side of the business we've seen over the past few quarter as it is generally the most profitable arm of the business and expect that trend to continue through 2024.

Gross profit for the quarter was \$113 million or 51% of revenue versus \$109 million or 48% of revenue in the prior year. The increase in gross profit was driven by higher third-party wholesale sales of Verano products.

SG&A expenses were \$90 million or 41% of revenue versus \$75 million in the prior year period or 33%. The increase in SG&A expense was primarily driven by new dispensary openings in addition to investments in people,

processes and technology. We had a net loss of \$5 million, driven by the provision for income taxes as we currently account for income taxes under the 280E tax code. Adjusted EBITDA for the quarter was \$67 million or 30% of revenue.

Turning to the balance sheet and cash flows. We maintain a strong balance sheet, ending the quarter with \$194 million in cash and cash equivalents, though notably, this balance does not reflect the \$50 million prepayment towards our credit facility made in April. Even inclusive of that, we are still well above \$100 million in cash reserves, providing us the flexibility for either continued deleveraging, CapEx or M&A.

Cash flow from operations for the quarter was a very strong \$31 million and we spent \$10 million in CapEx, largely on Florida cultivation expansion and various dispensary openings. Previously, we had guided to \$25 million to \$50 million in CapEx as a base for the full year, excluding opportunistic activity, such as Florida adult use preparation. As George mentioned, we have begun some expansion initiatives in our Florida facilities and will be studying the latest polling results to inform future large expansion initiatives. As always, we strive to remain one step ahead of growth; and based on our experience in six other transitioned markets, we are confident that we'll strike the right balance and remain a market leader in Florida.

Given recent industry news on the tax front, we have been following the situation very closely and have engaged third-party legal and accounting firms who are helping us execute our strategy. We are also eagerly awaiting rescheduling outcomes because of its impact on our tax liability.

Lastly, we expect flat to sequential top line growth in the second quarter, putting us back on what we see as a continued growth trajectory for the year.

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. We have very deliberately and strategically designed our footprint to be one of the most diverse and deep in the industry, offering strong upside in each of our markets. After a steady 2023, during which we deepened our moats versus competition, grew our roots deeper in our communities, and strengthened our financial foundation, I couldn't be happier about the momentum we have built and am confident in our growth opportunities. With this incredible start to the year, we are ready to propel forward.

With each passing year, more Americans acknowledge the medicinal properties of the cannabis plant and the benefits of swapping cannabis for unhealthy behaviors. 70% of 25 to 34-year-olds prefer cannabis to alcohol according to the latest poll from New Frontier Data. I want to repeat the statistic. 70% of what will soon be the largest consumer spending age group prefers cannabis to alcohol, which is currently over a \$250 billion market in the US alone. We look forward to realizing the benefits of operating as a normal business once we have a final rule from the DEA and cannabis is rescheduled.

We generated \$73 million of free cash flow in 2023 while operating under today's restrictive and punitive environment, so imagine what this company can accomplish once these metaphorical handcuffs are removed. And Verano has its own momentum on top of these positive structural shifts. In Illinois and New Jersey, two of our largest revenue contributors, we are strengthening our wholesale position and poised well for future growth as a top 4 and top 2 market shareholder, respectively. We have a new adult use market ahead of us this fall in Ohio, providing what we expect will be a 2.5 times lift in sales in the state. And most importantly, we have the possibility

of legalization of adult use on the Florida ballot this November. We see huge opportunity ahead of us given our footprint in Florida, the second largest in the state, alongside a history of maintaining a very strong market share.

In closing, our first quarter marked a period of remarkable achievements across multiple fronts. And while we're all patiently waiting for more news from DC, the industry has experienced a tremendous amount of momentum on which Verano is positioned to capitalize.

Operator, you may open up the line for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Thank you. Our first question comes from Matt McGinley from Needham. Please go ahead. Your line is open.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Q

Thank you. So, in Florida, what happened or how did your strategy change from the fourth quarter to the first quarter? In the fourth quarter, you had a nice bump in revenue and good market share gains in the first quarter. It looked like you gave some of that back. Was that related to you taking those wins down to increase the capacity or did something change for you competitively in the market?

George Archos

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

A

Well, a couple things. Good morning, Matt, by the way. Q4 was a very strong quarter for Florida. So, coming off of that, we anticipated a little bit of drop off in Q1 as we normally do. But the majority of it was the construction that was going on at the large facility in Apollo Beach, so it was anticipated, it was also needed, and we expect a big bounce back here coming into the summer.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Q

Got it. And then on the SG&A, you've been managing that pretty well with the store growth, and that's been steady on a dollar rate basis for the last few quarters. This quarter, you had a slight revenue decline, so rate went the wrong way for you, but you also had an increase in the core dollars. Was there something unique about the expense in this quarter or it's just the new G&A dollar level given the growth you're having at the retail level?

George Archos

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

A

Definitely new G&A dollars. And we do anticipate to hire throughout this year to get prepared for these new adult use markets. So we'll see a little bit of a hit there. But as we have in the past, we set these new adult use markets in a very strong and deliberate manner, and we expect to do the same coming up with Ohio and hopefully PA and Florida.

Matthew Robert McGinley

Analyst, Needham & Co. LLC

Q

Okay. Thank you.

Operator: Our next question comes from Aaron Grey from Alliance Global Partners. Please go ahead. Your line is open.

Remington Smith

Analyst, A.G.P. / Alliance Global Partners Corp.

Q

Hi. Good morning, and thank you for the questions. This is Remi Smith on for Aaron Grey. Just a quick clarification before I get my first question. The sales guidance, I think you mentioned near the end, that was a flat to up sequentially. And then for my first question, in Florida, I appreciate some of the color there with some of the grow rooms that you talked about with investments going ahead to potential ballot in November. But if you could speak a little bit more to specifics for any additional plant cultivation or how many stores you'd like to add just in case for the adult use scenario that'd be helpful. Thank you.

George Archos

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

A

Good morning, Remi. As for Florida, we're not giving specific guidelines yet on what we're going to be doing. We're evaluating our current sites as well as some additional sites. Store count, we'll grow throughout the year. We already have some stores located, planned out, under construction. We're also opening one up this Friday. So we'll continue to evaluate sites throughout the state, and we'll add store count as we see fit. As for guidance, flat top is what we said in the call. Brett, would you like to provide any further?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Yeah. I mean, flat top is usually what we see a little bit of an increase there, but we're also seeing some strength because we had a onetime true-up from a discount that we had been running in parts of the country. So, that won't repeat. That was worth about \$3 million in Q1, so that won't repeat, and we're going to see a little bit of a lift from there.

Remington Smith

Analyst, A.G.P. / Alliance Global Partners Corp.

Q

Thank you. And then my second question for taxes. Can you provide some update on your tax strategy? Any filings for refund, status of those refunds along with any planned treatment of taxes [indiscernible] (00:23:00) going forward?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Sure. So I can't talk to specifics on that other than to say we have engaged professional firms from a legal and from a tax perspective, and we're working through that right now.

Remington Smith

Analyst, A.G.P. / Alliance Global Partners Corp.

Q

Okay. Thank you. I'll hop back in the queue.

Operator: Our next question comes from Scott Fortune from ROTH MKM. Please go ahead. Your line is open.

Scott Fortune

Analyst, ROTH MKM

Q

Good morning. And thank you for the questions. Wanted to little focus on kind of retail partnerships in New Jersey, Connecticut and Illinois and driving that wholesale to really offset the kind of the retail sale pressure you're seeing in a couple of states there from that store competition. But can you provide color kind of on your social equity or retail partnerships looking to put in place here in New Jersey to continue to see that wholesale growth lift from their standpoint? And kind of the follow-up on that, are you seeing wholesale orders become bigger now that after initial kind of wholesale store – into the 90% of the stores you're selling to New Jersey from that side of things? Just a little more color on New Jersey as that grows the build out there from retail same stores.

George Archos

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

A

Good morning, Scott. Thank you for the questions. Our retail partnerships are always very important to us, have been. We started this business really focused on wholesale. And right now, we're starting to focus more on wholesale again. As you see, our wholesale numbers are going to be driving up, and we anticipate that to continue to drive up throughout the year, especially in markets like New Jersey, Connecticut and Illinois. We're in the majority of the stores throughout those three states, and we'll continue to be on the majority of the shelves as we see fit and the stores that make sense for us. So, again, wholesale is very important to us. We're going to continue to not only grow it in the new social equity joint ventures, but also grow market share in the stores that are currently open in those three markets.

Scott Fortune

Analyst, ROTH MKM

Q

Got it. And then real quick, on the cash flow side, the potential additional \$80 million from taxes potentially. But can you kind of provide kind of priorities? It seems like you want to still pay down debt and priority is for investment growth for M&A going forward here. And then, are you seeing on the debt financing side and potential talks there with lenders? Are they starting to treat Verano as a normal tax filer from a cash flow perspective? Just kind of a little color on the credit side from the lenders that you're talking to.

George Archos

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

A

Another great question. I mean, the three targets are, as you just mentioned to be: debt reduction, M&A opportunities that we continue to look at throughout the country, and CapEx where we see fit with three new adult use markets that we see coming on the horizon. We'll be spending some dollars there as well as some other markets to continue to upgrade our facilities, add new stores, et cetera, and there's plenty to do with the cash. Brett, any other comments?

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

No. I mean, I would just say, look, it's always a target-rich environment, in particular when you have a lot of money sitting on a balance sheet, like we do compared to some of our peers. A great place to be, but also we want to make sure we're deploying that cash and getting the highest returns we can. And frankly, this is a great year for M&A, this is a great year for expansion adult use, pre-adult use, and it's also a great year for thinking about what else we might want to do in terms of retiring debt. So, all of those are very attractive to us.

You had mentioned, is there different treatment from a tax perspective. Right now, we're not seeing anything like that. Schedule III is something that we're keeping our eyes on, but we haven't necessarily seen a lot of movement yet, and which I wouldn't expect until we see something officially official come through.

George Archos

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

A

Also, to touch base on the lending, we continue to work with local and state banks throughout the country and on a real estate, but we're not seeing any major shift yet in lender availability. But we anticipate it will come soon, and we'll be there ready to jump on the opportunity when it comes to us.

Scott Fortune

Analyst, ROTH MKM

Q

Appreciate the color. Thanks.

George Archos

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

A

Thanks, Scott.

Operator: Our next question comes from Russell Stanley from Beacon Securities. Please go ahead. Your line is open.

Russell Stanley

Analyst, Beacon Securities Ltd.

Q

Good morning and thank you for taking our questions. [indiscernible] (00:27:20) can you talk to what parts of the state might be of geographically particular interest now given the improved odds on adult use. I imagine there were tourist-heavy pockets that are underpenetrated medical markets that are now more attractive. And to the extent you can share, I'd love to hear your thoughts on how much greenfield opportunity there is there.

George Archos

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

A

Hey Russ. Unfortunately, you broke up in the first part of the questions. I didn't hear what markets you were referring to. Can you reestablish that question?

Russell Stanley

Analyst, Beacon Securities Ltd.

Q

Yeah. I was asking on Florida, given your plans to add additional stores there this year, given it's a tourist destination, I'm wondering if there must be pockets of greenfield or underpenetrated areas that you can add stores to. And I'd love to hear – to the extent you can share, I'd love to hear your thoughts on geographically where the best opportunities are.

George Archos

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

A

Yeah. Great question. I mean, we are looking into markets that we weren't looking at when we were just concentrating on medical patients. So, we're evaluating those now. We also had quite a few stores under development for this year and next year. So we're going to continue to build out those stores and look at these

new markets. We don't really talk about exactly which markets we're looking at, but there is a change in focus when adult use comes online versus medical, and we're looking in some different areas now.

Russell Stanley

Analyst, Beacon Securities Ltd.

Q

Thanks. That's helpful. And just moving to New Jersey, given the increase in store count, the benefit to wholesale more than offsetting retail, I'm wondering at what point the store count is you think there might be an oversaturation there where the benefits no longer outweigh the costs. Just wondering how much room, how much runway there is for additional retail growth before you becoming concerned about the level of competition. Thanks.

George Archos

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

A

I mean, for us, we always anticipated New Jersey to be a large wholesale market. When we entered the market there, the allowable amount of stores was only three. So, for us, we built out our capabilities to be able to wholesale to the entire market. So, as store count increases, we'll continue to increase our wholesale, and we feel very good about it. We're in a good position to continue to be a strong wholesaler there, and we don't know what the market is going to look like as a final store count, but we're ready to continue to wholesale to every store throughout the state.

Operator: Our next question comes from Frederico Gomes from ATB Capital Markets. Please go ahead. Your line is open.

Frederico Gomes

Analyst, ATB Capital Markets, Inc.

Q

Thank you. Good morning. And thanks for taking my questions. First on New Jersey and Illinois. Obviously, you're shifting the mix there from retail to wholesale. Can you just remind us what's the expected margin impact from that sales shift?

George Archos

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

A

Good morning, Frederico. I'll pass off to Brett to answer your question.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Yeah. So, whenever we think about the transition from retail to wholesale, Illinois or New Jersey, but in particular in New Jersey, for every dollar that we have in the retail side from a margin perspective, we essentially get \$2 worth – I'm sorry – for every dollar on the wholesale side, we essentially get \$2 worth on the retail side. So, to the extent that it's a 2:1 ratio, you can still be happy with the fact that total sales in the state are going down as long as the wholesale side is going up. And then what we are seeing is that the wholesale side is continuing to grow even while the retail side is declining. But right now, we're still pretty happy with the mix of that pace.

Frederico Gomes

Analyst, ATB Capital Markets, Inc.

Q

Thank you. And then my second question, just on Ohio, it seems that adult use sales could start maybe ahead of expectations maybe during the summer. So, just curious how likely do you think that's to happen and how prepared are you in the state in terms of your cultivation and manufacturing?

George Archos

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

A

Good question. We're prepared right now. We've put everything in place. People are in place. We're ready to start adult use sales immediately, although we don't feel it might happen in the summer, I think we're more anticipating a fall launch. Regardless, we're ready to go.

Frederico Gomes

Analyst, ATB Capital Markets, Inc.

Q

Thank you.

Operator: Our next question comes from Matt Bottomley from Canaccord Genuity. Please go ahead. Your line is open.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Q

Hi. Good morning, everyone. Just want to go back to the news from last week, understanding that rumors or even if the DEA announcement becomes more firm, it's nothing to do specifically with your operations or how you would change anything to do with your strategy. But just given the fact that there's a lot of questions coming in on it, without trying to crystal ball when things might happen, can you give us any sort of overview of what your expectation of the process is? Is there something that would be filed through the DEA? Is it something through the attorney general's office? Just without, again, trying to crystal ball timing, just what procedurally could be the next steps, in your view, if this process continues to go forward?

George Archos

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

A

Good morning, Matt. I'm going to pass this off to Darren. He's done a deeper dive there than we have. So, Darren?

Darren H. Weiss

President, Verano Holdings Corp.

A

Yeah. Thanks, George. And thanks for the question, Matt. Look, so, the next step at this point, as has been widely reported, is that we're waiting for OMB, the Office of Management and Budget, to complete their analysis. After that, the DEA is able to post proposed rules with a notice and comment timeline. And so, at this point, all indications are that the sort of guidepost for next steps would be that OMB determination. I think there's been a fair amount of reporting as to the overall process and the timeline, as you said. We feel very, very good about the status. We understand that this is not a quick process, believe it or not, as frustrating as it's been. The way this has gone has been at breakneck speed as compared to the way the wheels of government turn. So, that would be the next indication.

We would love to see a memo similar to the Cole Memo from the DOJ as part of this process that may or may not come. It's not required in order for this to flow through. But look, at the end of the day, as you said, the impact to

our business I think, other than taxes, is pretty minimal, other than the momentum, the fact that the conversation is happening at the highest levels of government. And we're looking forward to watching this develop.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Q

Great. I appreciate that. And then just next for me, more of a housekeeping item, but just to make sure I understood some of the prepared remarks. So you have a CapEx range of \$25 million to \$50 million, but there's a lot of commentary on Florida expansion, which some of it has undergone as well as preparations in Ohio. So I understand you're not going to adjust that number live, but can you just give us some context of where that range could be, considering there are some moving parts to it?

George Archos

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

A

I think we'll give you a better an idea of the number in the next quarterly call. We're still evaluating all of our opportunities, and we'll have a better idea here in the future.

Matt Bottomley

Analyst, Canaccord Genuity Corp.

Q

Okay. Fair enough. Thanks, guys.

Operator: Our next question comes from Andrew Semple from Echelon Capital Markets. Please go ahead. Your line is open.

Andrew Semple

Analyst, Echelon Wealth Partners, Inc.

Q

Good morning. Thanks for taking my questions. Pure balance sheet questions here. First off, I just want to start off with the inventory. Looks like that moved a bit higher in the first quarter. I think the earlier commentary from Q4, if I'm remembering correctly, was that inventory liquidations, the bulk of that had happened in Q4, but there might be some lingering amounts of that in Q1. So, just want to clarify whether you continue to see inventory liquidations in any specific markets and whether that had any of the headwind or impact to margins within this quarter as it did in previous quarters.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

A

Sure. Thanks, Andrew. So, two questions, two answers. So, the first question you had is the inventory movement. So, we had prepaid packaging – it was just an accounting movement, but the way we had accounted for packaging in the past was we would prepay for it and then amortize it over time. However, as part of our transition and our improvement in terms of systems and interacting with our ERP, we've moved prepaid packaging out of prepaid and into an inventory account. So, it's more handled now as true inventory as opposed to doing this amortization that we did before. So, it's literally left pocket, right pocket. The balance sheet doesn't change. It just moves a line item from a prepaid into an inventory.

And then on the second question, which is related to liquidations, there was a little bit of a benefit to inventory this quarter. It was about \$4 million, but it was not due to anything planned or specific. It was just the overall movement that we have of inventory in the quarter. I don't think \$4 million is much of a big deal, frankly, in that

regard. You don't have anything new or exciting in that space. There's no specific plans to cut or add, et cetera. We're just adding and subtracting as the markets move around.

Andrew Semple*Analyst, Echelon Wealth Partners, Inc.*

Q

Got it. That's helpful. And then a follow-up question would just be on the debt and your ability to continue to prepay that. How much more can you prepay, and would that unlock additional real estate collateral if you were to prepay additional amounts?

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

A

So we have optionality of paying off another \$50 million. The prepayment penalty has been paid with this first \$50 million payment, and there's a large chunk of our real estate that's being released with that first payment. So, it puts us in a very good position to be able to refinance that real estate in the future.

Andrew Semple*Analyst, Echelon Wealth Partners, Inc.*

Q

Got it. Great. Thanks for taking my questions. I'll get back in queue.

Operator: Our next question comes from Mike Regan from Excelsior Equities. Please go ahead. Your line is open.

Michael J. Regan*Analyst, Excelsior Equities LLC*

Q

Hey. Thanks a lot. Two quick questions on the Cabbage prepaid program. I guess, is there any insights in terms of – you've only launched it about a month ago in just a few markets. But I guess, any insight into how that's going, sort of what you're seeing with it, how many people have signed up, et cetera?

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

A

Like we said in the call, it's going very well. It's beating our internal expectations for customers that have come onboard. We're not giving specific guidance yet on how many customers have entered into the program, but we might do that in the future.

Michael J. Regan*Analyst, Excelsior Equities LLC*

Q

Okay. Okay. And then just a quick follow-up on that. I guess, can you help us understand how the accounting is going to work for that? So, like, when someone gives you \$250 to join the program today, is that revenue or is that like a deferred revenue that's then amortized as they purchase the product or over time or something?

Brett Summerer*Chief Financial Officer, Verano Holdings Corp.*

A

Yeah. So, the way that the revenue flows through is amortized over time. And then to the extent that the customer is using the credits, it comes through at the time of purchase within those stores.

Michael J. Regan

Analyst, Excelsior Equities LLC



Got it. Okay. Great. Thanks a lot.

Operator: [Operator Instructions] Our next question comes from Ty Collin from Eight Capital. Please go ahead. Your line is open.

Ty Collin

Analyst, Eight Capital



Hey good morning. Thanks for the question. George, I wanted to follow up on your remarks from earlier in the call about your pessimism, I guess, about uplisting on the back of the rescheduling news. If you could share any details of your conversations with some of the exchanges today, maybe why you're a little pessimistic on that, especially given one of your peers kind of came out after the rescheduling news and mentioned that they had some constructive conversations at the exchanges. So, yeah, maybe what makes you a little bit more pessimistic? And on the other hand, do you think safe banking is something that gets the exchanges across the line of rescheduling [ph] doesn't (00:39:27)?

George Archos

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



Thanks, Ty. I'm going to change your wording a little bit. I'm just going to call it more realistic versus pessimistic. We haven't been more optimistic about cannabis than we have been today, right. So many great things going on. But at the same time, we're also realistic about what's going to happen. I think uplisting is something that will definitely happen. I don't think it happens immediately after the rescheduling. I think some other things that have to happen with it, which we feel optimistic will. It's just we don't think the timing is going to be exactly the same. Darren can clarify further on the dynamics there, but we feel very good about where we're at and where we're headed.

Darren H. Weiss

President, Verano Holdings Corp.



Yeah. Thanks, George; and thanks for the question, Ty. Look, at the end of the day, as you might imagine, we're having the same conversations with the exchanges. The fact remains that it's pretty clear that Schedule III in and of itself is not going to be sufficient, most likely, depending, of course, on the rules and what the DOJ does. But we are optimistic in the long term that we're going to get there, of course, and that this momentum is significant. But as George said, we want to be realistic and not set expectations in a place that's not in line with reality at this point.

Aaron Miles

Chief Investment Officer, Verano Holdings Corp.



And Ty, this is Aaron. I just want to add one more thing, and George mentioned this on the call, but to reiterate the positioning of a senior exchange listing that we have on the Cboe Canada. Like, while we're not going to make guesses at timing, we're going to position ourselves when those opportunities open up. So, if the exchanges move much faster, we hope they do, we will be ready, and that was really part of the big reason of the move that we made to Cboe Canada.

Ty Collin

Analyst, Eight Capital



Got it. Okay. I appreciate all that color there. And then just for my follow-up, so a lot of helpful commentary around what you're planning to do and invest in Florida ahead of adult use. Obviously, very important to make those investments ahead of such a huge opportunity. But maybe just to take a bit of an angle on that questioning, how do you think about kind of hedging your investments there in the event that adult use doesn't go the way that we all hope it does? How do you think of managing that risk of kind of building out more than what you need for a medical-only market?

George Archos

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

A

Well, for one, unlike a lot of our peers, we own the real estate, and we'll continue to do that. So, owning the real estate gives us leverage for the future. And the market continues to grow. Fortunately for us, we're at a stage where we have to continue to add capacity regardless of what happens with adult use. So it's an investment we'd be making anyway, although it might be a little bit larger, we'll be in very good shape. So we'll have the facilities to be able to grow. If, for some reason, and we don't anticipate this whatsoever that the vote doesn't go our way, we'll be able to cease construction and keep it where it's at. So we feel very good about what we're doing and what we're planning on spending for the year and moving forward into adult use transition.

Ty Collin

Analyst, Eight Capital

Q

Great. Thanks for the questions.

Operator: We have no further questions. I would like to turn the call back over to Verano's CEO, George Archos, for closing remarks.

George Archos

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

Thank you, everyone, for your time this morning. Have a wonderful day, and we'll see you next quarter.

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

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