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Verano Holdings Corp. (VRNO.CA)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and thank you for standing by. Welcome to the Verano Holdings Corp. Second Quarter 2022 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. [Operator Instructions] During today's call, there will be a question-and-answer session and instructions will be provided at that time.

I will now turn the conference over to Julianna Paterra. Please go ahead.

Julianna Florence Paterra

Director-Investor Relations, Verano Holdings Corp.

Thank you, [ph] all (00:00:33), and good morning, everyone. Welcome to Verano's second quarter 2022 earnings conference call. I am joined today by George Archos, Chief Executive Officer and Founder; Brett Summerer, Chief Financial Officer; and Aaron Miles, Chief Investment Officer; as well as Rick Tarapchak, our Corporate Controller.

All financial results for the second quarter ended June 30, 2022 and related comparisons to prior periods included in this release are preliminary, have not been reviewed or audited, are based on the company's estimates and were prepared prior to the completion of the company's financial statement close process.

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, including our statements and MD&A for the quarter ended June 30, 2022. In addition, throughout today's discussion, we will [ph] refer (00:01:52) 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 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 will now turn the call over to George. Please go ahead.

George Archos

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

Good morning, and thank you for joining us today. I am extremely pleased with what we accomplished in the quarter and how we [ph] continued (00:02:37) to position the company as a top operator in the space to drive long-term growth and profitability.

To start, I will provide a high-level overview of the business. Then our CFO, Brett Summerer, and new Corporate Controller, Rick Tarapchak, will review our second quarter 2022 financial results in more detail. And lastly, we will open up the call to answer your questions.

Before I begin, I want to comment on the state of our pending audited financial restatements, which is still moving through quality control checks with Baker Tilly. However, we are comfortable enough with the numbers to share them with you today. As Julianna mentioned, though these are subject to change, but in our eyes, the numbers are final and in the name of transparency, we want to share everything possible.

Starting with financials. We generated solid revenue in the quarter of $224 million, an increase of 12% year-over-year and 11% quarter-over-quarter. Top line growth was driven mainly by strong sales in New Jersey as the state transitioned to adult use on April 21, and increasing market share gains in Illinois.

While we were pleased with top line performance in the quarter, our main focus was on investments in key markets to position the company ahead of anticipated growth. This was highlighted by an increased head count in both retail and cultivation to appropriately staff location to absorb the expected increase in demand. This included a significant focus on New Jersey, where we added over 200 employees this year. We also made significant investments in automation, making New Jersey one of the most efficient facilities in our footprint.

In addition, we opened 15 stores since the end of the first quarter, including 12 in Florida, 2 in West Virginia and 1 in Pennsylvania. We staffed up our Connecticut cultivation facility as we continue to bring more rooms online as we position ourselves in that state ahead of anticipated adult use transition. Also, we increased staffing levels in our Massachusetts and Nevada facilities. While these actions contributed to the higher than anticipated SG&A in the quarter, we fully believe that these investments will help continue to fuel the business for growth throughout the remainder of the year.

In addition to operations, and I will touch on this in more detail later on, we continued to beef up our back office capabilities. This includes significant investments in accounting, financial planning and analysis, as well as in our securities legal practice. In light of all these investments, we still produced a strong Adjusted EBITDA margin of 34%, which I believe is not only impressive given some industry headwinds but also given the challenging macroeconomic environment as a whole.

We have also enhanced our focus on opportunities to recognize efficiencies in the business. We firmly believe that we accept the benchmark in the space as the top tier operator, and we have demonstrated time and time again, we have the ability to adapt in a highly dynamic and rapidly growing space. Our focus will always be optimizing profitability, but not to the detriment of potential future growth.

That said, as we evaluated the performance of every retail location [ph] in our needed (00:05:40) cultivation capabilities, we were able to identify and eliminate a significant amount of cost from SG&A. We believe these savings, along with the anticipated growth from our recent investments, should have a positive impact on EBITDA.

We are currently viewing the business in three pillars: financial reporting, operations and capital allocation. We expect the standard we have set on the operational side to apply to financial reporting and we will not rest until we are operating at the Verano standard.

I will speak to all three areas today, but first I will begin with an update on financial reporting. As we've discussed on previous calls, we have been very active since going public, including 16 acquisitions with 14 closed, 1 equity raise in addition to our go-public financing round, 2 favorable debt amendments, and converting from IFRS to GAAP while transitioning [ph] to (00:06:33) a new auditor. We rapidly accelerated our presence as a publicly-traded company and to say our accounting team had a lot to manage is an understatement.

We have continued to funnel resources to the team while we maintain a firm commitment to enhance and streamline our financial reporting capabilities. As I highlighted, we have been building out our finance and accounting capabilities for the past few months, along with implementing updated standards and procedures. We want the efficiency of our financial reporting to mirror that of our operations and will continue to fine-tune this side of the business to make sure we are viewed as best-in-class from that perspective.

We recently welcomed our Controller, Rick Tarapchak from II-VI, where he served as Chief Accounting Officer. He also holds experience from Reynolds Group Holdings, where he served as Controller and was involved with go-public processes of two divisions during multibillion dollar spinoffs. Additionally, he served as Chief Accounting Officer of Navistar and is a board member of the Illinois CPA Society.

We will also continue to explore and implement other proactive measures as we work to instill the utmost confidence within the investor community. We will continue to bolster this department and further stabilize our footing with the ultimate goal to prepare the company for inclusion into the US capital markets once possible.

With the GAAP conversion behind us, we initiated a deep dive into the financials. This effort led to some discoveries, which resulted in the restatements. The main restatement issues focused on our accounting of restricted stock units issued under our Equity Incentive Plan in our Q1 tax provision calculation. We feel these restatements are indicative of the added bandwidth and resources to our team.

While we had to recognize higher SG&A and COGS, expenses related to RSUs, this had no impact on our cash flow statements and the increased COGS expense actually resulted in a reduced tax obligation for Verano. We have implemented additional procedures and added additional resources to address the issues identified.

Moving on to operations. The executive team has spent the last few months scrutinizing every aspect of the business, looking for opportunities to improve upon what was already a strong foundation. These include efficiency levels, improving margin levels and building Verano culture. We ran through this exercise simply because we are never satisfied with the status quo, especially as economic environment changes around us.

In that vein, over the last year and particularly over the last several months, we have seen dramatic shifts in consumer preferences. Despite having been historically focused on the premium and high-end of the value of price spectrum, we have been busy adapting and adjusting our portfolio of offerings to ensure that we're able to meet patients and consumers where they are.

Over the last quarter, we successfully rolled out our mid-tier Essence brand, aimed principally at creating a more accessible option for consumers wanting to get their hands on [ph] Verano's brand (00:09:28) and to widen our consumer base. Rounding out our tiered approach to value, we are proud to have announced yesterday the launch of our value brand, Savvy, which we discussed rolling out in Q3 during last quarter's earnings call. I am so proud of the team for quickly and efficiently bringing this line to market, demonstrating our agility and ability to address the changing consumer demand that we've seen given macroeconomic changes.

As our Savvy brand will be a lower priced item, we anticipate a subtle impact to margins related to the offering. However, as we deploy efficiency measures, including automation across the country, we anticipate being able to offset some of the margin impacts.

Moving to some of our key markets. In New Jersey, we are happy to report that demand remains robust. Basket sizes in our adult use locations have even increased slightly versus the first few weeks of adult use sales. We have one of the most robust menus in the state, measured by SKU count, across multiple form factors.

We also have ramped up capabilities at our state-of-the-art 120,000 square foot facility to meet the growing demand and will continue to position ourselves for future growth opportunities in the state. In addition, we are thrilled that Neptune, our Jersey Shore location, began selling to adult use consumers earlier this month. This location is approximately two miles from the Jersey Shore and popular landmarks such as the Asbury Park Boardwalk.

In Pennsylvania, we had a strong launch of our Verano product line earlier this month. We've generated excitement for the brand and launched the full product line within our [ph] 14 dispensary footprint, with plans to roll out the (00:10:59) dispensary partners throughout the state. And in Illinois, we continued to gain market share in flower. Our namesake brand gained 310 basis points of market share quarter-over-quarter, and I think this is only the beginning as we continue to roll out additional products across the value spectrum.

We are also looking forward to the recently awarded 185 social equity retail licensees, opening new dispensaries and becoming valued wholesale customers. We are excited to introduce new consumers to our brands and further supplying the Illinois market.

Overall, our portfolio is performing well despite external macroeconomic pressures. You've seen large, very established non-cannabis CPG companies struggling in this environment, but we believe in our ability to adapt and succeed. Of course, these pressures are not solely related to Cannabis, but are applicable across the board. We are cautiously optimistic, but we'll continue to watch consumer trends very carefully.

Lastly, I want to discuss our capital allocation strategy. Our goal has always been and remains to return value to shareholders in the most efficient way possible. We continue to employ this approach and are constantly assessing all investment opportunities in front of us to ensure we are making the right decisions at any point in time.

Year-to-date through the second quarter, we have spent $87 million on capital expenditure projects, largely in Pennsylvania and Florida, that we deemed as having high ROIs, given our initial internal projection on state level adult use legislation. However, our strategy has always been to invest ahead of growth, but never too far ahead of growth at the risk of diluting ROI. We strive for agility. When and if any legislative environments change, we will change alongside them.

Specifically, we now believe Pennsylvania, Maryland, and Florida will likely take longer to launch adult use programs than we were projecting a few months ago and are, therefore, adjusting the timing of the next phase of cultivation expansion in these states. Changes in demand and consumer preferences at retail have also caused us to modify some of our improvement and expansion plans to ensure that we are using capital to its greatest impact and effect.

We previously guided to $185 million to $250 million in CapEx spend for the year, but we now estimate a range of $130 million to $150 million. Given the age of our business and operation sites, maintenance CapEx is very low. We expect to spend less than $10 million this year. Our evaluation of capital is not solely based on what we're spending, but also what we could be saving. We recognize that we carry one of the higher income tax payable balances. However, part of our capital allocation strategy is to lengthen our tax payment cadence.

The strategy is not unique to Verano and has been utilized amongst other large US companies. The cost of penalties and interests for these are significantly below the available cost of debt. We continue to have multiple opportunities to tap into higher cost options to bring this balance down, including but not limited to unfavorable sale leasebacks. We have avoided these unfavorable agreements given they come at a very high cost of debt. Therefore, we have chosen to avoid this path.

We have one of the highest cash flow from operations to EBITDA conversions in the industry, which ran about 50% based on full year 2021 GAAP numbers. To fully understand what we were accomplishing by deferring our taxes, we believe investors should look at lease liabilities, taxes payable and gross debt to EBITDA for a fair leverage metric within the industry. If you account for the premium we carry on the income tax payable line in comparison to the industry average, we still have one of the highest cash flows to EBITDA conversion rates in the industry.

In addition, even inclusive of our taxes payable, which we consider the payables as a source of pseudo debt, we are under levered versus our peers. That said, we still do [ph] carry (00:14:51) what we feel is the appropriate amount of debt for the business. We have always had the mindset to take only what we need and move on to the next facility when required. Without delving into the specifics, we continue to have very productive conversations with potential lenders in light of our facility [ph] sparing waves (00:15:07) throughout the next year.

Before turning it over to Brett, [ph] we'll (00:15:11) go into more detail in some of the items I've highlighted, I want to reiterate our never-ending commitment to operating as a best-in-class company across all pillars of our business. Notwithstanding some of the growing pains we have experienced over the first half of this year, with respect to financial reporting, I am very proud of the effort and resilience of the Verano team and confident that we are moving in the right direction.

I will now turn it over to Brett before I give a final few thoughts on the remainder of this year.

Brett Summerer

Chief Financial Officer, Verano Holdings Corp.

Thanks George. Today, I'll review financial highlights from the second quarter of 2022, but first I wanted to go into a bit more detail regarding the restatements. We had a celebration grant of restricted stock units or RSUs and options when we went public last year. When calculating the stock-based compensation expense, the options were correctly accounted for. However, the expense associated with the RSUs was not.

As a reminder, the bulk majority of our subordinate shares were consolidated to proportionate shares on a [ph] 100:1 (00:16:08) basis, in part so we could maintain Foreign Private Issuer status. When accounting for the RSU expense, the total number of shares were viewed as subordinate when the total number was actually proportionate. Simply stated, the number of RSUs needed to be multiplied by 100.

To breakdown the impact, we previously recognized $742,000 of stock-based comp in 2021. $296,000 of that total were options grants that were correctly accounted for and did not need to be adjusted. However, the remaining $445,000 for RSUs was not and needed to be multiplied by 100. This will have an impact on both cost of goods sold and SG&A in 2021 and Q1 of 2022. The COGS component decreased gross profit in 2021 and Q1 2022, resulting in a lower tax obligation for the year. While SG&A absorbed the bulk majority impact, it is a non-cash item and had no impact on Adjusted EBITDA for the year.

Additionally, during this review, we took the opportunity to opt for a more direct valuation using the closing share price on the day of issuance to align it with the valuation methodology utilized for later grants. We also uncovered that we overstated our effective tax rate in the first quarter of 2022. Once fixed, the effective tax rate did decrease.

Lastly, because the account books were opened during our restatement period, we updated our acquisition consideration payable amount to reflect payments made subsequent to quarter-end. As some of these earn-outs were based upon specific profitability hurdles, we must estimate those payments until such hurdle time periods have been reached. Once that exact amount is apparent or once paid out, we will adjust acquisition consideration payable appropriately.

As George mentioned, we are investing in people such as our new Controller and an expansion of our internal control and internal audit functions while deploying processes and technologies in parallel, such as [ph] SAP and Wdesk (00:17:56), which will allow us to achieve world-class financial reporting capabilities so that finance can shift our focus to our efforts on future profitability, instead of continuing to review the past.

Moving on to the financial. Second quarter 2022 revenue was $224 million, up 12% compared to the second quarter of 2021 and up 11% sequentially, led by growth in New Jersey, dispensary addition to Florida and market share growth in Illinois. Gross profit for the quarter was $98 million or 44% of revenue, compared to $69 million or 35% of revenue for the same period in last year.

Looking at gross margin adjusted for the same exclusions used in our Adjusted EBITDA, such as excluding depreciation and amortization, we generated $133 million or 59% revenue. SG&A expenses were $100 million for the quarter or 45% of revenue. However, we typically think about SG&A, excluding depreciation and amortization, earn-outs [indiscernible] (00:18:52) which would be 30% of revenue. Sequentially, SG&A expenses increased by about $11 million as we made efforts to hire ahead of growth in New Jersey, along with additions to our corporate team in Illinois.

As George mentioned, we also identified some cuts within SG&A, [ph] knit (00:19:09) largely at the retail level and are looking to target approximately 27% in the long run, give or take a few points. We had a net loss for the quarter of $10 million and Adjusted EBITDA was $76 million or 34% of revenue for the second quarter and $81 million or 40% of revenue for the same period last year.

Turning to the balance sheet and cash flows. We ended the quarter with $93 million in cash and cash equivalents. Cash flow from operations for the first six months was $44 million after retiring the majority of our 2020 income tax payable. CapEx spend for the second quarter and first six months was $39 million and $87 million, respectively.

As George said earlier, we are matching the pace of our investment to overall macro trends and we now expect 2022 CapEx spend to be between $130 million and $160 million. This range includes projects in New York and Minnesota associated with pending close of the Goodness Growth acquisition.

Regarding taxes payable, we made a $37 million payment within the second quarter and have subsequently paid $14 million so far this quarter. As George mentioned earlier, we continue to efficiently manage our income tax payable line and continue to manage as a cheap source of capital and generally keep about a trailing 12- to 18-month balance outstanding.

I'd also like to add some clarity around the deferred tax liability. The bulk majority of this number is attributed to acquire license and technology, and we would only incur a true taxable event if we were to sell these assets. Essentially, that number represents our liability if we sold all acquired assets.

Lastly, we are quickly paying down our acquisition consideration payable. In Q2, we made cash payments of $33 million and have estimated cash payments of $14 million through the rest of 2022. I'm extremely confident that our strong financial standing will continue to allow for further reinvestment in the company to support future growth.

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

George Archos

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

Before opening the call to Q&A, I wanted to touch on the outlook for the remainder the year. I am extremely confident in the business we have built. While we have guided to a 40% margin in the past and though it's not out of the realm to achieve that this year, we do not feel it is prudent to reiterate that guidance due to the macroeconomic headwinds and uncertainties, which has impacted even the most mature industries.

However, we do believe that we can continue to operate at a premium from a margin perspective versus our peers. I want to leave you on this note: we have never been stronger from an operational and financial standpoint as a company. Our balance sheet is strong. Our cash flow is strong and we continue to reinvest in the company to drive long-term sustainable growth.

With that, operator, please open it up for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator instructions] Your first question comes from the line of Aaron Grey with Alliance Global Partners. Please go ahead.

Aaron Grey
Analyst, Alliance Global Partners Corp.

Q

Hi. Good morning. And thank you for the questions. So first question for me, just want to touch on New Jersey. Obviously, drove a good amount of the sequential growth there, seemed to be one of the better inventory stores in the early days. So [ph] let's give some further commentary on (00:22:35) where you stand right now on inventory for New Jersey, on how you view wholesale opportunities, particularly when you have Neptune still coming on. So your overall outlook for New Jersey and incremental sales growth opportunities [ph] for the remainder of the year would (00:22:50) be helpful. Thanks.

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

A

Hey, good morning, Aaron. Pleasure to have you today. New Jersey has been great for us. As far as inventory, we're well supplied. More importantly, we're adding additional SKUs almost on a weekly basis in multiple form factors. So we feel very comfortable with where we're at. Obviously, very excited about Neptune. That was a long time coming.

Very strong out of the gates. So it's been a whirlwind tour in Jersey. We went from the long regulatory delays to where we're at today, and we're very comfortable with where we're headed. We see good outlook in the wholesale side and on the retail side. And as the word gets out, sales continue to increase slowly. We're looking forward to more stores opening in the state, so we can supply them with our wholesale products and overall very positive.

Aaron Grey
Analyst, Alliance Global Partners Corp.

Q

Okay, great. [ph] Thanks for taking that (00:23:39) George. And second question for me, could you comment on the wholesale performance during the quarter? I know there had been some pressure there from Illinois in the past quarters. It seems like there's been some rebound there. And then kind of overall, as you kind of gave some color in terms of the CapEx for some key markets, such as Pennsylvania and cultivation expansion, we previously talked about [ph] inability (00:24:03) for you to start allowing some vertical integration of your own product being sold in stores [ph] and PA, been (00:24:08) offering a lot of opportunity for you.

So just given, we've seen some of your peers talk similar in terms of selling some of their – more of their own products within their stores amid pricing pressure. Can you speak to your own targets you might have in terms of vertical integration, your own brands being sold in stores, maybe new percentage targets you might have, or how you view that on a go-forward basis? Thank you.

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

A

I mean, vertical integration is an important component of the business. Obviously, we're very familiar with it having a 100% vertical business in Florida. In Illinois, [ph] we're capped as (00:24:39) how much vertical integration we can have here. In PA, the Verano launch has gone very well, both on the vertical side and on the wholesale side. So we're excited about the opportunity there.

Second quarter, there were some wholesale headwinds, but we're seeing incremental growth, not only in Q2 but going into Q3 here. It's been a nice [ph] trench up (00:24:59) for us, which is exciting. We rolled out the Essence brand. We have Savvy coming out here in pretty short order, which allow us to have form factors at different price points across the entire spectrum, which is an exciting opportunity for us on the vertical side.

We've always been known to just have the premium products. So now to be able to provide all those different SKUs at the different price points will allow us solid vertical integration in multiple markets. So it should be good for us in Q3 and moving into Q4.

On the CapEx side, we reiterated that we dropped CapEx in a couple of markets that we don't see transition to adult use as quickly as we saw it. So in PA, we slowed down construction there, finished the building and we'll phase out that facility when we see fit, but it puts us in a good position to be able to scale up quickly there when that time does come by completing that building.

Florida, same thing, second cultivation is online and we're doing all the work to be able to continue our footprint expansion there when needed. But for right now with the store account that we have and what's in the future pipeline, we're pretty well set. So there's no need to spend additional dollars there quickly. And that's something we evaluate on almost a weekly basis.

We're looking at the market, seeing what's happening, not only within our business but what's happening in the economy as a whole, and we adjust accordingly. So we're well capitalized with good cash flow and our projects will kick it back up when the time is right.

Aaron Grey
Analyst, Alliance Global Partners Corp.

Q

Okay, great. Thanks a lot for the detail. I'll jump back in the queue.

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

A

Thanks, Aaron.

Operator: Your next question comes from the line of Scott Fortune with ROTH Capital Partners. Please go ahead.

Scott Fortune
Analyst, ROTH Capital Partners LLC

Q

Yeah. Good morning and thanks for the questions here. You've been very active in introducing new brands like Savvy, like you mentioned on the value-oriented focus and many of – into many of the Verano's core markets here, along with Reserve and Essence. Can you provide a little color on kind of the initiatives? When do you expect to be fully rolled out on the offerings there and your national footprint relative to the full verticalization and just kind of the brand positioning as it affects kind of longer term gross margins as you look forward here?

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

A

First, good morning, Scott. Pleasure to have you again here today. As far as full rollout, it's kind of a loaded question. So each brand has multiple SKUs within it. So it'll be rolling out in waves. So we'll come up with flower, then vapes, then edibles, et cetera. So that Essence launch, it has happened in multiple markets, something that we've always said in the past. Even though we're rolling Savvy out in a handful of markets as well, it won't go everywhere immediately. And this is something that we scale out as we see fit.

So it will – by Q4, we'll have a lot more SKUs available in multiple markets, but they'll continue to go throughout the year and next year, we'll continue to launch additional SKUs. So again, we look at every market, what's happening, what's popular, what's not and we'll continue to increase our vertical integration with those products as well as our wholesale platform.

Scott Fortune
Analyst, ROTH Capital Partners LLC

Q

Got it. I appreciate the color. And then real quick, can you provide a little color on the margin profile? Obviously, with the macro environment a little bit challenging there, but you've made [ph] a line-based (00:28:12) investments in these last couple of quarters. Are you kind of seeing that slow down a little bit here, the [ph] spend (00:28:17)? But looking at the different operations, the different initiatives, you can continue to drive down those costs from that side. Kind of how do you look at the margin profile as you bring on more automation and the different operational cost savings from that standpoint going forward here?

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

A

So on the wholesale side, we'll see some efficiencies here throughout that back half of the year. The margin profile took a little bit of a hit in this quarter and it's very easily explainable. We had West Virginia, Massachusetts and Nevada cultivation come up [audio gap] (00:28:50-00:29:01)

Operator: Your next question comes from the line of Russell Stanley with Beacon Securities. Please go ahead.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Good morning, and thanks for taking my question. George, understanding your comments around EBITDA margins for the rest of 2022, but maybe looking beyond that with the investments that you've made in the rest of the business, do you think that the [ph] – all 40s (00:29:25) EBITDA margins are achievable in 2023 or on a two- to three-year basis? How are you thinking about your midterm margin targets at this point, please?

A

Hey, there. We – I think I got lost, George. This is [ph] Jacob (00:29:39) on the backup line.

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

A

Where did we leave off?

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Should I repeat the question?

A

Just take a picture [indiscernible] (00:30:03)

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Hello?

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

A

Hey, operator. We had some technical difficulties with the call. Can you confirm that you can hear us here?

Operator: Yes, we can hear you.

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

A

All right. And where did we leave off?

Operator: We have Russell Stanley with Beacon Securities asking a question.

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

A

Okay.

Operator: I'll get you to repeat that, please, Russell.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Sure. Thanks. George, I was following up in your comments around EBITDA margins for 2022 and I heard you loud and clear there. Just wondering if the [ph] low 40s (00:30:40), if you think those are achievable on a – are still achievable on a midterm basis, given the investments you've made in people and back office and so forth.

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

A

So we're not saying it's not achievable. We're just saying that right now, it's not prudent to be putting out margin profile with all the things that we're facing in the economy and with things going on today. So we're going to continue to be one of the best-in-class performers, but I think for right now, we're going to back off of the exact margin profile and continue to run our business accordingly.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Got it. And understand Florida, I guess, is one of the markets where your expectations for adult use have [ph] tempered (00:31:16), and of course we saw a legalization initiative recently launched there. Just wondering what your thoughts are on the initiative and it's [ph] always a passage (00:31:25). It sounds like you've got limited optimism there if we're reading it right. So just wondering what color you can provide on that.

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

A

It's not limited optimism. It's just reality check. There are things going on in the world today that we can't control. So, 2024 is a long time away and implementation is pretty far out. So for now, we're just looking at what's happening in the economy as a whole, and we just want to make sure that we're spending our capital wisely. And right now, we're set up with a very strong position in Florida.

On the medical side, we have a very good store pipeline coming up. The cultivation expansion went very well. We've also increased yield, which is part of the explanation of why we need to – we have the ability to be able to pull back on some of the expansion, but we're ready to expand when needed, right? We're set up with the second site, site plans all done, site work is there, building is there, power, water, et cetera, everything is needed. So we can quickly turn that back on when needed. Same thing with PA.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Got it. That's great. Thanks. I'll get back in queue.

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

A

Appreciate it, [ph] Russ (00:32:29).

Operator: Your next question comes from the line of Kenric Tyghe with ATB Capital Markets. Please go ahead.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thank you, and good morning. George, on Illinois, you called a share recovery, I think some 310 bps. Could you provide some insight on where you are today in the state in terms of your share levels and how much room there is not just to get back to perhaps where you were or where you would like to be, but also any indication there on sort of timelines and how we could expect that recovery [ph] to track (00:33:06)?

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

A

I mean, we've said this before. I mean, we've always had a very strong share in Illinois. We took a hit with kind of the expansion plan with the greenhouse, but that's back online. Quality is where it needs to be. It's inching up slowly on a monthly basis, but more importantly with the 185 licenses coming back online or finally coming online, I should say, we expect strong growth when those licenses open, right?

We have the SKUs, we have the credibility, we have everything we need to be able to come back in a strong way on the wholesale side. I won't put out exact numbers, but we're pretty confident when these stores open that we'll do very well here in Illinois.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thank you. And then George, just New York back in the headlines yesterday, one of your competitors electing to walk away from a deal there. How are you thinking about the evolution of that New York market, the timing of legalization and perhaps even the timing on your close of Goodness Growth today versus three or six months ago? Obviously, a lot of moving parts, but we're interested to hear your commentary on the New York market and the New York market dynamics.

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

A

Yeah, I mean, listen, very different assets and everyone makes their own decisions. We still think that New York is a very long-term viable market for us. We're positioned well there with the cultivation capacity, the stores. So we're excited about that opportunity. But for us, Goodness Growth is not only New York. And you know we look at New York as a good asset, but something I've always said is the jewel in that deal for us is Minnesota. That's the market we're really excited about and New York was kind of the cherry on top. So for us, we still view it the same way. Construction continues there. We're still doing everything with Goodness Growth to be able to get them ready for close and execute in a strong way, like we do everywhere else.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Cheers. Thanks, George. I'll get back in queue.

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

A

Thanks, Kenric.

Operator: Your next question comes from the line of Matt Bottomley with Canaccord Genuity. Please go ahead.

Matt Bottomley
Analyst, Canaccord Genuity Corp.

Q

Good morning, everyone. Hope you're all doing well. We talked a little bit about wholesale pricing pressures and this has been a bit of a theme with a lot of the MSOs that have reported so far, but just given – maybe if we just pivot to the retail portion of your business, given that about half of your stores are in Florida at the moment, is there any anecdotes you can give us with respect to what's been happening in that market? I know it's retail only. From a pricing standpoint or consumer preferences and how that's been tracking in sort of the recent quarters where we've seen headwinds in other markets. Just wanted to get sort of another temperature check on how Florida has been doing within this current environment.

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

A

Thanks, Matt. Good question. It's acting very similar to other markets. Basically what we're seeing here with what's going on in the economy today is a change in basket size to more premium products, to more value-oriented products. And that's the reasoning behind us launching Essence and now Savvy. So we have – we're competitive in all different categories. That's really what it's about for us.

Pricing pressure exists in every market, but it's not something that we're necessarily worried about. For us, it's making sure that we're competitive in all the different price points, which is something that we talked about last year, and we're just moving a little bit quicker this year based on what's happening in the economy. So we're excited to be able to compete with those different price points and making sure that we're efficient at it.

Matt Bottomley
Analyst, Canaccord Genuity Corp.

Q

Great. Got it. And then just my other question is Illinois related. So just for the sake of argument, if there was no friction or considerations within municipalities or any of these other regulatory things with opening up these 185 new stores, do you have any sense of what the overall population is out there of potential licensees that could fit the requirement of those stores? And if you think it's going to be sort of a longer pathway to ramping those up, just given that there's probably a bit of a limited more population out there, I'm just curious of what you – what you're anticipating with when those start becoming up for grabs.

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

A

So I don't know exactly how many are viable or not based on municipalities. I would say that I would anticipate that some of them start opening by year's end and they'll slowly start opening throughout next year. It's not that easy to get zoning and construction and go through different processes. A lot of these are first-time entrants to the market. So we're here to help as along as some of our other MSO participants.

But I don't think it's going to happen right away. I think – again, I think maybe we see some by year-end and slowly we'll start seeing openings, Q1, Q2 through waves next year. Again, we're really excited about it. I wouldn't want 185 to open all day one, probably not good for the market. You want to see them open up slowly, which I think that's what's going to happen and it'll be a positive for Illinois overall.

Matt Bottomley
Analyst, Canaccord Genuity Corp.

Q

Okay. Thanks again.

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

A

Thanks, Matt.

Operator: [Operator instructions] Your next question comes from the line of Andrew Semple with Echelon Capital Markets. Please go ahead.

Andrew Semple
Analyst, Echelon Wealth Partners, Inc.

Q

Hi there. Good morning. And thanks for taking my question. First one here, just want to ask on the SG&A step up we saw. Was that a first – sorry. Was that a full quarter contribution of the additional overhead you've added to the business or a partial quarter? What kind of proportion of kind of the overhead step up did we see in the Q2 results?

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

A

It's a full quarter. I mean there's a couple days where it's not, but I mean it's vast majority full quarter.

Andrew Semple
Analyst, Echelon Wealth Partners, Inc.

Q

Okay, great. And then, I just want to ask, with launching the Verano branded signature flower products across several core markets, have you seen any notable impact to demand or margins in the state when you launched these products? What sort of impact is this having at the store level in terms of financial performance and profitability?

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

A

Well, not having ever had these products before, we're seeing strong demand for it, which is exciting for us. Launching Essence has been a very positive outcome for us, and we're really excited about Savvy because again, although we've only traditionally had premium price products to be able to compete here, it's a positive for Verano and our consumers, especially with what's going on in the economy today. That's why it's pushed us to launch even quicker. And overall, we've become very efficient on the cultivation and production side. So we will see a little bit of a margin hit, but with the automation and efficiency that we created, I think some of that will get offset.

Andrew Semple
Analyst, Echelon Wealth Partners, Inc.

Q

Great. Thanks for taking my questions.

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

A

Appreciate it, Andrew. Have a good day.

Operator: Your next question comes from the line of Pablo Zuanic with Cantor Fitzgerald. Please go ahead.

Matthew Baker
Analyst, Cantor Fitzgerald

Q

Hi, this is Matthew Baker on for Pablo. Thank you for taking our questions. Can you talk about the market cadence in New Jersey? Yesterday, the state reported $80 million in rec sales from April 21 to the end of June after $24 million for the first 30 days, which implies close to double daily sales for the last 40 days versus the first 30. Any thoughts on those numbers and what about 3Q cadence so far versus 2Q? Thank you.

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

A

Good morning, [ph] Matthew (00:40:25). Thank you for the question. Like we said earlier, New Jersey has been very strong for us and we think that market is going to continue to grow. We look at it as a most likely a multibillion dollar market with 9 million people and very strong populations on its borders. So we're very excited about New Jersey. Getting Neptune open was a big positive outcome for us and we think there's a large wholesale opportunity as these new stores come online. So we think the cadence is going to be strong and will continue to increase for us.

Matthew Baker
Analyst, Cantor Fitzgerald

Q

And then for follow up, besides location, can you benchmark your stores versus New Jersey peers, whether on something like sales per store, SKU offerings, size or services? How do you think? I guess your stores in general just benchmark compared to peers and any color here would be very helpful. Thanks.

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

A

Yeah. The benchmarks I'm comfortable giving is all stores are located in very good high traffic locations with large parking lots, which is a very big deal for us to be able to put the throughput to the stores. Also, we have large POS counts at each store and we have large SKU variety because of the facility that we have, 120,000 square feet. We have multiple varieties of flower, multiple form factors, edibles, vapes, concentrates, tinctures, et cetera. So we feel very comfortable with our business there, both on the wholesale side and on the vertical integration side.

Matthew Baker
Analyst, Cantor Fitzgerald

Q

Got it. Thanks for the color.

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

A

Thank you.

Operator: Thank you. This concludes the question-and-answer session and concludes today's conference call. Thank you for joining us. You may now disconnect your lines.