10-Aug-2021

Ascend Wellness Holdings, Inc. (AAWH.CA)

Q2 2021 Earnings Call

CORPORATE PARTICIPANTS

Rebecca Conti Koar
Vice President-Investor Relations, Ascend Wellness Holdings, Inc.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

OTHER PARTICIPANTS

Russell Stanley
Analyst, Beacon Securities Ltd.

Bobby Burleson
Analyst, Canaccord Genuity LLC

Matthew Robert McGinley
Analyst, Needham & Co. LLC

Graeme Kreindler
Analyst, Eight Capital

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Jesse Pytlak
Analyst, Cormark Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good day and thank you for standing by. Welcome to Ascend Wellness Holdings Second Quarter 2021 Investors Call.

I'd now like to hand the conference over to your first speaker today, Rebecca Koar, Vice President of Investor Relations. Please go ahead.

Rebecca Conti Koar

Vice President-Investor Relations, Ascend Wellness Holdings, Inc.

Good afternoon and welcome to AWH's second quarter 2021 investor call. The presentation that accompanies this call can be found on our website, www.awholdings.com/investors.

Before we proceed, I would like to remind you that there are a number of risk factors and other cautionary statements contained in our SEC and SEDAR filings, including our 10-Q which we expect to file in the next week. We will not review those risk factors and other cautionary statements on this call. However, we encourage you to read them carefully.

Various remarks that we make on this call concerning expectations, predictions, plans and prospects constitute forward-looking statements. These forward-looking statements are subject to risks and uncertainties that may cause actual results to differ from historical or anticipated results. Any forward-looking statements reflect management's current view only and we undertake no obligation to revise or update such statements or to make additional forward-looking statements in the future.

During the [audio gap] (00:01:32-00:02:24)

Abner B. Kurtin

Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Operator?

Operator: Oh! My apologies.

Abner B. Kurtin

Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Did we lose sound? I'm not hearing anybody.

Operator: Yeah. We did just lose sound. I'm sorry. [audio gap] (00:02:39). I am hearing you now. Can you go ahead?

Abner B. Kurtin

Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Did Rebecca finish her remarks? I did not hear her.

Operator: Ms. Koar, do we still have you on the line? It seems we may have lost Ms. Koar.

Abner B. Kurtin

Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Okay. Well I'm just going to go ahead and if she has more to add, we'll get to it.

All right. Thanks everyone for joining the call this evening. The picture you see on the right here is of our Paramus area New Jersey store which opened in the quarter. This store is on heavily trafficked Route 17 by the Garden State Plaza Mall in Paramus and should be one of the highest volume stores in an adult-use New Jersey. The store is built to support the transition to adult-use we expect to see in New Jersey in early 2022.

As always, we appreciate the support from our loyal and committed investors who have helped us grow this business from three employees in 2018 to nearly 1,290 employees and operations in six limited license states across the country. This is an exciting time in the industry and particularly at Ascend. The momentum towards federal legalization is building, the market is in hyper growth and our customers are becoming more and more loyal and passionate about Ascend. One-by-one, the domino effect is benefiting the states as almost monthly another state legalizes either medical or adult-use cannabis consumption. Today, 19 states have fully legalized adult-use and 38 states have legalized medical-use consumption.

The most recent Gallup poll shows that 67% of Americans support cannabis legalization. This support is almost up over 3 times since the 1970s. For the most part, history has proven that for every major social issue in America after two-thirds of the country supports it, it eventually becomes federally legal and importantly mainstream. Estimates show that the US cannabis industry sales in 2020 were over $17 billion, a 40% increase over 2019. Some analyst projections predict industry legal sales will reach as much as $100 billion by 2030. The market is exploding and we believe we are well-positioned in leading states to capitalize on this exciting opportunity.

We are proud to share with you the highlights from Q2, our first full quarter as a public company. We remain committed to providing best-in-class disclosure. I will remind you that we are the first US cannabis SEC-registered IPO with Delaware governance and audited GAAP financials. We remain committed to good governance and transparency. With that, let's discuss the highlights from the quarter.

Since the end of Q1, we have opened three dispensaries bringing our total to 18. In addition to New Jersey, the second dispensary license we acquired through the Midway transaction became operational in Chicago Ridge, Illinois, increasing our total number of dispensaries in the Chicago area to four and our total in Illinois to eight. We are in process of rebranding all dispensaries to the Ascend name by the end of August.

On April 29, we opened our Boston flagship location which is the first retail location in the downtown of a major city on the East Coast. Our location is steps away from TD Garden and Faneuil Hall. Sales in this location continue to build despite downtown foot traffic being limited.

On the cultivation front, we added approximately 17,000 feet of canopy this quarter, bringing our total canopy to just under 100,000 square feet. We expect to bring online an additional 145,000 square feet by the end of the year, including expansions of our cultivation facilities as well as the addition of our new 120,000 foot greenhouse facility in Illinois.

In the quarter, we engaged Seaport Global Advisors as our bankers to assist us in refinancing our existing debt to lower the firm's cost of capital and provide additional cash to support investment. We expect to have an announcement soon. We currently have over $100 million of cash on the balance sheet and with this incremental debt raise; we will be fully funded to build out our current pipeline.

We also have significant updates on the product front. Last week, we launched our partnership with Lowell Smokes and now you can find Lowell pre-rolls on the shelf of our stores in Illinois. We are excited about this partnership as Lowell Smokes is the number one selling pre-roll in California and this is their first foray out-of-state. Also in Illinois, this month we launched Flower from our Ozone Reserve in-house top-shelf brand in all of our Illinois stores. This represents the culmination of the improvement of our cultivation team to produce best-in-class flower in the state.

On the M&A front, we are pleased to announce substantial progress in Ohio. We closed on our cultivation facility in Monroe, Ohio to add to our existing processing facility under construction. We also received approval for the acquisition of a dispensary in Carroll, Ohio and are moving to closing in the near future. We are excited about Ohio as it is one of the top medical markets with high potential to turn recreational in 2023. We expect to have more announcements about Ohio in the near future.

Lastly before moving on to financial highlights, I want to comment on our continued commitment to social justice. During the quarter, Ascend doubled down on our commitment to Last Prisoner Project. Following the early completion of our initial pledge made to the Last Prisoner Project, Ascend committed to a second pledge. Ascend retail locations currently ask customers to voluntarily donate $1 to LPP at checkout with a corporate match for each dollar donated up to $250,000 for a total of $500,000. This project is important to me personally. Social justice remains a top priority at Ascend as we continue to commit our time and resources as opportunities arise.

Let's discuss the financial highlights of the quarter. Total system revenue for the quarter was $97.5 million Net revenue which excludes intercompany sales was $83.4 million. On the top of the slide, you can see year-over-year net revenue which increased by $58 million or 228%. Quarter-over-quarter net revenue increased by $17.2 million or 26%. Revenue growth was driven by increases in cultivation and production activity, new store openings and heightened traffic at open stores. Just to remind you, this quarter represents the peak quarter-over-quarter growth of the year as the bulk of our 2020 openings have occurred at the end of this quarter.

Due to the strong performance in the quarter and improvements in both our retail and wholesale operations, we are raising revenue guidance for the full-year 2021 from $320 million to $340 million to $330 million to $350 million. We are pleased that we continue to execute in this hyper growth environment. Later in the presentation, I will turn it over to Dan Neville, our CFO, and he will dive deeper into the financials.

Let's talk about our footprint, as I have mentioned in the past we are primarily focused on flagship assets in limited license states east of the Rockies. We aim to have the best retail locations and have carefully curated our selection of assets. We continue our strong growth and currently have 18 dispensaries open and 90,000 square feet of canopy and a robust pipeline. Including the dispensaries set to open, we expect to have 26 dispensaries and 285,000 square feet of canopy by the end of next year. This just represents our fully licensed, fully financed and in-development pipeline. It does not include any additional assets or asset expansion and we fully expect to do more in the future.

We are pleased to develop such a robust portfolio assets in just three short years of operations.

So far this year, we've bought five dispensaries online. We plan to open four more early next year. We anticipate closing the transaction with MedMen New York by year-end which will provide us entry into the New York market. MedMen has four operating retail locations across the strait which are currently in New York's medical program including the flagship Manhattan location which is located on Fifth Avenue, just steps from Bryant Park. I will also note that most of the canopy we need to bring online is at existing cultivation sites. We believe canopy expansion has significantly less execution than greenfield projects.

Let's talk a little bit about more of the construction. I got a few pictures for you here with canopy expansions underway in Illinois, Mass, New Jersey and Michigan. The first picture on the upper-left is a drone image of our marquee Illinois cultivation facility. It provides us significant scale for our vertical operations in Illinois and we are one of the top wholesalers in the state. We currently have 55,000 feet of canopy in Illinois today and we will add 58,000 by the end of the year through the addition of our fully sealed greenhouse.

I like this picture because it really illustrates the scale of the operations. When we first took over, we inherited a 75,000-square foot building with a de minimis amount of canopy. Now, we have a fully built-out canopy, manufacturing and distribution center with another canopy expansion underway. Our Illinois facility is a blueprint for our cultivation expansions across all of our other states.

The next image on the top-right is a picture of seeds being planted in the first phase of our New Jersey cultivation facility. Around year-end, we expect to have the second phase of New Jersey expansion complete with additional canopy and processing capabilities. Our first phase of expansion began in April and is planting already. This shows our ability to move at lightning speed to take advantage of new adult-use markets. This was the playbook we used in Illinois and we are doing it again in New Jersey.

The image on the bottom-left is a new flower room that we recently added to our Massachusetts cultivation. While this project has been significantly delayed, we are finally in the final stages of construction. Tables and lights are being added and we expect to plant in October. And finally, the picture on the bottom-right is one of the flower rooms just before our first harvest in July at our Michigan facility.

Let's discuss our branding strategy. We continue to build our portfolio of brands. We have two in-house brands: One competes in the quality for value segment, Ozone; and the other is our higher-end brand, Ozone Reserve. We look to partner with West Coast brands to increase our product offering, particularly in the Best Category. In April, our Ozone brands brought in the second highest sales of any brand in the state of Illinois, above highly regarded brands like Rhythm, Verano and High Supply among others. The brand is developing a strong reputation in the market. We're continuously working to diversify our Ozone offering and provide all form factors to our customers. It is our strategy to deliver to every dispensary in Illinois every week and we believe this distribution strategy is a key part of our success.

Our brand partnerships provide Ascend with a unique opportunity to expand at high-end, key product categories and provide each of our stores with a variety of SKUs and form factors as well as consistent access to quality product. Our differentiated brand combined with our consumer-focused retail experience is paying off. Our stores are optimized at fast throughput, multiple points-of-sale and efficient layouts. We provide an exceptional digital experience with express pickup, curbside and delivery options. We have committed customers and we reward them through our loyalty program. Customer service is our priority.

Let's talk about our revenue and our revenue mix goals. Our adjusted gross margin and adjusted EBITDA margins for the quarter were 48% and 24% respectively. While we are comfortable with these strong margins, we think we can do substantially better over time through vertical integration and scale. There are four main drivers which will help us achieve these desirable margins: Increasing production capacity as we bring canopy online and we begin to harvest plants; continuing to add retail locations to achieve the maximum cap in each of our markets; optimizing product mix and finally reaching a more balanced retail wholesale revenue breakdown as well as carrying an appropriate amount of in-house and partnered brands in our own stores. By achieving these objectives we will gain scale, operating leverage and realize industry-leading margins.

We are moving towards the ambitious goal that 50% of our business comes from wholesale, 50% of our business from retail, and 50% of our products sold in our retail dispensaries across our network being our own in-house, Ozone, Ozone Reserve, and partner brands. Today, approximately 40% of our revenue is wholesale of roughly 35% of the products sold out of some dispensaries are AWH brands.

We want to give you some more insight into our M&A strategy. Both my CFO and I come from financial backgrounds. We were once in your shoes on the buy-side. As such, we are extremely judicious in how we allocate capital. We are acutely focused on return on invested capital and know that for every dollar we invest, we want make sure it is worth diluting our ownership in our existing portfolio of superior assets.

We have a disciplined two-prong M&A strategy: First, in keeping with our theme of going deep and not wide, our priority is to continue to expand in the states we are in and optimize and scale our existing footprint. While we have reached the regulatory cap in most of our states, we have room to expand from our eight retail licenses owned today in Illinois to the state cap. Our announcement today of Ohio acquisition shows our commitment to being a leader in that state. We would look to continue to expand in Ohio until we get to the five dispensary cap. We are committed to becoming a market leader in Massachusetts. And while we have a good start with our expansion of our cultivation facility, we are open to the possibility of expanding our cultivation, manufacturing and distribution capabilities through acquisition.

The second prong of our M&A strategy is to expand into other limited license adult-use or near adult-use markets. While we would focus on contiguous states east of the Rockies, we are also open to opportunities in other limited license states. At Ascend, we are opportunistic buyers, and if nothing meets our criteria, we are comfortable with our current portfolio.

On the topic of valuation, you have all noticed that the sector has traded lower over the quarter and many industry competitors traded significantly below target valuations and valuations of similarly growing companies in other industries. Even with that industry discount, AWH trades at a meaningfully lower valuation compared to some of the larger MSOs. AWH is trading at approximately 8.7x 2022 adjusted EBITDA estimates compared to the larger MSOs which were trading closer to 13.5x. Although these companies have much larger market share, AWH has premier assets in premier locations and we are positioned to operate and become leading players.

Before I turn it over to Dan, let me just reiterate the company's investment thesis which we've discussed with you in the past. We call ourselves MSO 2.0 because we are a company that didn't pursue a strategy of state applications but rather went out and actively bought what we believed to be the best portfolio of any MSO. We are now focused on building and scaling these attractive assets with intent to achieve scale before expanding to new opportunities. Within these markets, we are focused on premier asset flagship locations. As competition enters this business and states with limited caps, we strongly believe in the value and superior retail locations to create barriers-to-entry and long-term value creation.

We have a very disciplined capital allocation program and the bulk of our expansion has been fully funded through sale leasebacks and capital raise. We are not biting off more than we can chew and are very diligent with where we spend our money. We have successfully grown our portfolio through M&A and we see this as the fastest path to growth given the barriers-to-entry and regulatory environment. We have the team to succeed. Our management group is focused on executing and has already done so in Illinois. The team brings expertise from several areas spanning capital markets, cannabis industry, regulation and permitting, retail and more. The company has room for continued margin expansion with only about 30% of our cultivation assets generating revenue today. These are just a handful of the reasons why we are confident that Ascend is positioned to succeed.

Now, let me turn it over to my CFO, Dan Neville, to provide a detailed update on the financials this quarter.

Daniel Joseph Neville

Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

Thanks, Abner. Good evening everyone. Abner covered the revenue drivers earlier in the presentation, so for this slide I'll focus on adjusted gross profit and adjusted EBITDA. Adjusted gross profit dollars increased $7 million to $39.6 million or 22% sequentially, driven by Illinois wholesale production efficiency and retail stores coming online. This was partially offset by declines in Massachusetts wholesale.

Gross profit margin was 47.5% in the quarters, down approximately 170 basis points sequentially. This decline was driven by lower realized pricing and mass wholesale due to the bulk sale of lower testing product, partially offset by increased margins in Illinois. Unfortunately, we had some sick genetics that were brought into the building in Mass. We have since introduced new healthy strains that are achieving higher potencies but the old genetics are not completely flushed through our inventory yet.

Our adjusted EBITDA for Q2 was $20.3 million which represents an increase of $4.5 million or 28% sequentially. Our margin for Q2 was 24.4% which represents a 43-basis point increase sequentially. Despite our gross margin headwinds, we levered SG&A by 150 basis points quarter-on-quarter which allowed us to expand EBITDA margins.

As a reminder, approximately $6.1 million of rent expense is related to sale leasebacks that is accounted for above the line, the majority of which are in COGS. We have already built out the corporate infrastructure needed to run our assets and have centralized our overhead structure. This should allow us to continue to grow revenue faster than SG&A expenses.

Let's move on to discuss some of the key operating metrics for this quarter on slide 16. During the second quarter, AWH opened three dispensaries which brought the company total to 18 open dispensaries. Retail transactions in the quarter totaled 573,000 which is up from 146,000 last year and 411,000 last quarter. Average basket in the quarter was $101 which trended down quarter-on-quarter. We now have five cultivation sites online in five states with the closing of our Monroe, Ohio acquisition earlier in the quarter. In Q2, we sold approximately 11,000 pound equivalents of product at a very healthy average price per pound of approximately $3,600. Both of these metrics trended up for the company in aggregate.

Let's move on to slide 17 to dive deeper into the wholesale business. Gross wholesale revenue increased to $39.5 million, representing an increase of 30% sequentially, and that wholesale revenue which excludes intercompany sales increased to $25.4 million, representing an increase of 23% quarter-on-quarter. The increase was driven by increased output in pricing at the company's Illinois cultivation facility. Our pounds sold increased 28% quarter-on-quarter to [ph] 11,040 (00:22:54) pounds and our gross revenue per pound was $3,577. Pricing was up slightly quarter-over-quarter driven by an increase in pricing in Illinois, partially offset by declines in realized pricing in Mass due to the bulk sale of lower testing product.

Let's move to slide 18 to discuss the retail metrics for the quarter. Total retail revenue increased to $58 million, representing an increase of 28% sequentially. Retail transactions increased 39% quarter-over-quarter to 573,000. This was driven by an increase in transactions at our existing operations and the opening of three new stores within the quarter. Our revenue per transaction declined by 8.6% sequentially to approximately $101. This decline was driven by geographic and adult-use patient mix. In the quarter, we added two recreational dispensaries in urban locations which typically have a lower average ticket. Additionally, average tickets for medical customers are significantly higher than recreational. So as we serve more recreational customers over time, we expect our average ticket to tick down. Our annualized revenue per store was $13.9 million which was down 3% sequentially. However, I'd like to point out that this is a very healthy number, especially considering that we opened three new stores that we're still ramping over the course of the quarter.

Let's move on to slide 19 to discuss the increase in guidance. We are proud that our Q2 revenue growth came in above expectations and as a result we are increasing our full-year 2021 revenue guidance to a new range of $330 million to $350 million of net revenue. The new range represents a very healthy 130% to 144% growth over last year. We have line-of-sight to this new range as all of the assets required to achieve this revenue are already turned on.

While our revenue growth is impressive and our adjusted EBITDA dollar growth for the remainder of the year will follow, we don't anticipate significant margin expansion in Q3 and Q4. Instead, we expect moderate increases in margin due to a lower rate of sequential revenue growth for the remainder of the year and a ramp in wholesale expenses in Q3 and Q4. These expenses will support the planting and subsequent harvests out of our expanded cultivation footprint in early 2022.

As Abner mentioned, we have canopy expansions underway in Illinois, Mass, New Jersey and Michigan and expect to have approximately 235,000 square feet of canopy online by the end of 2021. These canopy expansions, combined with the additional stores we're bringing on around year end, will drive the next step-function change in revenue and margin expansion. Note that this guidance does not include the revenue associated with our pending transaction in New York.

Let's move on to slide 20 to discuss cash flow in the quarter and the state of the balance sheet. Before we dive in, I'd like to note that we are in the process of raising approximately $200 million of senior debt which will refinance our existing debt, fully fund our MedMen New York obligations and provide additional working capital to pursue M&A. We anticipate this will bring the average interest rate on our debt down significantly from our current rate. While there is no guarantee until we're closed, we're highly confident given where we are in the process.

On the top of the slide, you'll see a waterfall bridging to cash at the end of Q2. During the quarter, we increased cash by $41 million. We used approximately $4 million for operations and we invested $36 million in CapEx, the majority of which was used for cultivation expansions. Cash CapEx was elevated during the quarter due to a timing delay of a $14 million tenant improvement reimbursement that came in in early July. Finally, we received $86 million of net proceeds from the IPO. We continue to anticipate CapEx use of approximately $90 million for the full-year as we build out our cultivation expansions and continue to bring online stores in Massachusetts, New Jersey and Michigan. We ended the quarter with $104 million of cash and equivalents, $132 million of debt and net debt of $27 million.

In closing, this is a very exciting time at AWH and I'd like to personally thank all of the Ascenders across the organization for helping us get to where we are today. We're not done yet. And over the next 12 months we'll continue to be laser-focused on executing on our plans: Completing our cultivation expansions, opening the remaining dispensaries and taking the blueprint we've created in Illinois to our other markets.

With that, I'll turn it over to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions] Your first question comes from Russell Stanley from Beacon Securities. Please go ahead.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Good afternoon and thanks for taking my question. First with respect to the debt financing you're working towards, I understand you're looking for roughly $200 million. Just wondering if you can comment on what demand looks like and what the potential terms may come out of either what you're looking for there?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Hey Russ, thanks for the question. Yeah, we're looking to raise as I think Dan said about $200 million. The debt markets are very strong for cannabis-related securities. Obviously, while the rates are significantly lower than they have been in the past, we probably have an average cost of debt now close to 15%. And we're looking to bring that below 10% with this offering and this offering will be – basically represent all the debt of the company pro forma. We're in the closing process. And as Dan said, we got to get this done. But it's looking very, very strong now and we're very excited to work with this new group of debt investors.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

Great. Thanks for the color on that. Just a quick question around your cultivation expansion. So obviously a lot undergoing and we've heard more generally just issues; supply chain disruptions and challenges faced by various [indiscernible] (00:30:25) if anything really across US. Just wondering if you're seeing challenges on that front? And if so, how you're managing them and how you feel the schedule in that context?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

There's very little about cultivation builds that aren't challenging to be honest. I think the industry has done a good job. I think we've done a good job. But this is hard. I think in this current environment, it's hard to build any industrial facility. Supply chains are challenged. We have trouble getting building materials. Things get delayed. We rely on electrical utilities to bring us additional power; zoning, permitting, jobs. It's hard to get people to show up to work in a very difficult kind of construction environment and it's challenging.

With all that said, we're moving forward pretty close to target. I mean everything tends to get delayed in this industry by a little bit. But for the most part, when you look at our cultivation expansions as illustrated by that picture, you can see that in New Jersey our first expansion is planting. In Michigan, we're harvesting. In Mass, when you see fully built out rooms and you see they're putting in the tables and lights that's when you know you're really done. Until then, everyone can tell you that things are moving forward. But I want to see that interior picture of a fully built out room and lights in there and then I know we're ready for plants.

So I think we're in good shape. We have some – we have more – our second expansion in New Jersey is coming online. Additional expansions in Ohio and Michigan. But overall what's nice about our portfolio is we're in the later innings of this cultivation build. And so the certainty on timing, I said when we started in the very beginning, we were delayed years. Then we were delayed months. Now, we get delayed weeks. We're in the final process here and things are going well.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

That's great color. Thanks for that. And maybe if I could just sneak in a quick final question just around New Jersey and reading the local press see a number of local municipalities, some passing ordinances banning, at least temporarily anyway adult-use operations pending the final regs. Just wondering how you're situated and what that environment looks like in the three municipalities including Fort Lee which you intend to open later this year I believe. Just wondering how that environment looks for you now?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Yeah. Well, look I think you have to understand a little bit about the New Jersey process. The way New Jersey did it was that if you don't ban it by a certain date, I think it's this month you're automatically voted to opt in. What that did was that put pressure on the towns which weren't ready to pass an adult-use ordinance to ban.

But that ban for most of these – not for most but for some of the towns and certainly our towns really relates to giving those municipalities a chance to write a local ordinance the way they want. We feel very good about our prospects in all three locations: Montclair, we expect to – it basically is completed and we are looking forward to adult-use there. We're moving forward very aggressively in Rochelle Park; and we feel very good about Fort Lee. This is politics. This is local politics. Nothing is ever assured. But when we pick locations particularly in a state that we only have three locations, we pick these locations with an eye towards adult-use and with mayors and towns that are excited about those tax revenues. So nothing is ever assured but we feel very confident in all three towns.

Russell Stanley
Analyst, Beacon Securities Ltd.

Q

That's excellent. Thanks for the color. I'll get back in the queue.

Operator: Your next question comes from Bobby Burleson with Canaccord. Please go ahead.

Bobby Burleson
Analyst, Canaccord Genuity LLC

Q

All right. Thanks for taking my questions. So I guess the first one Abner would be with the news out of New York and it's been frustrating kind of a slow process there with moving forward on some of the legalization progress and with the governor resigning, with an incoming governor what are your thoughts there in terms of the calculus on how things play out? Is this a net positive in terms of how quickly we move forward from here or just any take on that would be helpful.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Thanks, Bobby. Was there news in New York today? I didn't know. No, just kidding. No. Everybody knows that New York has been a very frustrating market. I think while everyone's excited about it long-term and excited about the prospects of a market with 20 million people and very limited supply to be a really attractive market for the industry, it's been very slow going. And I think, even before you get into the problems of Governor, soon-to-be-former Governor Cuomo, even when he was kind of riding high, while he was pro cannabis he wasn't moving quickly and we all know that the Cannabis Board has yet to be seated and he didn't even move forward with whole flower as aggressively as hoped in the medical market. Then the state has gone into complete inaction as we've gone through this political drama. We do see it today as a very strong net positive. We see the ability of Albany to get back to work as being really important for this industry and this process. We believe the new Lieutenant Governor is very supportive of cannabis and we'll move very quickly to see the board and move forward.

That said, that's political, and my opinion is as good as anybody else's. But we definitely see this as a strong net positive. As someone going through the legal process to get our transaction approved, we're really excited about this move and our ability to work with the Department of Health and get this transaction closed.

Bobby Burleson
Analyst, Canaccord Genuity LLC

Q

Great. Thanks for that. Obviously 2022 has a lot of tailwinds from the cultivation you're bringing online in the second-half here. But in the second-half on a revenue basis hitting the guidance, just curious now that all your assets relative to that guidance are turned on, if you had to kind of rank your confidence level by geography or sales channel or what-have-you? How do you feel about tiering, what's contributing to you guys hitting the guidance here in the second-half?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

All right. Well, Dan and I aren't in the same room so I'll give you my answer and then I'll let Dan give it to you. I mean if you look at our guidance, if you look at what we did in the second quarter and you multiply that by four, we're sitting here on the run rate of our guidance for the year. So we're not really banking on significant growth to hit this – this target. We have the highest confidence I think that we've ever had in the near-term at AWH because these assets are on. And if you look back at Russ's question, the question is always when is it going to open? We played the when is it going to open game in Boston for about nine months. We've been delayed over a year in our Mass facility previously on the cultivation and others. And like others in the industry, this is just – this is part of doing business.

The fact that we have all our assets open right now is – really gives us a high confidence into outlook over the next six months, nine months. And then we have if you look at the pipeline slide, we have another wave of cultivation assets which – and some dispensaries that will really drive the next wave of growth. We always use the growth in our company as stair-steppy. We went through the stair-steps in 2021 and now we're going to kind of yield those results for the rest of the year. And now we've got to bring on the next set of assets, which are going to drive growth in 2022.

So I think that's kind of where we are. And I'd also say to remind you that when we look at our pipeline and our growth we're not building anything for M&A. No additional cultivation builds that we need and also New York is really not figuring in in most people's estimates. We view New York as a 2023 event. Therefore, 2022 has de minimis contribution from New York. So for all those reasons, you never want to be overconfident in a very difficult industry but we feel pretty good at where we are.

Dan, what are your thoughts on this year?

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Yeah. I'd just echo – I'd echo what Abner said. The assets are on. We're at a pretty healthy run rate today. We obviously do have a few minor openings in the balance of the year.

The Newton dispensary and some harvest out of Michigan and New Jersey that would hit before the end of the year. But we've kind of battle tested and put very unheroic assumptions around those assets. So we're pretty confident. We're very confident on the current performance of our assets today and achieving these results.

And I think Illinois is obviously the biggest driver here, right? But you continue to see robust growth out of that market. We're not banking on that for the remainder of the year but that tailwind continues to help us quarter-on-quarter and month-on-month.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Yeah. I mean I would just add Illinois has been a monster for us. We're so proud of that team out there. We were sitting here – if you were sitting here six or nine months ago on our call, we were looking to scale up that operation. We were looking to improve cultivation yields. We were looking to bring our kitchen online. And all those things have happened. We're achieving cultivation success. We're achieving manufacturing success. We're achieving distribution success. All of that indicates what we kind of have always thought that this industry is hard. You have to dial it in. But when you dial it in, it is really – it can be really successful. And I think you're seeing that with a lot of our competitors.

Everyone has states that they're struggling with in getting up to speed. But the better companies in the industry all have states that they're really killing it in. And for us that's Illinois.

Bobby Burleson
Analyst, Canaccord Genuity LLC

Q

Great. Thanks. I'll let somebody else ask some questions. Thanks for those answers.

Operator: Your next question comes from Matt McGinley with Needham. Please go ahead.

Matthew Robert McGinley
Analyst, Needham & Co. LLC

Q

Thank you. My first question is on the bulk sale revenue in Massachusetts. How much revenue was related to that lower testing flower in Massachusetts this quarter and how much of a gross margin impact did it have? And I think Dan said in his prepared remarks that you weren't completely through that inventory. So I'm curious that how much of an impact that could actually have into the third quarter?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

I'll let Dan answer that but let me just say on the macro question. This is, when you bring cultivation facilities online your initial set of genetics and your initial harvests are a bit of a crapshoot as you dial it in. In every one of our facilities and I would say for every company in the industry, no one is ever thrilled. Most people are not thrilled with their first harvest. So we got unlucky with a set of genetics that came in with some illness. And because of the timing, it takes three or four months to work through that.

But what's nice is that we're pretty much through the last harvest of really troubled product and everything that we see now is starting to test better, act better and we're rebuilding it. And we went through this in Illinois. So while we're never thrilled with something like this, we consider it kind of part of the business.

I'll let Dan answer the specific numbers on it.

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Yeah. So, Matt, it was a little over $1 million of product. To answer the second part of your question, what we have still in the vault and on the balance sheet today is about $350,000 worth of products. So while there's a little bit still that we have to flush through here, there's a lot lower – a lot less that we have left on the other side of this thing. So that kind of dimensionalizes where we're at. The overall impact on the margin side of things, so it's about 200 bps for the issues in Massachusetts.

Matthew Robert McGinley
Analyst, Needham & Co. LLC

Q

Okay. That's helpful. And thinking through the or [ph] taking in the (00:43:36) refi opportunity discussed but also thinking about your cash flow from ops, in this quarter you were fairly close to crossing over to positive and based on the revenue guide it looks like you would probably be positive in the back-half of the year and the working capital will be lumpy. But I mean do you think that you could be a cash flow positive in the back-half of the year?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Well, let me just – I'll turn it over to the Dan to go through this [indiscernible] (00:44:00) but once again I mean I think what's important is we are after-tax free cash flow positive significantly before expansion CapEx. And I think for any company we've all been doing this for a long time that's a good position to be in because every dollar that we're investing that puts us at negative overall cash flow is high-return capital to grow the business. So we like where we are and we like that the core business is essentially free cash flow positive. Dan, do you want to go through the timing?

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Yeah. So we should be in late-Q3 or early-Q4, we should be after-tax cash flow positive not accounting for the CapEx ramp – the CapEx spend that we have for these cultivation build-outs for the remainder of the year.

Matthew Robert McGinley
Analyst, Needham & Co. LLC

Q

Okay. That's great. Thank you very much.

Operator: Your next question comes from Graeme Kreindler with Eight Capital. Please go ahead.

Graeme Kreindler
Analyst, Eight Capital

Q

Hi. Good afternoon. And thank you for taking my question. I wanted to ask a follow-up regarding the comments made regarding M&A targets, particularly within new states. Looking at some of the targets that you laid out there, I'm just wondering do you have any sort of internal hurdle rates or do you look for businesses at a certain stage or lifecycle in terms of how that might fit in with the existing core business, what that might do to the financials? Just wondering if you get a bit more selective when you're looking at various greenfield opportunities? Thanks.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Thanks for the question. It's hard to – it's such a three-dimensional kind of matrix in terms of decision-making. It's hard to just give you – we have a quick answer to that. Certainly, when we bought our New Jersey asset, it was not profitable, didn't have a ton of revenue and we're really [ph] mining (00:45:55) assets and we were also taking a risk that adult-use didn't ever happen in New Jersey. So, very high discount rates but really high upside in the asset. When you get into a later-stage, existing adult-use market if we were to do something additional in Massachusetts for instance or if we were in a late-stage medical market, those are the things where we're looking to be really accretive pretty much immediately or in 2022.

So we're always looking for accretive acquisitions but I think you can get caught up in something it being accretive on a multiple basis but not accretive on a value basis. So we need to – it's great to do accretive acquisitions. We're looking to do some. We're talking to people that fall in that category but that isn't the only metric, right? We're looking at an industry just growing from $17 billion to $100 billion. There's plenty of upside for growth. There's plenty of assets that are underperforming and those can be tremendous pies opportunistically.

Also, you have to admit that we're not the only people out there looking for M&A, right? So the market has – is definitely more competitive now and we feel that we have a real competitive advantage in our existing states. And if you look at by going deep and not wide, when you look at we've done in Illinois and certainly what somebody like [indiscernible] (00:47:21) has done in Florida and Curaleaf in New Jersey, by getting significant market share you just drive huge profits in this industry. And that is something we would like to do in all our core markets. And so, in a lot of cases, our most accretive acquisition could be in our existing markets.

Graeme Kreindler
Analyst, Eight Capital

Q

Understood. Appreciate the color there. And then just as a quick follow-up in terms of what you're seeing in the private markets right now, are the valuations reflecting what we've seen in the public markets coming off the highs in February or is there a bit of a dislocation there as you're having these discussions? Thanks.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

There's a bit of a dislocation. I mean, look, the private market there's always an arbitrage between the private and public markets, so – but unfortunately when the public markets come down like they've had, you don't get that 20% or 30% reduction in private market values right away. And it's also a case-by-case basis. Forever in this industry, you have a lot of SSOs and smaller operators with stars in their eyes about either becoming MSOs or the high valuation of their assets. And that has really slowed down consolidation for us and a lot of other players. And that hasn't changed. But at the same time this industry is hard. People reach the level that they are capable of as operators and they see it's time that they can maybe create more value for themselves and their investors by partnering with somebody like us. We think that we have a very attractive stock. We're a company that kind of does what it says it's going to do, good people to work with that execute it. So we hope we're a good partner. There's a lot of memories in this industry on the private side of people who did deals with companies that had stock implosions. And so it's not just valuation. People want confidence in the stock that they're getting in the case that they're getting stock as well as the people involved. So those are all areas where we compete to get good deals and get attractive valuations.

Graeme Kreindler
Analyst, Eight Capital

Q

Okay. Thank you very much for that.

Operator: Your next question comes from Kendric (sic) [Kenric] (00:49:35) Tyghe from ATB Capital. Please go ahead. Kendric (sic) [Kenric] (00:49:45), your line is now open.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Sure. Apologies. Some technical difficulties. Good evening and thank you for taking my questions. Abner, just on Illinois and the capacity expansion there can you speak to or even just directionally provide any insights on how much more attractive either the yields will look through that expanded footprint and/or perhaps just speak to sort of what your expected margin profile could be that you would generate relative to what you're doing now in that much smaller footprint?

And then a follow-up question on Illinois and the capacity expansion there, as it relates to new resale licenses is it reasonable to assume that's part of what you've been building into here as you're sort of target of [ph] 113 (00:50:28) exiting the year is with a view to having room to support those additional new licenses as they come on through the lottery process in the second-half of next year?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Yeah. Let me take the macro point and turn it over to Dan on some of the specifics of the return on the greenhouse. Yeah, look Illinois has, what, just under 110 stores now with 14 million people. That's significantly under-stored, right? We – I think the industry is really excited about having additional stores. We're not worried about the competition. We're excited that customers are going to have more access to product and it creates a great opportunity for our wholesale market. That's clearly part of the thought process.

Secondly, we do see these licenses as potentially people we can partner with; to get our additional two licenses and get to 10 and we're having active discussions with people who have won the lottery or talking about it to partner with them in a way to become part of the Ascend family.

When we look at the greenhouse, we think the greenhouse can do similar results to the indoor. But as you know at greenhouse, we're looking – we're going to be a little bit more conservative. We're going to be – we're going to look for a little lower return and look for less flower and more product that's going to go into manufactured products and distillate. But we have a real shortage in our current facility in distillate. We've been very successful. And as a result, we need more biomass and we need more distillate. So this is product that's desperately needed for our existing business and [ph] has a home (00:52:17) right away.

Dan, you want to talk a little bit about the margin profile or give him a little...?

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Yeah. Sure. Yeah. So we don't really dive into margins on a state-by-state basis. But directionally I can kind of give a little bit of color. We do have a pretty substantial footprint today in Illinois. We have 55,000 square feet of canopy and then we're adding 58,000 square feet with the greenhouse. So it's – well, it's a significant expansion. We're not tripling our canopy or quintupling our canopy like we are in Massachusetts or New Jersey and leveraging that overhead.

With that being said, greenhouse it will obviously be a lower cost biomass. You don't have as much electricity related to that. And – but that will kind of be offset by the fact that we assume more of our product will go towards distillate products due to it being greenhouse product, although it will be fully conditioned and a sealed greenhouse.

I would say that we will be able to leverage our infrastructure that we have in place today at the very cultivation. So think the lab, we don't have to add any additional capacity at our lab. We don't have to add any capacity at our kitchen or with any of the automated equipment we use related to pre-rolls or flower [ph] bathing (00:53:51) so we can leverage that and leverage the capacity utilization there and that should be accretive to margins. And then the last point I would make directionally is that we are carrying the cost, not just in Illinois but across these expansions of the tenant improvements that we spent for these expansions within our sale leaseback today.

So we're paying full freight on the rent side of things to fund these build-outs. And that's included in the $6.1 million of rent that we paid in the quarter. Once we get production out of these facilities in Q1 that fixed cost along with the other fixed cost I talked about with the lab, kitchen and just overall management overhead should provide a nice bump in margins once we're productive out of that facility.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

And just to be clear that's a huge headwind to our business, right, because we only have 30% of our cultivation assets online. I mean if you were to look at most other industries, you'd be capitalizing the cost of additional projects until they start generating revenue. We're eating that full freight on rent. So that's why scale just immediately is so accretive to our bottom line as we bring this cultivation asset online.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thanks, Abner. I hear you and that's great color from you and Dan. [ph] If I just turn us (00:55:14) to a quick discussion on brand and related, you – interesting little exhibit there on your Ozone sort of positioning, particularly within the context of April. I'm just wondering recognizing those sort of ratings and rankings can be pretty noisy, is it safe to say that over time you're typically sort of puts-and-takes within that top five sort of grouping in Illinois? Could you provide any insight there as to how that sort of trended directionally and that's how you exited the quarter. And then just one further follow-up for me please.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Look, look, we're doing well. That was obviously a very favorable stat in April so we're happy to share it with you. I would say there's a number of great brands in Illinois and we're all kind of – Cresco is the biggest player not surprisingly; both the Cresco brand and the High Supply and others. After that on the wholesale side, GTI, well, we're ahead of Rhythm has other brands, but there's a bunch of us: Verano, ourselves and GTI are in that next group. Other players have great products but they don't have the canopy or the depth of market yet. They're building. They'll get there I assume but for right now it's a small group that a dispensary can say, look, I need you to fill my shelves every week and that's what we're trying to do for our dispensaries and for every dispensary, and that's been the contributor of our success; knowing if you as a customer can know that there's going to be a Flower pre-roll and a vape and a gummy delivered to your dispensary every week then you can be a great partner of that dispensary and we can do that at Illinois and we want to do that in all our states.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thanks, Abner. And just a quick final one, speaking of filling shelves. Does the cachet allow farms to create sort of demand, sort of – from natural demand pull [indiscernible] (00:57:11) a better way to put it of that product or what you need to be doing a big marketing push around Lowell, any sort of color on how you're going to get from here to there on Lowell. I mean we're familiar with the cachet obviously. But how does that cachet translates into shelf space in Illinois and how do you plan on driving that shelf space allocation for Lowell Farms?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Yeah. Well, I mean if you look at earlier states like Illinois and newly adult-use new stores, customers are clamoring for new products. I mean you see it when Incredibles and Mindy's launches new flavors. You see it. When GTI entered with Beboe, you saw it when we came to market with some Cookies product, the market responds really well to new products. It's just a matter of them then liking that product and holding onto it.

We're very bullish on the pre-roll segment. It is our biggest focus. When you look at the cannabis industry, only 20% of the people are buying pre-rolls. But when you look at the cigarette industry, 2% of the people roll their own cigarettes. So we see pre-rolls as the fastest-growing segment in the market for flower. We're very focused on it. And in order to do that, we want to bring in additional brands. Because we're not as focused on the best segment in the market, it makes us a natural player and partner for someone like Lowell because our Ozone and Ozone Reserve will play below that brand. And so we can use the cachet of Lowell to help build their brand at the top. And we can basically show the quality for value segment on the Ozone and Ozone Reserve.

That's why we think we're such a great partner. Look, we'd love to develop best brands. We are working on it but we also know there's some great brands out West and we'd love to partner with them as we think it goes great with the Ozone strategy.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thanks so much and congrats on the quarter.

Operator: Your final question...

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

I would also say – I would just also add that I think Lowell's category, which is multipack pre-rolls is an undersupplied category. They do a good job with it. But in general, the market does clamor for multipack pre-rolls. And so that is a segment that Ozone wants to fill on. I think Lowell does a tremendous job on the premium side.

Kenric Tyghe
Analyst, ATB Capital Markets, Inc.

Q

Thanks, Abner.

Operator: Your final question comes from Jesse Pytlak with Cormark Securities. Please go ahead.

Jesse Pytlak
Analyst, Cormark Securities, Inc.

Q

Hey. Good evening. Just on retail transactions. You had some very nice sequential growth and I'm just wondering if you can maybe elaborate a little bit on how much of that came from the new store openings versus just the higher throughput?

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

A

Thanks, Jesse. I'll turn that one over to Dan to give you the financial metrics.

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Yeah. Well, it's really hard to break that down I would say. I mean the vast majority of that would have come from new store openings. We did, despite only having three openings in the quarter we did open our Fairview Heights dispensary which is in Southern Illinois near St. Louis. That store came out of the gate very strong. That was not in the compare in – that was technically not a new opening but it opened in March 27. So that was a big contributor. So we have seen additional throughput through the dispensaries: Our Chicago acquisitions, the Boston dispensary has been ramping nicely as well but the vast majority is through the new openings.

Jesse Pytlak
Analyst, Cormark Securities, Inc.

Q

Okay. Understood. And then just switching to New Jersey, I'm just hearing kind of anecdotally [audio gap] (01:01:13-01:01:21)

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

Jesse, I think we...

Operator: Jesse, we've seen to have lost you.

Daniel Joseph Neville
Chief Financial Officer & Treasurer, Ascend Wellness Holdings, Inc.

A

I think you cut out.

Operator: Are you still there, Jesse? Oh, it looks like we've lost Jesse. There are no further questions at this time. Please proceed.

Abner B. Kurtin
Chairman, Founder & Chief Executive Officer, Ascend Wellness Holdings, Inc.

Yes. Look, thank you everybody for joining the call. We're very excited about what's going on. We continue to scale this business. It's hard but we're doing it and we're growing quickly and we look forward to speaking to you very shortly.

Operator: Thank you. Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a great day.