

IP Cannabis Show 2

Primary Trends and

What Makes for a Successful Cannabis Company

This is Investor Perspectives, I'm the host of Investor Connect, Hall T Martin, where we connect startups and investors for funding.

In our new Investor Perspectives series entitled "How to Solve the Cannabis Problem", you'll hear about primary trends and what makes for a successful company in the segment.

As the COVID pandemic passes, we emerge into a new world. The cannabis space is now undergoing tremendous change as we shift back to a normal way of life. Every state is reviewing its regulations and accelerating legalization across the board. We have investors and startup founders describe the changes coming up.

Our guests are:

William Muecke, Co-founder & Managing Director, Artemis Growth Partners, 00:56

Codie Sanchez, Managing Director, Entourage Effect Capital, 04:34

Michael Boniello, Managing Director, Poseidon Asset Management, 06:44

Sherri Haskell, Founder & CEO, Canna Angels LLC, 12:09

I hope you enjoy this episode.

Our first guest is William Muecke, Co-founder & Managing Director at Artemis Growth Partners. Artemis Growth Partners are a team of professional investors, operators, and advisors who have built and run successful, award-winning domestic and international impact funds. They started in cannabis in 2015, and since then have been working to bring the principles of ESG and impact investing to the cannabis industry on a global basis. William, thank you for joining us.

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[00:04:14] **Hall Martin:** So what do you see is the primary trend going forward here post pandemic?

[00:04:19] **William Muecke:** Well, I think that we kind of break it down into a couple of different markets. The trend overall is kind of up into the right, growth is continuing, deregulation is continuing, legalization and liberalization around cannabis laws worldwide is continuing. But the US market, I think, is almost a market unto itself; it really is the focus of what the future of a cannabis market can look like, where both medical and adult use products are sold side by side. So we see in some of the states, especially the limited license states in the Northeast, Midwest, and Mid Atlantic, is experiencing another kick up in growth as folks like New York legalize for adult use. And then here, I'm sitting in London, Europe only continues to move forward. I think there was a lot of early hype, in general, about cannabis, about where the markets would be today, and I think that Europe has demonstrated that the growth is significant. It may not be as high as it was three years ago, but the long term effect is, if the US is 300 million people, it's looking like a \$20 to \$40 billion market in the next year to two years. Europe is 750 million people as an addressable market starting with medical, and we see that Europe is really just opening up. So we're kind of three years behind perhaps the growth curve of America, but accelerating. And then you haven't even talked about what's happening in South America, Latin America, in general; and then Australia is open for medical, and even the Far East, is strangely, coming on. So it is a phenomenon that keeps on moving forward.

[00:05:58] **Hall Martin:** So what makes for a successful company in this segment at this time?

[00:06:04] **William Muecke:** That's a good question. I think one is obviously addressing the unmet need in the space, early on that was supplied just having cannabis plants to sell and being able to have what they call a seed to sale custody. So you could show that the growth of the plant is tracked all the way to the customer. That was one of the core competencies for delivering product to the medical patient, and then, ultimately, to the end market consumer and the adult use side. But now, it's really down to version 2.0, or maybe even 3.0, which is not just cultivation, it's where is cannabis going tomorrow. So tissue culture, genetics, all those plan to the importance of building up frankly, a better supply chain, as well as new product categories, like edibles and different versions of how you consume cannabis. And ultimately, into pharma – I think that there was a very notable transaction recently, which was Jazz Pharmaceuticals, a traditional specialty pharma company, paying \$7.2 billion for GW Pharma.

GW Pharma, its entire pipeline is based on the cannabis plant. And so, you're now starting to see the crossover of pharma, really it's biotech pharma, but specialty pharma, into cannabis as well. And so, it's starting with the core components of any market, good team, an unmet need, but now the iteration is going, what is the next evolution and that's better genetics into better products, and ultimately better medicines to treat the chronic pain and other categories that are coming up in cannabis.

Our next guest is Codie Sanchez, Managing Director at Entourage Effect Capital. Entourage Effect Capital is a private cannabis fund disrupting the rapidly evolving cannabis industry. EEC's mission is to actively leverage their sector and investment experience, networks, and investment process, and to identify, invest and accelerate high-quality emerging growth companies. Codie, thank you for joining us.

[00:17:27] **Hall Martin:** So what's the primary trend in the segment today?

[00:17:32] **Codie Sanchez:** Well, besides legalization, I mean, I think the companies are moving towards actual profitability now and we invest in companies, you know, there's really no company in the industry that has more than a couple of 100 million dollars in revenue, so the industry is still nascent. There are quite a few companies that are now unicorns worth billion plus in the space, but this is all new, developments, over the last, I would say, two years, three years. And so, cannabis is sort of getting into its teenage years from coming out of its very early stages.

[00:18:03] **Hall Martin:** And so what makes for a successful company in the cannabis space today?

[00:18:09] **Codie Sanchez:** What we look for in a successful company is a couple of things. One, the company needs to be profitable, so we're very close to or a path to profitability. So we can actually see that this is a stiff, sustainable company, unless it is an add-on to one of our other portfolio companies that we have, which we do plenty of those. Also, the company needs to have some sort of moat built around it, because there will be commodification and there already has been in this industry, so you want companies that can survive when a lot of big players come in and survive after the cost of the product, because it is a commodity at the end of the day, it's a plant, starts to come down, and there isn't as much margin in there, you want them to be able to survive that. And in tandem, I think you want a company that is starting to understand if they're a B2C company that's really starting to understand branding and how to distribute; and if they're B2B, that is very tight on their logistics and supply chain, because a lot of cannabis companies, since they have such huge margins, I mean, we're talking sometimes 80% margins, they have maybe been a little bit lenient, historically, and you're going to want that tightened up quite a bit now.

Our next guest is Michael Boniello, Managing Director at Poseidon Asset Management. Poseidon Asset Management was founded by siblings Emily & Morgan Paxhia in 2013, making their first fund one of the longest-running dedicated cannabis investment funds. The Poseidon team has focused on a diversified strategy covering a range of company stages and industry subsectors across the capital spectrum. Now in the eighth year of conducting due diligence, deploying capital, and serving on multiple company boards of directors, the team is considered a leader in the cannabis industry. Michael, thank you for joining us.

[00:08:21] **Hall Martin:** As we come out of COVID, what do you think is the primary trend we'll see in the sector at this stage?

[00:08:28] **Michael Boniello:** Sure. I think the trend of more legalization and across state markets will see new states, and with new states come new customers. And during COVID, the industry was really validated by being named an essential business in almost every single state that there was a medical or adult use legalization. The only state that hit the brakes when COVID first started was Massachusetts shut down the adult use market for about a month and then opened it back up. And we saw a lot of growth in both the cannabis and CBD markets over that time period, a lot of it had to do with people looking for alternative medications, for wellness around things like sleep disorders, around stress, around anxiety. And with everything going on in COVID, a lot of people had a lot of those things in 2020, and what we saw was a lot of new consumers coming into the industry, and so we're going to see more of that. I think we'll start to see some federal regulations coming down the pike here. I don't think we'll have federal legalization anytime soon, but I think we'll start to see things like banking and tax reform and social equity programs rolled out at the federal level. So a lot to come for the industry, a lot of opportunity.

[00:09:49] **Hall Martin:** So what makes for a successful company in the cannabis space today?

[00:09:54] **Michael Boniello:** Great question. So a lot of that has to do with what makes for successful companies in traditional industries, and the first and foremost thing around that is the people, and when we invest in companies, sure, we are investing in a product or a service, but what it really comes down to for us as investors is the people that we're working with. We are looking for people that not only understand the industry today, but understand where the industry is going and maybe _____ understand the timeline of the history, in that, regulations and laws don't change overnight. There's a long process for these things, and so you have to have realistic expectations around your growth and around what the regulators are doing; and I say that, because if you're going to make a bet that there's going to be federal legalization in the next 12 months, I hope that happens; but if it doesn't happen, and you've made a bet around that, the company might be in trouble. So not making major bets around regulations, being prudent around your spending, you know, in this industry, 2020 was a defining period, in terms of separating the haves and the have-nots in terms of companies. And we see the companies that excelled in 2020, and got to a point a lot of the – a number of them

got to a point of being profitable. What they've been doing since their inception is focusing on prudent spending and on executing their business plan, and not getting over their skis, not trying to jump into five states at the same time – we don't have economies of scale in this industry, every state has its own economy – having focus to build out your core business, and then growing that business from there, rather than raising \$50 or \$100 million and spending it all in six to 12 months, which we've seen, and buying assets in every state. It comes down to being able to execute on that.

The other thing I think is businesses who really understand the product and the consumer, there's a lot of similarities to the alcohol industry in this business, but cannabis is not alcohol, it's a very different product. We've seen a lot of brands in the cannabis industry that have failed over the years, because you have to think of cannabis a little bit differently than alcohol. Personally, I enjoy good IPA, and when I'm drinking an IPA, I drink it for flavor, quality. But no matter what IPA drink, I'm probably going to have a very similar effect in terms of the alcohol other than, you know, one having a lot more alcohol content than the other. It's not the same when you're talking about cannabis products, because cannabis products, you have to think more of a pharmaceutical side of things where they affect everyone differently. And so, when I see a brand come out and the brand, they maybe have a celebrity behind it, and it's great packaging, I won't hesitate to try the product. But if the product doesn't have a good effect, no matter how much I love the packaging and love the brand, I'm moving on to a different strain, and that's one of the challenges. I think that's one of the challenges when people have tried to build brands in this industry and looked at other industries in replicating those models. The product itself just has a very different effect on every customer, and we're seeing more and more mature customers shopping based on strains, based on terpenes, rather than based on the brand itself, not to say that there aren't going to be brands and the Coca-Colas cannabis, that's definitely coming down the pike, but it's going to be a different pathway than other consumer branded products.

Our final guest is Sherri Haskell, founder & CEO at Canna Angels. Canna Angels is the leading angel investment consortium dedicated to the cannabis industry in the U.S. They are in their 5th year with over 50 stellar companies in their portfolio. With 5 exits (four as acquisitions, one as public issue to the CSE) in less than three years, their track record of identifying rising stars is solid. Sherri, thank you for joining us.

[00:06:07] **Hall Martin:** During the pandemic, we saw cannabis listed as an essential service and saw a lot of growth. And now that we're coming out of COVID, and the pandemic, what do you think is the primary trend going forward?

[00:06:24] **Sherri Haskell:** Well, when you are asking me for primary trend, are we talking about capital markets, are we talking about products? Are we talking about innovations with regard to

capital markets, which is very much my area? That's the sandbox that I play in – go ahead, what you're going to...

[00:06:40] **Hall Martin:** Yeah, let's talk about the capital markets.

[00:06:42] **Sherri Haskell:** Okay. So if you're an investor listening to this, tuning in, as far as capital markets, there are a number of different things that we're seeing. Let's talk first about how the private entities are becoming stronger. The private markets are becoming stronger; they're getting more recognition because the industry is getting more recognition. Even though on a legal, federal basis, cannabis is still federally illegal, that actually gives the privates a bit of opportunity, believe it or not, because the privates now are more open to individual investor investment, we're seeing greater value and opportunity within those private markets. On the public markets, what we're seeing is massive M&A, massive deals, massive transactions; we're seeing these weekly, almost daily. And it is really funny, because a few years ago, when Canna Angels was launching and getting, we were so excited if we would see any kind of institution stepping up to the industry. Every time we would see a venture capital make a play in the industry or something like that, we would make a big note to our investors and a big announcement to our investors, it was very exciting. Now, we're seeing conglomerates, one massive MSO actually buying another MSO, and these are on the public market. So there's a lot of activity, it's going to bode very, very well for our industry.

[00:08:18] **Hall Martin:** Well, great. So what makes for a successful company in this segment – you talked a little bit about that already, but can you go into more detail, like, what specifically about the infrastructure companies make it a good fit?

[00:08:31] **Sherri Haskell:** You know how this is, I've been in the financial markets for decades, won't tell you how many, and it really comes down to the same _____ formula. I mean, once you've got a company that has a good structure, a good foundation, it is almost always up to the performance of the team. You can have a great product. You can have a great technology. And we've seen this before in the tech sectors, but if you don't have a stellar team that can execute on that mission or on that business model, it's going to fail. So it always comes down to the team. What we're seeing more in a startup environment, which is a lot where I am very, very active, the developmental stage companies, what we're seeing now is an integration of legacy players in the industry that are partnering with veteran financial people, that can bring sophistication and experience to the table. And when you've got a good combination, such as we have found in a few of the companies that we've worked with, it's sort of off to the races as long as the egos can get out of the way.