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Cresco Labs Inc. CNSX:CL

Earnings Call

Thursday, August 8, 2024 1:30 PM GMT

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Presentation

Operator

Good day, and welcome to Cresco Labs' Second Quarter 2024 Earnings Conference Call. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the call over to TJ Cole, Senior Vice President, Corporate Development and Investor Relations for Cresco Labs. Please go ahead.

TJ Cole

Thank you. Good morning, and welcome to Cresco Labs' Second Quarter 2024 Earnings Conference Call.

On the call today, we have Chief Executive Officer and Co-Founder, Charles Bachtell; Chief Financial Officer, Dennis Olis; and President, Greg Butler, who will be available for the Q&A.

Prior to this call, we issued our second quarter earnings press release, which has been filed on SEDAR and is available on our Investor Relations website. These preliminary results for the second quarter of 2024 are provided prior to completion of all internal and external reviews and therefore, are subject to adjustment until the filing of the company's quarterly financial statements. We plan to file our corresponding financial statements and MD&A for the quarter ended June 30, 2024, on SEDAR and EDGAR.

Before we begin, I want to remind you that statements made on today's call may contain forward-looking information. Actual results may differ materially. The risks, uncertainties and other factors that could influence actual results are described in our earnings press release and in the MD&A filed with the securities regulators. This call also contains non-GAAP measures, also outlined in our earnings press release and in the MD&A filed with the securities regulators. Please also note that all financial information on today's call is presented in U.S. dollars, and all interim financial information is unaudited.

With that, I'll turn the call over to Charlie.

Charles Bachtell
Co-Founder, CEO & Director

Good morning, everyone, and thank you for joining us on the call today.

I'm pleased to walk you through our Q2 results and demonstrate the sustainability of the improvements we've made to the business over the past year. We entered this quarter building on the strong foundation we've developed and with growing momentum in the industry. The DEA's comment period on rescheduling recently closed with roughly 92% of the over 40,000 comments submitted in overwhelming support of reclassifying cannabis to a Schedule III substance or declassifying cannabis entirely. Recent polls also show energy swelling around Florida's Amendment 3 initiatives to legalize cannabis for adult-use this November.

As the pace of reform challenges, even the most patient of us, it's important for all stakeholders to remember that cannabis reform consistently pulls higher than any candidate in any election, and the public has made it clear that it's time for change. Reform is imminent, and we are ready. Our Q2 results show how strengthening our core and emphasizing free cash flow are laying the groundwork for profitable growth and strategic positioning for the transformational catalysts ahead.

In the quarter, we generated $184 million in revenue at a 52% adjusted gross profit margin and a 29% adjusted EBITDA margin. Year-over-year, we generated a 565 basis point improvement on our adjusted gross profit margin and removed approximately $34 million in annualized adjusted SG&A spend. Our consistent focus on margin expansion enabled us to deliver $54 million in adjusted EBITDA, up $13 million year-over-year. And finally, we generated $54 million in operating cash flow year-to-date, which is $32 million more than the first half of last year. This, combined with our revised tax strategy that Dennis will cover later in the call, will allow us to continue to strengthen our balance sheet and enable strategic capital deployment to support future growth.

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Cresco Labs is creating the financial profile and perfecting the playbook we need to win. Our branded product and retail portfolio performance are evidence of our differentiated capabilities. We consistently outperform our markets, maintaining leading share positions in the largest markets like Illinois, Pennsylvania and Massachusetts and gaining share in some of the most competitive markets like Florida. Our unique skill set and financial discipline have enabled us to drive scale and improve margins as we look towards new markets to replicate our winning strategy.

Now, I'm going to share more on the 3 pillars we're executing against to create the strongest and most valuable Cresco Labs for the years to come. Number one, we're ensuring we have the most strategic footprint. We're strengthening our positions in Ohio, Pennsylvania and Florida, the 3 largest likely near-term catalysts in our industry that will drive significant growth in the years to come. Adult-use sales officially launched earlier this week in Ohio, and it's been energizing to be a part of another major milestone for cannabis. The seventh most populated state in the country will be another example of a responsible, respectable and robust legal cannabis program.

I want to thank Ohio's division of cannabis control for working so hard to design a program that's going to bring incredible value to their state and opportunities for their residents. I also can't say enough about the Cresco team, manages all the complexities of this conversion with grace and expertise. We're already seeing some of the impact from recent cultivation upgrades we've made in Ohio, including a 26% increase in yield per square foot and a 23% increase in average potency as we drive full utilization of our canopy. This will allow us to meet the increased adult-use demand, while still maintaining our existing supply to serve medical patients and wholesale customers.

Our next project is to expand Sunnyside's reach by opening our 3 additional dispensaries in Ohio. Kudos to our real estate team who've already identified sites that will complement our existing leading retail portfolio in the state. In Pennsylvania, there's a lot of momentum behind bipartisan adult-use legislation, and we see a path to legalization as lawmakers reconvene this fall. In the meantime, we're deepening our #1 position in the state through smart capital allocation.

In addition to the upgrades to cultivation we talked about last quarter, we just expanded our dispensary operations by acquiring 2 existing locations and the ability to open one additional dispensary. With the nominal impact in Q2, this is an incremental non-material investment that will have a high ROI. We see a clear pathway to unlock strategic value as we convert these stores to the Sunnyside platform, optimize operations and ramp-up on potential adult-use legalization.

In Florida, we've more than doubled revenue year-over-year as we continue flexing every muscle to improve edible and vape throughput, increased potency and maximize cultivation yields. We're currently executing an expansion plan to support the growing demand for our products under the state's medical program, with additional plans that we can turn on if the adult-use is legalized in November. We're focused on making smart investments in these markets, where our strong retail and wholesale capabilities could add value quickly.

Over the last few quarters, we've used the capital-efficient approach to add more Sunnyside dispensaries and increase cultivation capacity. We're preparing to scale up strategically so that we're capturing maximum share, while generating high returns on our investments, regardless of where each of these state adult-use regulations land. Number two, we remain the leader in branded wholesale products. We continue perfecting our branded product playbook, enabling us to beat out competitors and hold the #1 overall share position in Illinois, Pennsylvania and Massachusetts. For BDSA, we also have top portfolio positions nationally in branded flower, concentrates, vapes and edibles.

As we discussed last quarter, continuous improvement in portfolio evaluation are foundational to that playbook. For instance, to maintain the strong growth we've seen in the pre-roll category, we've been diligently testing new processes and technology to increase productivity and margins. The early results are promising with a 10x increase in throughput. This is a good example of how we're leveraging our scale to test new processes in one state before rolling them out across our footprint to capture the benefits of large buying power. We're also creating tailored wholesale plans to adapt to continued retail fragmentation across the industry. In markets like Massachusetts, we're exercising discipline and finding the right retail

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partners to invest in, going deeper with our highest value accounts, while reducing exposure to non-performing accounts to preserve top line while also protecting margin.

In markets like Illinois, we're getting our products on every new shelf and expanding our points of distribution, while keeping our menu depth and introducing new innovations and forms, flavors and strains. Our focus on providing innovative products at the highest quality while constantly finding efficiencies in our cost structure continues to deliver one of the strongest cannabis portfolios in the industry.

And number three, we're building a highly productive retail portfolio in the most strategic states. In Q2, we increased our index to fair share across our markets, with Sunnyside performing 36% better than comparable dispensaries. In fact, we're outperforming average fair share in almost all of our markets, with our fair share in Florida consistently making gains and growing more competitive every quarter. We're more than twice as productive in some of our most important states, and we're expecting even more fair share improvement across our footprint in the quarters ahead.

Last quarter, we talked about how our tech capabilities contribute to our market-winning results, but in-store optimization is another important lever we pull. We continue to refine our assortment and display of accessories in non-cannabis products, ensuring we're meeting consumer trends while maximizing every inch of our dispensaries. Over the last year, we've increased non-cannabis revenue in our stores by 9%. We're also constantly evolving our approach to customer engagement. We're complementing the e-commerce tactics covered last quarter with a unique push marketing strategy.

We're leveraging the sunnyside.shop platform, customer segmentation and purchase history to create targeted high ROI campaigns. In trialing this method, customers we've targeted are making more repeat purchases and have increased average monthly spending by 20%. We have a proven track record of generating above-average retail productivity across our markets, thanks to repeatable operating procedures, a proprietary tech stack, and the team's collective dedication to continuous improvement. These capabilities will continue to be invaluable as we ramp up additional dispensaries to meet Sunnyside standards in the months ahead.

In closing, our strategy is simple; win in strategic markets with a brand portfolio consumers love and best-in-class retail operations. And we'll continue making smart investments to strategically target new growth markets where these established capabilities will help us generate premium returns.

With that, I'll turn it over to Dennis to provide more details on our Q2 performance.

Dennis M. Olis
Chief Financial Officer

Thank you, Charlie, and good morning, everyone.

We continue to demonstrate that the changes we've made in the last year and our improved profitability are sustainable. The increased cash flow we're generating, along with the normalized taxes will allow us to strengthen our balance sheet, increase our footprint and invest in strategic growth opportunities to drive our results in the years to come. In the quarter, we generated $184 million in revenue while generating more gross profit. Our operations team continued to impress, finding incremental improvements to lower cost of goods and increased gross profit, even in an environment that is inflationary for cost and deflationary for cannabis pricing.

We increased absolute adjusted gross profit to $97 million and adjusted gross margin of 52%. That represents a 565 basis point improvement year-over-year. We've continued to maintain strong cost controls across the organization, with adjusted SG&A as a percentage of revenue at 29%, a 229 basis point improvement from last year. We had a small increase sequentially in absolute adjusted SG&A to support and maximize the opportunity of the adult-use conversion in Ohio and the 2 additional stores acquired in Pennsylvania.

Q2 adjusted EBITDA was $54 million or 29% of revenue, up 33% year-over-year. This is our third consecutive quarter generating over $50 million of adjusted EBITDA. This consistency demonstrates the

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sustainability of the actions we took last year. Our Ohio going adult-use and the potential conversions in Florida and Pennsylvania, we can support much higher revenue and generate significant operating leverage on our current cost structure. In Q2, we generated $18 million in operating cash flow and $11 million in positive free cash flow as we paid our semi-annual interest payments.

At $54 million for the first 6 months of the year, we've generated more than double the amount of cash we did in the same period last year. We're going to put this cash to use by strengthening the balance sheet, investing in our core growth states and pursuing strategic growth opportunities. We spent $6 million on CapEx during Q2. We expect to spend between $40 million to $60 million for the full year, inclusive of upgrades already made to our Ohio cultivation and production facility, as well as expansion in Pennsylvania and Florida in advance of potential adult-use.

2024 has developed much as we expected, and we are maintaining the expectations we set on our Q4 call and reiterated in Q1. We expect Q3 revenue to be relatively flat compared to Q2, with the late start of adult-use in Ohio and limited initial incremental supply and new form factors. We expect it to start contributing growth in Q4. We're looking forward to Ohio's adult-use conversion and the anticipated conversion in Florida and Pennsylvania to generate significant year-over-year growth in both 2025 and 2026.

Strategically, we are targeting to keep gross margins around 50%, as we believe that's an appropriate operating structure for our business. Having said that, there can be quarterly variability driven by price pressures, revenue composition by state and portfolio mix. We expect to maintain SG&A as a percentage of revenue consistent with Q2. As we've talked about previously and delivered through the first half of the year, operating cash flow will be significantly higher than last year. On a quarterly basis, like in Q2, Q4 will have lower cash flow because of our semi-annual interest payments.

Regarding taxes, we intend to file as a normal business for 2023 and beyond. This new position will result in estimated tax savings of $65 million in 2024, directly impacting our cash flow and bolstering our balance sheet. For the time being, a corresponding uncertain tax position or UTP, relating to these tax savings will be recorded on the balance sheet. We have worked closely with our expert advisers to be incredibly thoughtful in how we designed this approach. We're comfortable with our read on Section 280E and its implications.

As a result of the new tax position and our corporate structure, a step-up to fair market value in the company's tax receivable agreement liability has been recorded in our financial statements. Most of the assets being stepped up to fair market value will be amortized over 15 years, effectively decreasing our annual tax expense by a corresponding amount over that period, creating a net neutral impact. This one-time charge is reflected in the other expense line in our income statement this quarter. Our 2024 results so far show how our focus on the core and prioritization of free cash flow are laying the groundwork for profitable growth for years to come.

With that, I'll pass it back to Charlie.

Charles Bachtell
Co-Founder, CEO & Director

There are exciting and meaningful legislative shifts on the horizon, and the public has never been louder with their support for cannabis. We've reached a tipping point, with almost half of all states in the country representing more than half the country's population, having legalized cannabis for adult-use and more adopting common sense regulations every day.

Still, while we're encouraged by plans for rescheduling and adult-use conversions, we're putting our energy and resources into building a growth business that's designed for sustainable success regardless of what happens legislatively. We continue to prove out our strategy in every state we operate in, maintaining and gaining share in some of the country's largest and most competitive markets. We're leaning into our improved operating cash flow and profitability to seize on our business' momentum. This means making smart, high ROI investments in our core markets, reinforcing the capabilities and infrastructure needed to win in states with adult-use potential and exploring accretive incremental M&A

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and new business opportunities. A big thank you, and congratulations to the Cresco team on producing a great quarter.
And with that, I'll open the call for questions.

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Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Aaron Grey with Alliance Global Partners.

Remington Smith

This is Remy Smith on for Aaron Grey. My first question in regards to your gross margin. It remains healthy with 4Q -- 4 quarters about 50%, 52% in the Q. I know you kind of touched on -- you expected to remain around 50% in 2H. But just seeing if you could provide some more color on, if there's any additional margin improvements. I mean, you said you made a number of efficiency gains. You'll get a little bit of benefit from Ohio adult-use, but there seem to be some pricing pressure in the market. Just wanted to see if you could provide a little bit more color on the 52% gross margin this quarter and how you think about it on the back half of the year?

Charles Bachtell
Co-Founder, CEO & Director

This is Charlie. I'll start, and then Dennis will add some more color. But really, really pleased with the team's execution in the quarter and managing the puts and takes that are inherent across the industry and our footprints. And so it's really active management of the business that produces the gross profit margins that you've been seeing from us over the last few quarters, and it's the same approach that we'll take in the quarters ahead. There are -- as we said in the prepared remarks, there's certain levers that really sort of drive margin profiles, including state mix, product mix, et cetera. We're excited about Ohio's adult-use program launch from Tuesday. We know that, that will be a driver of our business for quarters and years ahead. And as far as pricing pressure, I think you mentioned pricing pressure in Ohio specifically. I think that, that typically what we see from a transition to medical to adult-use follows that same trend. But when adult-use launches, it tends to -- you see an increase in pricing for a period of time.

Dennis?

Dennis M. Olis
Chief Financial Officer

Yes. Just building on what Charlie said, look, we saw some favorability in the state mix in Q2 that had an impact, a favorable impact on our margins in the quarter. So, again, Florida was very strong for us in Q2 that helps drive margins up. With the price pressures that we're seeing in the marketplace, that does put some pressure on margins overall. I think we've done a great job in offsetting that with some efficiencies in our cultivation and manufacturing facilities. As we look to the second half of the year and as we see some growth in Ohio, particularly in fourth quarter with adult-use, that will have a slight negative impact on margins. That'll get us back, we think, closer to the 50% margin as we exit the year until we get our facilities in Ohio up to speed and get them to our average margin performance.

Remington Smith

All right. That was really helpful. And then my second question. In regards to New York, I know it's a market you've been constructive on historically. And while there been a little bit of hurdles in terms of the illicit market initially, actions taken by the illicit -- by the state against the illicit stores, coupled with material amount of legal store openings really helped drive some growth in the market. Just wanted to get your take on -- are you viewing the market, particularly with the wholesale side and then potentially allocating some CapEx there?

Charles Bachtell
Co-Founder, CEO & Director

So, our position on New York has not changed from prior calls. We're optimistic that New York is going to be a large market going forward. But the start to the legal program there has been challenging. And

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as we're looking at our total footprint and being super diligent with allocation of capital, there's other opportunities in our footprint and in our business. When you compare the New York opportunity today to the other opportunities that we have in trying to drive the highest ROI in the reasonable period of time, it's a challenge. So, we're encouraged by what we're seeing there. We do think long term, New York is going to be a big, robust program that we'll be happy to be a part of. But in the interim and in the immediate term, there's other opportunities that we're pushing forward with.

Operator

Your next question comes from the line of Scott Fortune with ROTH Capital Partners.

Nicholas Steven Anderson
ROTH MKM Partners, LLC, Research Division

Yes. This is Nick on for Scott. Congrats on the good quarter here. First question for me is just on product mix. I know it differs by state, but can you give us just a general sense of what you saw from the consumer on the quarter, given the potentially kind of tempered macro backdrop here? And just wondering if that translated to any changes in spending behavior and how that impacted your mix between the good, better and best categories.

Charles Bachtell
Co-Founder, CEO & Director

So, we'll have Greg start with this one.

Gregory Butler
President & Chief Transformation Officer

Nick, in general, for the major trends across states, I mean, I'll start by saying each state does have a little bit of nuance that makes it unique. But on a macro level, for trends, not surprising, what you are seeing is shoppers are looking for value across all categories, all consumer goods categories that includes cannabis. We're seeing growth in our value formats are high. And we're seeing growth in value formats across the categories are high as consumers looks to save ways -- find ways to save money.

It doesn't mean, though, that just value segments are growing. We're actually seeing higher priced, more premium products, especially interesting products that are different and new, are able to generate and pull dollars from consumers' wallets and drive some excitement. But I think the macro trend is that there is a value shopper out there. Things are expensive. And as more cannabis becomes available at lower prices and better product quality, it becomes a competitive offering for them.

Nicholas Steven Anderson
ROTH MKM Partners, LLC, Research Division

Got it. I appreciate that color. Second one for me, just on the in-house breeding program. You mentioned the goal of 50% of your menus to be Cresco-exclusive strains by 2025. Could you just provide some color on the difference in economics from selling and growing those strains, and just where you're at today in terms of reaching that target?

Gregory Butler
President & Chief Transformation Officer

I'll take that, too. I think what we're finding is, obviously, there's a benefit of selling house brands in your own retail. But for us, what's really important is we look at how our products perform and the quality of products we're putting out there and what we're really proud about. And what you see in our #1 share position across most of our states is that the products that we're making drive really, really strong velocity. Now, that's important for us because, obviously, better velocities, better turns, means better profitability. But we also think that's the winning equation for all of our partner accounts out there, too, because if our brands turn faster and warrant better pricing, that's a win-win on profitability for Cresco and our Sunnyside stores, but it's also a win-win for our partners as well. So it is much more of a focus on

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the best quality product that drives the highest velocities, which we're pretty confident we're doing okay there as we see our #1 share still hold.

Operator

Your next question comes from the line of Pablo Zuanic with Zuanic & Associates.

Pablo Ernesto Zuanic
Zuanic & Associates

Look, 2 questions. One for Dennis. In terms of the statement you made on planning normal company for '23 and '24, but will you also be asking for tax refunds for 2020 to 2022? And if not, why not, right?

And then the second question for Charlie, if I may. Can you just share your latest expectations in terms of the rescheduling process? Are you still confident that we'll get this done by inauguration day?

Charles Bachtell
Co-Founder, CEO & Director

All right. So, we'll start with Dennis.

Dennis M. Olis
Chief Financial Officer

Yes. Thanks, Pablo. As you noted, yes, we did file -- or taken the taxes for '23 and '24. We will plan on looking protective claims for 2020 through 2022 in the coming quarters.

Charles Bachtell
Co-Founder, CEO & Director

All right. And then I'll take the second part of the question. Yes, Pablo. So latest expectations on rescheduling, don't have the crystal ball, but I know that the relevant parties are actively reviewing the next steps that they want to take, whether it relates to the hearing or no hearing. And we will know as soon as they are ready to communicate that publicly. I think that's the best position that everybody involved can take. As I said in the prepared remarks, I know it tests the patience of even the most patient of us. But this is a very popular issue. This is a very active political cycle. And so I think you're optimistic here, but we'll see. They'll let us know as soon as they're ready to let us know.

Pablo Ernesto Zuanic
Zuanic & Associates

And if I can, just a follow-up on Ohio. We can say that maybe perhaps the adult-use there, it's a bit of a light start, right, that they call it non-medical. The rules for AU are not fully out yet. I mean, is that a big deal or we should see a very strong ramp anyway? Or if we don't see a strong ramp right now, when do we start getting those AU rules? If you can just give some context into the nuance there.

Charles Bachtell
Co-Founder, CEO & Director

Sure. So, I think you articulated it well. The best way to think about the Ohio adult-use launch in the immediate term is that it really is -- everything is being done pursuant to the medical program structure and rules, except you're allowed to let non-patients into the dispensary to make purchases, too. So from a awareness standpoint, from a marketing standpoint, it's still pursuant to the rules that have been in place there for years under the medical structure, nothing there has changed. So, you may have seen that if you were in market right now, it still looks and feels very similar under the medical program.

The expectations on adult-use rules are this fall, and we're encouraged by the work that the division is putting in there to kind of try and produce the best launch to the adult-use program as possible. We really do appreciate the effort that they put into launching the adult-use access as soon as possible. It's a really important part of successfully having an adult-use law and program is making sure that there's not a giant

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gap between when a law gets passed and when a program gets launched. So it's really important, and we look forward to the rules coming out again. Expectations are this fall for the adult-use rules.

Operator

Your next question comes from the line of Najib Islam with Canaccord Genuity.

Najib Islam
Canaccord Genuity Corp., Research Division

It's Najib speaking in for Luke. So one question I have is within Florida, what's been some of the key factors helping you gain market share there? And how would your growth plans kind of shift gears if adult-use goes through November?

Charles Bachtell
Co-Founder, CEO & Director

So, this is Charlie. I'll take the second part of that first. So as we talked about, I think, on our last call, we've got a phased approach to Florida that we think it puts us in the most appropriate position possible. We are really encouraged by the growth that, that team has been able to create over the last year in the medical structure. So, we are in a position where we know that we can continue to grow in that state even if it stays a medical program. And so we're taking actions in this phased approach to put us in the best position possible for medical or adult-use. It'll also help for the initial stages of adult-use if it passes. If adult-use does pass, then we do have a Phase 2 approach that would be an increase in production capacity to go along with that law passing.

But rationale or reason behind the growth, I'll pass it over to Greg.

Gregory Butler
President & Chief Transformation Officer

I think as we look at what we've always said in these calls, our view and every market we go into is that we can compete well to get to a leading market position. We're seeing that across states. And in Florida, we're starting to see us grow in that state. I would say the key drivers for us, one, is we believe in our platform. The Sunnyside platform we built is showing great results across many of the markets we operate in, Florida being one of them on how it's both attracting customers to our stores and delighting them with the products that we're offering in our stores. The quality of team of running those stores are doing their best to continue to recruit and bring new customers into Sunnyside to see the difference.

And then finally, from a product perspective, what we're able to produce in the market from our facility is not only are we producing what we believe is superior products, but also we're able to increase our supply coming out of our footprint that enables us to fuel our stores that helps us drive that growth. So it's a really great story for us. We're very proud about of our teams really getting the market, understanding the market and building a platform that we think is going to be competitive if it remains medical and will only be supercharged if it goes into adult-use.

Najib Islam
Canaccord Genuity Corp., Research Division

Sure. Got it. And another question I have is, once you implement pre-roll manufacturing improvements in one state, how easy is it to roll out across your footprint? And is there any meaningful CapEx associated with that?

Gregory Butler
President & Chief Transformation Officer

I'll take that question as well, how we think about our SOPs. We do try to find consistent, repeatable, scalable solutions across each of our states. That's why you're seeing the margin improvement that Dennis talked about. So when it comes specifically to pre-rolls, as we or any capability, as we finalize a form that we think gets us to the best unit economics at the best quality, we will look to roll out across states. We

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will prioritize states where we think there's room for us to get in there and take share. So, not every single state will turn on all at once. And from a CapEx perspective, it's pretty minimal CapEx for us to do that, especially as we think of a staged approach that goes market by market to find out where we have an opportunity to take share in that segment of the market.

Operator

Your final question comes from the line of Andrew Semple with Ventum Financial.

Andrew Semple
Echelon Wealth Partners Inc., Research Division

First of all, congrats on the results. First question would just be getting a sense on the Cresco team stance on Florida ahead of the November votes and how aggressive you plan to be in terms of deploying capital in the states. I know Florida was mentioned as a state where you're planning some capital investments later this year. Just wondering if there's the potential to go much larger than you've already stated if the vote were to be successful.

Charles Bachtell
Co-Founder, CEO & Director

Sure. So, this is Charlie. I'll take that. So how we're feeling about Florida as it relates to the ballot initiative, we follow the news. We're actively engaged in the efforts down there. And look, we're optimistic. We're encouraged by what we're seeing. And so that does make us optimistic for the likelihood of it passing come November. That said, as we mentioned, this phased approach we think is the most prudent and appropriate because it'll be successful for us regardless of the outcome. And that's an important thing that we've just learned over the 10 years that we've been in the cannabis space, is try to put yourself in a position where you're going to have success and you're going to win regardless of a binary situation is a positive or not. And so it's an appropriate next step for us. Yes, if adult-use passes, we do have a fairly substantial Phase 2 approach that will go along with it. So, feeling good about where Florida is at, and we're feeling really good about our approach.

Andrew Semple
Echelon Wealth Partners Inc., Research Division

Great. That's helpful. And just a follow-up question would just be more broadly across your retail portfolio over the past couple quarters. Has there been any major shifts in the vertical integration you've deployed at your Sunnyside store shelves in terms of carrying more Cresco-branded products, just as it relates to some of the margin improvement that we've seen over the past few quarters? Has there been any shift in strategy there? Or has that been fairly consistent?

Gregory Butler
President & Chief Transformation Officer

It's Greg. Let me take that. Our view and how we run our assortment in our stores is we do look for what is the highest velocity SKUs we offer, and we think velocity that's truly showing you what our shoppers demand and what they prefer. Now, as I mentioned on an earlier question, a lot of the times that tends to be our brands. So, that's really encouraging. But then as we think about others, if there's another brand or another format that has really strong velocity, that's also ideally accretive to what we're offering in our assortment. That certainly is going to be something that we're going to pick up and put in our stores.

And there's also new segments that are emerging, which maybe we're not quite ready to get into yet. But we'll do a test and learn other assortment in our stores to see how it's going to unfold and how the economics look behind it. So, I wouldn't say that there's a force requirement of how much we're putting into our stores, but rather we are looking at how do we optimize own brands and third-party brands to make sure that the profit story is the strongest. And that really does come down to consumer pull velocities. And as I mentioned before, that does tend to lead us to our own brands. but always opportunity for other brands in there as well.

Operator

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That concludes our Q&A session. I will now turn the call back over to Charles Bachtell for closing remarks. Please go ahead.

Charles Bachtell
Co-Founder, CEO & Director

Yes. I just want to thank everybody for joining in today. And most importantly, I want to thank the Cresco team for a really solid quarter. Thank you, guys. Congratulations. And we'll talk to everybody in a couple of months. Goodbye.

Operator
Ladies and gentlemen, that concludes today's call. Thank you all for joining. You may now disconnect.

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