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**The webinar will be starting  
soon...**

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# Valuations: Manufacturing, Distribution and Ancillary Cannabis Operations

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# Agenda

- Recap of previous webinar
- DCF Model Overview
- Manufacturing, Distro, Ancillary Businesses Valuations
- Wrap-up

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# GreenGrowth CPAs



## About Us:

- Tax Preparation: completed over 500 Annual Tax Returns for cannabis operators spread across all verticals: dispensary, distribution, cultivation, manufacturing, delivery and testing.
- >300 clients based in California, Colorado, Michigan, Oregon and Washington
- Performed over a dozen audit related projects in the last year
- Expected to hit 7-digits in revenues in our second full business year (2018).
- Thorough and deep understanding of tax, compliance and assurance related requirements for the cannabis industry

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# To Recap...

When assessing the value of a cannabis cultivator or retailer:

- Understand the key assumptions driving the business valuation
- Do your due diligence by looking at POS systems, payroll systems, accounting software, and by visiting the operation
- Bad companies can be turned around...many opportunities
  - But: are they compliant in their taxes, licensing etc. – this is too important to miss.

# DCF Valuation Overview – Business vs Valuation Assumptions

DCF Model						
		Long Term Growth Rate			1.50%	
		Market Participant Tax Rate			25.00%	
	Year 1	Year 2	Year 3	Year 4	Year 5	Normalized Terminal Period
Revenues/Sales	\$ 1,000,000	\$ 1,367,911	\$ 2,000,000	\$ 3,000,000	\$ 3,500,000	\$ 3,552,500
Growth	N/A	N/A	46.2%	50.0%	16.7%	1.5%
EBITDA	150,000	205,187	300,000	450,000	525,000	532,875.00
Depreciation & Amortization	4,941	28,541	29,178	29,834	30,505	20,489
Operating profit (EBIT)	145,059	176,646	270,822	420,166	494,495	512,386
Income tax payments (refunds)	36,265	44,161	67,706	105,042	123,624	128,097
New cash flow (after interest income and taxes) as a percentage of net sales	\$ 108,794 10.9%	\$ 132,484 9.7%	\$ 203,117 10.2%	\$ 315,125 10.5%	\$ 370,871 10.6%	\$ 384,290 10.8%
Plus: Change in net working capital (increase)/decrease	3,000	3,100	4,000	2,000	6,000	6,090
Less: Capital expenditures	7,593	20,489	19,200	19,200	20,489	20,489
Plus: Depreciation & Amortization	4,941	28,541	29,178	29,834	30,505	20,489
<b>NET CASH FLOWS</b>	<b>\$ 109,142</b>	<b>\$ 143,636</b>	<b>\$ 217,095</b>	<b>\$ 327,759</b>	<b>\$ 386,887</b>	<b>\$ 390,380</b>
<b>VALUATION ASSUMPTIONS &amp; CALCULATION</b>						
Period (mid year convention)	0.08	0.65	1.65	2.65	3.65	
Present Value Factor	9.0%	0.99341	0.94531	0.86740	0.79592	0.73032
Present Value of After tax Cash Flows	\$	\$ 108,423	\$ 135,781	\$ 188,309	\$ 260,868	\$ 282,551
Residual Value						
Terminal Period Net Cash Flow	\$	\$	\$	\$	\$	\$ 390,380
Discount Rate	9.0%					
Less Long Term Growth	1.5%					
Capitalization Rate	7.5%					7.5%
Residual Value						\$ 5,217,640
Present Value Factor						0.73032
Present Value of Residual Value						3,810,542
Present Value of After-tax Cash Flows (P12-2018)	\$	\$	\$	\$	\$	\$ 975,932
Present Value of Residual (2019+)						3,810,542
<b>Fair Value of the Business</b>						<b>4,786,473</b>

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# Valuing Manufacturing & Distribution, and Ancillary Commercial Cannabis Businesses

- Similar criteria for manufacturing, distro, and ancillary
- B2B companies operating within the industry
- Slight variations depending on role/vertical

# Summarized Pro-Formas & Business Assumptions

	<u>Annual Information</u>								
<b>Revenues</b>	<b>3,090,507.73</b>								
<b>COGS:</b>									
Raw materials, labor, packaging	<b>(1,236,203.09)</b>								
<b>Gross Margin</b>	<b>1,854,304.64</b>								
Selling, Marketing, Overhead	(500,000.00)	distribution cost, sales personnel payroll, marketing spend, rent, utilities, accounting, legal							
Depreciation & Amortization	(600,000.00)								
<b>Operating Income</b>	<b>1,254,304.64</b>								
<b>EBITDA</b>	<b>1,854,304.64</b>								



# DCF Valuation Overview

## Business vs Valuation Assumptions

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# Cannabis Manufacturing & Distro Operations - Assumptions

## 1. Revenue

- a. Bottom up - what's the capacity of the machinery & equipment, i.e. how many units it can produce
- b. Top Down - dispensaries selling to, average size of purchase, mix
- c. Break out between own brand and white-labeled

**Due Diligence** - this information would be contained in the billing software & for equipment capacity can be determined based on the type & vendor

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# Cannabis Manufacturing & Distro Operations

**2. COGS/Cost of Production - Unit economics & how much is going into making each product type - edible, concentrate**

**Due Diligence - this information would be captured in inventory costing software or taking total costs per the ledger and dividing by items produced**

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# Cannabis Manufacturing & Distro Operations

3. **Selling** - understand the selling models
4. **Distribution** - understand the distribution cost

**Due Diligence** - this information should be captured in their general ledger/accounting software

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# Cannabis Manufacturing & Distro Operations

**5. Marketing Expense** - marketing ROI, marketing strategy, relationship between marketing spend and revenues

Due Diligence - this information should be captured in marketing analytics platforms and their general ledger

**6. Fixed Operating Costs:** rent, utilities, salaries, security

Due Diligence - this information should be captured in their general ledger/accounting software

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# Cannabis Manufacturing & Distro Operations

## **7. Balance Sheet - Cash, receivables, inventory, equipment, liabilities**

**Due Diligence - this information should be captured in their general ledger/accounting software**

## **8. Controls & Financial Reporting - strength of controls around cash, inventory, and financial reporting**

**Due Diligence – Review their Standard Operating Procedures**

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# Cannabis Distribution Companies

Things to look for when evaluating a cannabis distribution company:

- 1. Number of regular clients**
- 2. Equipment:** how many vehicles does the company have? What are they worth?
- 3. Fixed operating costs:** things like gas, software, leases, rent, security, etc.

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# Cannabis Ancillary Businesses

What is an ancillary business? An ancillary business could be:

1. Cultivation equipment
2. Extraction Equipment
3. Dispensary Displays
4. Labels and Packaging
5. Cannabis Software: track and trace, point-of-sale, manifest generating, security software
6. Professional Services: accounting, legal, marketing
7. Merchandise: t-shirts, caps, lanyards
8. Accessories: vape pens, bongos, cannabis butter makers, rolling paper, diffusers



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# Distress Situations & Synergies

**-Understand their key strengths and weaknesses and your key strengths and weaknesses**

**-Low margins - understand what is the cause, i.e. costs them too much to produce an item, terrible extraction yield, bad raw materials resulting in spoilage, bad deals with brands for white-labeling**

**-Low sales - understand what is the cause, i.e. bad sales and marketing strategy, need to bring brands on board**

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## Key Takeaways



- Evaluate these B2B cannabis operations along the same criteria.
- Branding, financial projections, fixed costs, and operating costs are all important things to understand
- If a business is in distress, figure out what it will take to turn it around.
- Compliance, licensing, and taxes need to be in order *before* you make an acquisition.

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**Questions or need help with a valuation?**

**Contact Green Growth CPAs today!**

**[www.greengrowthcpas.com](http://www.greengrowthcpas.com)**

**(800) 674-9050**