FINAL TRANSCRIPT

**GH Group Inc.**

**Glass House Brands - Second Quarter 2021 Conference Call**

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## CORPORATE PARTICIPANTS

**Kyle Kazan**
*Glass House Brands — Co-founder, Chairman and Chief Executive Officer*

**Derrek Higgins**
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**Graham Farrar**
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## CONFERENCE CALL PARTICIPANTS

**Scott Fortune**
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**Aaron Edelheit**
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## PRESENTATION

**Operator**

Good morning, everyone. Welcome to Glass House Brands Second Quarter 2021 Conference Call for the three-month period ending June 30, 2021.

Listeners are reminded that certain matters discussed in today's conference call, or answers that may be given to questions asked, could constitute forward-looking statements that are subject to risks and uncertainties relating to Glass House Brands' future financial or business performance. Actual results could differ materially from those anticipated in forward-looking statements. The risk factors that may affect results are detailed in Glass House Brands periodic filings and registration statements. These documents may be accessed via the SEDAR database.

I'd like to remind everyone that this call is being recorded today, August 17, 2021.

I'd now like to introduce Mr. Kyle Kazan, Chairman and Chief Executive Officer of Glass House Brands. Please go ahead, Mr. Kazan.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Thank you, Operator.

Good morning, everyone, and thank you for joining us for today's call. With me are Derrek Higgins, our Chief Financial Officer, who will review our financial results, and our President, Graham Farrar, who will join us for the Q&A later on.

As this is our first quarterly call, we'd like to take a few minutes this morning to review our strategic priorities and provide an overview of our business and positioning. Then, Derrek will discuss our financial results. Afterwards, Derrek, Graham and I will take your questions.

Following the completion of our business combination with Mercer Park Brand Acquisition Corp. in late June, we have successfully created Glass House Brands, Inc. with the vision of becoming the largest cannabis brand building platform in California. That vision remains constant and unchanged. Today, we operate one of the strongest retail and wholesale networks in the state, supported by our best-in-class cultivation processes and our scaled and highly efficient cost structures. It's been approximately 50 days since completing the transaction and I am incredibly proud of the work that has been done to transition into a publicly traded company.

Following the transaction, we are well funded and remain well positioned to capitalize on the growing California national CPG opportunity ahead of us. Our strategic priorities coming out of our qualified transaction continue to be to scale our cultivation, increasing our capacity, our quality, while reducing our costs to improve the breadth and depth of our product portfolio and execute our growth strategy through planned cultivation and retail dispensary acquisitions and mergers. I am pleased to report we have made significant progress against these strategic goals. With our expansive cultivation, retail, and wholesale footprint, we continue to leverage our position in California to introduce high quality, sustainably grown craft cannabis to the market in an effort to support the growing demand we are seeing from our consumers while having a lighter and greener touch on our environment.

Today we operate a cultivation footprint of over 500,000 square feet, producing over 80,000 pounds dry equivalent of biomass per year. We recently provided an update on our pending acquisition of a 5.5 million square feet state-of-the-art, Southern California facility. The additional capacity is expected to increase our current footprint up to approximately 2.5 million square feet by 2023 and our total targeted footprint of 6 million square feet will position us as the largest cultivation capacity in California by far. We continue to believe that the Southern California facility is a unicorn asset that will allow us to produce cannabis on par with the very best in the state and the country at an eventual scale that will allow us to service the entire country when that opportunity arrives.

Since our inception in 2015, we have focused on incorporating leading-edge technologies and cultivation techniques to produce exceptional cannabis products for medical patients and consumers. We continue in our commitment to finding innovative techniques that allow us to expand our output while being as efficient and sustainable as possible. On the retail front, we currently operate four award-winning dispensaries in California and during the quarter announced that we were awarded two additional retail licenses de novo in Santa Barbara County, one in Santa Inés and one in Isla Vista, both of which we expect to open in the first half of 2022, bringing our internal retail footprint to six. We continue to make progress towards our goal of rolling out an additional 13 dispensaries, which will bring our total retail footprint to 19 open locations by the end of Q2 2022.

Looking at our CPG business, we ended last year with a top five brand in the flower category. That is the largest category, which equates to 49 percent of all sales in the world's largest market of California. We ended the second quarter with approximately 340 retail doors to our CPG distribution and have maintained our position as a top five brand. Depending on the chart, we are number one, number three, or number five. Our aim is to continue reaching many more dispensaries state-wide and we'll leverage our leadership position in California to capitalize on the potential nationwide opportunities that would result from federal legalization.

In addition to our cultivation and retail footprint, I'm very proud of the progress we have made in building a differentiated brand portfolio to meet the needs of our consumers. Our portfolio includes Glass House Farms, our first flower brand for the everyday cannabis consumer, Forbidden Flowers, a female, millennial, and Gen Z targeted brand through our partnership with Bella Thorne, as well as Mama Sue, built with well-known industry activist Sue Taylor. We continue to build out our portfolio and look forward to introducing new brands and products to consumers. We believe that the combination of a large-scale, high-quality cultivation combined with a large retail footprint will allow us to build a portfolio of strong brands that will be a critical component of our success.

Looking briefly at the quarter before turning it over to Derrek to provide a more in-depth view, we generated net sales of $18.7 million and sustained positive Adjusted EBITDA. This was short of our target, and I'd like to provide some context on the operational challenges we faced which caused the miss. Our primary challenges related to the ramp up of production at our new and larger cultivation facility, the 355,000 square foot property, in the second quarter which had an outsized impact on both our anticipated yields and cost of goods sold. We fully planted all five greenhouses at the Padaro facility in the fourth quarter of 2020 and commenced our first harvest at the beginning of the quarter. Our original plans, however, proved to be aggressive, given that we made them prior to running the facility at full capacity. We extrapolated projections using a combination of data from our smaller facility, the 150,000 square foot property at Casitas, coupled with promising early results achieved at Padaro in the second half of 2020.

There were three primary issues at Padaro which contributed to our underperformance in cultivation. We have been working on a new processing warehouse on the site and initially planned to fresh freeze a significant amount of biomass since we had insufficient onsite dry cure space. Market and product conditions caused us to re-evaluate, reducing our fresh frozen and increasing our dry allocations. As a result, we had to make a number of operational decisions, including utilizing space at our manufacturing facility for post processing and outsourcing capacity to third-party vendors. Neither of these changes were ideal and have raised our processing COGs. The Padaro Farm climate controls proved to be inadequate for the more humid times of the year. As the initial results came in favourably and with the desire to conservatively manage our capital resources, we opted to try to save between $1 million and $1.5 million by not replacing the heating system. This proved to be a poor decision as the lack of climate control resulted in reduced yields and increased processing costs.

The roof material at Padaro Farm had a lower light transmission than was expected. Our initial data was collected at the highest light time of the year and was used to forecast for the full farm output. At the lower light periods of the year, the impact of the lower light transmission had a significantly higher impact, reducing yield. We are currently halfway through replacing the roofs on all five greenhouses with higher light transmission material, which are expected to significantly improve results.

As we pride ourselves on being one of the best low-cost, high-quality growers in the state, we determined to fix this quickly so that we can maximize that efficiency. This, along with being careful stewards of our and our investor's capital has resulted in us making additional data supported capital investment decisions. While the issues at Padaro were different than the problems we tackled at Casitas, they are all solvable. The difference now is that we are under contract to purchase the Camarillo facility, which, on its worst day, it's worst day, is far better than both of our current farms on their best days.

The silver lining is that we feel that our investment thesis has been proven correct. Higher light levels and more climate control produce better quality flower at lower cost. This is exactly why we remain excited about the Camarillo Farm acquisition, especially as the media is beginning to report just how large the carbon footprint is in growing cannabis indoors, both locally and around the country. As an example, 10 percent of Massachusetts' electrical grid is being used by cannabis operators. Given that, we are looking to accelerate the shift in our focus to flower production going to Camarillo. We decided to limit the investment at Padaro to installation of a new roof system to allow more natural light into the greenhouses, enabling us to continue improving both yield and product quality without increasing our carbon footprint or operational costs. In addition, we expect upon completion to reduce the energy required to produce each pound of flower by approximately 20 percent.

We are considering changing the heating system to dry heat, as the humidity problem exacerbates during flowering, we have determined the use of this farm after the shift to Camarillo and we'll make the investment decision shortly. With the addition of the Camarillo facility, we are evaluating if it is still necessary to invest the approximate $6 million to $7 million needed for a new warehouse if we can instead relocate all processing to the Camarillo facility. While the team is ready and quick to find efficiencies, I expect that some problems will persist until we bring our production in Camarillo online.

Before I turn the line over, I'd like to remind our listeners of our strategic priorities coming out of our go-public transactions.

First, as previously mentioned, we remain committed to scaling our cultivation activities and expect to close on our previously announced acquisition of the 5.5 million square foot state-of-the-art Southern California greenhouse shortly. Southern Cal greenhouse currently operates as an agricultural producer, consisting of six high-tech, environmentally controlled agricultural greenhouses totalling the 5.5 million square feet, located on 160 acres in Ventura County, California, that will transition in phases to a cannabis facility upon regulatory approval. We believe that this asset in combination with the Glass House team will give us a competitive advantage that few will be able to compete with. Earlier this month we announced that we agreed to amend the closing terms of the agreement with the seller and will now close escrow following receipt from Ventura County that the flower building permit issue at the facility has been signed off.

In addition, as sellers we agree to carry a $30 million note on favourable terms through the issuance of the California State cannabis license, or the end of 2021, whichever is sooner. We expect to complete this acquisition this quarter, in quarter three of 2021, using cash on hand, subject to local regulatory approval. Once we close, we expect to immediately begin the first phase of conversion of the agricultural greenhouses to cannabis cultivation, which will result in the upgraded retrofit of approximately 1.7 million square feet of the facility. With this acquisition, we'll be ideally positioned to lead the California cannabis market with our unmatched capacity and we'll be well positioned to scale our production to yield some of the highest quality cannabis to meet consumer demand and support the expansion of our wholesale business.

Second, we have an aggressive retail dispensary acquisition plan, which will fuel the rapid growth of our business as we move into 2022. We continue to make progress here and during the second quarter we announced that we were awarded two new retail licenses in Santa Barbara County to open adult use dispensaries in the highly sought-after Santa Inés and Isla Vista locations. We expect these two locations to be operational by the end of the first half of 2022. With these two additional licenses, we increase our internal retail footprint to six locations throughout California, adding to our existing operating locations in Santa Barbara, Berkeley, Santa Ana, and Los Angeles. With a population of more than 500,000 in Santa Barbara County, the new retail dispensary locations are strategically positioned along U.S. 101, or Pacific Coast Highway, to service local residents and support the region's robust, year-round tourism industry. Each of the planned dispensaries are located in regions that are only approved for a single license, which is a testament to our team's history of quality operations and ability to secure licenses in complex and competitive regulatory environments.

In addition to our current footprint, we previously entered into an agreement to merge with 17 in-process retail license entities from Element 7, a California company with a proven track record in winning licenses. These licenses together with the two new recent Santa Barbara license awards are expected to bring our retail footprint to 23 locations in total, with 19 operational by the end of the first half of 2022, which will represent the highest state-wide store count of any single California cannabis operator.

Finally, we continue to focus on building world-class leadership and management teams, and earlier this month we were thrilled to welcome Erik Thoresen as our new Chief Business Development Officer. Erik will be responsible for spearheading M&A initiatives as we capitalize on our California based and potential national CPG opportunities. He joins us from nearly 20 years of global investing, capital allocation, and transactional experience and with 15 years of experience in M&A and 12 years of non-market proprietary deal flow experience. Erik will play a critical role as we continue to roll out and scale our wholesale business. We also recently announced that Joe Aulenta has joined our team as our new Director of Retail Construction. He has 15 years of construction and store design management experience and over 20 years of merchandising experience, most recently working as a senior project manager of real estate construction for Foot Locker. He will be instrumental in managing the execution and build out of our retail network as we execute against our goal of 19 stores by the end of the second quarter of 2022.

All of these efforts together with our unique leadership position in California and strong balance sheet have positioned our Company for sustainable, long-term growth. I look forward to continuing to update you on our progress as we continue to execute over the coming weeks and months. With that being said, at this point I would like to now turn the call over to Derrek, who will discuss the financial highlights of the second quarter.

**Derrek Higgins —** Chief Financial Officer, Glass House Brands

Thanks, Kyle, and good morning, everyone.

As a reminder, the results I'll be sharing today can be found in our financial statements and Management Discussion and Analysis, published on the SEDAR database, which are reported in U.S. dollars and prepared in U.S. GAAP.

Starting with our income statement highlights, revenue for the quarter ended June 30, 2021, totaled $18.7 million, climbing $7.1 million or 62 percent year-over-year. We separate revenue into two business categories: wholesale and retail. Wholesale is our B2B business, selling bulk biomass and consumer products to other licensed cannabis businesses. Wholesale revenue increased by $4.3 million, or 54 percent year-over-year. This increase was primarily due to an increase in cannabis production from our second greenhouse cultivation facility at our Padaro Farm, which commenced limited operations in Q1 2020 and was fully operational by the end of the year.

Retail is our B2C business, selling packaged products to end consumers through retail stores we control. Our Los Angeles based dispensary, The Pottery, is reported as an equity method investment, given its current ownership structure, and therefore is not consolidated with our retail revenue. Our cannabis retail dispensaries contribute consistent revenue growth, increasing $2.8 million or 77 percent in Q2 2021 compared to Q2 2020. Our Berkeley store, which we acquired in Q1 of this year, accounted for $1.7 million of this revenue growth. This past quarter, we made modifications to our rewards and loyalty program that resulted in a one-time favourable adjustment to revenue of $1.2 million. Excluding this adjustment, existing store revenue declined 4.7 percent year-over-year, consistent with the broader California market as the state eased stay at home restrictions.

We ended last quarter with $8.6 million of gross profit and a 46 percent gross margin, compared with a gross profit of $5.5 million and a 48 percent gross margin in Q2 2020. The decrease in gross margin percent was driven by increased product, labour, and overhead cost associated with our previously mentioned post harvest processing challenges we experienced ramping up the Padaro Farm.

In Q2 ’21, total operating expenses increased $3.4 million year-over-year to $9.6 million, compared to total operating expenses of $6.2 million in Q2 2020. The majority of this increase was associated with professional fees, which increased $1.4 million year-over-year for legal, accounting, and other consulting services supporting our go-public transaction and other key initiatives that occurred during the second quarter of 2021.

General and administrative expenses increased $1.3 million year-over-year to $5.9 million on increased investment in operational expansion initiatives to support our corporate, cultivation, and retail operations.

Sales and marketing expenses increased $600,000 year-over-year to $1 million, with an additional investment in digital media, marketing, and royalty expenses.

We define Adjusted EBITDA as earnings before interest, taxes, depreciation, and amortization, adjusted for transaction costs, restructuring costs, share-based compensation, and other non-cash operating costs. We ended last quarter with an Adjusted EBITDA of $2.2 million, compared to $1.1 million in Q2 2020. The increase in Adjusted EBITDA was primarily due to higher gross profit, which was partially offset by our higher operating expenses.

Moving to the balance sheet items, cash increased by $129.8 million year-over-year, primarily from capital raised through our go-public transaction. We ended the quarter with $134.3 million in cash and ample liquidity to close the Southern California greenhouse acquisition Kyle discussed earlier. Additionally, during the quarter the Company eliminated $38.3 million of debt through the completion of a preferred stock offering, exchanging both principal and interest accrued to participating investors and issued both company preferred stock and warrants, which triggered the equity conversion of all of the Company's outstanding convertible promissory notes.

As Kyle mentioned, we are well funded and well positioned to continue to execute on our growth strategy, and with our significantly improved balance sheet and large portfolio of unencumbered cannabis real estate assets, we are actively evaluating additional, non-dilutive sources of capital to help fuel our future strategic initiatives. We are very pleased with the progress we have made this quarter and even more excited for what lays ahead of us in 2021.

I would like now to turn it back over to the Operator to open the line for questions. Ma'am?

## Q & A

**Operator**

Thank you. Your first question comes from Scott Fortune with Roth Capital Partners. Please go ahead.

**Scott Fortune** — Analyst, Roth Capital Partners, LLC

Good morning, and thanks for the questions.

Real quickly, I want to focus on kind of the CAPEX or the cash levels you're at now and kind of the build out as you look out into 2021/2022 as you bring on the big greenhouse operations going forward. Can you step us through kind of the costs associated with building that out going forward here?

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Scott, good morning. Nice to hear from you. Let me ask Graham to comment on that if that's okay.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Yes, sure thing. Hi, Scott. Good morning. Thanks for your question. I appreciate it.

Just on a quick note, too, as we say good morning here to recognize all the work of the Glass House team. Obviously, we're here presenting, but there's an entire team of people doing great work behind us and wanted to make sure that we recognize the contribution that all of them are making.

I think initially worth noting is that there is no change to our strategy, right. Our goal is to build brands and products that consumers love. We believe that the way to do that is with high quality, efficient, large-scale cultivation coupled with retail to be able to create a brand by deciding to create a brand. As we get ready to move into Camarillo, there's some things that we need, largely unchanged from, you know, our initial conversations that we've had around the build out of additional retrofits around black out, dry rooms, and, you know, systems such as that to allow the conversion from cannabis, I'm sorry, from tomatoes to cannabis. You know, as we mentioned though, that greenhouse as it sits now is better than any of the greenhouse facilities we have today.

While we had some challenges, particularly at the new farm, the silver lining to that, right, is that the things that we've been saying matter. We've showed matter, right. More light, better climate control, produce a higher quality cannabis at lower prices. As we go into this, of course you know, we wake up and put our feet on the ground every morning. The shareholder is first. We think about our consumers. We think about our employees, and we think about the shareholders behind them. Everything we do, we try and do as the most efficient stewards of capital as possible.

One of the benefits I think that we have is the six-plus years of experience in doing these retrofits. This will now be the third one. We learned some lessons on the first one. We learned some lessons on the second one. As we go forward on this, it should actually be one of, on a per square foot basis, the easiest conversions that we've done. We've got an initial plan there, measured in the tens of millions of dollars, which will be done to start things off, licensing specific, cultivation specific, and processing specific so that we can get started down there as quickly as possible.

**Scott Fortune —** Analyst, Roth Capital Partners, LLC

That's great, appreciate the colour. Then, real quickly, as you expand the DTC, as you expand your retail doors, I know for the CPG side you're at 340 doors here and looking to expand that in California. Can you step us through any kind of target level or what kind of coverage, percentage coverage of California do you have right now as far as selling your brands into all the different dispensaries there? Just step us through kind of the cost associated with it or the expansion of distribution for your brands into California retail stores.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

So, Scott.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Yes, sure, so—go ahead.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Let me just, so Scott, this is Kyle. What I would tell you is, we work with Herbal, and so the breadth of their reach is very long. We also have a sales team which we are actively growing as well so that we are touching the stores. I would say the coverage right now is under 50 percent, so we feel pretty good that, again, whether we're number one, two, three, four, or five, you know, top flower brand, we have, you know, a lot of stores to capture. There is plenty of growth there, and also, we've added different SKUs to our product selection so that we can get our flower out in many different forms to the different stores. The answer to your question is, our direct sales team works both with Herbal and with the customers, and we're continuing to build that robust team.

**Scott Fortune —** Analyst, Roth Capital Partners, LLC

Guys, is there expectation for, you know, 50 percent coverage of California, where kind of how we look at the cadence of getting up to, you know, the higher 90 percent coverage for all of California over time here?

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

You know, there is quick growth and smart growth, and we're trying to make sure that when we pick up a store shelf, we're properly servicing that client so that we hold the shelf. You know, we certainly have goals to continue to grow that footprint, but you know, it's a measured approach by, you know, opportunities that are good for the stores and good for us.

**Derrek Higgins —** Chief Financial Officer, Glass House Brands

One of the fastest areas—this is Derrek speaking, one of the fastest areas that we see growth in CPG in the retail market is through our own stores that we own and control, where we see anywhere between 20 percent and 30 percent of the share of basket being devoted towards our products. As we expand our retail footprint, we're excited to be able to expand the momentum that we achieve with our CPG brands in the end retail market.

**Scott Fortune —** Analyst, Roth Capital Partners LLC

Well, I appreciate the colour (multiple speakers). Go ahead.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

I'll comment on that, too. I think as we mentioned before, you know, you see 10 to 15 times the sales in our stores as we see in an average third-party store for our products. As you can do the math, as we bring these new stores online, what that equals to in terms of kind of, you know, third-party store equivalents. That's part of the synergy that makes us really excited about the strategy of combining large-scale, high-quality cultivation with brand creation and our own owned retail, so I think that will be a large driver too of the brand growth. The other thing that we're seeing is as we've launched new SKUs throughout the year, we're seeing very good receptivity of broadening the shelf, right, so versus the more doors, we're broadening the shelf and the accounts that we're in, and that's driving significant CPG growth for us as well.

**Scott Fortunate —** Analyst, Roth Capital Partners, LLC

I appreciate it. Thanks for the colour. I'll jump in the queue.

**Operator**

Ladies and gentlemen…

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Thanks, Scott.

**Operator**

…your next question comes from Aaron Edelheit with Mindset Capital. Please go ahead.

**Aaron Edelheit —** Analyst, Mindset Capital

Hi, guys. I wanted to ask, strategically, when you think about your current greenhouses, versus the new state-of-the-art facility, can you tell me just in terms of quality and the type of cannabis, like, where you expect the new greenhouse to kind of fit in the landscape of outdoor greenhouse and indoor? Because I think that you're aiming towards higher than greenhouse and I'm just wondering if you can give some colour on what—where you expect that flower to position in the market?

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Thank you for the call, Aaron. Let me ask Graham to field that one.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Sure, yes, and it's a great question, and very much what we're aiming to do is compete with, you know, the quote unquote indoor quality flower that's in the market today. What we are not trying to do is compete with the bulk, machine trimmed, you know, bulk dried outdoor flower, right. I think it's worth stepping back and remembering that growers didn't go into a warehouse because the sun did something bad to the plant, right. They went into a warehouse to hide, and in the process, they discovered that if you have very good climate control, you can grow very good cannabis, right. If you think of indoor growing or warehouse growing as shorthand for perfect climate control, our goal, particularly with the Camarillo facility, is to have perfect climate control but do it without throwing away everything that Mother Nature has given us, right.

That's what happens when you go in a warehouse, and you use fossil fuel powered lights. When you need twice as much fossil fuel powered energy to remove the heat and then you need to add your own fuel, too because there's none that's naturally occurring, right. We see this in some of the recent press around the massive amounts of energy and the massive carbon footprint that's required to grow cannabis in a warehouse. Our belief is that with the Camarillo facility in one of the best climates for growing cannabis in the world, in one of the nicest, most high-tech, and best climate-controlled facilities on the planet, with the Glass House team and their experience behind it, that we will be able to grow indoor quality cannabis at very close to outdoor quality cannabis cost. And that the consumer, as they become more and more educated around the impacts of growing indoors versus growing in a greenhouse, will prefer that product and get it at a better value. You know, our target is really to go out there and provide some of the best cannabis in all of California, which we believe is some of the best cannabis on the planet.

**Aaron Edelheit —** Analyst, Mindset Capital

Thank you for that. And switching to the dispensary roll out, you just mentioned in a previous question that you sell 10 to 15 times more of your own product in your own store. I believe there was some mention that either Kyle or you, Graham, had talked about the opportunity to scale up the number of licenses you can take down. I think about, you know, if you just by the second half if you used the 15 times number, it’s the equivalent of you adding 200 new stores, if you just do 15 times, you know, the number, you know, the 13 stores you’re going to roll out.

Can you talk a bit about, you know, how aggressive you can become on dispensaries? Also, I saw a report like a week or two ago about the potential for an explosion in the number of dispensaries. You know, California is very under penetrated in terms of dispensary per population, and it looks like a lot of counties and cities are about to roll out a lot of retail or allow retail dispensaries. I’m wondering if you can talk about those, just those two things.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

You know, Aaron, this is Kyle. I would tell you that I think the statistic I see is about 70 percent of local jurisdictions in the state are still illegal. There is, as you mentioned, there is a massive opportunity there. I would tell you that in working with Element 7, we expect more licenses to avail themselves in that bucket. Also, Erik, you know, our Chief Business Development Officer, he's out there talking to a lot of different folks, and I would tell you, if you're a single Mom and Pop operator, it's tough with 280E and everything else. If you can connect in with the right culture, hopefully that's us, and we can provide that vertical integration. It's a one plus one equals three. That's very high on the list in your mathematics that you used; coincidentally gets thrown around here in our shop, too. We think of it the same way you do. I would tell you that we are out there actively having conversations and looking to expand that.

**Aaron Edelheit —** Analyst, Mindset Capital

Got you and last question—go ahead, sure.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Aaron, I saw an interesting stat along those lines that there is as many retail licenses in the pipeline today, currently, as has been issued total since the start of Prop 64 four years ago, right. I think we expect, as Kyle you know mentioned, the vast majority of communities and municipalities were fairly slow in the conversion, but a lot of them are going through the pipeline together, so we expect a rapid transition there, and that explosive growth of the retail is exactly what California needs to see. I think there's a really interesting dynamic that happens on the conversion between illicit and legal. When you have no legal options, there's not a lot of political will to shut down illegal shops, right. The populous of California voted for Prop 64 because they wanted more access, not less. As soon as you issue that first legal license, that entire dynamic switches. Now you have an operator flaunting the rules and not paying taxes and you have an operator who worked hard to follow the rules and they're paying taxes.

The second thing that happens is that operator now following the rules and paying taxes, typically one of the first buckets that the cannabis specific taxes they pay land in is the enforcement budget to now multiply with the political will to now get rid of the operators who are flaunting the rules and not playing fairly in the game. That is all tremendously valuable for Glass House and our strategy, our belief that, you know, the illicit market is probably still two to three times as big as the legal market. Those are all real customers. They're just not in our bucket yet, but just as sure as there are no gas stations that you can go to and buy gas for half price, we do not expect there to continue indefinitely to be cannabis dispensaries where you can go buy cannabis for half price and pay no taxes. As you put that mechanic together, I think it's all tremendously positive for us.

Also, you know, we're seeing a lot of interest and recognition from, you know, the single store operators out there and the synergy that comes with putting things together with our vertical integration and with our desire to be a brand making factory. The ability not only to sell 10 to 15 times of our brands, but also be able to get the feedback and the data and the analytics and have a beta platform to create those brands and get feedback on them, so we know when we're right, and more importantly, when we know where we're wrong and need to adjust. It's, you know, it's a tremendous value towards that long-term goal of brands and products that customers love.

**Aaron Edelheit —** Analyst, Mindset Capital

Thanks for that. Last question, can you give any kind of colour, specifics just on the interest rate that you agree to for the sellers financing? Is this something where you're paying like a double-digit interest rate or, you know, any kind of colour you could give would be helpful on just how you amended that, you know, the seller financing for the Camarillo facility.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Sure, sure. Aaron, and I will tell you I've been anxious to answer that question because we weren't so specific, I think in our release. I don't think we were, but we've had the question a bunch of times. It's nice to be able to just fully answer the question since we're on an investor call.

You know, the sellers have been fantastic to work with. They are finding out that when it comes to cannabis, local governments, they react a little bit more stringently, and it's taken longer for them to get a signoff of notice of violations. The notice of violations happen on almost all properties and in prior deals, like Padaro, we asked the seller to clear those, because it's a lot easier for an orchid farmer or tomato farmer to go talk then say Graham who everybody knows is the cultivation guy in California for cannabis. What was originally envisioned was we would close, after the notice of violation was signed off, there would be a local license sign off which we expected about 60 days after the notice of violations were off. We were supposed to close escrow at that point, or even it was contemplated originally that we might wait, you know, for after the state license which would come thereafter.

Unfortunately, they have faced some delays. They were running a massive tomato operation on the 5.5 million square feet that they had to wind down, and so the timing has taken so long that they're down to about the last 1 million to 2 million square feet and they're rapidly closing up that operation, so they came back to me and said, listen, why don't we agree to close when the notice of violations are signed off, which is earlier than contemplated. We basically, what we negotiated was yes, let's do that.

We want the farm. We want it faster than, you know, Graham can't wait to sink his teeth in out there, and so we said, why don't we do this to make it a fair transaction. They decided to carry the $118 million purchase price. They're carrying $30 million. They agreed to do it at and yes, I know the market is 10 percent or higher, double digit as you pointed out, but they're carrying it for zero. Yes, something does come free in this world for a little bit, and that's all the way through the end of the local licensing. Then, between the local licensing and the state licensing, between that time or the end of the year, whichever comes sooner, they're charging just a simple 8 percent.

We look at this as it's probably a 4 percent loan through the whole thing is what we were thinking. We're really excited about that. We think the seller has been more than gracious and we think they'd say the same about us but, yes. It's the cheapest loan to cannabis I have seen to date, so I'm really proud of that.

**Aaron Edelheit —** Analyst, Mindset Capital

That's great and just speaks to the credit of, you know, the strong balance sheet you have and that you all know your real estate. It's a credit to your team. Congrats on your first quarterly call. I hope you're having fun.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Thanks, Aaron. Really appreciate your questions.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Thanks, Aaron.

**Operator**

There are no further questions at this time. Please proceed.

**Kyle Kazan** — Co-founder, Chairman and Chief Executive Officer, Glass House Brands

Thank you for joining us today.

I would like to take this opportunity to thank our team who has worked diligently to move forward with expanding our cultivation and distribution footprint, improve supply chain and production efficiencies, and enhance our consumer brand profile.

We look forward to speaking to you in November when we announce our third quarter results. Have a great day. And a special shout out, I'm getting a text from team members that are wide awake here at 5:00 a.m., so thank you guys for getting up early. Thanks, everybody.

**Derrek Higgins —** Chief Financial Officer, Glass House Brands

Thank you.

**Graham Farrar —** Co-founder, President and Board Director, Glass House Brands

Thanks, everyone.

**Operator**

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.