Transcript of
KushCo Holdings, Inc.
Fiscal Second Quarter 2021 Earnings Call
April 08, 2021

Participants

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Aaron Grey – Alliance Global Partners
Scott Fortune – ROTH Capital Partners

Presentation

Operator
Greetings, and welcome to the KushCo Holdings Fiscal Second Quarter 2021 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Mr. Najim Mostamand, KushCo's Director of Investor Relations. Mr. Mostamand, you may begin.

Najim Mostamand – Director of Investor Relations, KushCo Holdings, Inc.
All right. Thank you, operator. Good afternoon and welcome to the KushCo Holdings' fiscal second quarter 2021 earnings conference call. A replay of this call as well as a copy of the supplemental earnings slides will be archived on the Investor Relations section of the KushCo Holdings website, ir.kushco.com.

Before we begin, please let me remind you that during the course of this conference call management may make forward-looking statements. These forward-looking statements are based on current expectations that are subject to a number of risks and uncertainties that may cause actual results to differ materially from expectations. These risks are outlined in the Risk Factors section of our SEC filings. Any forward-looking statements should be considered in light of these factors.

Please also note, as a Safe Harbor, any outlook we present is as of today and management does not undertake any obligation to revise any forward-looking statements in the future.

With me on the call today are our Co-Founder, Chairman and CEO, Nick Kovacevich and our CFO, Stephen Christoffersen.

With that, I would now like to hand the call over to Nick. Nick?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks, Najim, and thank you all for attending our fiscal second quarter 2021 earnings call. I know many of you tuned in last week to listen to the exciting news of our announced merger with Greenlane. We certainly have been receiving a lot of positive feedback and congratulatory messages since that announcement. And we look forward to continuing to provide updates and more information, as we move closer toward the expected closing date, which is targeted for late Q2 or early Q3 in calendar 2021. But of course, this is our earnings call and I want to shift gears and focus on our financial results for fiscal Q2 before opening it up for Q&A.

So with that, let's turn to slide five of the supplemental earnings slides, where we go over our financial highlights for the quarter. Starting at the top of the slide, we generated $32.9 million in revenue for fiscal Q2, representing 23% growth over fiscal Q1. Even if you exclude the roughly $3 million we estimate slipped from fiscal Q1 to fiscal Q2, due primarily to the shipping delays at the ports, we still experienced strong quarter-over-quarter growth, as we continue to make progress on our strategy of aligning deeper with the top MSOs, LPs, and Leading Brand customers.

More importantly, fiscal Q2 saw a return to year-over-year revenue growth after several quarters demonstrating an acceleration of our top line following nearly a year of disciplined execution and cost cutting. What we're perhaps most excited by with this significant growth is the fact that an increasingly larger portion of it is coming from an elite customer group that we have been nurturing for the last two years now. In fact, more than three-fourths of our total revenue for Q2 came from our top 25 customers, up from 61% the same period a year ago. We believe this validates our strategy to deepen our relationships with these customers, as they continue to rapidly scale and consolidate the industry.

A key part of this strategy is locking in these customers to long-term supply contracts where we can become stickier with them, and where we can have more predictable and steadier streams of revenue. Last quarter we announced securing a large top five publicly traded MSO into a long-term supply contract. And during Q2, we locked in a leading West Coast operator bringing the total to five contracts signed to date with several more in the pipeline. And our efforts to secure long-term contracts with our customers do not just end with our vape and custom packaging solutions, but also extends to our energy solutions as well.

As of today, we have 38 executed contracts for our stainless steel tanks, up from 22 at the start of the year. Revenue for fiscal Q2 2021 would have been slightly higher than 32.9 million but we did continue to experience the uncontrollable shipping delays we experienced in fiscal Q1 due to record shipments in the US ports and not enough people at these ports to offload all of the shipping containers, as well as a shipping container shortage globally. As a result, some of the revenue that we were expecting to land in Q2 will be pushed out into Q3. It's worth reminding that these delays have impacted virtually all importers of goods, and have been exacerbated by the COVID-19 restriction. In addition, they continued to increase freight costs, putting pressure on our gross margins, which brings me to the next item on the slide.

On a GAAP basis, we generated 20% gross margins for the quarter, which is down from 21% we generated in fiscal Q1 2021. The decrease was due to the shipping delays I mentioned earlier but fortunately, we are starting to see these delays slowly clear up. In the meantime, we are doing the best we can to preserve margins, while still getting products to our customers on time. As mentioned on the last call, we are working diligently with our network of freight providers and suppliers to expedite shipments and provide solutions that can reduce the impact to our customers.

It's uncertain when the backlog will be completely cleared but we are starting to see some progress, which should only be accelerated by the continued COVID-19 vaccine rollout and the overall relaxing of the restrictions at the ports. As the backlog gets cleared, we do expect these margin headwinds to stabilize, which should help us get back to the mid-20% gross margin target we've been tracking internally.

Moving on to cash SGA, we did see an increase this quarter sequentially, largely related to items that we believe are one-time in nature, including expenses related to our proxy, D&O insurance, warehouse transfers out of our soon to be closed Washington and Michigan warehouses and the opening of our new 130,000 square foot West Coast warehouse in Moreno Valley, California. This new facility is almost three times bigger than our current Garden Grove facility and we believe it will enable us to increase our speed to fulfill orders, reduce our transfer costs, and ultimately better serve our customers.

With this new facility going live last week, we now have substantially completed our warehouse consolidation strategy going from a peak of seven major warehouses at the start of the pandemic to just two operating warehouses here in the next couple of weeks. Entire effort has allowed us to reap in aggregate $1.3 million in annual cost savings due to lower rent expense and inventory transfers between warehouses while still providing exceptional service to our customers.

Even though we are pleased to see the revenue growth returning nicely, we are not taking our eyes off the ball when it comes to maintaining our cost structure to ensure a solid platform for profitable growth. And although we weren't able to continue our streak of positive adjusted EBITDA this quarter, due to the margin headwinds and increased one-time costs that we talked about, we are encouraged by the overall work we have done to support profitable growth going forward. We've already completed it twice in the last three quarters and as we expect revenues to continue to climb higher, both as a result of our own sales efforts as well as industry tailwinds, we should be getting back into positive adjusted EBITDA territory very soon.

With that, I'd like to now turn to slide six, where we break out our sales by our top 25 customers versus the rest of our customer base. Notice that we are now providing metrics on our top 25 customers rather than the top 100 customers, which we have done historically. This is because we really want to highlight and focus on how the vast majority of our growth is being driven by the leading operators in our industry today; the folks who are continuing to expand, open new locations, acquire competitors, raise significant capital and repeat the success.

Sales to these elite top 25 customers were up 35% sequentially. They made up 61% of our revenue in fiscal Q2 of last year, and have been climbing ever sense to now make up 77% of our total revenue for fiscal Q2 of this year. We really believe we are hitching your wagon to the right horses.

And you can see this through the financial results of many of the publicly traded multi-state operators and Canadian LPs who are aggressively securing new licenses, opening new stores and acquiring competitors.

Next, we'll look at slide seven, where we break out our sales by geographic market. Both adult recreational and medical markets experienced strong healthy growth in fiscal Q2 with a few notable call outs. First, you can see that California rebounded again after a different fiscal Q1. We have been focusing a lot more on our home state and investing our sales force to capture the resurgence that has occurred in the state. More and more operators, including several new sparx are now beginning to enter the world's largest cannabis market and we are positioning ourselves to capture this growth, especially with our new California warehouse.

Illinois was a hands down best performing market for us during the quarter, as we saw revenue more than double sequentially to $3.3 million. As we mentioned on the last call, we had more revenue in Illinois in just the first month of fiscal Q2 than we did in all the fiscal Q1. This was largely a result of our strong relationships with the key operators in the state, as they work to increasingly fulfill the significant demand in this market.

Massachusetts is also another important market, especially as we are starting to see more MSOs deepen their presence in that state. We generated revenue of $2.4 million in fiscal Q2, the highest ever in company history, as our customers continued to expand operations, particularly in wholesale in this very key East Coast market. And even more encouraging is the fact that some of our legacy markets such as Washington, Nevada, and Oregon saw a healthy rebounding Q2, suggesting a stabilization of revenue, as these markets open up further following a challenging year of COVID-19 restrictions.

Turning now to our medical markets, where we had one of our strongest quarters ever in Q2 with $12.6 million in revenue. This was driven by a record quarter in Florida, Ohio and Pennsylvania, as well as strong quarters in Maryland, New York and Arizona, which we are classifying here as a medical market but will separate out as an adult rec market going forward, given the adult use program went live in January. And finally, we reached over $3 million in sales in Canada for the second time in company history, representing 30% sequential growth as our customers continue to expand their Rec 2.0 offerings and more retail stores open up in provinces despite some of the recent COVID-19 related lockdowns.

Next, I'd like to dive into slide eight, which is our revenue by product mix. Following a flat Q1, vape grew nearly 30% to $23.3 million in sales for Q2. We're starting to secure some large vape orders with our new MSO customers including a $1 million vape order that landed in Q2 with a new customer of KushCo, who happens to be a publicly traded MSO. Going forward, we're excited to continue selling higher margin pod systems by CCELL. But the real game changer will happen when once the anticipated Greenlane merger closes, as we not only will leverage our deep relationship with CCELL but also Greenlane's premium third party brands and wide customer base to become a formidable player across the board in the vape market.

The same goes for packaging where once the merger is closed, we will be combining two premier and complimentary packaging platforms led by Greenlane's innovative Pollen Gear and our expertise in delivering highly custom solutions for our premier MSO, LP and Leading Brand customers. With over 200 plus articles of intellectual property, the combined company will have a strong innovation platform to enhance value for our customers and deliver the product lines their consumers are seeking.

But as it relates to our business today, packaging papers and supplies saw another strong quarter of sequential growth, as we continue to recognize the revenue of some of our higher value custom packaging projects. This pipeline of projects is continuing to build, especially as other customers who are not currently taking advantage of our capabilities are starting to see what we can do when these products hit the market.

In fact, just to name one prominent example, which is all public for everyone to check out, is GTI's brand new RYTHM packaging. This highly innovative product line utilizes our custom packaging expertise to create something sleek and truly differentiated that also works with high volume automation equipment. We have been building on this momentum by launching new packaging innovations that are thoughtfully tailored to specific customer needs.

This includes a line of patent pending, certified child resistant compatible bags as well as certified child resistant compatible vape packaging. It goes without saying that we are continuing to make the investments necessary to ensure a robust pipeline of innovative new products and we are very excited to marry KushCo and Greenlane's distinct yet complimentary packaging capabilities once the merger closes.

And last, I want to take a brief look at our Energy and Natural Products bucket which generated $1.5 million of revenue for the quarter, slightly down from last quarter. As we shared on our last call, energy has been an area of focus this fiscal year, not just on the ethanol side, where we have seen some meaningful traction with MSOs, but also on the butane front as well, which is higher margin and a key stepping stone to cross selling our customers into some of our other offerings.

Of course, our key differentiated offering in the butane market is our stainless steel tank, for which we've been seeing strong adoption from our customers. Today we have just shy of 40 supply contracts executed for these tanks and we're on track to hit our internal goal of getting 100 contracts executed by the end of our fiscal year. These tanks are not only great for our customers, like the fact that they are considered a cleaner vessel, but they're also great for us as they create an attractive razor blade model with strong revenue economics.

And with that, I'd like to turn the call over to Stephen who will walk us through our Q2 financial summary.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.
Thanks, Nick. I'll now turn to slide 10, which displays a snapshot of our income statement for the quarter. Total net revenue increased 9% year-over-year and 23% quarter-over-quarter to 32.9 million. As Nick mentioned, we're seeing stronger growth from our MSO and LP customers as part of our strategy to align with the industry's leading operators. On a GAAP basis, gross profit for the quarter was 6.4 million or 20% GAAP gross margins.

As Nick mentioned, gross margins were down sequentially, primarily due to an increase in shipping charges. But looking ahead, we believe that these shipping charges will normalize and we will continue to ship more product on boat, which should help drive a rebound in gross margin in future periods. On a non-GAAP basis, excluding the impact of the China trade tariffs, gross profit was approximately 6.9 million or 23% of revenue. For a complete reconciliation of GAAP to non-GAAP financial information, please visit the reconciliation table at the end of this presentation or in our fiscal Q2 earnings release.

Sales, general and administration expense for fiscal Q2 2021 was approximately 10.9 million, which was down from 27.2 million in fiscal Q2 2020. The big drivers year-over-year were reduced headcount, bad debt expense, consulting spend, and travel and entertainment expenses, as a result of the COVID-19 pandemic as well as the implementation of our 2020 plan to right size our business and align with the leading operators in the cannabis industry. Cash SGA, which excludes non-cash expenses such as bad debt, stock-based compensation, depreciation and amortization was 8.4 million, which was up sequentially but down from 13.6 million in fiscal Q2 2020. The big drivers year-over-year were reduced consulting spend and lower facilities cost.

Turning to the next item, on a GAAP basis, net loss for fiscal Q2 2021 was $5 million or negative $0.04 per share, but which represents an improvement from the net loss of approximately 44.4 million or negative $0.40 per basic share in Q2 2020. The significant year-over-year improvement was driven by our restructuring initiatives, which led to a prepaid inventory write offs of 3.3 million as well as excess and obsolete inventory charges of 11.9 million in fiscal Q2 2020. On a non-GAAP basis, excluding the impact of certain non-reoccurring charges, our net loss for the quarter was approximately 3.1 million or negative $0.02 per share, compared to a net loss of 17.5 million or negative $0.16 per share in fiscal Q2 2020.

And finally, adjusted EBITDA for the quarter was negative $0.7 million compared $0.5 million positives in Q1 2021 and a negative 14.8 in Q2 2020. The decrease was due to lower gross margins and increased cash SGA, as Nick touched on earlier, while the improvement year-over-year was driven by the aforementioned cost reductions.

As you can see on the next slide, slide 11, we're starting to realize meaningful growth in the business and have returned to year-over-year top line growth. While we did not achieve positive adjusted EBITDA in fiscal Q2, we are right on the cusp of profitability and expect to return to positive adjusted EBITDA once some of the shipping related delays resolves, as we continue to grow revenue. As we have said before, our goal is to continue growing the business profitably and we believe we have a nice foundation to do so.

Turning now to slide 12, which provides a snapshot of our balance sheet, as of the end of fiscal Q2. Our AR for Q2 decreased sequentially from 12 million in fiscal Q1 to 10.4 million in fiscal Q2 due to strong collections activity, including from some of our smaller customers. Total inventory as of the end of Q2 increased sequentially from 34.7 million in fiscal Q1 to 50.8 million in fiscal Q2. As we shared on the last call, we ramped up our purchases during fiscal Q1 and even in fiscal Q2 ahead of Chinese New Year, and to do our best in order to avoid supply disruptions caused by the COVID-19 pandemic. With that being said, we are encouraged by the fact that a sizable portion of these products are linked to custom projects for some of our larger MSO and LP customers who have the financial wherewithal to pay for these products and are eager to differentiate their brands.

Cash during fiscal Q2 was up significantly quarter-over-quarter due to the late February capital raise where we raised $40 million in a highly oversubscribed offering anchored by some key and long-term institutional investors. As we announced via press release in late March, we have used a portion of the proceeds from that offering to completely pay down the 17 million term note that was due at the end of this month and have also used the portion of the proceeds to pay down our entire line of credit, leaving us with virtually no debt and a healthy amount of working capital to support our continued growth.

With that, I'll turn it back now to Nick.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

All right. Thanks, Stephen. Now, just to quickly wrap up, we're pleased with how the quarter finished, especially given some of the shipping-related headwinds we continue to face. Looking ahead, we remain encouraged by the rapid pace of new states legalizing cannabis, as we've already seen this year with Virginia, New Jersey, New York, and New Mexico, leaving actually only one state starting with the word new that is yet to legalize cannabis in the US. These catalysts, along with a meaningful momentum at the federal level for cannabis reform coincide nicely with our anticipated strategic merger with Greenlane. Once the transaction is closed, the combined company will be well positioned to capitalize on these macro-tailwinds through our enhanced scale, differentiated customer offering and significant cross-selling opportunities.

Due to the pending merger, which we expect to close in late second quarter or early third quarter of calendar 2021, we are retracting our net revenue and adjusted EBITDA guidance for fiscal 2021. That being said, we could not be more excited for the attractive opportunities that lie ahead as we joined forces with another industry pioneer to create the leading ancillary cannabis products and services company.

And with that, I'd like to turn it over to the operator for Q&A session.

Operator

Thank you. At this time, we will be conducting a question-and-answer session. [Operator Instructions] Our first question is from Owen Bennett with Jefferies. Please proceed with your question.

Q: Afternoon guys.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Hey, Owen. How are you?

Q: Yeah, good. Thank you. And just a quick one for me, so you're getting – gaining strong momentum on the stainless steel tanks, I just want you to understand how incremental growth can be here, if you hit your target of 100 contracts, I think you said? And so can you remind us what the economics look like on the solvents specifically and what's the average sales contribution per contract and what are the gross margins? As I recall, I think margins on the solvents overall were around 40%, so would it be fair to assume that butane is somewhat higher than the 40 and ethanol is below 20?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks, Owen. Great question. I'll let Stephen give some color, but first -- on the margins. But at first at a high level, the way you should be thinking about the stainless steel tanks and the butane business, it's not going to be so much of a driver of top line revenue growth. But I think a lot of people have said, hey, what is KushCo going to be doing when other companies come into the sector that are larger, that are maybe from outside industries. And so we're showing people what we're doing to protect against that, right. Obviously, we feel that we have a unique product portfolio. We can get very sticky by selling across multiple categories. We feel we have intellectual property that will protect us.

However, these are some additional things that we're doing right. We've innovated with these stainless steel tanks, nobody else is in the market, to our knowledge, with these tanks. And then we're going out and signing contracts, which are typically one year with auto renew. But if somebody loves the vessel that they're in, they're not just going to change back to a carbon steel vessel, right, these are superior vessels. So once they become accustomed to it, they're likely to stay in it for the long haul. So we like to think people to think of this business as just highly reoccurring, highly sticky, something that's under contract, and does have very good margin profile.

It's not going to be the revenue growth driver but it's a very nice anchor to build, and just continue to churn. And then where we also can drive some revenue off of this is via cross selling. We know that everybody's buying butane is either making oils or concentrates are likely going to need vape pens and concentrate containers and vape packaging to go along with it. So for those reasons, it's very strategic but again, I would caution people as to looking at this as something that's going to significantly move the needle from a top line perspective. And then, Stephen why don't you to go ahead and give some additional color on the margin profile there, as Owen zone is asking.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.

Sure. Hey, Owen. Thanks for the question. So you get on the material margin, so butane is higher, obviously, than ethanol. So on the direct material margin, that category is running right around 46%, factoring in freight, I mean, because we basically keep – we keep the driver up there and COGS as well, you get sort of call it a landed margin, 39%, 40%, for that category. And then the salesperson, there's a really small sales team out there that can kind of sit down and meet the product team and can scale across the enterprise. I just wanted to give one call out, obviously it looks like the sequential decline -- it looks like a sequential decline in energy.

Previously we include energy and natural products in this bucket, so there was a fair amount of terpene business that was being captured in this bucket. So, two things happen in the terpene category. Number one, obviously, on the back of the vape crisis, the demand for botanical terpenes drops significantly. Obviously, this is non cannabis derived terpenes, botanical terpenes dropped. So we saw that impact in the bucket.

And then we also change the accounting methodology, where we basically reworked our contract with Abstrax, who's our vendor there. And it's basically just capturing the margin as revenue whereas previously, we were sort of transferring the product and recognizing revenue on the full amount. So just a little bit of accounting noise in the way that we are accounting for that natural products bucket but that's really what's driving the decline in the overall energy bucket.

Q: Okay. That was really helpful. Thanks, guys.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
Thanks, Owen.

Operator
Thank you. Our next question is from Aaron Grey with Alliance Global Partners. Please proceed with your question.

Q: Hey, guys, thanks for the question. First one up for me is on State of Illinois saw a nice jump quarter-over-quarter. So just want to get some more color there, whether or not there was anything timing going on there because I know there are some big operators that might have had an impact for the big step up, or whether or not that represents kind of a good run rate kind of going forward? And also how much that might be tied to additional 75 social equity licenses being opened up and kind of seeing more growth or continued growth, I guess, at the state level there in Illinois. Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
Yeah, look, I think just at high level, we're seeing the same data everyone else sees. Illinois seems to be really growing. Cannabis consumption is up significantly, seemingly like every single month, right, that they report the data. So that's great. Obviously more access is going to drive the growth, we're seeing that in California, we have been talking about that forever. As more retail stores open up, we're going to see higher cannabis consumption numbers. So, I think it's just a healthy market. We happen to be positioned with a few of the leading MSOs that are well set up in Illinois. So, we're benefiting from the fact that we're with the right customers.

I won't say, specifically, I don't believe that the additional social equity licenses are a contributing factor to this number, at least at this point but I do think it's great for the market, just on a personal note. So look, I think this is going to be a market that continues to grow. And certainly with more access, it will only grow faster. I mean, this is a market where the economics are making sense for large MSOs to invest resources into. And so, as a company that's trying to align with those MSOs, we should continue to track very well on this Illinois market.

Q: Alright, great. Thanks. That's helpful. And the second question for me, so I know you guys still had some freight issues during the quarter that impacted the gross margins, looking to get to mid-20s kind of over time. Any color that you could kind of offer in terms of -- I think, prior, we're talking about fiscal 4Q, is that potentially going to get pushed out a little bit now? Still uncertain, just because you're still having some impact, at the freight level or any kind of color in terms of the timing of when you get to that kind of mid 20s target? Thanks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
Yeah.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.
Nick, I can take that. Go ahead.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
You know, looks -- yeah, sorry. I'll give the high level so and then I'll let Stephen jump in. But, at the high level, ultimately, we feel that we have the direct material margin or direct product margin to hit the mid-20s even today, although freight and other issues have dragged that down. Tariffs alone, right, we estimate it cost us between two and three points of margin. So again, if the tariffs were to go away, we would jump up considerably.

So, there's those factors, but still with that, yeah, I mean, I think we feel confident. We don't know how the freight is going to clear up but then the bigger point that I wanted to drive home before I give Stephen the floor, is that that's one of the -- also one of the driving factors with the Greenlane merger is a path to significantly higher margins, because of the fact that they have company-owned brands that demand a margin premium and they're going through direct-to-consumer channels, which are typically higher margin than the enterprise channels that we service.

So the KushCo business, certainly can execute on the mid-20s but the combined Greenlane KushCo business has a higher ceiling for margins, especially as Greenlane continues to gain traction on their company-owned brands. Go ahead, Stephen.

Stephen Christoffersen – Chief Financial Officer, KushCo Holdings, Inc.
Yeah, I was just going to make a point, while we are starting to see some of the freight headwinds get a little bit better and that might sort of materialize, certainly before the end of our fiscal year. Keep in mind, Aaron, the inventory that we purchased, we capitalize a lot of those freight and tariff costs on the balance sheet, right. So we've already spent a lot of that money, right. So as we sort of sell through that inventory, we're almost going to be thinking about it that the freight headwinds are going to have a little bit of a lag. So I just want you to be -- if you're thinking about your model, sort of taking those into consideration, but we certainly do start to see it normalize and get back to that mid-20s GAAP gross margin, but obviously, as Nick alluded to, a big driver, a big selling point for us, as a management team for the Greenlane merger was a path to significantly higher gross margins for the combined pro forma company.

Q: Alright, great. Thanks and I'll jump back into queue.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
Thanks Aaron.

Operator
Thank you. Our final question is from Scott Fortune with ROTH Capital Partners. Please proceed with your question.

Q: Good afternoon and thank you for taking questions. Just a little bit of clarity here since 77% of revenues come from the top 25 MSOs, are you seeing longer-term supply orders out there, larger purchasing orders ahead of, as these MSOs are ramping up into new states in the second half of ’21 here. Just kind of incremental outlook on the kind of second half, as your order purchasing are coming through ahead of that?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.
Yeah. Yeah, we are, Scott. Great question. We're seeing the MSOs planning for growth, getting some orders either forecasted or actually put in that are larger, as they're growing. We're also seeing some of the MSOs managing acquisitions and obviously, that's hard not knowing exactly when those are going to close. But we've even had scenarios where -- again, factoring into the freight, where we helped out some of the MSOs that were in a jam, because of the fact that acquisitions close and volumes kind of spike ahead of them being ready from an inventory supply standpoint, also some other vendors that have dropped the ball.

So, again, we'll go ahead and air freight in some vape pens for them, but kind of setting our expectation going forward in a more normal cadence, we'll be receiving forecasts, we'll be planning against those, and we'll be able to evoke freight in goods and preserve margin. So, some of the margin stuff was one-time, just in terms of customer dynamics as well, so that's an important call out. But yeah, I mean, we're seeing the ramp. There was some COVID lockdowns that, I think, suppressed Canada and they're coming out of those.

So, every market is a little bit different but yeah, for the most part, we're tracking that growth with our key MSO clients and that's why we're not concerned about growing our business. We know it will grow as long as we take care of our top clients and then ultimately, like I tell my sales team, almost every day is, if we can add another client that have the same profile of these top 25, it can really move the needle. So in addition to maintaining and cross selling our current client base, we want to be able to add a meaningful client or two every single quarter going forward.

Q: Nice color. I appreciate that. And then on the national side, congratulations, Canada is up pretty significantly quarter-over-quarter. You call that a little bit 2.0 products, and more stores are coming on board, kind of stepped up to even in a tough COVID environment, right, but kind of stepped up to the international side and the opportunity you bring on Greenlane, going into

Europe, potentially, as a strategy going forward, but kind of on the Canada side, you see upside there?

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Yeah, I think Canada is a good market. It's going to get better. There's consolidation taking place, as we expected. There's -- 2.0, I think was -- obviously, it was brand new when it hit and I think there were decisions made in terms of supply chain, based on historical relationships, maybe based on price. Whereas, I think the US had already gone through a lot of that maturation in terms of understanding which vape hardware can lead to the best performance and ultimately win market share with the end consumer. And I think people -- operators in Canada are now switching to CCELL for that reason, so that's a good sign. And again, I think we will help feed the 2.0 market there with just better quality vape devices in the field. So that's good.

And then that's a launching point for global cannabis. We know that Canadian LPs have the ability to ship their product and also expand globally into Europe and Australia. And so being aligned with them will allow for our global expansion on the KushCo side, but we've always looked at global expansion for KushCo alone as maybe something later down the road and simply because the enterprise clients aren't as large and the markets aren't as concentrated of you just don't have the ability to drive the volume that you do here in North America.

However, with the Greenlane business model, it's different. They're able to go directly after consumers. And we know cannabis consumption, globally, still remains very high and is growing only higher, right. So having that ability to now go after consumers with CPG products and to ship company-owned brands into traditional and specialty retail, that's a compelling argument to strengthen and actually invest more in global operations; Europe being probably the main one, given the population, given the trajectory and also given the existing footprint and presence that Greenlane has; also Canada where Greenlane has a significant presence.

And we're going to actually be able to see in these federally legal markets like Canada how much adoption of these CPG products are going to be in mainstream retail. We know that in the US there's more adoption in specialty retail and smoke shops today. We're expecting significant adoption into cannabis retail stores over the next few years. But at some point, when are these CPG products going to be sold in mainstream retail? Well, I think in a federally legal environment, that's likely to happen sooner; Canada being one of them. We're going to be closely monitoring how that market plays out, as sort of a proxy to how future legal country markets are going to play out as well.

Q: Appreciate. Thanks for the color.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Thanks, Scott.

Operator

Thank you. Ladies and gentlemen, we have reached the end of the question-answer-session. And I will now turn the call over to Nick Kovacevich for closing remarks.

Nick Kovacevich – Chief Executive Officer, Co-Founder and Chairman, KushCo Holdings, Inc.

Okay. Thank you all. Appreciate you attending. We appreciate the thoughtful questions as always and for you continuing to be up to speed on the latest with the company. I know, we just did the merger call last week. A lot of fun things going on. A lot of exciting things, both from an industry perspective but perhaps, more importantly, from a company perspective, as we are preparing to get all the necessary approvals to consummate this merger with Greenlane. It's truly a game changer. As I mentioned, on the call last week, we believe it just makes sense, makes a ton of sense.

First and foremost, it's coming together of two successful pioneers in the industry, right 25 plus years of combined operating experience, and bringing together two complementary product portfolios and customer bases. It also is effectively diversifying our business and giving us substantial cross selling opportunities to execute on. Together, we'll achieve a level of size and scale and we can build a strong platform that will ensure profitable growth over the long haul and it would take -- arguably takes much longer for us or for them to do that on a standalone basis. We know these businesses need scale and this merger will accelerate that.

On top of that, KushCo shareholders will benefit from the NASDAQ listing, which many of you know has been a goal of ours for quite some time and we're now almost there doing it in this creative way that we believe is going to add incremental value for our shareholders. Together with Greenlane, we're creating an ancillary powerhouse that is anchored by the leading MSOs, LPs and brands with a strong portfolio of company-owned brands and retail and consumer channels.

Upon closing, we expect to finally get the recognition in the market that we believe KushCo deserves as more institutional investors will be able to invest in our stock and participate in our go forward success. This is especially true given the likelihood that federal legalization will not occur for the next several months, if not quarters. Given this scenario, investors that want to invest into top MSOs, US operators but don't want to own non-exchange listed or non-NASDAQ listed stocks, can now directly invest in our combined company upon closing and by proxy receive that meaningful exposure to the top US cannabis operators.

Overall, we're incredibly excited by the opportunities in front of us, with both this merger and the industry in general. And we look forward to providing more updates here in the coming months. So again, thank you all for listening. We hope you all take care. Stay safe, and we'll see you on the next earnings call. Cheers.

Operator

Thank you. Ladies and gentlemen, this concludes today's conference call. You may now disconnect.