

Transcript of Interview with Merida Capital's Mitch Baruchowitz

Interview by Aaron Edelheit

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*Lightly Edited for readability

Aaron: Mitch, thank you so much for allowing me to interview you and to learn from you, and I want to start out with your thesis that the legal market, the legal cannabis market is eating the illegal market. And I'd like for you to explain that and what the implications are.

Mitch: Well, first, Aaron, thanks for having for me and for bringing Merida to a broader audience. Well, you know, I've written a lot about this specific subject about normalization and our thesis that the illegal market is definitely being cannibalized by the legal market and how covid actually accelerated that. And I think a lot of that thesis is really driven by just data and information. We know what the sort of the total consumption in our country is for the United States. Right. It's something around one hundred billion dollars. And we know that the illegal market makes up the vast majority of that right now call it 60 to 70 billion. And that the legal market, that's easy to track. Very easy track because you just take the receipts and stubs from every state which New Frontier or BDS or HeadSet can do so. We know the legal markets in the 20-billion-dollar range for 2020. So, 2020 marked a tremendous milestone for the legal market, which is it's the first year where the total growth of consumption, which is around three to four percent. So, think of it, it's 100 billion dollars now. It's one hundred and three billion at the end of 2021. And I'll get into that maybe a little bit later. Why that will accelerate when more legality comes because stigmas as they drop, you'll see an increase in what we call the the looky loos, the people who are curious but not necessarily consuming just yet. But when you look at that number, it's a sliding chart. So, you have illegal up here, legal here. And it just is starting to normalize. And so, we know that the legal market outgrew the illegal market for the first time in 2020. So, if there was three billion of additional consumption, the legal market was one point eight billion or two billion of that of new consumption. Now, obviously, the legal market is growing much faster as consumption only grows three percent, the legal market is running at 30, 40 percent. So, we know just intrinsically QED in math that the illegal market is not growing as fast, that the legal market is going much faster than the total addressable market of cannabis consumption. So, we know that the legal market must be getting those sales from somewhere. So, we obviously know that the legal market's growing. Now, add to the fact that we are a big investor in companies like New Frontier and Simplify and Media Gel and companies that collect information related to consumption. And when you do that, you can see clearly that if you do a

survey of the average consumer, there are someone who has had a lot of experience in the illegal market. So why did covid affect it? Well, curbside and delivery are things that people in the illegal market are quite familiar with, delivery in particular. So being able to access cannabis in the manner in which they normally access in the illegal market has driven a lot of consumers into the legal market. We also know that access, choice, quality has far, far moved beyond what the illegal market can provide. So, if you're someone and you love flower, the legal market is now producing some of the best flower in the world. The illegal market still produces good flower, but the legal market, because of the Capex, because of the supply chain, the certainty of what you're getting is so far superior in the legal market where you can read a label. And then most importantly, safety. Safety became a real focus in covid. So, people who may consume an oil illegally now want it, coming out of a vape crisis as well, which is late 2019, you know, two different events that essentially drove safety as a concern. And so, when you look at those things, we call it the CAQS. Choice, Access, Quality and Safety really drove the illicit consumer to give the legal market a chance. And, you know, you can see that in California where the legal market numbers are now exploding. And we just think that in general, the pandemic has put a real crimp in the supply chain of the illicit market. The ability to ship product in New York is far diminished when all of the pallets are filled with Amazon or other products in e-commerce. So that uptick really put a dent in the illicit market's ability to ship to these markets, which means people can only get their products through the legal means. So, we've seen a real dramatic shift and I bet you you'll see a huge acceleration of that in in 2021, 2022 where just the pure operational mechanics, the only thing you really see an advantage of in the illegal market still is price. And it's getting to scale in the legal market, which means you will see a diminution in price, which once you see parity in legal and illegal markets, you will see a huge shift and also obviously driven by any potential legalization at the federal level as well. So, we think taxation, the only thing left is for regulators to make taxation a little smarter. Once you see taxation, maybe get a little bit more sane in places like California, then the legal market becomes gangbusters. And I bet you'll see that the cannibalization of the illegal market going hyperspeed.

Aaron: Wow. So, you're making an argument that the what we've seen so far is just the beginning.

Mitch: Absolutely.

Aaron: Where do you see where we're I mean, if you take an estimate, you assume go out three to five years and assume maybe the total cannabis market is, I don't know, \$110, \$120 billion, like, what would you guess would be the legal versus the illegal market? The split.

Mitch: Well, if you go back far enough into, well, there's another element that you and I spoke about, probably, but I'm not scared to say in public what I say in private, which I'll get to in one second. But if you look at some of the things, we've written in like 2018 and 2019, we often talk about the size of the general market, what is the real TAM (total addressable market) of cannabis? And one of the arguments we made back then was that no rational analytics can actually predict the size of it because there's no analogues that we have. That anyone has it. Whether you're Market View Research or any of the research shops, you have to underestimate because to overestimate is to lose your credibility. So New Frontier, Headset, BDS, all the data companies, and New Frontier. When you look their analytical methodology it almost has to underestimate how big the market can be because cannabis has a scrutiny that you just don't get in the regular world. So, we think when people predict 20 billion. So, what argument we made two years ago was that ignore predictions of market size because everyone is guessing, and that guess is actually driven by almost an opposite bias to be too conservative. So, when we saw people predicting twenty-five billion of sales by 2025, we knew that that was going to be wildly underestimated. So, in just two years, look at how quick the estimates have moved from a lot of people were predicting 2020 to be eighteen/nineteen. It did more than twenty. 2021 maybe to be a twenty-two, twenty-three. It'll probably be twenty-six, twenty-seven. You know, you're talking about now you're seeing estimates in the forties. We think that it's getting better, it's getting closer. But I mean think of one of the arguments you make, think of the other unknown, the medical side. So how quickly traditional pharma or anecdotal pharma. So, let's call that the empirical evidence of cannabis's effectiveness in certain places. Pain, neuropathy, sleep, anxiety, PTSD, the things that people aren't currently self-medicating for. Now, they could be self-medicating in the illicit market, they can be self-medicating in the legal market because

Aaron: They could be self-medicating with opioids, with alcohol

Mitch: Sure, but I'm not making a qualitative judgment. Just talking about the numbers of how many people are taking cannabis or CBD for sleep, how many people are taking cannabis or CBD for PTSD without really a doctor saying, "hey, try it". The doctor's giving them a recommendation, and then one of the failings right now of the market and why illegality matters

so much to the future of medical is because it stops research. And doctors typically don't want empirical or anecdotal research. They want hard science. So, you're finding that 70 to 80 percent of doctors are still just skeptical or if not skeptical, aren't going to put the weight of their reputation and credentials on the line to recommend something where they haven't seen the tangible results. And I know this from my early days in 2012, 2013, 2014, working with doctors, convincing them early on to recommend in Connecticut. Watching my partner to try to convince doctors to, you know, to get that treatment in Connecticut, in Minnesota, where these were really greenfield markets.

Aaron: Ya, what's the upside for a doctor? There's no upside, right?

Mitch: Right. It's no upside. And it's not like a pharmaceutical rep who comes in. I'm not going to say, you know, I don't want to bring too much shade at doctors because deserve nothing but credit for going through this immense amount of pressure. And they care about their patients. But the reality is, what is the upside when someone comes in with reflux? A doctor knows there are eight medicines that are largely effective for reflux. Right? Nexium, Prevacid. Zantac, whatever it might be. Right. And I've seen like lighter versions of those on the OTC market. Great I've always said, at least for the last four years, that cannabis is the ultimate OTC medicine eventually because you'll have like cannabinoid-based medicines that are just going to be, it may not be the active component of cannabis, which is why the CBD craze, it's not a craze. CBD is going to be in much of the OTC medicines that want that anti-inflammatory effect. Right. It might be ibuprofen and CBD. It might be aspirin and CBD. But consider it. That's why the DEAs meddling and not giving certainty has put such a crimp in CBD. But just assume in the next three to five years CBD will be found in many over-the-counter products. And you know, that's, that's up to. So just think of that vertical that no one's even factoring in. OK, so put that aside. But just from the cannabis perspective, we know very little about this threat. The endocannabinoid system wasn't really discovered or, you know, discovery isn't the right word because it's been there. It wasn't even really thought of as anything until the mid 90s when Raffaella Shulem in Hebrew University really noticed that when cannabis was consumed, interacted with a certain system, a certain receptor system in your body. Right. The CB1 receptors, the CB2 receptors. And now they've added a whole bunch of other receptors that weren't originally even recognized. So the reason, you know, sometimes people go, well, that's such a weird system, why is it named like cannabis? Well, because it reacts with cannabis. It reacts with THC.

Aaron: The endocannabinoid system, right?

Mitch: Right. So that you know, and that's why you see companies named Endoca or you know. Yeah, there's a very big twist. You know, I love the I mean, I'm named Merida because I didn't want to necessarily be put into the quote unquote cannabis ghetto right from day one.

Aaron: Yeah. Yeah.

Mitch: But let's just say the Green Leaf and a lot of other... There's a CB1 Capital run by my friend Todd Harrison. There's a CB2 Insights which became Skylight, which you know is my medical data play in the space.

Aaron: Yes.

Mitch: Look, I'm not going to say anything about the naming and the nomenclature hierarchy in cannabis, but let's say there's a lot of companies named Green Leaf and a lot of other funky names with a V.

Aaron: That are all based on this discovery and research.

Mitch: Yeah, sure. About the medical side. You know, the so I think that's interesting. But anyway, going back to the original question of the TAM, when you look at the medical side and how we know very little about the system, you know, 20 years, 30 years is virtually nothing for a system in our body of receptors and transient elements and how cannabis or THC or CBD really transfer around the body as they discover more, doctors will start to get much more interested. And then they're going to start to look for delivery form. So why are we investing in a medical dosing tool or a set of a patch delivery company? Because we believe there is a normalized medical industry coming in this space. And we believe deeply that when that comes, the whole TAM changes because now you're talking about the pharmaceuticalization and the medicalization and that TAM cannot be predicted rationally, just like consumption can't be predicted rationally, so whatever the estimates are, we think it will over exceed. Now, there'll be a point where the estimates start to grow. But we truly believe, and we predicted this in 2018, you know, which was almost three years ago at this point that it's very hard for any rational, sane and tethered analyst to over predict because they have to underpredict by the very nature of what they do.

Aaron: So that's really great. There's a lot to unpack there. The first thing that we're going just to, let's put the medical aside for a second, because that's super fascinating. You combine two of my favorite ideas that you have that you've advanced that I really haven't heard elsewhere. One is that you have the legal market kind of eating into the illegal market and your idea that it's going to accelerate and then you have the medical side as well. Let me just go into the legal eating the illegal side and ask you about the implications. What it brings out in me is that there's these multi-state operators or just single-state operators that grow, distribute and sell or some of them just sell, some distribute, etc., but that the legal market for cannabis and in the states where it's legal and where it's going to become legal. Just from your viewpoint of the legal market, eating the illegal, what your thesis tells me is that the runway for these companies is much greater than what people may currently be thinking. Just putting aside, the federal legalization and if eventually cannabis, let's not consider that for a second. But is that a correct way to kind of interpret what you're saying or what are your thoughts on what?

Mitch: Absolutely. Yeah, that is the underlying theme. Now, I'm not saying every company is going to succeed, and I'm not saying, you know, certainly the point about that companies may not be recession proof, but industries are. You know, there are countless numbers that might fail in the pandemic, but that ultimately the growth, the intrinsic growth is so huge that the industry itself is recession proof. That's absolutely true. I mean, yes you just summarized the thesis of it. Directionally this industry is on hyper-speed right now. That's one thing. I do want to make one point about the illicit market transition, which, yes, it is something that we do a lot of research on and we talk about publicly and I obviously talk about that publicly. I've written about it, you know, done a white paper or two or three at this point on the data underpinning it. But it's not like it was Merida's idea all along. I do want to give some credit, I did hear something which we used to think about this deeply because we watched, you know, if you're in California, you don't understand it quite as well, because it always felt, quote unquote, legal, you know? For many years, you know, most people growing up with it, it was kind of a legal cooperative system. So, it grew up

Aaron: Or you knew your friend who was growing it.

Mitch: Sure, and it was quasi legal. The Californians really grew up in a much more open lipped sort of liberal marketplace, where in New York you saw the distinct change when medical became legal. People that you weren't expecting were getting medical cards. You could see that transition really in just fine detail. Right. That distinction. Now, I don't think you see it as well in

the West Coast. And I used to make this point to my West Coast friends who I was learning a tremendous amount from. That is the East Coast markets where you will see this more distinction and why I do believe the MSOs who are more exposed to those limited license markets have much more upside than an MSO per say that that's in maybe like Denver

Aaron: Because it's a much heavier illegal. I see what you're saying. It's a much heavier illegal. And so, when that translates to legal...

Mitch: Yeah, yeah, yeah. It's driving Verano. It's driving Cresco. It's driving GTI. It's driving A Sudden Wellness, which is private. It's driving Pharma King. I mean, you look at companies who are on the flip the switch space, right? Now, MSOs early on in California, had a hard time because the rules were just so hard to get in place and then they kept changing. Whereas in Illinois, because it was so structured from the first, from the get-go, because it was a limited market, when they flip it, guys like Cresco, and GTI and Verano could really turn around and go into, you're basically just opening up a spigot. But I do want to finish my point about we're not the first person to bring up that point. So, I was thinking about this in 2016/2017 and I heard Adam Biermann actually of Medmen originally, who deserves a lot of credit. You know, he gets a lot of shade. I still think the guy was an amazing operator who really just got in over their heads, you know, too big, too big of an opportunity, too much capital, all those things, but he said once, I don't know if it was like in a small setting, I don't remember what it was. He said something like, it's an evolution, not a revolution. And we had already been noodling over this in a deep data way at Merida. And when I heard him say it, it was exactly what we were saying to people, you don't have to identify the market for cannabis consumption. So, it's not a revolution. It's not like what people use, the end of prohibition. The end of prohibition is not a good analogue at all because alcohol was largely legal in the rest of the world when the 21st amendment came. Right. I think it's the I hope it's the Twenty First Amendment, I really just stepped in it if it wasn't! I think it's the 18th that made it illegal and the 21st, which made it legal. When that amendment came, the end of Prohibition Amendment, if I'm wrong on the number, please fact check me, but again, America already had a very robust smuggling operation. Right. But think about the end of this federal legality hen it eventually comes. There are already growers. You know, the first legal distillery won't be found - it already exists. Verano, Cresco, Vireo. They all own these things. Right. All the MSOs already own these, so it's a much different industry. But, you know, people try to put things in pattern. And I also think it's important to recognize how much affect either federal or state-based legality or illegality affects consumption. It does. Right. Most people want to comport with the law. And so that's why we talk about the

early adopters. I mean, most legal cannabis consumption or formerly illegal were really the low hanging fruit of consumption because those people could only consume it in a flower form, which is smelly. You know, you can't hid that - if you're outside a party and everyone else is drinking wine, you're going to come in and everyone in the party is going to go, that guy just consumed. Now with edibles and other form factors, it definitely brings a bigger tent for people that may want to consume more discreetly or in micro dose forms, whatever it might be. But the point is that illegality in general does create a stigma which affects underlying sales. That's something it and we created like a four-step sort of analysis of that where, you know, cannabis will be the first substance or first really industry which will be normalized before it's legalized, which is just nuts. When you think of commerce, think of potato chips being illegal, but everyone's consuming it.

Aaron: No, that's really that's another one of your ideas that I really like is the normalization and what it means.

Mitch: Yes. Which means by the time legalization comes, then you really have to understand what the business models are or what are the parts of the space. There are going to be perfectly functioning parts of the cannabis space that are completely disrupted by legalization. None of them are going to be disrupted by normalization day one, but legalization itself is going to disrupt certain functioning elements of cannabis. And so, I quite understand those elements.

Aaron: Like what? What will be what will be disrupted? For example, not naming any companies, but if you had to guess.

Mitch: OK, so we're keeping an eye on what would be the way that interstate commerce could or could not take shape. Which states are large are likely to allow interstate commerce, which ones aren't? I think that's worth, knowing that is worth billions because which MSOs are going to stand up the test of time that a lot of which MSOs are going to understand state by state distribution. Right. One of the reasons when people used to ask me about Cresco and why we sold ValleyAg to Cresco in 2019 when we had a chance to sell to virtually any MSO that wasn't currently in New York, that was a New York private company. And, you know, and I'm in that position,

Aaron: Which I believe you're up some ridiculous amount on, right?

Mitch: Yeah. Yeah. The returns are quite well. I mean, I think we ended up and we probably made a 700 percent return or so. And if you look at the fact that we were also partnered with what eventually became Jushi on that. And you factor in what our investment in Jushi combined with that. Yeah, that's a double-digit bagger for that 2 ½ year period. But in terms of Fund One, I mean, Fund One's looking like it could almost have a double digit MOIC when all is said and done for a five-year period, which for a fund feels to me like a pretty strong return.

Aaron: That's all! That's the only return you have!

Mitch: Yeah. I mean, you know, I have two other funds that are doing quite well too. But I think compliance will clip this if I say anything else about the open funds!

Aaron: It's all good, but specifically, so help me think about

Mitch: So, Cresco. So, what someone was asking, like, why do you really like Cresco? And, you know, obviously I love the management of it and there's a lot of MSOs I love. But in particular, I said, well, you know, I like their investment in Canna Royalty, which became Origin House, which became basically Cresco's West Coast distribution, because I said down the road, when the federal government starts to liberalize their rules, distribution and understand sort of gross brand distribution at a high level, it could be a very valuable expertise to understand because you could see interstate commerce. Now, I've been on Twitter and I know I've said a lot about interstate commerce and how I'm hesitant to say it's going to happen quickly. I actually think it's going to take longer, but it's going to happen in pockets just the way that everything else has happened in pockets. So, if you're an MSO, when you're in a state or two states, let's say you have a 6 state footprint and two of those states are likely to allow a lot of interstate commerce, you're probably looking at a net importation, which could diminish, now, you could control that distribution, I don't know how that's going to unfold, but let's just say that that could easily hurt your hypergrowth. And so, understanding each state by state is something I think Merida has done a really good job of because of our origins in the space, you know, starting in Connecticut, Minnesota, Nevada and now with one with Merida with our third fund has one licenses in West Virginia and Missouri. We have a license pending in Georgia. We bought one of the Virginias, which obviously every person now that rec has passed in Virginia wants, I would say that we're having a lot of robust conversations with MSOs similar to our ValleyAg discussion. And so, when you look at those things, understanding the state-by-state model, having those thousands of discussions with regulators, you know, having one of our former advisors was Bill Rubenstein,

who ran the Connecticut program, having the former CEO of Leafline Labs Manny Munson-Regala, who ran the Minnesota program, being able to pick their brains on a weekly, monthly basis for years.

Aaron: It's an incredible, incredible competitive advantage, because based on what I could tell what either the Biden administration or what the current what I feel is they're going to push it all down to the states and then and it's going to really matter what the states do. It's been fascinating.

Mitch: I think so. I could be biased, but I think that is one. If people often in quiet moments, I'll have a discussion with people that says what is really Merida's is sort of differentiation. You know, what does it do that other people aren't doing? And I think I think there's so many amazing investors in cannabis, pioneering investors. There are other funds that have done a great job. And I think one of the things we bring to the party as just a steward of the industry is because we were more operationally focused originally Merida it even existed. I think that gives us a perspective on that state by state, to a granularity that you're not going to find because of how fast things move now, you can only focus on so much information. And that's having a large team. I have an 18-person investment team who are we're all just voracious consumers of information. And I think cannabis, a lot of investments going to perform very well. But how do you outperform? And I think understanding that state by state dynamic, understanding the friction points, what might happen and understanding normalization and having done a lot of work on the data on consumers and understanding a thesis, I mean, our next white paper to come out is going to be something around, it's basically going to be some predictive analytics we've seen that show that the heavy consumer who largely stayed in the illicit market as late as they could, you know, the "over my dead body" consumer, right? The person who's like I am not going to consume in the legal market no matter what happens, that consumer is absolutely starting to nibble, if not a lot more than nibble, you know, into the legal market. And that is going to drive the basket size. That is going to drive the form factors. That is going to make a big, big change. And we think the other thing that people are really missing in some of the story around cannabis is if you look at the cross tabs on a lot of the data around alcohol consumption over the last year, we think that there's been a lot of smoothing and adjusting that people are doing to show that alcohol consumption is staying level. And we think next year is the year or 2021 being next year, although we're already March, which is kind of scary, we think you're going to start to see the degradation of alcohol usage and that you're just not seeing it because of the pandemic and because of seasonal and other smoothing that the crosstab show. But we know from a New Frontier study a while back, that they interviewed 500 people who are not current

consumers and they really went through what these people do, how much they drank, et cetera, et cetera. And of the 500, more than 50 said, more than 50 percent said that they would consume if it was state legal or legal federally. And that of that consumption, that would probably reduce their alcohol consumption by 25 percent or more. And so, if you think of the forty-five million people that we kind of know are consuming in a casual way, at least monthly, if not more, right. In the US alone, that's forty-five million people whose alcohol consumption is really dropping off a cliff. I mean, you look at I think I saw something; I don't know who put it out. It could have been actually been New Frontier, I don't want to not give them credit because they're a portfolio company. But someone put out that the average cannabis consumer has reduced their alcohol consumption by more than 35% during the pandemic.

Aaron: So, this ties into your normalization thesis. That as this gets normalized, the stigma goes away and this becomes legal, and more people start consuming. You could see alcohol really take a hit because a lot of these are fixed business, you know, you have a fixed cost business, the sales dropped three or five percent, makes an outsized impact on your bottom line.

Mitch: Absolutely and that's why you see tobacco as well. I don't know if tobacco ties to me. I feel like anyone who is already addicted to nicotine, kind of tough. It's not necessarily the same thing because it's not like, you don't think nicotine can be mind-altering in some ways. And I know there's been studies and I don't really want to it's not worth kind of talking. That's less exciting than what we're talking about here. But we've done work on nic-oids and other stuff around nicotine just to understand what are other industries that might touch cannabis. But I will say it's not shocking to see Altria or Constellation or other beverage companies lobbying now and trying to get into the conversation. Maybe they want distribution. Maybe they want, you know, to be further involved. We know that Constellation has done always done a remarkably good job with government, their whole purchase of Crown Holdings, which gave them the Modelo empire, you know, and the distribution of Corona and stuff was just an absolute coup. And I wrote about that for New Cannabis Ventures years ago. And that's, we know a lot about their strategy. We think Constellation's a great company, but they're absolutely doing it. It is not just that they love cannabis. It's a hedge on their core business because we do think 2021 is absolutely the year where you see the true degradation of alcohol vis a vis cannabis usage.

Aaron: And they can't be blind to this. They have to have access to this data. They have to know what's coming so you'll probably heat up like M&A or investments or things like that. That's really interesting. I wanted to shift for a second back to the medical side and think about like one

of the things that when we were talking privately, you were talking about how I believe it was form factors and precision was going to be very important with medical side. And if you think about down the road as this is normalized, as it is legalized, and doctors start prescribing it and insurers start thinking about reimbursing it.

Mitch: Right.

Aaron: How do you think about whether the insurers will reimburse me, just going to the dispensary, buying a joint, or will they want to know exactly what I'm getting? Is it going to be in a pill form? Like have you had any conversations with insurers or in terms of the insurance markets, when I think medical, I think insurance and I think talking about the size of the market if insurance starts reimbursing this as a treatment as opposed to opioids and other pharmaceuticals, it has dramatic implications. And I'm just curious of how you see that playing out and what the implications are.

Mitch: Yeah, well, one good thing is it's something we thought about a lot. So, this question doesn't just come out of left field to us. And it's also an area where there are some good analogs around how this could unfold. And I'm not saying it will unfold exactly like this, but there are some good analogs and there's also some great information, you know, on Twitter, I've definitely put out a few nuggets on directionally. Obviously, we make investments in private, but we don't mind sharing information that we can create directional knowledge. And so, let's start with the analog. I think chiropractic care would be a pretty good analog, like a modern day. Which is very early in the 80s, chiropractic wasn't largely reimbursed by any insurance company. You know, it was seen as sort of like an alternative homeopathic remedy for quote unquote, pain. It's, you know, which is interesting because that same thing as cannabis, is what is pain and how does it get affected by this treatment. So, when you look at chiropractic care, when it started to get reimbursed in a large way in the mid 80s, you had a lot of effect on society. Number one, you had a lot more entrants to chiropractic care schools. You had osteopathy schools. Right. So now you can get a doctor in osteopathy or osteopath. Right. That you didn't really have in wide form, you know, to be a doctor in pain management, you have a lot of different sort of medical professions came out of that, which meant a better robust treatment modality, so instead of just chiropractic care it became whole body care. It became preventative care. And guess what? People are using it. When you go to a physical therapy nowadays, a lot of that comes they owe that ease of getting physical therapy for ailments to the early chiropractic reimbursements of the 80s and 90s. And so, you know, it's 20 years later. But, you know, people go to physical therapy

now when they hurt their wrist or insurance companies had to create a whole infrastructure around evaluating those claims. That's why when you go and let's say you fall down and sprained your wrist and you want to go get therapy, you know, instead of taking the opioids, your insurance company clearly going to you know, they're going to reimburse you for that therapy. But you're also going to get a letter that says, Aaron, were you injured in a car accident? Could there be, I mean, I don't know if you've ever used physical therapy, but you first of all, you get a letter that most insurance companies now have an outside company to evaluate your claim because it's specific and whether you're getting enough physical therapy and whether you should take other medicines. And also, when your hurt in a car accident, could there be another payer for your medical care? And so that infrastructure is something I mean, it's wonky and quirky, but it's something we believe that is kind of coming to cannabis. And so, we think that the form factors when you look at, let me just lay out three specific things that tell you it's coming and it's coming faster than anyone predicts. Number one, New Jersey, a case that's sitting before the Supreme Court in Jersey has already been to the Court of appeals. It's Hager versus I'm sorry, I can't remember the defendant, but it's someone who was hurt years ago in a worker's comp claim. He started using his own cannabis and actually sued for reimbursement, saying that he was using it responsibly and under the care of a doctor and that this was helping him, and he didn't have to use opioids which had damaged him. He had used opioids for a matter of years, and it didn't really offer the relief. And he had to take other medicines and it hurt his ability to think in all these other things. And so, you know, the judge in the court of appeals went deep or the court did went deep, deep into whether it's an effective treatment, you know, the efficacy of medical cannabis. And what would be the options for someone in this man's position who had like a pile of bricks fall on his back and literally could not work, you know? And so, the quality-of-life aspects from using cannabis versus opioids, those, etc. So, New Jersey now has a bill, it's the first time it's made out of committee that actually would force workers comp insurers in Jersey to reimburse for medical cannabis. That's one big thing.

New Mexico also had an administrative court decision on reimbursement of cannabis and actually both New Mexico and Jersey were the first courts that ruled that the reimbursement, even if these are insurance companies, even if it's a town like Egg Harbor Township in New Jersey, that you don't violate the Controlled Substance Act by reimbursing for medical cannabis because you're not aiding and abetting in illegal activity. That's number one or two.

Then the third, there's been a Massachusetts setback where that court, a court in Massachusetts, ruled that insurers do not have to reimburse. So, when you look at the jersey out of committee,

the fact that New York now reimburses for your initial meeting, and that's, this has been years. New York, if you go to a doctor and he gives you a medical card recommendation, you can get full reimbursement for that doctor's visit. Most other states you can't. And so, when you look at these little radio signals from space of whether there's intelligent life out there, you start to see there's a lot of signals, not just noise. And so, there's another state that now has a bill for reimbursement for forcing workers comp insurance. Now, if I was a worker's comp insurer, I would probably want to be involved in that legislative process and make sure that the form factors I reimburse for are more medically focused. So, I don't know if it's going to be joints. It could be. It could be, but it's more likely to be more precise forms of dosages. It could be oil, pills, transdermal, sublingual. It could be anything. But I would see that over time, I would guess that you can start with a more constrained reimbursement regime. And obviously our investment in Skylight SHGFF. Right. The public company that owns something called Cannacare, which issues, it also does telemed, which is a separate line of business. And medical clinics at this point, but their knowledge of the cannabis prescriber's world is vast. And one of our investment theses of investing them was to get access to this database of this HIPPA complaint anonymized information on who is getting medical cards and why and what is kind of the way that they're accessing this, quote unquote, alternative non-reimbursed treatment, because insurers are going to want to know these things. And so, I do think it's coming in a big way. And I do think it's going to drive specific medical forms, cannabinoid research, et cetera. And I do think as pharmaceutical companies like Pfizer or whoever gets involved, they're going to start doing medical research and you're going to start to see a much more virtuous flywheel of medical adoption. And, you know, that's why we're invested in a company called Mode that does a precision dosing tool where you can use anyone's products and it can read the vapor and tell you the cannabinoid profile of that vapor. And we like those sorts of let's call them platform based, information based, medically focused opportunities. And it's something that we're investing now. We could be on the leading edge. We could be on the cutting edge. But we've done these investments before and we've, you know, we've been remarkably good at and maybe lucky at picking sort of the spots where normalization has landed.

Aaron: No, that's really great, and I have to also tip my hat to you, because I believe you're up like something like 10 times on Skylight Health as well.

Mitch: We think it could go up further. But, you know, we've had a company in the telemed, that's timing sometimes in the market where, you know, they happen to be a telemed company who can buy medical clinics at really great EBITDA multiples because we all know that, you

know, the mom-and-pop doctor isn't really scale. And that's why a lot of clinic groups are growing up in these sorts of conglomerations of or conglomerates of patient focused care. Yeah, we think that that company is a phenomenal company. We think it's going much higher. But, you know, it's moved very far from our investment. And that was a Fund 2 portfolio company as well. So, we had to show some patience there. And, you know, as a funny aside, they were very close to selling at about 20 cents a share or less to a very cannabis focused company that itself is doing quite well. But we sort of stepped in and blocked that and said whatever resources you need that you think you were going to accomplish in this sale, please just tell us what that list is. We will give you the money. And that was the offering we did; at I think something like 12 or 13 cents.

Aaron: And what does it trade at now?

Mitch: I think it's a dollar twenty. They're worth like five X what the acquirer would have been. So, thank God. I mean, we just felt like this medical thesis, we didn't want to give up on it and have them give up on it. And the truth was, though, it was a time in early 2020, when there were almost no resources in the space, you know money had dried up for a lot of people.

Aaron: I remember it well. I think that's important. And this is why I thank you and I value this interview so much, because I think it's not enough to say, oh, well, cannabis is becoming legalized. I think it's really important to understand what the driver in this big thing that's is happening. What do you really believe in that's going to happen? That's going to give you an edge or give you conviction so that if you have setbacks or the stocks fall a lot, that you understand what you own. And that's why I love the idea of, you know, the legal eating the illegal, the medicalization kind of insurance reimbursement, the idea of normalization. I would have to think that normalization, if I was an investor in any alcohol company, I would be really worried by that trend. But that's why thank you for kind of sharing this stuff with us, because that allows the investor, public or private, to say, no, don't do this, even though it was probably a good decent win, what we see is much more valuable than what the market's sees. So, thank you for that. I wanted to dive into what your best guess is for kind of the pathway to legalization. I know, I've got to put you on the spot, I know what you're seeing, my thesis, my own thesis is that they're probably going to there's going to be some kind of Federal law, that'll say whatever the states say they can do it, you won't get in trouble or some version of that. They'll declassify, they'll still make it strict and have rights, but they're just going to say we don't really want to deal with it at a federal level. And they'll allow some of these companies to allow basic legalization

that is a little more legal than what we currently have. That's my operating thesis. I would love to hear yours.

Mitch: Yeah, no. So, I'm going to answer that question. But I will say that I think what most people maybe get a little bit too far out in front of, especially in like if you're you know, if you're in cannatwit on Twitter is the timing of these things. And I think having been involved in a lot of the state-based processes, you really see how much friction there is to changing this time.

Aaron: Massachusetts has been amazing to watch.

Mitch: Yeah, but I mean, at the federal level, you know, you had the Cole memo incident eight years ago, now right? Before the Cole memo, you know, there was the Ogden Memo which essentially said the federal government is not going to jail medical patients which helped drive medical adoption in Colorado. I mean, you would not have Colorado adult use without the Ogden Memo. Right. And that's kind of like if you look back to years before the Cole memo, the argument really helped in a great way. And so, because that that drove sort of legal adoption in the early days. And so, you know, I do think, so let's just talk about the timing for a second. I think it is much more difficult, there are a lot of people who have done incredible jobs and advocacy for cannabis and there's a lot of money now going into this, and I think there's a lot of smart, sane voices that are trying to push this. Now, the problem is, though, is that you have a lot of tension from a perfect bill or a good bill. So, I think most people in my position or in the industry in general would be somewhat OK with a bill that just says sort of like how alcohol is treated. Alcohol does not have a lot of federal rulemaking. You know, even though there is an Alcohol, Tobacco and Firearms Commission, they don't do a lot of alcohol at the quote unquote, federal commerce level. You know, clearly, if you don't have a 21-year-old drinking age, you don't get federal highway matching funds. Right. That's really one of the main federal sort of levers to making sure everyone has a twenty one year drinking age, right, because at one point, New Orleans or Louisiana had an 18 and they wanted to get their hands on that money. So, they went with the flow. So, I do think you could easily find a somewhat, you know, 50 page bill that says we hereby de-schedule cannabis off schedule one. And therefore, this now opens the door because that takes it off the Controlled Substance Act list of proscribed substances. Now, that would be a way of, kind of is what happened with CBD essentially. Now, I think that alone isn't going to be enough for the institutional participation. So, you are likely to see a safe banking at a more distinct act that does something. So, let's call this a more agency based operational act that allows for loan making and listing on the larger markets. It takes a US based operator and puts

them in complete legality. So, I think that's the most likely path. You know, there's a combination of one of two things. I don't think there's a silver bullet. I don't think a silver bullet will happen simply because to get to a silver bullet omnibus, let's fix it all in one shot, I think then you run into social equity related issues because then you have to really incorporate things that probably are better dealt with on a local basis. So, I think you're likely to see more of this. We here by take off the schedule and that means that it's legal, right? Or it's no longer illegal. And we also declare that now that cannabis is no longer on schedule, it is hereby legal and that states may make any rules here by as long as there isn't you know underage issues. You know, but those are local issues. And I think, you know, what I've seen recently, and I pushed back a little bit because I think it's a debate worth having. And I don't think it's easy to predict is will there be the just like day one interstate commerce? Will someone be shipping cannabis from California to Texas? And I just don't see that happening in any way, shape or form. I also don't think a state that has worked its butt off to build an infrastructure, likes the tax revenue, is just going to allow their local industry to become a wholesale distributor of California based cannabis. I'm not saying it can't happen. But you're definitely like wine, wine. You could not ship wine from a local wine store to another state.

Aaron: I completely agree. I think the best example that I use is if you want to buy liquor in the state of New Hampshire, you can only buy it from a state liquor store.

And it's like, you know, people forget. It was like I don't even 15, 20 years ago, alcohol couldn't cross state lines.

Mitch: Well, there was no state lines unless it was sent to an approved.

Aaron: That's right. Right. That's right. And that goes to your point of the importance of the distributorship and everything.

Mitch: Right. That's why I was talking about distribution before and understanding that it's not, look, I'm not saying that someone if they understand distribution, they're definitely going to make a trillion dollars. But I would think that a company that understands wholesale distribution, brand distribution, how to navigate the friction of those elements is going to do better or be more positioned to see the potential headwinds and friction than someone who's just a great on the ground operator and any one individual state.

Aaron: Yeah, no, no, that's great. I really appreciate it. The other thing that's really struck me and it's really held me back from investing more in the industry is it's been shocking to me as an investor now for twenty-five years in the public markets of just how much the publicly traded industry is like the Wild West. You have, you know, some good operators, you have some people that are just way in over their heads. You have some unethical people. You have like a wide gamut that you really don't necessarily see in the broader market. And it is just like a wide delta between what you get, and I guess it's held me back. And I would be curious what you would say to investors who are interested in the industry, who didn't have access to the private market like you did, or the know-how. What are some things generally that you would recommend that they avoid or be careful of when they see and not to mention any specific companies? But just I'd be curious of how you would caution people or just be "Hey, you can be excited, but just be careful of this. What would you say to that?"

Mitch: Well, I think I would start with a really macro thought, which is what are you betting on if you're investing in a company in this space? So, you know, we often do this at Merida when it's a private company. So, what is let's say this we often pick areas to invest in, not necessarily the company, until we find the company that fits everything we want to do. Like we were looking for someone who was doing medical prescribing and had a data capture background. We didn't know Skylight originally. We thought, you know, we found someone that did what we thought was a good thing to do. So if you're going to invest in a company, whatever the company is a public company, understand what the bet you're making is. So if it's a company and you know, it's kind of the stock looks pretty high and they're trading at higher EBITDA margins or EBITDA multiples than someone else, if your bet is that the market's that this company is in, are going to flip the switch and go rec and that their position to take advantage of it, then I don't know if it matters if you get in today or yesterday, you know, like obviously these are really volatile companies, but then the entry point, maybe not as important. Or are you making a bet that this company has a specific technology or like a GrowGen, which is ancillary? You know, you're making a bet that more consumption means more AG, which means more equipment being bought. And so, we often just look at each other in the eyes before we do the deeper analytics. And we run something through what we call the adoption score. We call it the add score now because adoption is the wrong word, but we have one hundred thirty-five-point filtering mechanism that we use on companies to sort of make sure we're doing all the work and all the analysis that we often think is important. So, it could be you know, we have a lot of really idiosyncratic points that we've just learned over the time in cannabis. And then there's some basic things like do they have the right EBITDA margins? Are they executing on the ground the

right way? So, we will look at each other and say, so what is the bet we're making? You know, like if you're investing in Vireo, let's just use an example, because I think that's an easy one that Merida Fund 2 is invested in. When you're investing in Vireo, are you making a bet on the patents that they filed? Are you making a bet on the markets they're in, whether it's Arizona, Minnesota, New York, you know, what are you betting on? And then you have to look at is there an inevitability to that bet or is that bet really rely on five or six other things happening? So, like a Cresco, their markets, you know, Vireo, we think is a little bit more of a medically focused one. So that's why I kind of brought them to the fore. We think they're more medically focused as an MSO than a lot of the other operators, not that they're better or worse, we're not making the qualitative judgment, it's more of we just feel based on how much they've done from a patent and IP perspective, that they're deeply interested in really focusing on medical or, you know, or at least having that in their quiver to shoot. So, you know, whether it's a Cresco or Vernao or GTI or Harvest or Trulieve. Like Trulieve you're making a bet on the continued growth of Florida and the new markets that Trulieve was acquired into

Aaron: It could be AYR Wellness, which I own!

Mitch: Right. AYR Wellness. Who we love, Jamie and Michael, they're great people. You know, we obviously get along with, you know, all the MSOs. They're buying a lot of the ancillary products and we've sold companies to them and we deal with them. And you know, it's, it's so I'm just want to be clear, I'm not making saying, look, buy Vireo. What I'm saying is if a company like Vireo, if you're like, I like where their stock is trading, you are making a bet in Vireo on medical and the expansion of the current states they're in. Those are the two things. If you're making a bet on Cresco, you're making a bet on a large California presence at this point and a growth of the limited license markets they're in. Of which they're in great ones. GTI, Same thing. Right. So. If you're making a bet on like a Slang Wellness, which is not really MSO, which Merida just recently made a big investment, you're making a bet on brands penetrating markets. Now, obviously, our goal there is to get them on the shelves that we own operators, and that's easy. But you just, know what the bet you're making because the bet you're making is what your downside and your risk mitigation is, because ultimately, if the bet you're making is right, the company may go through some volatility anyway. Obviously, there's always going be hiccups, but if the bet you're making right, then you'll be fine over time. You know, and I think that sometimes people get really wrapped up in, like, the price today. Yeah, a lot of these companies have seen huge growth in their equity pricing, but some of them are really cheap still on a relative basis, if you compare them to like specialty retail or other thematically specific

companies in the broader ecosystem. You know, it's hard to say that Trulieve is like crazy expensive when you look at what other things trade at in other industries or consumer goods or like a GTI, it's hard to say they're like crazy expensive. So, I think, you know, same thing with Cresco and a lot of companies, I mean, there's a lot of companies that are not expensive if you look at the broader adoption of cannabis. So, if you look at the growth rate of CAGR (Compound Annual Growth Rate) of 30, 40 percent and in some of the limited licensed medical markets, you're talking about CAGRs of 80, 90 for the next three or four years. So how is something expensive?

Aaron: No, no, no, I absolutely

Mitch: I'm not saying I'm not saying go and buy stocks. I think entry points matter. And obviously Merida is a very discerning investor. But, you know, there's so many companies doing a great job. And if you believe the growth in Illinois and if you believe New York, New Jersey, like, you know, GTI as a New Jersey license, Verano has one. So those are going rec. Just like Illinois, there's going to be a lot of opportunity there, so you look at the companies out of Jersey. Look at states that are turning rec, Arizona, who's operating there? What is their footprint? You know, people do this all the time. Virginia just passed an adult use. Canaccord puts out a note, it's three public companies or two, Columbia Care bought gLeaf, Jushi and Merida's own It's Private Darma. So, when you look at those companies, I mean that's a way to really kind of get any information just focus on the markets and what those potential markets are when adult use flips and which markets are not going to flip very quickly to adult use.

Aaron: Yeah, no, that's great. Can you tell me about your SPAC and how you're thinking about that? And what I'd be curious about is, you know, you're an investor in private companies, you're an investor in public companies. And I believe you launched the SPAC last year before the stock craze and things went nuts

Mitch: Yeah, yeah, we did beat the rush by a little bit.

Aaron: But I'm curious, there aren't that many cannabis focused SPACs. Right. And I'm sure you're working on it. And, you know, obviously you can't share specifics, but I'm curious of how does that fit in your portfolio or how you think about investing money and what's the overall strategy there?

Mitch: Right. Well, one thing is I have to give a lot of credit to the guys on my team, guys and gals, who really saw a way to create an efficient capital because we launched it in early, late nineteen when we saw, so we I guess we got lucky again. I don't know if it's expertise or what, but we kind of predicted that late 2019, early 2020 was going to be a capital desert and we wanted to have an efficient sort of capital for bigger deals. You know, everyone in cannabis, I think for a long time was capital constrained. And so, we wanted an alternative method for people to invest sort of in Merida's strategy, but in a public way, knowing that we were not going to buy a quote unquote, Merida asset in the SPAC. Right. We are the sponsor of a SPAC. So, Merida is the largest investor on the promote side, on the sponsor side. And then we look at it as just a way to acquire a large stake in another company that we love. It's not going to be a Merida, it's unlikely to be a Merida portfolio company. I mean, we've looked at hundreds and hundreds of deals. You know, the one challenge has been that non-cannabis SPACs, desperate to, running out of time, have stepped in and really mucked things up a little bit by either these are people that have no idea about price discovery and, you know, just opportunism. So that has been a challenge. But what I would say is we've done the work and Kiplinger's late last year, named us one of the 10 stocks to watch because they felt like if any company could find a great deal, it would be Merida. And I thank them for that. And I agree with them. I think there's a lot of other people that would do a great job as well. And we know that there's been some SPACs recently that de-SPAC'd and we did do something a little different. We both listed on the NEO and on the Nasdaq. So that allowed us to either plant touch or not plant touch and stay listed without a de-listing moment. So, I think that's a big advantage to getting a deal done because you can then touch an American focused operator. That's one thing. And I think the other thing is there are price discovery matters on a SPAC if you're Merida, that's one thing that people should take note of is rather than just do any deal, one thing that's important to us is our reputations as savvy deal makers. And so, we've been extremely careful of what we've looked at and what we get serious about in the SPAC. And I think that sometimes by restricting yourself, it might take you a little longer to find the right deal. But I think when we find a deal and it gets announced and, you know, I have to be a little coy because obviously we're in a million discussions at any one point. But I think when something gets announced, I think the market will find it to be a Merida type of deal. You know, a subtle yet good

Aaron: Well, thought out something that plays into your broad thesis.

Mitch: I'd like to think we're a thoughtful investor. You know, I'd like to think that. And I think that whatever we do is going to be consistent with what we've done from the first day we launched Merida.

Aaron: No, that's really great and we've mentioned some of you, you know, Grow Generation, the first outside investor, you know, the stock's up 10 times in a year. Skylight we mentioned. Oh, yeah, you're up a lot. So, your track record is just fantastic and really appreciated. Thank you so much for your time from learning from you. This has been awesome. Big one request is that we can do this again later this year, because I'm sure there's going to be a lot to change and there'll be a lot to announce, especially maybe with your SPAC or other things that we'll have a lot more to unpack and discuss.

Mitch: Yeah and thank you. I mean, I think it's amazing for like sort of people to really grab onto the cannabis opportunity and dig in. It's not an easy space to educate yourself. There's a lot of false flag information. There's a lot of hype. But when you fundamentally look at it, the reason we love talking about it so much and why I'm I guess I say, you know, love what you do and never work a day in your life. It's kind of like a it's been great coming from the corporate world where, you know, I was in the corporate war for a long time and this has been such an amazing run, watching just these incredible operators come to the space and build things. These, you know, a lot of these MSOs, those other funds, you know, they deserve so much credit. So many of our peers have made it easy or easier to be the kind of investor we want to be. And I'm so proud of what other people have done. What I would say is it's like you deserve a lot of credit. People who are intellectually curious and want to really dig in. They can read our commentary, visit us on Twitter @meridacap, you know, sign up for the newsletter at info@MeridaCap. It's you know, we try to have an ongoing dialogue with the industry and with investors. We always want to hear we think we can always get better and smarter and to understand where this is going. One thing I will say, though, the inevitable it is very much the matrix moment when, you know, when the agents hold Neo down and say, you know, you hear that? That's the sound of inevitability. Yeah. That cash register ringing in cannabis is the inevitability of its growth. It's normalization. And the fact is the disruption that's going to come along many verticals, and I think people should definitely look at it as a non-correlated investment or even a correlated investment at this point, but it offers some of the best growth will ever see in our lifetimes. And it doesn't mean every company is going to win. But if you to do the work, there's a great chance for even retail investors to make some incredible returns.

Aaron: Well, thank you so much for this, this has been fantastic.

Mitch: Well, thanks for having me on. My pleasure.