

CANNABIS INTELLIGENCE BRIEFING

Retail: The \$23 Billion Opportunity



Executive Summary



Cannabis Intelligence Briefing

CANNABIS RETAIL: THE \$23 BILLION OPPORTUNITY

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**Every single licensed cannabis
retail location could be the nucleus
of a specialty store chain that could
dominate its local market, its state,
or potentially a sizable chunk
of the overall North American,
or even worldwide, market.**

Letter From the Editor

Welcome to the first Cannabis Intelligence Briefing: “Cannabis Retail: the \$23-Billion Opportunity”. And welcome as well to a whole new data-driven era in cannabis industry research and analysis.

Arcview Market Research, the leader in market projections and industry analysis since 2011 and BDS Analytics which has the most robust and precise dataset in the sector have teamed up for your benefit.

That pays off in this report with a deep-dive into everything from top-line revenue comparisons between adult-use and medical dispensaries, to detailed and accurate product-mix trend analysis, to a pro-forma analysis of the typical retail P&L, with and without the impact of IRS rule 280e.

This report also includes some of the highlights from BDS’s first-of-their-kind consumer surveys. Read on to find out not only who cannabis consumers are, but how and why they consume cannabis.

This is just the first of eight Cannabis Intelligence Briefings we will release over the coming year. That’s in addition to our flagship annual State of Legal Marijuana Markets and the Mid-Year Update.

I hope you’ll subscribe to Cannabis Intelligence Briefings, and that you enjoy learning along with me and the Arcview and BDS teams.

And we hope you’ll take the initiative to be in touch with your ideas and questions as we all enjoy working together to build what Arcview CEO Troy Dayton has suggested can be “not just a new industry, but a new kind of industry.”

It’s an honor to serve you.



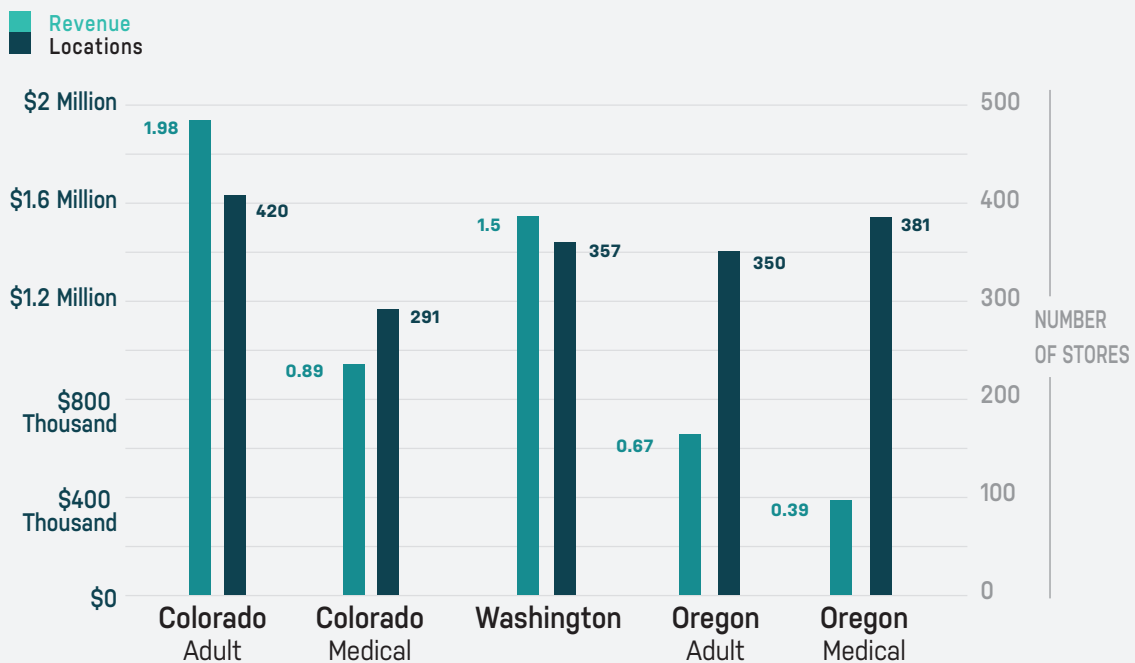
Tom Adams
Editor in Chief
Arcview Market Research
Managing Director
BDS Analytics

The Front Line of the Cannabis Revolution

The cannabis retail business is rapidly transitioning from its single-store roots into a classic specialty chain opportunity. Because of federal prohibition, however, these specialty chains, unlike specialists in earlier new product categories, will have several years to expand their footprints and establish their brands before major retailers come charging into the business, probably with the end of federal prohibition.

That window is now expected to extend at least to 2021, barring veto-proof Congressional action. Retailers will be in pursuit of market share in an overall North American legal cannabis market that Arcview Market Research forecasts will grow at a 27% compound annual growth rate from \$6.7 billion to \$22.6 billion.

2016 Average Revenue Per Store (in Millions)



Source: GreenEdge by BDS Analytics.

THIS IS ONLY THE EXECUTIVE SUMMARY

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The roots of cannabis retail are in the medical dispensaries that cropped up after California voters passed the Compassionate Care Act in 1996. Inevitably, however, adult-use retail stores will capture most of the growth going forward. Adult-use revenue is expected to surpass medical revenue in 2019 and reach almost twice its size in 2021 (\$14.9 billion vs. \$7.7 billion).

The lion's share of that adult-use growth will come in two new markets—California and Canada. There were only three functioning adult-use markets and 24 medical markets in 2016, including Canada and Washington, DC. Cannabis retail will likely remain a medical-only opportunity in 17 of the 34 markets forecast to have a legal cannabis program in 2021.

There is one benefit for investors going after licenses in the lower-growth medical markets—government-enforced limits on competition in tightly licensed states. Retail is typically one of the most competitive economic sectors, with minimal barriers to entry and, thus, razor-thin margins. Not so in, for example, Florida's or New York's tightly controlled medical programs.

Liberally licensed states, most of which are moving now to allow all adults to purchase cannabis openly, probably

offer the larger long-term opportunity to aggressively build out a chain's footprint and brand. That is a process already well underway in the first adult-legal states—Colorado, Washington, and Oregon—and it is dramatically changing the economics of cannabis retail (see graphic, pg 4).

Pioneering medical dispensaries from Harborside in California to Wellness Connection in Maine have been able to drive mid-seven-figure to eight-figure revenue annually. Per-store revenue in liberally licensed adult-use states is, in contrast, averaging less than \$2 million annually. Medical dispensaries with their much smaller customer bases are averaging under \$1 million in revenue, and in Oregon under \$400,000.

Adult-use revenue is expected to surpass medical revenue in 2019 and reach almost twice its size in 2021 (\$14.9 billion vs. \$7.7 billion)

Recent research by BDS Analytics Consumer Insights in California and Colorado found that even adult-use retail Consumers in Colorado cite a wide variety of health-related reasons as part of their motivation for cannabis consumption. The health motivations explain why Consumers are looking for an information-rich retail experience with budtenders who can recommend products that fit their particular needs.

Although the retail opportunity varies dramatically by market in the United States, Canada's situation is truly unique: because of federal-level medical legalization, a well-established mail order market is already in place. Now the country is looking ahead to a major shift to include brick-and-mortar retail stores in at least some provinces as adult-use legalization arrives as early as July 2018.

History is replete with examples of major wealth creation through the building of specialty retail chains ranging from McDonald's to Blockbuster to Starbucks and many more. But most of those happened with public equity investors backing the store-building drive through the major stock exchanges.

For cannabis retailers, federal prohibition closes the public equity window, so they will have to build their chains through innovative financing approaches. The upside of federal

prohibition is that it also protects them from pre-emption of the cannabis opportunity by mass merchant, drug and grocery giants, or e-commerce services with immediate national reach.

Arcview's forecast model suggests that there are super-charged revenue growth rates lying ahead for cannabis retailing pioneers. BDS Analytics' Consumer reports show the demographic breadth of the dispensary-shopping Consumer of today, and the open-mindedness of even many non-current customers to the possibility of consuming cannabis, at least under some circumstances. The BDS GreenEdge point-of-sale tracking data shows the expansive range of products being consumed already in these very early days.

Taken together, the research points to a bright future for cannabis retailers as the public-facing front line of the effort to bring cannabis out of the shadow economy.

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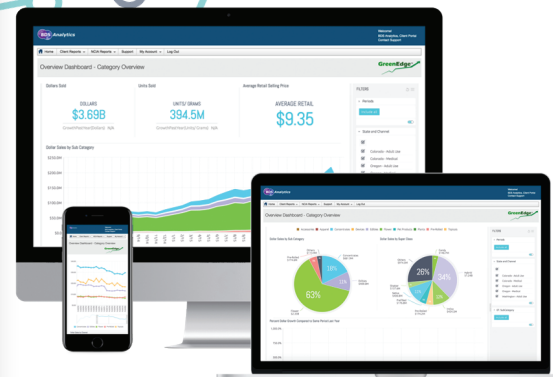
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"BDS Analytics has been a great partner from Day 1. The retail data they provide our business helps us in so many ways. We're able to track trends, more smartly merchandise our dispensary, and just make better business decisions all-around."

Debby Goldsberry, Executive Director, Magnolia Wellness



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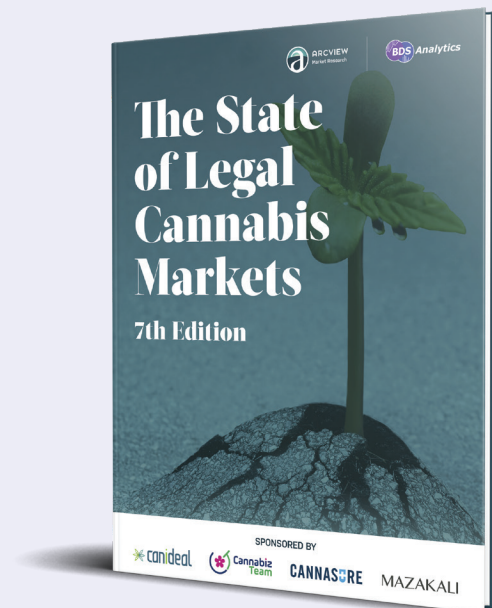
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Just Released



The State of Legal Cannabis Markets, 7th Edition

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