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YCBD.A - Q4 2020 cbdMD Inc Earnings Call

EVENT DATE/TIME: DECEMBER 22, 2020 / 9:15PM GMT

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PRESENTATION

Operator

Good afternoon. Welcome to the cbdMD, Inc. Fourth Quarter and Fiscal Year Ended September 30, 2020, Earnings Call and Update. This afternoon, the company issued a press release that provided an overview of its fourth quarter and fiscal year-end results, which followed the filing of its annual report on its Form 10-K. Today's conference call is being recorded and will be available online at cbdmd.com in accordance with cbdMD's retention policies. (Operator Instructions)

At this time, I would like to now turn the call over to your host, Ronan Kennedy, the company's Chief Financial Officer. Ronan, please go ahead.

T. Ronan Kennedy - *cbdMD, Inc. - CFO*

Thank you, Catherine, and thank you all for joining the cbdMD Fourth Quarter and Fiscal Year End September 30, 2020, Earnings Call and Update. On the call today, we also have our Chairman and Co-CEO, Marty Sumichrast; as well as our Chief Marketing Officer, Ken Cohn.

Following the safe harbor statement, Marty and Ken will provide an overview of our business, then I'll provide a summary of the quarterly and fiscal year-end financial results. Following that, we'll open up the call for questions.

We'd like to remind everyone that various remarks about future expectations, plans and prospects constitute forward-looking statements for purposes of safe harbor provisions under the Private Securities Litigation Reform Act of 1995. CbdMD cautions that these forward-looking statements are subject to risks and uncertainties that may cause our actual results to differ materially from those indicated, including the risks described in the company's annual report on Form 10-K for the year ended September 30, 2020, and our other filings with the SEC, all of which can be reviewed on the company's website, cbdmd.com or on the SEC's website at www.sec.gov.

Any forward-looking statements made on this conference call speak only as of today's date, Tuesday, December 22, 2020, and cbdMD does not intend to update any of these forward-looking statements to reflect events or circumstances that would occur after today's date, except as may be required by federal securities laws.

With that, I'd like to turn the call over to cbdMD's Chairman and Co-CEO, Marty Sumichrast.

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Ronan, thank you, and welcome to everyone who is joining us this afternoon. We believe cbdMD is now one of the most successful CBD companies in the world. And cbdMD and Paw CBD have become 2 of the world's most recognizable and valuable CBD brands. cbdMD continues to attract international attention from customers and investors alike. Our brand social media dominance has fueled our online business, which continues to

drive our sales growth. In fact, based upon the November 2020 Google Analytics report, cbdmd.com ranks at the top as one of the most visited CBD websites in the world.

As we look ahead into 2021, we believe our plan to expand our reach into new product categories will not only drive sales but will also diversify and expand our customer demographics. As we continue to attract world-class partnerships, as we did with Bubba Watson, Bellator MMA, Life Time Fitness and Barstool Sports, our brands grow in status and recognition on the world stage.

Here is another example of how our brands attract world-class partners. Today, I'm proud to announce that cbdMD has become the exclusive CBD partner of the Joe Rogan Experience Podcast, which plays exclusively on Spotify and has over 200 million monthly downloads. We believe that these achievements help our brands dominate in the CBD industry and also help us deliver on our financial goals as well. Since taking the cbdMD brand public in December 2018, we have grown quarterly sales over 900% in 8 quarters. We've done this by remaining focused on our core competency, which is our direct-to-consumer engine.

Despite the COVID-19 pandemic, we continue to show remarkable growth throughout fiscal 2020. We have maintained one of the strongest balance sheets in the CBD industry. And in fact, recently, more than doubled our liquidity, which now stands today at approximately \$30 million in cash with virtually no debt.

To put this in context, we built 2 brands and operated a U.S. listed company for 2 years with less cash than we have in the bank today. Furthermore, we dramatically reduced our non-GAAP adjusted loss from operations from over \$10 million in the first half of fiscal 2020 to approximately \$1.3 million in the second half of fiscal 2020.

Earlier this goal -- earlier this year, we set a goal of achieving positive adjusted operating income during calendar year 2020, a non-GAAP financial measure. We are presently confident that we will reach this milestone in early fiscal 2021. However, based upon marketing opportunities that may arise during the year, achieving this goal may be extended later into the fiscal year. We believe we are positioned to take advantage of a unique opportunity, which is to gain a meaningful amount of the \$2 billion-plus total addressable global CBD market, a market which according to several industry analytic firms, including leading analytics firm, the Brightfield Group, is expected to grow to over \$10 billion by 2025.

We believe we are demonstrating our ability to gain significant market share by reporting quarter-over-quarter net sales growth of 23% and year-over-year net sales growth of 77%, both resulting in record quarterly and annual net sales of \$11.7 million and \$41.9 million, respectively, as of September 30, 2020. While we have not committed to any financial guidance, we do expect robust sales growth to continue into fiscal 2021.

Finally, with respect to the regulatory climate for CBD, with continued attention on COVID-19 and the pending change in presidential administrations, we do not expect any FDA regulatory guidance from the CBD -- for CBD in the near future. Therefore, we remain focused on maintaining the highest manufacturing standards under GMP and compliance with state regulations, as states take the regulatory lead related to hemp-derived cannabinoid products.

It is now my pleasure to introduce Ken Cohn, our Chief Marketing Officer, who will talk about our branding and marketing strategies. Ken, please go ahead.

Ken Cohn - *cbdMD, Inc. - CMO*

Thanks, Marty, and welcome, everyone. I believe that 2020 is the year of separation within the CBD category. And for cbdMD, 2020 has offered a landscape of opportunities to continue to drive and solidify both our cbdMD and Paw CBD brands distinction. We continue to lean heavily on making data-driven decisions with insights garnered each quarter. We faced a number of questions and challenges coming into this most recent quarter. How do we continue to accelerate the brand, drive our consumers' trust and capitalize on our surging e-commerce traffic, while at the same time, educate, inform and convert our new and returning customers?

As we considered these important questions, we focused on key performance indicators, or KPIs, such as average order value, retention rate and website traffic, to name just a few. We utilized these non-GAAP measures in internally analyzing the effectiveness of our advertising spend and

marketing initiatives and believe these metrics are important to our investors in their review of our financial performance. Our customer retention rate, representing existing customers who purchased at least once during the quarter, continue to increase throughout the year. In this past quarter, returning customers spent more money per order, reaching approximately \$88 in average order value; purchased more frequently, now a median of once every 39 days; and bought more items per order as compared to the previous 3 quarters. And regarding our direct-to-consumer website traffic, in the fourth quarter of fiscal 2020, our new website traffic increased 13% over the prior quarter with the largest increase being via organic traffic.

Data continued to aid us in amplifying the effectiveness of our e-mail marketing. While we sent less e-mails to our entire growing database, we focused on segmented, relevant content and information. As such, we have experienced continued growth in our open and click-through rates. This past quarter, we launched cbdMD's first nationally viewed TV advertising campaign. cbdMD's 30-second Conquer the Day commercial was broadcast across multiple national cable networks with very promising metrics, followed by a 15-second version as well. You can view the commercial on the homepage of cbdmd.com. Average orders continue to strengthen since launching in September 2020, which is bolstering our confidence in this advertising media, as we look to expand our TV advertising campaign in 2021.

Paw CBD showed excellent first full year net sales of approximately \$4.5 million for fiscal 2020, and the brand's metrics continue to move in a positive direction. We are seeing the direct-to-consumer power of cbdmd.com translate into significant growth for pawcbd.com as Paw CBD's direct-to-consumer sales account for over 70% of the brand's net sales during the 2020 fiscal year. We continue to focus on cross-selling, customer retention and education and are planning to roll out Paw CBD subscription and reward programs in fiscal 2021. As we seek to mimic the expansion of cbdMD's success, our goal is to make Paw CBD the dominant brand in the CBD pet market.

We also were very proud of the awards and accolades we received for many of our products. The Brightfield Group named cbdMD a top 10 domestic brand in 2 booming categories, topicals and skincare beauty. CbdMD was also ranked the highest in terms of overall consumer satisfaction as well as the highest in unaided consumer awareness of any of the top 20 CBD brands in a survey conducted by Brightfield Group of more than 3,500 CBD users. Brightfield Group also ranked cbdMD as the top brand for high-quality, innovative and reliable. Paw CBD has also won several awards, including Pet Innovation Award for best dog calming product in 2020 and 2019's Pet Business Magazine industry recognition award for dog calming aid. During fiscal 2020, Paw CBD also launched a category first partnership with TripAdvisor.

Our B2B brick-and-mortar business has seen numerous achievements as well. First, our GNC partnership is both live on the GNC e-commerce site as well as on shelves in 90 GNC franchise locations. Second, several of our regional partners continue to expand distribution of our products, such as Save Mart, who increased their distribution from 5 to 100 of their locations. Life Time is another example of our retail expansion success story. After strong customer demand, Life Time expanded their distribution from 23 to 124 locations. Third, we are also excited to announce that ShopHQ launched with us this month, and we look forward to providing more updates in the coming weeks. And fourth, we have solidified our expansion into the lucrative c-store distribution channel and have secured distribution for up to 3,000 new locations with an expected launch in January 2021.

With that, I'll now turn the call over to our CFO, Ronan Kennedy, to review our most recent financial results.

T. Ronan Kennedy - cbdMD, Inc. - CFO

Thank you, Ken. I'm going to start with a brief summary of our GAAP-based results. On a GAAP basis, total net sales for the fourth quarter hit another all-time high of \$11.7 million or a 23% year-over-year increase and a 10% sequential quarterly gain. For the fiscal year ended September 30, audited net sales were \$41.9 million. This was a 77% increase over the fiscal 2019 results.

Our quarterly direct-to-consumer sales also hit a record high of \$8.6 million in the fourth quarter of fiscal 2020, a 58% year-over-year increase. For fiscal 2020, direct-to-consumer sales totaled \$30.5 million and representing a 106% increase over fiscal 2019. Our marketing investments and emphasis on developing a direct relationship with our customers paid off well during the year, resulting in our direct-to-consumer sales growing to 73% of our total net sales in fiscal 2020 compared to 63% in the prior year.

Our wholesale business generated \$11.3 million of net sales for fiscal 2020. Despite the challenges presented by COVID-19 during the fiscal 2020, this still represents a 29% year-over-year increase. We did see a rebound during the fourth quarter in wholesale business, which generated a total of \$3.1 million in net sales, representing a 29% sequential quarterly growth.

Our goal has always been to maintain a gross profit margin between 63% to 70%. Our GAAP gross profit as a percent of net sales came in at 54.4% for the fourth quarter of fiscal 2020 compared to 56% for the comparative prior year period. For fiscal 2020, our gross margin was 63% compared to 61.4% for fiscal 2019. The fourth quarter GAAP gross profit margin was after accounting for a noncash inventory adjustment of \$1.6 million. We generated a fourth quarter non-GAAP adjusted gross profit of 68%. The \$1.6 million noncash adjustment is mostly due to writing off old raw materials and the net realized value adjustment of noncore inventory. Going forward, we expect to maintain our gross profit margins between 63% and 70%, as we seek to maintain strong direct-to-consumer revenue and take advantage of increasing operating leverage.

We ended this year with \$14.8 million in cash and cash equivalents on hand. Coupled with the approximate \$15.7 million in net proceeds from our preferred stock offering completed earlier in December of 2020, we believe we have a very strong cash position going into calendar 2021 and more than ample capital to execute on our fiscal 2021 strategy. We believe this puts us in an enviable position in our industry and allows us to utilize our balance sheet to make further scientific and regulatory investments, continue to invest in incremental strategic marketing efforts, including increasing our TV spend and support our efforts to expand our product portfolio.

Our operating expenses for the September 30, 2020, quarter were \$10.8 million, which was an increase of 1.7% over September 30, 2019, quarter. Overall, this resulted in a GAAP loss from operations of approximately \$4.5 million for the September 2020 quarter, a 14.2% reduction in loss from the prior year period. For the fiscal 2020, our operating expenses were approximately \$43.9 million, resulting in a GAAP operating loss from operations of \$17.5 million, an 18.8% increase in loss from fiscal 2019.

The company spent considerable time in the third and fourth quarters of fiscal 2020, focusing on reducing our cash expenses. And during the fourth quarter, we spent additional time focused on our balance sheet. We believe the cost control measures made during fiscal 2020, along with our September 30, 2020, balance sheet position us very well for fiscal 2021. Along with the \$1.6 million in noncash inventory expense previously mentioned, we incurred a number of accruals and nonrecurring or discretionary expenses during the fourth quarter. Our nonrecurring operating expenses for the fourth quarter included \$438,000 onetime crude expense related to severance, \$102,000 write-down of old receivables, \$200,000 expense in discretionary bonus accrual and together with the \$760,000 in noncash stock expense resulted in a non-GAAP adjusted operating loss of \$1 million for the fourth quarter of fiscal 2020 compared to a \$4.1 million non-GAAP adjusted operating loss for the fourth quarter of fiscal 2019.

The increase in non-GAAP adjusted operating loss over the June 30, 2020, quarter was mainly attributed to management's decision to increase discretionary marketing and affiliate expenses by \$533,000 for the quarter and allocate expenses toward IT-related items. The 2020 full year non-GAAP adjusted loss from operations totaled \$11.5 million, similar to the comparative prior year period. As previously mentioned, approximately 89% or over \$10 million of this year's non-GAAP adjusted operating loss occurred in the first half of the 2020 fiscal year.

Other income expenses on our consolidated income statement include a noncash contingent liability charge related to the December 2018 acquisition of Cure Based Development. The contingent liability is revalued at the end of each quarter and during the fourth quarter of fiscal 2020, we had an increase in value of \$800,000 to approximately \$16.2 million, which created a corresponding other noncash expense. For the fiscal year, the total noncash gain from the contingent liability was \$29.8 million. The changes in the valuation of the contingent liability was primarily a result of the change in the market price of our common stock from period to period.

We had cash and cash equivalents of approximately \$14.8 million and working capital of approximately \$16 million on September 30, 2020, compared to a cash and cash equivalents of approximately \$4.7 million and working capital of \$12 million as of September 30, 2019.

Our current assets as of September 30, 2020, increased 51% from the prior year-end to \$23.7 million. A primary driver of the increase in current assets was the increase in cash and prepaid sponsorship expenses, which was offset partially by decreases in accounts receivable, marketable and other securities, merchant reserve, prepaid expenses and assets from discontinued operations.

As of September 30, the company's total current liabilities was \$7.6 million, of which approximately \$2.8 million is accounts payable and \$2.9 million is accrued expense. The company has approximately \$224,000 of financing notes on equipment for our manufacturing facility as well as a \$1.45 million SBA loan from the Paycheck Protection Program.

We consider 2020 to be a success in many ways beyond our strong gains in revenue and second half adjusted earnings improvement. Our operations team made significant strides this past year too. We moved from a 5,000 square foot warehouse fulfillment space to an 80,000 square foot facility. We expanded our lab space by 130% and upgraded environmental parameters to meet NSF audit standards. We completed the audit and registration for both GMP and NSF, obtaining FDA-registered facilities, and we introduced over 200 new SKUs to our portfolio. All of these accomplishments have been completed while maintaining budget levels and controlling payroll and while navigating through COVID-19 this year. We are proud of our team's success and excited to see what they can accomplish in the coming year.

With that, I'd like to now turn the call back over to Marty.

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Thanks, Ronan. With that, I'd like to open the call up for Q&A. Catherine?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question is coming from Paul Cooney.

Paul Cooney - *Joseph Gunnar & Co., LLC - Senior VP & Director of Structured Products*

Congratulations on a great year, a great quarter. I'd love to see the growth in the company and the brand. Marty, I'm just -- outside of what you're talking to us about in the conference call, what else can we expect going forward as far as the products are concerned? Just like what are the kind of surprises can come up for us in the coming quarters as far as your product and your brand?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Well, thank you, Paul, and really appreciate your support. Look, I think we've always been innovative. I think you're going to see us rolling out some new product lines first of the year. And we're excited to start talking about that shortly. I think the other thing that we, I think, have done a really good job of is partnering with some really great brands. We mentioned Joe Rogan, Barstool, Life Time, Bellator, Bubba, so many of our athletes. I think you'll see us expanding that list and really matching up with some very large brands that want to get into the CBD space and have really come to us to be their partner in it. And I think that's going to not only help the brand value and the recognition as we partner with some of these bigger brands but also certainly helps us on a customer side and the sales side.

Paul Cooney - *Joseph Gunnar & Co., LLC - Senior VP & Director of Structured Products*

Now as far as that's concerned, Marty, are you talking about like getting more sponsorships? Or are you talking about like maybe somebody coming in and using your brand to enhance their brand?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

I would say both, Paul. I'd say we are talking to groups to do all the above. It's a very exciting time for us next year because we think all the work we've done to grow the brand to get such high brand recognition and on the regulatory side, really meet the challenges in front of us and being around a few companies that are existing in the CBD space that can achieve that both with our organization and also our balance sheet and our financial wherewithal. I think big companies are concerned about who they partner with. And when they see us and they see our financial performance and they see our strong balance sheet, I think they're very comfortable. And I think that's going to pay off for us next year, and we're excited to get these deals done and get them announced and start working on them.

Operator

Your next question is coming from Michael Galantino.

Michael Anthony Galantino - *Boenning & Scattergood, Inc. - MD of Equity Capital Markets*

Congratulations on a great quarter. This growth is incredibly impressive. And our firm just got introduced through this transaction, and we're thrilled to be working with you guys. We're excited to be involved with the company.

I have 2 questions. Number one, do you have exclusivity when it comes to the Joe Rogan relationship and also the Barstool Sports relationship? Do you have like concentrates on that? Do you have them for a year? Do you have them for, I don't know, for whatever?

And then the second question I have is, do you see the direct multilevel marketing guys out there regarding CBD to be any kind of competition to you going forward?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Yes. Thank you. Joe Rogan is an exclusive deal for 2021. We've had a good strong relationship with Joe. We were very excited that he got on with Spotify, which just enhances his brand, which certainly enhances our position being his partner. So that one is exclusive. Barstool is not exclusive, but we think we're probably one of the biggest CBD brands that are through their platform. And we love Barstool and everything they're doing. So we're going to continue a very strong commitment to Barstool.

As far as the multi-level marketing, look, we don't really see that the MLM guys are necessarily our competition because they don't really focus on brand as much as we do. And I think that's such a big distinction. And I'm not sure -- certainly, our distribution channels are significantly different. So look, it's a huge market out there. As I said, it's about \$2.5 billion now. It's growing to -- depending on who you talk to \$10 billion, \$15 billion, \$20 billion in the next 3 to 5 years. And the current, say, top 20 CBD companies only have about 20% of the market share. And so you have this huge piece of market out there that other 80% that we are gaining into on top of you've got the pie getting bigger. So there's just an enormous amount of runway for us. We sit at the top of the branding space in CBD, both at cbdMD and of course, our Paw brand is doing really great for us. So we don't necessarily see the MLM crowd as a direct competitor. Certainly, they sell CBD product, but not certainly the way we do it.

Michael Anthony Galantino - *Boenning & Scattergood, Inc. - MD of Equity Capital Markets*

That's what I thought. One follow-up question on the Paw brand. What kind of growth do you expect in 2021 in that division?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Well, we haven't given out guidance, but I will tell you that we were really pleased with our growth. I mean we basically started it from scratch and did \$4.5 million in the first 10, 11 months of operation, and that's also in a COVID environment where a lot of that was -- the other thing I'll tell you

is this, unlike cbdMD, where there is a lot of competition, the pet business, the CBD pet business, there's just not a lot of competition. So we went from nowhere to the top in 1 year we think the opportunity is really big in the pet market. And if anybody on the call knows, if you own a pet, you spend just about anything on your pet. So we think it's a great market. We're excited, and we think we got a great opportunity to grow that brand very quickly into next year, but we haven't given out guidance, but we expect to see significant growth.

Operator

Your last question is coming from Ben Mandel.

Unidentified Analyst

Yes. [Barry Mandel]. A couple of things. How are you going to market your pet brand, your Paw's brands, kind of marketing program you have? Number one. And number two, can you talk about pricing in the CBD area? What the competitive landscape looks like in the CBD area?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Yes. Ken, why don't you talk about the marketing on Paw CBD?

Ken Cohn - *cbdMD, Inc. - CMO*

Sure. What has happened is we've been able to take a lot of the learnings that we've gained on the cbdMD side of the business and apply it successfully on the Paw CBD business. And certainly, when it comes to tactics, whether it be e-mail, whether it be display, whether it be social, whether it be influencers, we've seen a very similar trajectory as Paw CBD becomes synonymous with the CBD category, like we're seeing on the consumer side, on the human side. So we're going to continue to let the success on the MD side kind of point us in the right direction on Paw because it's done so since the outset. So Marty, why don't you jump on the second question?

Martin A. Sumichrast - *cbdMD, Inc. - Chairman & Co-CEO*

Yes. Look, as far as pricing, pricing has held firm, and we don't see right now much price compression out there.

Operator

With no further questions in the queue, that does conclude our conference call for today. Thank you for your participation. You may now disconnect.

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