

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) is intended to assist in the understanding and assessing the trends and significant changes in our results of operations and financial condition. Historical results may not be indicative of future performance. This discussion includes forward-looking statements that reflect our plans, estimates and beliefs. Such statements involve risks and uncertainties. Our actual results may differ materially from those contemplated by these forward-looking statements as a result of various factors, including those set forth in “Risk Factors” in Part I, Item 1A and “Cautionary Statement Regarding Forward-Looking Statements” of our Annual Report on Form 10-K for the year ended December 31, 2019.

This MD&A should be read in conjunction with the condensed consolidated financial statements and related notes. Financial information presented in this MD&A is presented in thousands of United States (“U.S.”) dollars, unless otherwise indicated.

Overview

Acreage Holdings, Inc. (“Acreage”, “we”, “our” or the “Company”) is a vertically integrated, multi-state operator of cannabis licenses and assets in the United States. Our operations include (i) cultivating cannabis plants, (ii) manufacturing branded consumer products, (iii) distributing cannabis flower and manufactured products, and (iv) retailing high-quality, effective and dosable cannabis products to consumers. We appeal to medical and adult-use customers through brand strategies intended to build trust and loyalty.

Highlights from the three months ended March 31, 2019

- We closed our acquisition of Acreage Florida, Inc. (“Acreage Florida”) effective January 4, 2019. Acreage Florida has a vertically integrated cannabis license in Florida, which allows for growing, processing, and retail dispensary operations in Florida.
- We closed on our definitive agreement to purchase Thames Valley Apothecary, LLC, a licensed dispensary in Connecticut, increasing our footprint to three dispensaries in the state.
- We acquired the remaining 70% ownership interest in NCC LLC (“NCC”), a dispensary license holder in Illinois.

Operational and Regulation Overview

We believe Acreage’s operations are in material compliance with all applicable state and local laws, regulations and licensing requirements in the states which we operate. However, cannabis is illegal under U.S. federal law. Substantially all our revenue is derived from U.S. cannabis operations. For information about risks related to U.S. cannabis operations, please refer to Item 1A entitled “Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2019.

Results of Operations

The following table presents selected financial data derived from the consolidated financial statements of the Company for the three months ended March 31, 2019, compared to the three months ended March 31, 2018. The selected financial information set out below may not be indicative of the Company’s future performance.

Summary Results of Operations

	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
Revenues, net	\$ 12,897	\$ 2,197	\$ 10,700	487 %
Operating loss	(32,013)	(4,038)	(27,975)	(693)%
Net loss attributable to Acreage	(23,377)	(4,836)	(18,541)	(383)%
Basic and diluted loss per share attributable to Acreage	(0.29)	(0.10)	(0.19)	(9)%

Revenues, net, cost of goods sold and gross profit

The Company derives its revenues from sales of cannabis and cannabis-infused products through retail dispensary, wholesale, manufacturing and cultivation businesses, as well as from management or consulting fees from entities for whom we provide management or consulting services. As of March 31, 2019, Acreage owned and operated five dispensaries in Oregon (three in Portland, one in Eugene and one in Springfield), four in New York (Buffalo, Farmingdale, Middletown, and Queens), three in

Connecticut (Bethel, South Windsor and Uncasville), one in Baltimore, Maryland, one in Worcester, Massachusetts, one in Rolling Meadows, Illinois and one in Fargo, North Dakota. Acreage has cultivation facilities in Sinking Spring, Pennsylvania, Sterling, Massachusetts, Syracuse, New York, Freeport, Illinois and Cedar Rapids, Iowa. Acreage also collects management services revenues, substantially all in Maine.

Gross profit is revenue less cost of goods sold. Cost of goods sold include costs directly attributable to inventory sold such as direct material, labor, and overhead. Such costs are further affected by various state regulations that limit the sourcing and procurement of cannabis and cannabis-related products, which may create fluctuations in gross profit over comparative periods as the regulatory environment changes.

Gross profit in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
Retail revenue, net	\$ 9,909	\$ 2,197	\$ 7,712	351 %
Wholesale revenue, net	2,815	—	2,815	n/m
Other revenue, net	173	—	173	n/m
Total revenues, net	\$ 12,897	\$ 2,197	\$ 10,700	487 %
Cost of goods sold, retail	(5,881)	(1,289)	(4,592)	(356)%
Cost of goods sold, wholesale	(1,696)	(67)	(1,629)	n/m
Total cost of goods sold	\$ (7,577)	\$ (1,356)	\$ (6,221)	(459)%
Gross profit	\$ 5,320	\$ 841	\$ 4,479	533 %
Gross margin	41%	38%		3 %

The increase in total revenues during the three months ended March 31, 2019 was primarily driven by acquisitions, which contributed 363%. Acquisitions drove 350% and 4% of retail and wholesale revenue increases, respectively. The remaining increase in wholesale revenue was primarily driven by our Pennsylvania cultivation facility.

The increase in total cost of goods sold during the three months ended March 31, 2019 was primarily driven by acquisitions, which contributed 349%. Acquisitions contributed 360% and 140% to the retail and wholesale costs of goods sold, respectively. The remaining increase in wholesale cost of goods sold was primarily driven by our Pennsylvania cultivation facility.

The increase in gross profit was driven by the factors discussed above. Acquisitions contributed 386% to the increase. Gross margin for the three months ended March 31, 2019 was 41.2%, compared to 38.3% for the three months ended March 31, 2018.

Revenue by geography

While the Company operates under one operating segment, the production and sale of cannabis products, the below revenue breakout by geography is included as management believes it provides relevant and useful information to investors.

Revenue by region in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
New England	\$ 7,084	\$ —	\$ 7,084	n/m
Mid-Atlantic	3,093	—	3,093	n/m
Midwest	596	—	596	n/m
West	2,124	2,197	(73)	(3)%
Total revenues, net	\$ 12,897	\$ 2,197	\$ 10,700	487 %

Total operating expenses

Total operating expenses consist primarily of compensation expense at our corporate offices as well as operating subsidiaries, professional fees, which includes, but is not limited to, legal and accounting services, depreciation and other general and administrative expenses.

Operating expenses in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
General and administrative	\$ 10,158	\$ 1,796	\$ (8,362)	(466)%
Compensation expense	6,489	2,368	(4,121)	(174)%
Equity-based compensation expense	18,977	501	(18,476)	n/m
Marketing	801	204	(597)	(293)%
Depreciation and amortization	908	10	(898)	n/m
Total operating expenses	\$ 37,333	\$ 4,879	\$ (32,454)	(665)%

Increases to compensation expense during both the three months ended March 31, 2019 and 2018 were primarily driven by stock compensation to attract and retain talent and increased headcount to scale our operations. Increases to general and administrative expenses were primarily driven by the increased volume and complexity of services such as legal and other professional services required as the Company's operations increased during the three months ended March 31, 2019 and 2018.

Total other income (loss)

Other income (loss) \$ in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
Income from investments, net	\$ 2,727	\$ 218	\$ 2,509	1,151%
Interest income from loans receivable	730	91	639	n/m
Interest expense	(118)	(1,051)	933	n/m
Other income (loss), net	92	(42)	134	n/m
Total other income (loss)	\$ 3,431	\$ (784)	\$ 4,215	538%

The increase in income from investments, net was due to the mark-to-market of certain equity method investments. The decline in interest expense during the three months ended March 31, 2019 compared to the same periods in the prior year was due to the conversion of our convertible notes to equity at the time of our public listing. Interest income from loans receivable increased as our amount of outstanding loans increased.

Net loss

Net loss \$ in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
Net loss	\$ (30,804)	\$ (4,992)	\$ (25,812)	(517)%
Less: net loss attributable to non-controlling interests	(7,427)	(156)	(7,271)	n/m
Net loss attributable to Acreage Holdings, Inc.	\$ (23,377)	\$ (4,836)	\$ (18,541)	(383)%

The increases in net loss are driven by the factors discussed above.

The increase in loss allocated to the non-controlling interests was driven by the shift in ownership structure resulting from the RTO transaction. Certain former HSCP members contributed their units in HSCP to Acreage Holdings, WC, Inc. ("USCo2") in exchange for non-voting shares of USCo2, and certain executive employees and profits interests holders remained unitholders of HSCP. These non-voting shares and units are exchangeable for either one Subordinate Voting Share of the Company or cash, as determined by the Company.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity

Sources and uses of cash

Our primary uses of capital include acquisitions, capital expenditures, servicing of outstanding debt and operating expense. Our primary sources of capital include funds generated by cannabis sales as well as financing activities. To date, we have primarily used private financing as a source of liquidity for short-term working capital needs and general corporate purposes. In February 2020, we closed on a financing transaction described in detail in Note 17, entitled Subsequent Events in the Company's Annual Report on Form 10-K for the year ended December 31, 2019. Our ability to fund our operations, capital expenditures, acquisitions, and other obligations depends on our future operating performance and ability to obtain financing, which are subject to prevailing economic conditions, as well a financial, business and other factors, some of which are beyond our control.

We expect that our cash on hand and cash flows from operations, along with our ability to obtain private and/or public financing, will be adequate to support the capital needs of the existing operations as well as expansion plans for the next 12 months. While our liquidity risk has increased since our RTO transaction as a result of the Company's rapid growth and continued expansion resulted in negative operating cash flow for the year ended December 31, 2019, we believe we have alleviated the risk. See Item 7A - "Liquidity Risk" in the Company's Annual Report on Form 10-K for the year ended December 31, 2019.

Cash flows

Cash and cash equivalents were \$64,183 as of March 31, 2019, an increase of \$57,526 from March 31, 2018. The following table details the change in cash, cash equivalents and restricted cash for the three months ended March 31, 2019 and 2018.

Cash flows \$ in thousands	Three Months Ended		Better/(Worse)	
	March 31,		2019 vs. 2018	
	2019	2018	\$	%
Net cash provided by (used in) operating activities	\$ (13,630)	\$ (8,545)	\$ (5,085)	(60)%
Net cash provided by (used in) investing activities	(16,719)	(3,643)	(13,076)	(359)%
Net cash provided by (used in) financing activities	(10,411)	2,345	(12,756)	n/m
Net increase (decrease) in cash, cash equivalents and restricted cash	\$ (40,760)	\$ (9,843)	\$ (30,917)	(314)%

Net cash used in operating activities

The increases in cash used in operating activities were primarily driven by an increase in general and administrative and compensation expenses during the three months ended March 31, 2019 and compared to the three months ended March 31, 2018.

Net cash provided by (used in) investing activities

Cash used in investing activities during the three months ended March 31, 2019 was primarily driven by \$77,567 spent on the advanced payments and purchases of cannabis license holders and management contracts, \$8,288 spent on capital expenditures to build out our owned operations, and \$5,794 advanced to entities, net of collections, with which we have a management or consulting services arrangement. Partially offsetting these cash disbursements were cash proceeds of \$74,768 from the maturing of short-term investments.

Cash used in investing activities during the three months ended March 31, 2018 was primarily driven by \$2,687 spent on capital expenditures to build out our owned operations, \$480 spent on long-term investments, \$275 advanced to entities, net of collections, with which we have a management or consulting services arrangement, and \$250 spent on the advanced payments and purchases of cannabis license holders and management contracts. Proceeds of \$49 related to distributions from investments partially offset these outflows.

Net cash provided by (used in) financing activities

Cash used in financing activities during the three months ended March 31, 2019 was primarily driven by \$7,621 in debt repayments and \$2,790 paid to settle taxes withheld.

Cash provided by financing activities during the three months ended March 31, 2018 was primarily driven by \$2,750 related to net capital contributions from non-controlling interests. Partially offsetting these proceeds were payments of \$400 used to purchase additional ownership in non-controlling interests and \$5 in debt repayments.

Capital Resources

Capital structure and debt

Our debt outstanding as of March 31, 2019 and December 31, 2018 is as follows:

Debt balances	March 31, 2019	December 31, 2018
NCCRE loan	\$ 507	\$ 511
Seller's notes	7,507	15,124
Finance lease liabilities	382	—
Total debt	\$ 8,396	\$ 15,635
Less: current portion of debt	7,528	15,144
Total long-term debt	\$ 868	\$ 491

Commitments and contingencies

Commitments

The Company provides revolving lines of credit to several of its portfolio companies. Refer to Note 5 of our Annual Report on Form 10-K for the year ended December 31, 2019 for further information.

Definitive agreements

GCCC Management, LLC

During the year ended December 31, 2018, the Company entered into a definitive agreement to acquire all ownership interests in GCCC Management, LLC, a management company overseeing the operations of Greenleaf Compassionate Care Center, Inc., a non-profit cultivation and processing facility in Rhode Island, for cash consideration of \$10,000.

Surety bonds

The Company has indemnification obligations with respect to surety bonds primarily used as security against non-performance in the amount of \$5,000 as of March 31, 2019, for which no liabilities are recorded on the unaudited Condensed Interim Consolidated Statements of Financial Position.

The Company is subject to other capital commitments and similar obligations. As of March 31, 2019 and 2018, such amounts were not material.

Contingencies

The Company's operations are subject to a variety of local and state regulations. Failure to comply with one or more of those regulations could result in fines, restrictions on its operations, or losses of permits that could result in the Company ceasing operations. While management of the Company believes that the Company is in compliance with applicable local and state regulations as of March 31, 2019, cannabis regulations continue to evolve and are subject to differing interpretations. As a result, the Company may be subject to regulatory fines, penalties, or restrictions in the future.

The Company may be, from time to time, subject to various administrative, regulatory and other legal proceedings arising in the ordinary course of business. Contingent liabilities associated with legal proceedings are recorded when a liability is probable, and the contingent liability can be reasonably estimated.

New York outstanding litigation

On November 2, 2018, EPMMNY LLC ("EPMMNY") filed a complaint in the Supreme Court of the State of New York, County of New York, asserting claims against 16 defendants, including NYCANNA, Impire State Holdings LLC, NY Medicinal Research & Caring, LLC (each, a wholly-owned subsidiary of High Street) and High Street. The Index Number for the action is 655480/2018. EPMMNY alleges that it was wrongfully deprived of a minority equity interest and management role in NYCANNA by its former

partner, New Amsterdam Distributors, LLC, which attempted to directly or indirectly sell or transfer EPMMNY's alleged interest in NYCANNA to other entities in 2016 and 2017, including Impire, NYMRC and High Street. EPMMNY alleges that it is entitled to the value of its alleged minority interest in NYCANNA or minority ownership in NYCANNA. EPMMNY also alleges that certain defendants misused its alleged intellectual property and/or services, improperly solicited its employees, and aided and abetted or participated in the transfer of equity and/or business opportunities from EPMMNY. High Street intends to vigorously defend this action, which the Company firmly believes is without merit. EPMMNY alleges that it was improperly deprived of its equity stake in NYCANNA before NYCANNA was acquired by High Street. High Street is also entitled to full indemnity from the claims asserted against it by EPMMNY pursuant to the purchase agreement pertaining to its acquisition of NYCANNA and personal guarantee by the largest shareholders of the seller.

Contractual obligations

Our contractual obligations include amounts reflected on our balance sheet, as well as off-balance sheet arrangements. There were no material changes in our contractual obligations during the three months ended March 31, 2019 and 2018.

Critical accounting policies and estimates

The preparation of financial statements in conformity with GAAP requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, revenues and expenses. Actual results may differ from these estimates. The estimates and underlying assumptions are evaluated on an ongoing basis and are based on historical experience and other assumptions that we believe are reasonable.

The estimates and assumptions management believes could have a significant impact on our financial statements are discussed below. For a summary of our significant accounting policies, refer to Note 2 of the Condensed Consolidated Financial Statements.

Taxes

Provisions for taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. It is possible, however, that at some future date, an additional liability could result from audits by taxing authorities. If the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

Business combinations

The Company must assess whether an entity being purchased constitutes a business, which requires an assessment of inputs and processes in place at the acquiree. The fair value of assets acquired and liabilities assumed requires management to make significant estimates. Judgment is required to determine when the Company gains control of an investment. This requires an assessment of the relevant activities of the investee that significantly affect its returns, including operating and capital expenditure decision-making, financing of the investee, key management personnel changes and when decisions in relation to those activities are under the control of the Company or require unanimous consent from the investors. Investments in which the Company does not gain control are accounted for as equity-method investments (if the Company has significant influence) or as investments held at fair value with changes recognized through net income (if the Company has no significant influence). Refer to Note 3 and Note 4 of the Condensed Consolidated Financial Statements for further discussion.

Impairment on notes receivable

At each reporting date the Company assesses whether the credit risk on its promissory notes receivable has increased significantly since initial recognition.

Impairment of intangible assets

Goodwill and indefinite-lived intangible assets are not subject to amortization and are tested for impairment annually or more frequently if events or changes in circumstances indicate that they might be impaired. Finite-lived intangible assets and other long-lived assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

Emerging growth company status

We are an "emerging growth company" as defined in the Jumpstart Our Business Startups Act (the "JOBS Act"). Under the JOBS Act, emerging growth companies can delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have elected to use this exemption from new or revised accounting standards and, therefore, we will be not subject to the same new or revised accounting standards as other public companies that have made this election.

For as long as we continue to be an emerging growth company, we intend to take advantage of certain other exemptions from various reporting requirements that are applicable to other public companies including, but not limited to, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. We cannot predict if investors will find our subordinate voting shares less attractive because we will rely on these exemptions. If some investors find our subordinate voting shares less attractive as a result, there may be a less active trading market for our subordinate voting shares and our stock price may be more volatile.

We will remain an emerging growth company until the earliest of (i) the last day of the year in which we have total annual gross revenue of \$1.07 billion or more; (ii) the last day of the year following the fifth anniversary of the first sale of common equity securities pursuant to an effective registration under the Securities Act; (iii) the date on which we have issued more than \$1.0 billion in nonconvertible debt during the previous three years; or (iv) the date on which we are deemed to be a large accelerated filer under the rules of the SEC.