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

Investors should read the following discussion in conjunction with the unaudited financial statements and notes thereto included under Part 1, Item 1 of this Quarterly Report on Form 10-Q. In addition, investors should refer to our audited consolidated financial statements and notes thereto and related Management's Discussion and Analysis of Financial Condition and Results of Operations appearing in our Annual Report on Form 10-K for the fiscal year ended December 31, 2023.

Disclosure Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking information about the Company that is intended to be covered by the safe harbor for "forward-looking statements" provided by the Private Securities Litigation Reform Act of 1955. Forward-looking statements are statements that are not historical facts. Words such as "guidance," "expect," "will," "may," “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “suggests,” “potential” and similar expressions are intended to identify forward-looking statements. The statements include information regarding our plans, strategies, and expectations of future financial performance and prospects. Forward-looking statements are not guarantees of performance. These statements are based upon the current beliefs and expectations of our management and are subject to significant risk and uncertainties that could cause actual results to differ materiality from those expressed in, or implied or projected by, the forward-looking information and statements. Although we believe the expectations reflected in the forward-looking statements are reasonable, we cannot assure investors that the expectations will prove to be correct. Among the factors that could cause actual results to differ materially from the expectations are acts of war or terrorism and the impact on the social and economic conditions in the United States, and changes in the legalization of marijuana across the United States. More information on factors that could cause actual results to differ materially from those anticipated is included from time to time in our reports filed with the Securities and Exchange Commissions, including our Annual Report on Form 10-K for the year ended December 31, 2023. New risk factors emerge over time and it is not possible to predict all such risk factors, or to assess the impact such risk factors have on the business. We undertake no obligation to update publicly any forward-looking statements whether as a result of new information, future events or otherwise, except as required by law.

Overview

4Front Ventures Corp. ("4Front", the "Company", "we" or "our") has two primary operating segments: THC Cannabis and CBD Wellness. With regard to its THC Cannabis segment, the Company operates five dispensaries and four production and cultivation facilities in Massachusetts and Illinois as of March 31, 2024. The Company's five "MISSION" branded dispensaries are located in: Brookline, MA; Georgetown, MA; Worcester, MA; South Shore (Chicago), IL; and Calumet City, IL. The Company's four cultivation and production assets are detailed in our Annual Report on Form 10-K for the year ended December 31, 2023.

4Front’s operations are strategically situated in key geographic locations across its major markets to allow the Company to efficiently scale its operations, and competitively position it to take advantage of future growth opportunities as cannabis legalization efforts continue across the U.S. Management intends to continue scaling its operations in Illinois and Massachusetts to further increase its market share. The Company has made significant investments in manufacturing and production facilities in each of these markets. The Company remains focused on scaling and driving operational effectiveness throughout its portfolio, in addition to developing trusted brands and products to continue to grow revenue, build customer loyalty, and increase market share.

As part of its THC Cannabis segment, the Company also eases real estate, sells equipment and supplies, and licenses intellectual property to cannabis producers in the state of Washington.

The Company’s CBD Wellness segment is focused upon its ownership and operation of its wholly owned subsidiary, Pure Ratios Holdings, Inc. (“Pure Ratios”), a CBD-focused wellness company that sells non-THC products throughout the United States.

While marijuana is legal under the laws of several U.S. states (with varying restrictions), the United States Federal Controlled Substances Act classifies all “marijuana” as a Schedule I drug, whether for medical or recreational use. Under U.S. federal law, a Schedule I drug or substance has a high potential for abuse, no accepted medical use in the United States, and a lack of safety for the use of the drug under medical supervision.

Recent Developments

Amendment of Senior Secured Debt

On January 29, 2024, the Company agreed with LI Lending, LLC to convert $23.0 million of the senior secured debt into 244,680,852 Class A Subordinate Voting Shares and issued LI Lending, LLC a warrant to purchase 36,702,127 shares of Class A Subordinate Voting Shares at a price of C$0.14. In addition, the Company issued LI Lending, LLC a restricted stock unit agreement providing that, in the event of a financing by the Company at less than C$0.125 per share of Class A Subordinate Voting Shares, LI Lending, LLC shall be entitled to receive a number of shares necessary to restore it to 18.43% of the voting interests of the Company. Refer to Note 9 of the financial statements for further information.

Critical Accounting Policies and use of Estimates

Our management’s discussion and analysis of our financial condition and results of operations is based on our financial statements, which we have prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”). Critical accounting policies and estimates are identified and discussed in our Annual Report on Form 10-K for the year ended December 31, 2023, as filed with the SEC on April 15, 2024. Although we believe our estimates and judgments are reasonable, they are based upon information available at the time the judgment or estimate is made. Actual results may differ significantly from estimates under different assumptions or conditions.

Results of Operations

Three Months Ended March 31, 2024 Compared With Three Months Ended March 31, 2023

The following table sets forth our results of operations for the three months ended March 31, 2024 and 2023:

	For the Three Months Ended March 31,		Change	
	2024	2023	$	%
Revenue from Sale of Goods	$ 16,933	$ 23,339	$ (6,406)	27 %
Real Estate Income	1,909	2,940	(1,031)	35 %
Total Revenues	18,842	26,279	(7,437)	28 %
Cost of Goods Sold	(11,268)	(12,713)	1,445	11 %
Gross Profit	7,574	13,566	(5,992)	44 %
Total Operating Expense	12,345	15,007	(2,662)	18 %
Income (Loss) from Continuing Operations	(4,771)	(1,441)	(3,330)	231 %
Total Other Expense, net	(13,577)	(3,303)	(10,274)	311 %
Net Income (Loss) from Continuing Operations Before Income Taxes	(18,348)	(4,744)	(13,604)	287 %
Income Tax Expense	—	(3,066)	3,066	100 %
Net Loss from Continuing Operations	**$ (18,348)**	**$ (7,810)**	**$ (10,538)**	**135 %**
Net Loss from Discontinued Operations, Net of Taxes	(105)	(3,582)	3,477	97 %
Net Loss	**$ (18,453)**	**$ (11,392)**	**$ (7,061)**	**62 %**

Revenue from Sale of Goods

Revenue from sale of goods related to continuing operations for the three months ended March 31, 2024 was $16.9 million, representing a decrease of $6.4 million or 27% when compared to the three months ended March 31, 2023. Refer to the segment discussion below for specific revenue drivers.

Real Estate Income

Real estate income from leasing cannabis production facilities for the three months ended March 31, 2024 was $1.9 million, versus $2.9 million recognized for the three months ended March 31, 2023. This decrease of $1.0 million was largely attributable to lower sales revenue from the Washington tenant.

Total revenue from continuing operations in the reportable segments from which we operate were as follows:

	For the Three Months Ended March 31,		Change	
	2024	2023	$	%
THC Cannabis	$ 18,657	$ 26,063	$ (7,406)	28%
CBD Wellness	185	216	(31)	15%
Total Net Revenues	**$ 18,842**	**$ 26,279**	**$ (7,437)**	**28%**

Net revenues for the THC cannabis segment were $18.7 million for the three months ended March 31, 2024, representing a decrease of $7.4 million or 28% when compared to the three months ended March 31, 2023. Net revenues decreased in Illinois by 12% and Massachusetts by 35%. The decrease was primarily attributed to price compression in Illinois, as well as lower volumes experienced in Massachusetts due to higher competition and lower than expected yields. Net revenues for the CBD wellness segment for the three months ended March 31, 2024 were relatively consistent with the prior year.

Cost of Goods Sold

Cost of goods sold for the three months ended March 31, 2024 was $11.3 million, resulting in a decrease of $1.4 million or 11% when compared to $12.7 million for the three months ended March 31, 2023. The decrease of 11% in cost of goods sold was not directly correlated with the 27% decrease in revenue from the sale of goods as the Company was not able to pass through increased operating costs, such as labor, utilities, and purchased material, due to strong price competition in its respective markets.

Gross Profit

Gross profit for the three months ended March 31, 2024, was $7.6 million or 40% of revenue, compared to $13.6 million or 52% of revenue for the three months ended March 31, 2023. The decrease in gross profit was primarily due to the decrease in revenue outpacing the decrease in cost of goods sold as described above.

Total Operating Expenses

Operating expenses consist of selling, general and administrative expenses and depreciation and amortization. Total operating expenses for the three months ended March 31, 2024 was $12.3 million, representing a decrease of $2.7 million or 18%, as compared to the three months ended March 31, 2023. This decrease was primarily attributable to a $2.5 million decrease in selling, general and administrative expenses. Specifically, the Company saw a decrease in rent and lease related expenses of $1.1 million, salaries and benefits of $1.0 million, and advertising and promotions of $0.3 million. Refer to Note 19 of the Consolidated Financial Statements includes further detail on selling, general and administrative expenses.

Total Other Expense, net

Other expense consists primarily of interest expense, change in fair value of derivative liability, gain/loss on extinguishment of debt, and other expenses. Total other expense for the three months ended March 31, 2024 was $13.6 million, compared to $3.3 million for the three months ended March 31, 2023. The increase of $10.3 million was primarily due to a loss on extinguishment of debt of $11.8 million from the conversion of $23.0 million of the senior secured debt into 244,680,852 Class A Subordinate Voting Shares. Interest expense decreased $0.7 million from prior year as a result of the debt amendments during the fiscal fourth quarter of 2023. In addition, the Company recognized a gain of $0.8 million in changes in fair value of derivative liability for the three months ended March 31, 2024, versus no such transactions in the prior year.

Net Loss

Net loss from continuing operations for the three months ended March 31, 2024 was $18.3 million, compared to $7.8 million for the three months ended March 31, 2023. The increase in net loss from continuing operations of $10.5 million for the three months ended March 31, 2024 was primarily attributable to the loss on extinguishment of debt resulting from the January 2024 amendment and conversion of the senior secured debt with LI Lending, LLC.

Non-GAAP Financial and Performance Measures

In addition to providing financial measurements based on GAAP, we provide additional financial metrics that are not prepared in accordance with GAAP. Management uses non-GAAP financial measures, in addition to GAAP financial measures, to understand and compare operating results across accounting periods, for financial and operational decision making, for planning and forecasting purposes and to evaluate the Company's financial performance. Management uses the non-GAAP measurement of adjusted EBITDA, which we believe reflects our ongoing business in a manner that allows for meaningful comparisons and analysis of trends in the business, as it facilitates comparing financial results across accounting periods. We also believe this non-GAAP financial measure enables investors to evaluate the Company's operating results and future prospects in the same manner as management. This non-GAAP financial measures may also exclude expenses and gains that may be unusual in nature, infrequent or not reflective of the Company's ongoing operating results. As there are no standardized methods of calculating non-GAAP measures, our methods may differ from those used by others, and accordingly, the use of these measures may not be directly comparable to similarly titled measures used by others. Accordingly, non-GAAP measures are intended to provide additional information and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with GAAP.

Adjusted EBITDA

Adjusted EBITDA is a financial measure that is not calculated in accordance with U.S. GAAP. Adjusted EBITDA is defined by the Company as detailed below. This measure provides investors with additional useful information to measure the Company's financial performance, particularly with respect to changes in performance from period to period. The Company's management uses Adjusted EBITDA (a) as a measure of operating performance, (b) for planning and forecasting in future periods, and (c) in communications with the Company's board of directors concerning the Company's financial performance.

The Company's presentation of Adjusted EBITDA are not necessarily comparable to other similarly titled captions of other companies due to different methods of calculation and should not be used by investors as a substitute or alternative to net income or any measure of financial performance calculated and presented in accordance with U.S. GAAP. Instead, management believes Adjusted EBITDA should be used to supplement the Company's financial measures derived in accordance with U.S. GAAP to provide a more complete understanding of the trends affecting the business.

Although Adjusted EBITDA is frequently used by investors and securities analysts in their evaluations of companies, Adjusted EBITDA has limitations as an analytical tool, and investors should not consider it in isolation or as a substitute for, or more meaningful than, amounts determined in accordance with U.S. GAAP. Some of the limitations to using non-GAAP measures as an analytical tool are (a) they do not reflect the Company's interest income and expense, or the requirements necessary to service interest or principal payments on the Company's debt, (b) they do not reflect future requirements for capital expenditures or contractual commitments, and (c) although depreciation and amortization charges are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and non-GAAP measures do not reflect any cash requirements for such replacements.

The prior year reconciliation of Net Loss to Adjusted EBITDA has been adjusted for consistency with current year presentation. These adjustments did not affect net loss, revenues and stockholders' equity.

The following table reconciles Net Loss to Adjusted EBITDA for the three months ended March 31, 2024 and 2023:

	For the Three Months Ended March 31,	
	2024	**2023**
Net loss (GAAP)	$ (18,453)	$ (11,392)
Less: Net loss from discontinued operations, net of taxes	105	3,582
Net loss from continuing operations	(18,348)	(7,810)
Adjusted for:		
Interest income	(5)	(14)
Interest expense (1)	6,745	7,361
Income tax expense	—	3,066
Depreciation and amortization (2)	2,082	2,276
EBITDA (Loss) Income from Continuing Operations (Non-GAAP)	**$ (9,526)**	**$ 4,879**
Share-based compensation (3)	1,008	1,020
Change in fair value of derivative liability	(763)	—
Loss on extinguishment of debt	11,752	—
Loss on disposal and lease termination	5	—
Adjusted EBITDA (Loss) Income from Continuing Operations (Non-GAAP)	**$ 2,476**	**$ 5,899**

(1) For the current period, interest expense includes interest related to leases of $4.3 million for the three months ended March 31, 2024. Prior year amounts of $4.2 million for the three months ended March 31, 2023 have been reclassified for consistency with the current year presentation. Non-cash interest expense related to leases was previously presented as a reconciling item from EBITDA from Continuing Operations (Non-GAAP) to Adjusted EBITDA from Continuing Operations (Non-GAAP).
(2) For the current period, depreciation and amortization expense includes amortization related to leases of $0.8 million for the three months ended March 31, 2024. Prior year amounts of $0.9 million for the three months ended March 31, 2023 have been reclassified for consistency with the current year presentation. Non-cash amortization expense related to leases was previously presented as a reconciling item from EBITDA from Continuing Operations (Non-GAAP) to Adjusted EBITDA from Continuing Operations (Non-GAAP).
(3) Although share-based compensation is an important component of employee and executive compensation, determining the fair value of share-based compensation involves a high degree of judgment and as a result the Company excludes share-based compensation from Adjusted EBITDA because its believes that the expense recorded may bear little resemblance to the actual value realized upon future exercise or termination of any related share-based compensation award.

Adjusted EBITDA should not be considered in isolation from, or as a substitute for, Net Loss. There are a number of limitations related to the use of Adjusted EBITDA as compared to Net Loss, the closest comparable GAAP measure. Adjusted EBITDA, as defined by the Company, excludes from Net Loss:

- Interest income and expense, including interest expense related to leases;
- Current income tax expense;
- Non-cash depreciation and amortization expense, including amortization of leases;
- Non-cash share-based compensation expense;
- Non-cash changes in fair value of derivative liability;
- Loss on extinguishment of debt; and
- Loss on disposal of assets and lease terminations.

Liquidity and Capital Resources

As of March 31, 2024 and December 31, 2023, we had total current liabilities of $109.2 million and $104.0 million, respectively, and current assets of $32.9 million and $33.9 million, respectively, to meet our current obligations. As of March 31, 2024 and December 31, 2023, we had a working capital deficit of $76.3 million compared to $70.1 million. The decline in working capital of $6.2 million was primarily driven by a decrease in cash of $0.5 million as the Company executes its retail expansion strategy and completes the build-out of the cultivation and production facility in Matteson, Illinois, which was completed in February 2024. This was coupled with an increase in accounts payable of $2.5 million.

The Company is an early-stage growth company. It is generating cash from sales and is deploying its capital reserves to acquire and develop assets capable of producing additional revenues and earnings over both the immediate and near term. Capital reserves are being utilized for capital expenditures and improvements in existing facilities, product development and marketing, as well as customer, supplier and investor and industry relations. Historically, the Company has raised capital as needed however there is no guarantee the Company will be able to continue to raise funds in the same manner it has historically.

Cash Flows

Cash Flows from discontinued operations are separately presented on the statement of cash flow for each operating, investing, and financing section of the statement. For liquidity purposes, the focus of this section is on the cash flow from continuing operations which is expected to affect future liquidity and capital resources.

Net Cash Provided by Continuing Operating Activities

Net cash provided by continuing operating activities was $2.5 million for the three months ended March 31, 2024, an decrease of $6.1 million as compared to net cash used in continuing operating activities of $3.6 million for the three months ended March 31, 2023. The decrease was primarily attributable to the increase in accounts payable, coupled with the decrease in selling, general and administrative expenses and interest expense. These positive changes were the result of management's decisive action to reduce its cash burn.

Net Cash Used in Continuing Investing Activities

Net cash used in continuing investing activities was $1.8 million for the three months ended March 31, 2024, an increase of $1.3 million as compared to $0.4 million for the three months ended March 31, 2023. The increase was primarily attributable to an increase in purchases of property and equipment related to the completion of the Matteson facility during the fiscal first quarter of 2024 and the construction of the Norridge dispensary.

Net Cash Used in Continuing Financing Activities

Net cash used in continuing financing activities was $1.0 million for three months ended March 31, 2024, a decrease of $2.2 million as compared to $3.3 million for the three months ended March 31, 2023. The decrease was due to a decrease in repayments of notes payable resulting from amendments to its debt agreements during the fiscal fourth quarter of 2023 and the current period.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies

We review new accounting standards as issued. Although some of these accounting standards issued or effective after the end of our previous fiscal year may be applicable to the Company, we have not identified any standards that we believe merit further discussion. We do not expect the adoption of any recently issued accounting pronouncements to have a significant impact on our financial position, results of operations, or cash flows.