Trickle Research

Every raging river, every great lake, every deep blue sea starts … with a trickle

2Q-F21 Earnings Update

VEXT SCIENCE

Vext Science, Inc.

(symbol: VEXTF)

(http://www.vapenmj.com/)

Report Date: 09/02/21

12- 24 month Price Target: $1.60

Allocation: 6

Closing Stock Price at Initiation (Closing Px: 01/30/20): $.55

Closing Stock Price at Allocation Upgrade (Closing Px: 06/02/20): $.33

Closing Stock Price at Allocation Upgrade (Closing Px: 07/13/21): $.67

Closing Stock Price at This Update (Closing Px: 09/01/21): $.62

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Disclosure: Portions of this report are excerpted from Vext's filings, website(s), presentations or other public collateral. We have attempted to identify those excerpts by *italicizing* them in the text. Unless otherwise noted, all prices in this report are in US Dollars.

For 2Q-F21, VEXT reported revenues of $9.376 million versus our estimate of $8.31 million and they reported net income of $1.875 million versus our estimate of $1.809 million. In short, the Company posted a strong quarter, which outperformed our estimates. Recall, much of our challenge from a research perspective has been trying to model the Company's results in the context of the unusual relationship the Company has with its two major customers, both of which are not-for-profit entities. We will briefly recap.

Recall Arizona cannabis laws require that operators/licensees be not-for-profit entities. As a result, while VEXT essentially manages the entire "seed-to-sale" operations of its two not-for-profit customers, it does not technically own those operations. As a result, it must essentially find creative ways to bill its "customers" for the management of those cannabis assets. As we have argued, that process is difficult to model and lacks the sort of visibility and transparency that public markets rely on. To be quite honest, given those challenges, were it not for what we think is a compelling combination of assets *and management*, we would not be covering VEXT. By extension, we understand why the street has perhaps had a difficult time embracing the story as well. That said, as we alluded to in prior research, the passage of recreational use in Arizona includes the repeal of requirements that licensees be not-for-profit entities. Among other things, that change opens the door for VEXT to officially own what today are its "customers" and our understanding is that they will be able to begin reflecting that ownership in Q1-F22. We believe that visibility and transparency will be a positive catalyst.

In addition to change in the not-for-profit posture of the assets, we think the Arizona recreational laws will provide a boost for incumbent players like VEXT that is clearly not reflected in the valuation today. Moreover, we also are beginning to think that changes in the Federal cannabis landscape could provide positive catalysts for incumbent cannabis players as well. For instance, we have heard a number of market watchers suggest that a change in federal posture on cannabis that would even just relax banking laws and perhaps decriminalize cannabis, would bring a considerable amount of institutional investment into the space that by charter cannot participate as long as federal prohibitions remain. We think federal legislation of some sort is becoming more likely and again, we think that could be positive for valuations in the domestic space.

More specifically, along with what we believe will be better transparency as a result of VEXT's new "ownership" of the assets they currently manage, as they discussed on the call, fiscal 2022 should include some new initiatives that we think will impact their comparative results. First, as the Company has discussed along the way, and specifically noted on the call,

> *"We're on track to almost triple our indoor cultivation capacity during the first half of twenty twenty two to approximately fifty eight thousand square feet under canopy from our current twenty thousand feet. In a growing limited license state, cultivation and manufacturing leadership are important strategic advantages that help drive margin expansion and retail support growth and wholly-owned brands and open up additional opportunities to manufacture for others or sell high quality flower to other players in the market without capacity".*

In our view, the added cultivation space is a milestone for the Company. Recall, VEXT, through its licensee customers, has had to periodically purchase flower in the open market, so we think the added cultivation provides them flexibility/control in their seed-to-sale approach. Moreover, as they allude to above, the addition of recreational use in a limited cultivation license environment, may speak to better margins for "high quality" (indoor cultivation) product. While we will have to continue to *muddle through the modeling* until the non-profit yoke is removed at the end of 2021, we would reiterate, in our view, the added cultivation should prove considerably additive from a handful of perspectives.

Second, as the Company has also reported on in the past and elaborated on in the call, they are adding two new THC based beverage lines to their product offering in Arizona. Here are a few particulars on each:

1) **Wynk THC Seltzers** - Each 8.4 oz. can of Wynk is a microdose of 2.5mg of both THC and CBD per can. We believe it currently comes in three fruit flavors. Wynk is presumably positioned as a seltzer

alternative to (perhaps) alcohol based seltzers. Notice, they contain a relatively low dose of THC (2.5 mg), which is a similar amount that one might find in a low dose edible. As such, again like an alcohol seltzer, as a result of the lower dose, consumers may drink multiple units over the course of an afternoon/evening. We would add, we believe Wynk was launched in Ohio, and if we understand it correctly, it is the only market with any measurable penetration. Again, as we understand it, Wynk is positioning to provide portable manufacturing/canning capabilities that they will license to operators in various jurisdictions.

2) **SoRSE Technology/MAJOR THC beverage brand -** Alternatively, the Company's agreement with SoRSE Technology, which owns and sells the MAJOR THC beverage brand, involves a different type of beverage. MAJOR is designed as a high dose cannabis beverage that is sold in a 200ml (6.7 oz.) serving size, *with 100mg of THC,* but with *"no cannabis taste or smell".* To edify, that is a smaller serving size than the Wynk product above, but it contains *50X more* THC than the Wynk product. Clearly, MAJOR is aimed at a different cannabis consumer (think: energy shot) than Wynk. We would add, with respect to the original announcement, the Company also noted, *"Vext may also choose to manufacture SōRSE's other existing formulations and/or use SōRSE emulsions to develop additional products under the Vapen brand, for which it will pay SōRSE a royalty".* Clearly that leaves open the possibility of VEXT leveraging SoRSE's technology to provide a VEXT (Vapen) branded beverage.

To summarize, as we see it the beverage initiatives provide two benefits to VEXT. The most obvious is that they will have two new products to sell that should prove collectively additive to VEXT's results. While it is too early to tell just how additive those lines will prove to be, we think they will be meaningful. Second, as the Company alluded to, the additional of these lines enhances the Company's overall product lineup to its retail/dispensary customers. The Company believes (and we tend to agree) that many dispensaries may be looking to reduce the number of vendors they deal with, which suggests they are looking for vendors with more extensive product lines.

The third major initiative the Company addressed on the call was their expansion into Ohio. The Company noted that they view Ohio as similar to Arizona on a variety of fronts. Here is a bit of that narrative from the call:

> *"Currently, Vapen is being stocked in most dispensarys', shelves and Ohio is selling well and we continue to expand the product offerings. On March fifteen, we announced that we have signed an LOI that will enable facts to establish a retail presence in the state through a joint venture with an Ohio LLC. And on July twenty seventh, we announced that the current license holder had received a certificate operation by the Ohio Board of Pharmacy and was fully operational".*

The Company further noted:

> *Once the license holder has been operational for twelve months, Vext and its joint venture partner may apply to the Board for a change in ownership of the provisional license.*

Succinctly, that 12 month clock started ticking on July 27, 2021, which means that 12 months or so from now VEXT may operate and own cannabis assets in Ohio. Ostensibly, given the Company's constructive views of the Ohio market, that event will be another milestone for the Company. That said, at this point, the Company is unable to provide any guidance with respect to how the interim 12 month period of operations in Ohio will be reflected at VEXT. We will revisit that when we get some clarity.

To recap, we thought the Company posted a highly positive 2Q-F21 quarter, which exceeded our expectations, and perhaps more importantly provided some clarity on new initiatives that we think will help drive positive fiscal 2022 comps. We admit, while we feel like we are getting a bit better at projecting at least the aggregate results of the revenue "levers", that endeavor remains difficult, so for the balance of 2021 we will have to continue to "muddle through" that analysis. The good news is, they expect to own these assets and begin reporting as such, beginning in calendar 2022. We believe that issue alone will provide better visibility and perhaps a catalyst for higher VEXT share prices.

Finally, on the back of the napkin, the Company reported adjusted EBITDA of $3.4 million. If we annualize that, it comes to $13.6 million, which means the stock is currently trading at about 3.2X EBITDA. Further, if we annualize the first half revenues (we think the second half will be higher) the result is about $37 million, which means VEXT is trading at about 1.2X Sales. To be clear, the metrics of public cannabis stocks are a mixed bag, with many of the larger players garnering higher valuation metrics than their smaller counterparts. In that regard, we think VEXT's relative valuation (based on the Px/EBITDA and the PX/Sales metrics delineated above) is amongst some of the most modest cannabis valuations we can identify. To translate, as cannabis stocks go, we think VEXT is undervalued. That said, we submit, for a handful or reasons as generalists we are not prone to using comparative industry analysis to derive our price targets or allocation decisions. Rather, we typically attempt to identify what we believe are reasonable measures of intrinsic value based on our risk adjusted DCF/NPV models. From that approach we also continue to view VEXT as considerably undervalued. That being the case, we reiterate our 12-24 month price target of $1.60 and our allocation of 6.

Projected Operating Model

Vext Science, Inc.					
Projected Operating Model					
By: Trickle Research LLC					
	(actual)	(actual)	(estimate)	(estimate)	(estimate)
	3/31/2021	**6/30/2021**	**9/30/2021**	**12/31/2021**	**Fiscal 2021**
REVENUES					
Management Fees	$ 1,800,000	$ 2,100,000	$ 2,100,000	$ 2,100,000	$ 8,100,000
Professional Fees	$ 3,122,053	$ 2,649,714	$ 3,020,980	$ 3,206,623	$ 11,999,370
Product Sales	$ 3,641,085	$ 3,254,852	$ 3,234,546	$ 3,664,789	$ 13,795,272
Equipment Leasing	$ 554,907	$ 1,260,425	$ 1,156,767	$ 750,789	$ 3,722,888
Property Leasing	$ 42,246	$ 110,783	$ 110,783	$ 100,000	$ 363,812
Total Revenues	**$ 9,160,291**	**$ 9,375,774**	**$ 9,623,076**	**$ 9,822,201**	**$ 37,981,342**
COST OF SALES					
Cost of Goods	$ 2,472,081	$ 2,216,540	$ 2,202,726	$ 2,495,721	$ 9,387,068
Salaries Wages and Contractors	$ 2,064,835	$ 2,447,776	$ 2,198,677	$ 2,226,269	$ 8,937,558
Property & Equipment Leasing, Utilities and Property Tax	$ 19,655	$ 15,210	$ 36,657	$ 36,657	$ 108,179
Amortization	$ 443,833	$ 479,033	$ 437,496	$ 437,496	$ 1,797,858
Total Cost of Goods Sold	**$ 5,000,404**	**$ 5,158,559**	**$ 4,875,556**	**$ 5,196,144**	**$ 20,230,664**
Gross Profit	**$ 4,159,886**	**$ 4,217,215**	**$ 4,747,520**	**$ 4,626,057**	**$ 17,750,678**
OPERATING EXPENSES					
Advertising & Promotion	$ 134,513	$ 137,741	$ 133,726	$ 149,828	$ 555,807
Amortization & Accretion	$ 332,960	$ 473,912	$ 375,759	$ 375,759	$ 1,558,390
Bank Charges and Interest	$ 158,840	$ 171,277	$ 166,173	$ 168,324	$ 664,614
Consulting	$ 139,743	$ 219,638	$ 140,863	$ 141,427	$ 641,671
Insurance	$ 42,208	$ 56,628	$ 43,235	$ 43,665	$ 185,735
Office and General	$ 355,872	$ 252,262	$ 330,864	$ 341,620	$ 1,280,617
Professional Fees	$ 325,025	$ 151,846	$ 299,691	$ 283,296	$ 1,059,858
Rent, Property Tax and Utilities	$ 53,847	$ 13,312	$ 39,407	$ 41,989	$ 148,555
Repairs and Maintenance	$ 113,231	$ 35,089	$ 114,987	$ 122,301	$ 385,609
Research and Development	$ 42,883	$ 37,036	$ 29,197	$ 36,866	$ 145,982
Shared Based Compensation	$ 424,953	$ 220,410	$ 140,637	$ 144,346	$ 930,346
Salaries, Wages and Commissions	$ 294,596	$ 273,482	$ 364,382	$ 381,592	$ 1,314,051
Travel, Entertainment & Training	$ 55,709	$ 42,992	$ 79,845	$ 84,148	$ 262,694
Total SG&A	**$ 2,474,380**	**$ 2,085,625**	**$ 2,258,765**	**$ 2,315,159**	**$ 9,133,929**
Operating Income (Loss)	**$ 1,685,506**	**$ 2,131,590**	**$ 2,488,755**	**$ 2,310,898**	**$ 8,616,748**
Loss on Acquisition/disposal					
Interest Income (Expense)	$ 160,767	$ 196,983	$ (57,000)	$ (62,000)	$ 238,750
Contribution from Joint Ventures	$ -	$ (102,938)	$ (74,218)	$ (116,540)	$ (293,696)
Investment Income	$ (303,157)	$ -	$ 38,936	$ 17,684	$ (246,538)
Other					$ -
Income Before Tax	**$ 1,537,976**	**$ 2,308,501**	**$ 2,396,472**	**$ 2,150,041**	**$ 8,392,991**
Income Tax	**$ 398,900**	**$ 433,636**	**$ 599,118**	**$ 537,510**	**$ 1,969,164**
Net Income - After Tax	**$ 1,139,076**	**$ 1,874,865**	**$ 1,797,354**	**$ 1,612,531**	**$ 6,423,826**
					$ -
Other Comprehensive Income (Loss)	**$ 265,803**	**$ -**	**$ -**	**$ -**	**$ 265,803**
Less: Non-Controling Interests	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**
Total Comprehensive Income (Loss)	**$ 1,404,879**	**$ 1,874,865**	**$ 1,797,354**	**$ 1,612,531**	**$ 6,689,629**
Basic Earnings per Share	**$ 0.01**	**$ 0.01**	**$ 0.01**	**$ 0.01**	**$ 0.05**
Weighted Average Earnings per Share	**$ 0.01**	**$ 0.01**	**$ 0.01**	**$ 0.01**	**$ 0.05**
Basic Shares Outstanding	**99,951,301**	**136,712,134**	**136,932,568**	**137,138,247**	**127,683,562**
Weighted Average Shares Outstanding	**99,951,301**	**148,436,272**	**150,681,784**	**152,728,444**	**137,949,450**

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Portions of this publication excerpted from company filings or other sources are noted in *italics* and referenced throughout the report.

Rating System Overview:

There are no letters in the rating system (Buy, Sell Hold), only numbers. The numbers range from 1 to 10, with 1 representing 1 "investment unit" (for my performance purposes, 1 "investment unit" equals $250) and 10 representing 10 investment units or $2,500. Obviously, a rating of 10 would suggest that I favor the stock (at respective/current levels) more than a stock with a rating of 1. As a guideline, here is a suggestion on how to use the allocation system.

Our belief at Trickle is that the best way to participate in the micro-cap/small cap space is by employing a diversified strategy. In simple terms, that means you are generally best off owning a number of issues rather than just two or three. To that point, our goal is to have at least 20 companies under coverage at any point in time, so let's use that as a guideline. Hypothetically, if you think you would like to commit $25,000 to buying micro-cap stocks, that would assume an investment of $1000 per stock (using the diversification approach we just mentioned, and the 20-stock coverage list we suggested and leaving some room to add to positions around allocation upgrades. We generally start initial coverage stocks with an allocation of 4. Thus, at $1000 invested per stock and a typical starting allocation of 4, your "investment unit" would be the same $250 we used in the example above. Thus, if we initiate a stock at a 4, you might consider putting $1000 into the position ($250 * 4). If we later raise the allocation to 6, you might consider adding two additional units or $500 to the position. If we then reduce the allocation from 6 to 4 you might consider selling whatever number of shares you purchased with 2 of the original 4 investment units. Again, this is just a suggestion as to how you might be able to use the allocation system to manage your portfolio.

For those attached to more traditional rating systems (Buy, Sell, Hold) we would submit the following guidelines.

A Trickle rating of 1 thru 3 would best correspond to a "Speculative Buy" although we would caution that a rating in that range should not assume that the stock is necessarily riskier than a stock with a higher rating. It may carry a lower rating because the stock is trading closer to a price target we are unwilling to raise at that point. This by the way applies to all of our ratings.

A Trickle rating of 4 thru 6 might best (although not perfectly) correspond to a standard "Buy" rating.

A Trickle rating of 7 thru 10 would best correspond to a "Strong Buy" however, ratings at the higher end of that range would indicate something that we deem as quite extraordinary..... an "Extreme Buy" if you will. You will not see a lot of these.