UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2023

OR

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For transition period from to

Commission File Number: 001-39773

Hydrofarm Holdings Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**81-4895761**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

1510 Main Street
Shoemakersville, Pennsylvania 19555
(707) 765-9990
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol	Name of each exchange on which registered
Common Stock, $0.0001 par value per share	**HYFM**	**Nasdaq Global Select Market**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the Registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Smaller reporting company	☒
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes ☐ No ☒

As of July 31, 2023, the registrant had 45,546,289 shares of common stock, $0.0001 par value per share, outstanding.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained in this Quarterly Report on Form 10-Q other than statements of historical fact, including statements concerning our business strategy and plans, future operating results and financial position, as well as our objectives and expectations for our future operations, are forward-looking statements.

In some cases, you can identify forward-looking statements by such terminology as “believe,” “may,” “will,” “potentially,” “estimate,” “continue,” “anticipate,” “intend,” “could,” “would,” “project,” “plan,” “expect” and similar expressions that convey uncertainty of future events or outcomes, although not all forward-looking statements contain these words. Forward-looking statements include, but are not limited to, statements about:

- industry conditions, including oversupply and decreasing prices of our customers' products which, in turn, has materially adversely impacted our sales and other results of operations and which may continue to do so in the future;
- the potential for future charges associated with the impairment of our long-lived assets, inventory allowances and purchase commitment losses, and accounts receivable reserves;
- our liquidity;
- our ability to meet the continued listing standards of Nasdaq;
- our restructuring activities may increase our expenses and cash expenditures, and may not have the intended cost saving effects;
- potential dilution that may result from equity financings while our stock prices are depressed;
- general economic and financial conditions, specifically in the United States and Canada;
- the conditions impacting our customers, including related crop prices and other factors impacting growers;
- the adverse effects of public health epidemics, including the COVID-19 pandemic, on our business, results of operations and financial condition;
- interruptions in our supply chain;
- federal and state legislation and regulations pertaining to the use and cultivation of cannabis in the United States and Canada;
- public perceptions and acceptance of cannabis use;
- fluctuations in the price of various crops and other factors affecting growers;
- the results of our acquisitions and strategic alliances;
- our long-term non-cancellable leases under which many of our facilities operate, and our ability to renew or terminate our leases;
- our reliance on, and relationships with, a limited base of key suppliers for certain products;
- our ability to keep pace with technological advances;
- our ability to execute our e-commerce business;
- the costs of being a public company;
- our ability to successfully identify appropriate acquisition targets, successfully acquire identified targets or successfully integrate the business of acquired companies;
- the success of our marketing activities;
- a disruption or breach of our information technology systems or cyber-attack;
- our current level of indebtedness;
- our dependence on third parties;
- any change to our reputation or to the reputation of our products;
- the performance of third parties on which we depend;

- the fluctuation in the prices of the products we distribute;
- competitive industry pressures;
- the consolidation of our industry;
- compliance with environmental, health and safety laws;
- our ability to protect and defend against litigation, including claims related to intellectual property and proprietary rights;
- product shortages and relationships with key suppliers;
- our ability to attract and retain key employees;
- the volatility of the price of our common stock;
- the marketability of our common stock; and
- other risks and uncertainties, including those listed in “Risk Factors.”

We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our business, financial condition, results of operations, prospects, and financial needs. These forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q and are subject to a number of risks, uncertainties and assumptions described in the section titled “Risk Factors” and elsewhere in this Quarterly Report on Form 10-Q. Because forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified, you should not rely on these forward-looking statements as predictions of future events. The events and circumstances reflected in our forward-looking statements may not be achieved or occur and actual results could differ materially from those projected in the forward-looking statements. We disclaim any intention or obligation to publicly update or revise any forward-looking statements for any reason or to conform such statements to actual results or revised expectations, except as required by law.

“Hydrofarm” and other trade names and trademarks of ours appearing in this Quarterly Report on Form 10-Q are our property. This Quarterly Report on Form 10-Q contains trade names and trademarks of other companies, which are the property of their respective owners. We do not intend our use or display of other companies’ trade names or trademarks to imply an endorsement or sponsorship of us by such companies, or any relationship with any of these companies.

Unless the context otherwise indicates, references in this Quarterly Report on Form 10-Q to the terms “Hydrofarm”, “the Company,” “we,” “our” and “us” refer to Hydrofarm Holdings Group, Inc. and its subsidiaries.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(In thousands, except share and per share amounts)

	June 30, 2023	December 31, 2022
Assets		
Current assets:		
Cash and cash equivalents	$ 26,682	$ 21,291
Accounts receivable, net	18,209	17,227
Inventories	95,120	111,398
Prepaid expenses and other current assets	5,952	5,032
Total current assets	145,963	154,948
Property, plant and equipment, net	50,403	51,135
Operating lease right-of-use assets	59,407	65,265
Intangible assets, net	288,606	300,366
Other assets	1,852	1,845
Total assets	$ 546,231	$ 573,559
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$ 12,394	$ 13,633
Accrued expenses and other current liabilities	9,546	13,208
Deferred revenue	2,370	3,654
Current portion of operating lease liabilities	8,888	9,099
Current portion of finance lease liabilities	993	704
Current portion of long-term debt	1,450	1,307
Total current liabilities	35,641	41,605
Long-term operating lease liabilities	52,321	56,299
Long-term finance lease liabilities	9,193	1,200
Long-term debt	117,266	117,461
Deferred tax liabilities	2,686	2,685
Other long-term liabilities	4,566	4,428
Total liabilities	221,673	223,678
Commitments and contingencies (Note 13)		
Stockholders' equity		
Common stock ($0.0001 par value; 300,000,000 shares authorized; 45,540,217 and 45,197,249 shares issued and outstanding at June 30, 2023, and December 31, 2022, respectively)	5	5
Additional paid-in capital	785,893	783,042
Accumulated other comprehensive loss	(5,695)	(7,235)
Accumulated deficit	(455,645)	(425,931)
Total stockholders' equity	324,558	349,881
Total liabilities and stockholders' equity	$ 546,231	$ 573,559

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(In thousands, except share and per share amounts)

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Net sales	$ 63,051	$ 97,508	$ 125,229	$ 208,885
Cost of goods sold	48,578	90,169	99,375	184,940
Gross profit	14,473	7,339	25,854	23,945
Operating expenses:				
Selling, general and administrative	23,468	25,974	47,899	66,221
Impairments	—	189,572	—	192,328
Loss from operations	(8,995)	(208,207)	(22,045)	(234,604)
Interest expense	(3,768)	(2,424)	(7,460)	(4,790)
Other (expense) income, net	(420)	458	(380)	356
Loss before tax	(13,183)	(210,173)	(29,885)	(239,038)
Income tax benefit	318	6,861	171	12,430
Net loss	$ (12,865)	$ (203,312)	$ (29,714)	$ (226,608)
Net loss per share:				
Basic	$ (0.28)	$ (4.53)	$ (0.66)	$ (5.06)
Diluted	$ (0.28)	$ (4.53)	$ (0.66)	$ (5.06)
Weighted-average shares of common stock outstanding:				
Basic	45,412,627	44,910,193	45,338,636	44,814,881
Diluted	45,412,627	44,910,193	45,338,636	44,814,881

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS (UNAUDITED)

(In thousands)

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Net loss	**$ (12,865)**	**$ (203,312)**	**$ (29,714)**	**$ (226,608)**
Other comprehensive gain (loss):				
Foreign currency translation gain (loss)	**1,428**	**(4,355)**	**$ 1,540**	**$ (2,171)**
Total comprehensive loss	**$ (11,437)**	**$ (207,667)**	**$ (28,174)**	**$ (228,779)**

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

(In thousands, except for share amounts)

	Common Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount				
Balance, March 31, 2022	44,822,866	$ 4	$ 778,463	$ 802	$ (163,812)	$ 615,457
Common stock issued upon exercise of options	518	—	5	—	—	5
Issuance of common stock for vesting of stock awards	262,176	—	—	—	—	—
Shares repurchased for withholding tax on stock awards	(73,908)	—	(630)	—	—	(630)
Stock-based compensation expense	—	—	2,073	—	—	2,073
Net loss	—	—	—	—	(203,312)	(203,312)
Foreign currency translation loss	—	—	—	(4,355)	—	(4,355)
Balance, June 30, 2022	45,011,652	$ 4	$ 779,911	$ (3,553)	$ (367,124)	$ 409,238
Balance, March 31, 2023	45,362,276	$ 5	$ 784,101	$ (7,123)	$ (442,780)	$ 334,203
Issuance of common stock for vesting of stock awards	200,994	—	—	—	—	—
Shares repurchased for withholding tax on stock awards	(23,053)	—	(25)	—	—	(25)
Stock-based compensation expense	—	—	1,817	—	—	1,817
Net loss	—	—	—	—	(12,865)	(12,865)
Foreign currency translation gain	—	—	—	1,428	—	1,428
Balance, June 30, 2023	45,540,217	$ 5	$ 785,893	$ (5,695)	$ (455,645)	$ 324,558

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS’ EQUITY (UNAUDITED)

(In thousands, except for share amounts)

	Common Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholder Equity
	Shares	Amount				
Balance, January 1, 2022	44,618,357	$ 4	$ 777,074	$ (1,382)	$ (140,516)	$ 635,1
Common stock issued upon exercise of options	8,283	—	75	—	—	
Issuance of common stock for vesting of stock awards	540,178	—	—	—	—	
Shares repurchased for withholding tax on stock awards	(155,265)	—	(2,219)	—	—	(2,2
Issuance of common stock under cashless warrant exercise	99	—	—	—	—	
Stock-based compensation expense	—	—	4,981	—	—	4,9
Net loss	—	—	—	—	(226,608)	(226,6
Foreign currency translation loss	—	—	—	(2,171)	—	(2,1
Balance, June 30, 2022	45,011,652	$ 4	$ 779,911	$ (3,553)	$ (367,124)	$ 409,2
Balance, January 1, 2023	45,197,249	$ 5	$ 783,042	$ (7,235)	$ (425,931)	$ 349,8
Issuance of common stock for vesting of stock awards	438,327	—	—	—	—	
Shares repurchased for withholding tax on stock awards	(95,359)	—	(148)	—	—	(1
Stock-based compensation expense	—	—	2,999	—	—	2,9
Net loss	—	—	—	—	(29,714)	(29,7
Foreign currency translation gain	—	—	—	1,540	—	1,5
Balance, June 30, 2023	45,540,217	$ 5	$ 785,893	$ (5,695)	$ (455,645)	$ 324,5

The accompanying notes are an integral part of the condensed consolidated financial statements

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)
(Page 1 of 2)

	Six months ended June 30,	
	2023	2022
Operating activities		
Net loss	$ (29,714)	$ (226,608)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation, depletion and amortization	16,257	24,776
Provision for doubtful accounts	9	81
Provision for inventory obsolescence	964	13,443
Restructuring expenses	744	—
Stock-based compensation expense	2,999	4,981
Non-cash operating lease expense	5,407	4,804
Impairment charges	—	192,328
Change in fair value of contingent consideration	—	(1,560)
Deferred income tax benefit	—	(12,430)
Other	744	294
Changes in assets and liabilities:		
Accounts receivable	(897)	6,182
Inventories	15,437	21,301
Prepaid expenses and other current assets	(406)	(814)
Other assets	(188)	(118)
Accounts payable	(1,209)	(2,893)
Accrued expenses and other current liabilities	(3,261)	(6,381)
Deferred revenue	(1,323)	(6,708)
Lease liabilities	(4,548)	(3,375)
Other long-term liabilities	(54)	(35)
Net cash from operating activities	961	7,268

Continued on next page

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)
(Page 2 of 2)

	Six months ended June 30,	
	2023	2022
Investing activities		
Business combinations, net of cash and cash equivalents	—	190
Capital expenditures of property, plant and equipment	(3,306)	(4,522)
Other	43	(411)
Net cash used in investing activities	(3,263)	(4,743)
Financing activities		
Proceeds from Sale-Leaseback Transaction	8,598	—
Borrowings under foreign revolving credit facilities	483	646
Repayments of foreign revolving credit facilities	(351)	(781)
Repayments of Term Loan	(625)	(625)
Payment of withholding tax related to stock awards	(148)	(2,105)
Other	(510)	(484)
Net cash from (used in) financing activities	7,447	(3,349)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	246	(115)
Net increase (decrease) in cash, cash equivalents and restricted cash	5,391	(939)
Cash, cash equivalents and restricted cash at beginning of period	21,291	28,384
Cash, cash equivalents and restricted cash at end of period	$ 26,682	$ 27,445
Non-cash investing and financing activities		
Right-of-use assets (relinquished) acquired under operating lease obligations	$ (748)	$ 10,991
Assets acquired under finance lease obligations	185	—
Supplemental information		
Cash paid for interest	6,884	4,165
Cash paid for income taxes	659	3,298

The accompanying notes are an integral part of the condensed consolidated financial statements.

Hydrofarm Holdings Group, Inc.
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(dollars in thousands, except share and per share amounts)

1. DESCRIPTION OF THE BUSINESS

Description of the business

Hydrofarm Holdings Group, Inc. (collectively with its subsidiaries, the “Company”) was formed in May 2017 under the laws of the state of Delaware to acquire and continue the business originally founded in 1977. The Company is a leading independent manufacturer and distributor of branded hydroponics equipment and supplies for controlled environment agriculture ("CEA"), including grow lights, climate control solutions, growing media and nutrients, as well as a broad portfolio of innovative and proprietary branded products. Products offered include agricultural lighting devices, indoor climate control equipment, nutrients, and plant additives used to grow, farm and cultivate cannabis, flowers, fruits, plants, vegetables, grains and herbs in controlled environment settings that allow end users to control key farming variables including temperature, humidity, CO_2, light intensity and color, nutrient concentration and pH.

2. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and the requirements of the U.S. Securities and Exchange Commission (“SEC”) for interim financial reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by U.S. GAAP can be condensed or omitted. These condensed consolidated financial statements have been prepared on the same basis as the Company's annual consolidated financial statements and, in the opinion of management, reflect all normal and recurring adjustments which are necessary for the fair statement of the Company’s financial information. The Company reclassified balances of $704 and $1,200 as of December 31, 2022, previously reported in "Current portion of long-term debt" and "Long-term debt", respectively, into "Current portion of finance lease liabilities" and "Long-term finance lease liabilities", respectively, on consolidated balance sheet as of December 31, 2022, to conform to the current period presentation. The Company made reclassifications to the condensed consolidated statement of cash flows for the prior period to conform with the current period presentation. These interim results are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2023, or for any other interim period or for any other future year. All intercompany balances and transactions have been eliminated in consolidation.

The condensed consolidated balance sheet as of December 31, 2022, has been derived from the audited consolidated financial statements of the Company, which is included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022 ("2022 Annual Report"). These condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and the notes thereto included in the 2022 Annual Report.

Use of estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Significant estimates include provisions for sales returns, rebates and claims from customers, realization of accounts receivable and inventories, fair value of assets acquired and liabilities assumed for business combinations, valuation of intangible assets, estimated useful lives of long-lived assets, incremental borrowing rate applied in lease accounting, valuation of stock-based compensation, recognition of deferred income taxes, recognition of liabilities related to commitments and contingencies and valuation allowances. Actual results may differ from these estimates. On an ongoing basis, the Company reviews its estimates to ensure that these estimates appropriately reflect changes in its business or new information available.

Business combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition date fair values of the assets transferred, liabilities incurred to the former owners of the acquiree, and the equity interests issued in exchange for control of the acquiree. Acquisition related costs are recognized in net loss as incurred.

When the consideration transferred in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition date fair value and included as part of the consideration transferred in a business combination. Contingent consideration is established for business acquisitions where the Company has the obligation to transfer additional assets or equity interests to the former owners if specified future events occur or conditions are met. Contingent consideration is classified as a liability when the obligation requires settlement in cash or other assets and is classified as equity when the obligation requires settlement in the Company's own equity instruments. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with a corresponding adjustment to goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the measurement period (which cannot exceed one year from the acquisition date) about facts and circumstances that existed at the acquisition date. All other subsequent changes in the fair value of contingent consideration classified as a liability are included in net loss in the period. Changes in the fair value of contingent consideration classified as equity are not recognized. During 2022, the Company settled contingent consideration for certain acquisitions that were completed in 2021. Refer to Note 14 – *Fair Value Measurements*, for further discussion of the contingent consideration.

For a given acquisition, the Company may identify certain pre-acquisition contingencies as of the acquisition date and may extend its review and evaluation of these pre-acquisition contingencies throughout the measurement period to obtain sufficient information to assess these contingencies as part of acquisition accounting, as applicable.

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer’s previously held equity interest in the acquiree (if any) over the net of the acquisition-date fair value amounts of the identifiable assets acquired, and the liabilities assumed.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Company reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period, or additional assets or liabilities are recognized, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognized at that time. Upon conclusion of the measurement period or final determination of the values of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to net loss.

During 2021, the Company completed five acquisitions of branded manufacturers of CEA products, resulting in a significant expansion of its portfolio of proprietary branded products and manufacturing capabilities. The 2021 acquisitions included (i) Heavy 16, a manufacturer of plant nutrients and additives, in May 2021; (ii) House & Garden, a manufacturer of plant nutrients and additives, in June 2021; (iii) Aurora Innovations, a manufacturer of soil, grow media, plant nutrients and additives, in July 2021; (iv) Greenstar Plant Products, a manufacturer of plant nutrients and additives, in August 2021; and (v) Innovative Growers Equipment, a manufacturer of horticultural benches, racks and grow lights, in November 2021. The Company finalized the determination of its allocation of the purchase price relating to the acquisitions during 2022.

During the first quarter of 2022, the Company evaluated and adjusted the useful lives of certain intangible assets associated with entities that were acquired during 2021. In addition, the Company determined that the preliminary allocation of assets acquired related to indefinite lived trade names have a finite useful life because the expected usefulness of the trade names is limited. As a result of these adjustments to the provisional amounts, the Company recorded $5,894 of additional amortization expense during the first quarter of 2022, which related to amortization expense that would have been recorded in the previous reporting period from the acquisition date through December 31, 2021. The intangible assets were assigned estimated useful lives as follows: (i) customer relationships: 7 to 12 years, (ii) technology, formulations and recipes: 8 to 12 years, (iii) computer software: 3 years, and (iv) trade names and trademarks: 15 to 20 years.

Restructuring

The Company began a restructuring plan during the three months ended December 31, 2022, and undertook significant actions to streamline operations, reduce costs and improve efficiencies. The major initiatives of the restructuring plan include (i) narrowing the Company's product and brand portfolio and (ii) the relocation and consolidation of certain manufacturing and distribution centers, including headcount reductions and reorganization to drive a solution based approach. The Company's strategic product consolidation entailed removing approximately one-third of all products and one-fifth of all brands relating to the Company's primary product portfolio, which excludes the garden center business in Canada.

During the three and six months ended June 30, 2023, the Company recorded pre-tax expense of $788 and $2,199, respectively, relating primarily to the relocation and termination of certain facilities in Canada. The Company incurred $417 and $744 of non-cash charges during the three and six months ended June 30, 2023, respectively, relating to asset dispositions and write-downs. The Company recorded $720 and $1,957 of restructuring related charges within Cost of goods sold on the consolidated statements of operations for the three and six months ended June 30, 2023, respectively. The Company recorded $68 and $242 within Selling, general and administrative ("SG&A") expenses on the consolidated statements of operations for the three and six months ended June 30, 2023, respectively. The following table presents the activity in accrued expenses and other current liabilities for restructuring costs for the three and six months ended June 30, 2023:

	Three Months Ended June 30, 2023
Restructuring Accruals as of April 1, 2023	**$ 624**
Expense	**371**
Cash Payments	**(502)**
Restructuring Accruals as of June 30, 2023	**$ 493**

	Six Months Ended June 30, 2023
Restructuring Accruals as of January 1, 2023	**$ 696**
Expense	**1,455**
Cash Payments	**(1,658)**
Restructuring Accruals as of June 30, 2023	**$ 493**

The Company expects to finalize the remaining actions associated with the previously disclosed restructuring plan in the second half of 2023. In addition, the Company may determine to implement a second phase of actions beginning in the second half of 2023. Refer to *Item 2. Management's Discussion And Analysis Of Financial Condition And Results of Operations – Market Conditions* for further explanation. The amounts the Company will ultimately realize or disburse could differ from these estimates. Total costs incurred since the restructuring plan commenced in the fourth quarter of 2022 are (i) $6,790 relating to inventory markdowns and (ii) $3,096 relating primarily to the relocation and termination of certain facilities in Canada.

Segment and entity-wide information

Segment information

The Company's chief operating decision maker is the chief executive officer ("CEO") who reviews financial information for the purposes of making operating decisions, assessing financial performance, and allocating resources. The business is organized as two operating segments, the United States and Canada, which meet the criteria for aggregation, and the Company has elected to present them as one reportable segment, which is the distribution and manufacture of CEA equipment and supplies. Aggregation is based on similarities which include the nature of its products, production or acquisition of inventory, customer base, fulfillment and distribution and economic characteristics.

Since the Company operates as one reportable segment, all required segment financial information is found in the condensed consolidated financial statements and footnotes with entity-wide disclosures presented below.

Hydrofarm Holdings Group, Inc.
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Entity-wide information

Sales to external customers and property, plant and equipment, net and operating lease right-of-use assets in the United States and Canada, determined by the location of the subsidiaries, are shown below. Other foreign locations, which are immaterial, individually and in the aggregate, are included in the United States below.

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
United States	$ 48,748	$ 79,236	$ 96,497	$ 172,094
Canada	14,565	19,337	29,584	40,839
Intersegment eliminations	(262)	(1,065)	(852)	(4,048)
Total consolidated net sales	$ 63,051	$ 97,508	$ 125,229	$ 208,885

	June 30, 2023	December 31, 2022
United States	$ 75,068	$ 80,380
Canada	34,742	36,020
Total property, plant and equipment, net and operating lease right-of-use assets	$ 109,810	$ 116,400

All of the products sold by the Company are similar and classified as CEA equipment and supplies.

Fair value measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company has applied the framework for measuring fair value which requires a fair value hierarchy to be applied to all fair value measurements. All financial instruments recognized at fair value are classified into one of three levels in the fair value hierarchy as follows:

Level 1 — Valuation based on quoted prices (unadjusted) observed in active markets for identical assets or liabilities.

Level 2 — Valuation techniques based on inputs that are quoted prices of similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not in active markets; inputs other than quoted prices used in a valuation model that are observable for that instrument; and inputs that are derived from or, corroborated by, observable market data by correlation or other means.

Level 3 — Valuation techniques with significant unobservable market inputs.

The Company measures certain non-financial assets and liabilities, including long-lived assets, intangible assets and goodwill, at fair value on a nonrecurring basis. The fair value of contingent consideration was classified within level 3 of the fair value hierarchy. Refer to Note 14 – *Fair Value Measurements*, for further discussion of the contingent consideration.

Inventories

Inventories consist of finished goods, work-in-process, and raw materials used in manufacturing products. Inventories are stated at the lower of cost or net realizable value, principally determined by the first in, first out method of accounting. The Company maintains an allowance for excess and obsolete inventory. The estimate for excess and obsolete inventory is based upon assumptions about current and anticipated demand, customer preferences, business strategies, and market conditions. Management reviews these assumptions periodically to determine if any adjustments are needed to the allowance for excess and obsolete inventory. The establishment of an allowance for excess and obsolete inventory establishes a new cost basis in the inventory. Such allowance is not reduced until the product is sold or otherwise disposed. If inventory is sold, any related reserves would be reversed in the period of sale. During the year ended December 31, 2022, and the three and six months ended June 30, 2023, the Company estimated inventory markdowns relating to restructuring charges based upon current and anticipated demand, customer preferences, business strategies, and market conditions including management's actions with respect to inventory products and brands being removed from the Company's portfolio. Hydrofarm's strategic product

consolidation entailed removing approximately one-third of all products and one-fifth of all brands relating to the Company's primary product portfolio.

Note receivable and Investment

In 2019, the Company executed a note receivable secured by equipment to a third-party, the terms of which were amended and restated during the first quarter of 2021. The note receivable provided for interest and installment payments to the Company, and full maturity of the note in 2024. During the first quarter of 2022, the third-party defaulted on interest payments, and the Company measured an impairment on the note receivable based on the estimated fair value of the collateral. The Company recorded impairment losses of zero and $2,636 during the three and six months ended June 30, 2022, respectively, in Impairments on the condensed consolidated statements of operations. As of December 31, 2022, the note receivable carrying value was $475 and it was classified in Other assets on the condensed consolidated balance sheet. During the first quarter of 2023, the Company agreed to forgive the note receivable in exchange for interest in a third-party equity investment. The investment is recorded at an estimated cost basis of approximately $530, inclusive of capitalized transaction costs, which is reported within Other assets on the condensed consolidated balance sheet.

Revenue recognition

The Company follows Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 606, *Revenue from Contracts with Customers* (“ASC 606”) which requires that revenue recognized from contracts with customers be disaggregated into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors. The Company has determined that revenue is generated from one category, which is the distribution and manufacture of CEA equipment and supplies.

Revenue is recognized as control of promised goods is transferred to customers, which generally occurs upon receipt at customers’ locations determined by the specific terms of the contract. Arrangements generally have a single performance obligation and revenue is reported net of variable consideration which includes applicable volume rebates, cash discounts and sales returns and allowances. Variable consideration is estimated and recorded at the time of sale.

The amount billed to customers for shipping and handling costs included in net sales was $2,718 and $5,286 during the three and six months ended June 30, 2023, respectively, and $3,679 and $7,558 during the three and six months ended June 30, 2022, respectively. Shipping and handling costs that occur before the customer obtains control of the goods are deemed to be fulfillment activities and are accounted for as fulfillment costs included in cost of goods sold. The Company does not receive noncash consideration for the sale of goods. Contract consideration received from a customer prior to revenue recognition is recorded as a contract liability and is recognized as revenue when the Company satisfies the related performance obligation under the terms of the contract. The Company's contract liabilities, which consist primarily of customer deposits reported within deferred revenue in the condensed consolidated balance sheets, totaled $2,370 and $3,654 as of June 30, 2023, and December 31, 2022, respectively. There are no significant financing components. Excluded from revenue are any taxes assessed by governmental authorities, including value-added and other sales-related taxes that are imposed on and concurrent with revenue-generating activities.

Income taxes

The income tax provision is calculated for an interim period by distinguishing between elements recognized in the income tax provision through applying an estimated annual effective tax rate to a measure of year-to-date operating results referred to as “ordinary income (or loss),” and discretely recognizing specific events referred to as “discrete items” as they occur. The income tax provision or benefit for each interim period is the difference between the year-to-date amount for the current period and the year-to-date amount for the prior period.

Recent accounting pronouncements

The Company considers the applicability and impact of all Accounting Standards Updates ("ASUs") issued by the FASB. There were no ASUs that were assessed and determined to be applicable or expected to have a material impact on the Company's condensed consolidated financial statements.

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3. GOODWILL AND INTANGIBLE ASSETS, NET

Goodwill

Primarily due to a sustained decline in the Company's market value of common stock and market conditions, the Company identified a triggering event requiring a test for impairment as of June 30, 2022. The Company completed its goodwill impairment testing and recorded an impairment charge of $189,572 as the test determined that the carrying value of the U.S. and Canada reporting units was in excess of the fair value. The recognized impairment reduced the goodwill balance to zero as of June 30, 2022. The impairment was primarily due to a deterioration in customer demand in the U.S. and Canada caused by macroeconomic and industry conditions.

The Company determined the fair value of the U.S. and Canada reporting units based on an income approach, using the present value of future discounted cash flows, and based on a market approach. The fair values were reconciled to the market value of common stock of Hydrofarm to corroborate the estimates used in the interim test for impairment. Significant estimates used to determine fair value include the weighted average cost of capital, financial forecasts, and pricing multiples derived from publicly-traded companies that are comparable to the reporting units. Refer to Note 14 – *Fair Value Measurements*, for further discussion of valuation inputs. The changes in goodwill are as follows:

	Goodwill
Balance at December 31, 2021	**$ 204,868**
Acquisition - Innovative Growers Equipment - measurement period adjustments	**(21,304)**
Acquisition - Greenstar Plant Products - measurement period adjustments	**7,000**
Acquisition - all others - remeasurement adjustments and foreign currency translation adjustments, net	**(992)**
Impairments	**(189,572)**
Balance at June 30, 2022	**$ —**

Intangible assets, net

Intangible assets, net comprised the following:

	June 30, 2023			December 31, 2022		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Finite-lived intangible assets:						
Computer software	$ 9,441	$ (8,194)	$ 1,247	$ 9,408	$ (7,976)	$ 1,432
Customer relationship	100,165	(28,248)	71,917	99,933	(24,533)	75,400
Technology, formulations and recipes	114,246	(20,249)	93,997	114,187	(15,344)	98,843
Trade names and trademarks	131,603	(13,415)	118,188	131,410	(10,052)	121,358
Other	4,806	(4,350)	456	4,778	(4,246)	532
Total finite-lived intangible assets, net	360,261	(74,456)	285,805	359,716	(62,151)	297,565
Indefinite-lived intangible asset:						
Trade name	2,801	—	2,801	2,801	—	2,801
Total Intangible assets, net	$ 363,062	$ (74,456)	$ 288,606	$ 362,517	$ (62,151)	$ 300,366

Amortization expense related to intangible assets was $6,047 and $12,092 for the three and six months ended June 30, 2023, respectively. Amortization expense related to intangible assets was $6,245 and $20,991 for the three and six months

ended June 30, 2022, respectively. The following are the estimated useful lives and the weighted-average amortization period remaining as of June 30, 2023, for the major classes of finite-lived intangible assets:

	Useful lives	Weighted-average amortization period remaining
Computer software	3 to 5 years	3 years
Customer relationships	7 to 18 years	10 years
Technology, formulations and recipes	8 to 12 years	10 years
Trade names and trademarks	15 to 20 years	18 years

The estimated aggregate future amortization expense for intangible assets subject to amortization as of June 30, 2023, is summarized below:

	Estimated Future Amortization Expense
For the period of July 1, 2023 to December 31, 2023	**$ 12,279**
Year ending December 31,	
2024	**24,466**
2025	**24,365**
2026	**24,151**
2027	**23,820**
Thereafter	**176,724**
Total	**$ 285,805**

4. EARNINGS (LOSS) PER COMMON SHARE (“EPS”)

Basic EPS is computed using net income (loss) divided by the weighted-average number of common shares outstanding during each period, excluding unvested restricted stock units (“RSUs”) and performance stock units ("PSUs").

Diluted EPS represents net income (loss) divided by the weighted-average number of common shares outstanding during the period, including common stock equivalents. Common stock equivalents consist of shares subject to warrants and share-based awards with exercise prices less than the average market price of the Company’s common stock for the period, to the extent their inclusion would be dilutive. Regarding RSUs subject to a market condition, before the end of the contingency period, the number of contingently issuable shares (i.e., RSUs) to be included in diluted EPS would be based on the number of shares of common stock issuable under the terms of the arrangement if the end of the reporting period was the end of the contingency period, assuming the result would be dilutive. Those contingently issuable shares would be included in the denominator of diluted EPS as of the beginning of the period, or as of the grant date of the share-based payment, if later.

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The following table presents basic and diluted EPS for the three and six months ended June 30, 2023 and 2022:

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Net loss	$ (12,865)	$ (203,312)	$ (29,714)	$ (226,608)
Weighted-average shares of common stock outstanding	45,412,627	44,910,193	45,338,636	44,814,881
Dilutive effect of warrants and share based compensation awards using the treasury stock method	—	—	—	—
Diluted weighted-average shares of common stock outstanding	45,412,627	44,910,193	45,338,636	44,814,881
Basic EPS	$ (0.28)	$ (4.53)	$ (0.66)	$ (5.06)
Diluted EPS	$ (0.28)	$ (4.53)	$ (0.66)	$ (5.06)

The computation of the weighted-average shares of common stock outstanding for diluted EPS excludes the following potential shares of common stock as their inclusion would have an anti-dilutive effect on diluted EPS:

	Three months ended June 30,		Six months ended June 30,	
	2023	2022	2023	2022
Shares subject to warrants outstanding	17,669	17,669	17,669	17,669
Shares subject to unvested performance and restricted stock units	2,369,483	1,071,053	2,369,483	1,071,053
Shares subject to stock options outstanding	648,518	695,769	648,518	695,769

5. ACCOUNTS RECEIVABLE, NET, AND INVENTORIES

Accounts receivable, net comprised the following:

	June 30, 2023	December 31, 2022
Trade accounts receivable	$ 19,173	$ 18,204
Allowance for doubtful accounts	(1,660)	(1,556)
Other receivables	696	579
Total accounts receivable, net	$ 18,209	$ 17,227

Inventories comprised the following:

	June 30, 2023	December 31, 2022
Finished goods	$ 66,844	$ 83,134
Work-in-process	4,314	5,403
Raw materials	34,434	38,558
Allowance for inventory obsolescence	(10,472)	(15,697)
Total inventories	$ 95,120	$ 111,398

Inventories are stated at the lower of cost or net realizable value, and the Company maintains an allowance for excess and obsolete inventory that is based upon assumptions about future demand and market conditions. The allowance for excess and obsolete inventory is subject to change from period to period based on a number of factors including sales of products, changes in estimates, and disposals.

6. LEASES

The Company leases its distribution centers and manufacturing facilities from third parties under various non-cancelable lease agreements expiring at various dates through 2038. Also, the Company leases some property, plant and equipment under finance leases. Certain leases contain escalation provisions and/or renewal options, giving the Company the right to extend the leases by up to 20 years. However, these options are generally not reflected in the calculation of the right-of-use assets and lease liabilities due to uncertainty surrounding the likelihood of renewal. The Company recognizes operating lease costs over the respective lease periods, including short-term and month-to-month leases. The Company incurred operating lease costs of $3,078 and $6,725 during the three and six months ended June 30, 2023, respectively, and $3,022 and $5,619 during the three and six months ended June 30, 2022, respectively. These costs are included primarily within SG&A in the condensed consolidated statements of operations.

The Company has operating subleases which have been accounted for by reference to the underlying asset subject to the lease, primarily as an offset to rent expense within SG&A. For the three and six months ended June 30, 2023, the Company recorded sublease income of $586 and $1,172, respectively. For the three and six months ended June 30, 2022, the Company recorded sublease income of $293 and $549, respectively.

In January 2023, Gotham Properties LLC, an Oregon limited liability company and a subsidiary of the Company ("Seller"), consummated a Purchase and Sale Agreement with J & D Property, LLC, a Nevada limited liability company ("Purchaser") pursuant to which certain real property located in the City of Eugene, County of Lane, State of Oregon (the "Eugene Property") was sold to Purchaser for $8,598 and then leased back by Seller (the "Sale-Leaseback Transaction"). The new lease has a term of 15 years with annual rent starting at $731 and fixed increases to the final year when annual rent is $964. The Company is accounting for the transaction as a failed sale-leaseback which requires retaining the asset associated with the property and recognizing a corresponding financial liability for the cash received. The Eugene Property serves as the manufacturing and processing site for certain of the Company's grow media and nutrient brands. The Company intends to reinvest the net cash proceeds into certain permitted investments, such as capital expenditures. The foregoing description of the reinvestment provisions does not purport to be complete and is qualified in its entirety by reference to the provisions of the Term Loan.

Total right-of-use ("ROU") assets and lease liabilities were as follows:

	Balance Sheet Classification	June 30, 2023	December 31, 2022
Lease assets			
Operating lease assets	Operating lease right-of-use assets	$ 59,407	$ 65,265
Finance lease assets	Property, plant and equipment, net	10,017	2,005
Total lease assets		$ 69,424	$ 67,270
Lease liabilities			
Current:			
Operating leases	Current portion of operating lease liabilities	$ 8,888	$ 9,099
Finance leases	Current portion of finance lease liabilities	993	704
Noncurrent:			
Operating leases	Long-term operating lease liabilities	52,321	56,299
Finance leases	Long-term finance lease liabilities	9,193	1,200
Total lease liabilities		$ 71,395	$ 67,302

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The aggregate future minimum lease payments under long-term non-cancelable operating and finance leases with remaining terms greater than one year as of June 30, 2023, are as follows:

	Operating	Finance
For the period of July 1, 2023 to December 31, 2023	$ 5,768	$ 757
Year ending December 31,		
2024	10,732	1,443
2025	10,658	1,305
2026	9,335	852
2027	8,995	855
2028	8,433	806
Thereafter	16,994	8,038
Total lease payments	70,915	14,056
Less portion representing interest	(9,706)	(3,870)
Total principal	61,209	10,186
Less current portion	(8,888)	(993)
Long-term portion	$ 52,321	$ 9,193

7. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment, net comprised the following:

	June 30, 2023	December 31, 2022
Machinery and equipment	28,363	27,832
Peat bogs and related development	11,791	10,761
Building and improvements	9,927	9,920
Land	6,205	6,107
Furniture and fixtures	3,970	3,921
Computer equipment	3,336	3,337
Leasehold improvements	5,045	4,177
Gross property, plant and equipment	68,637	66,055
Less: accumulated depreciation	(18,234)	(14,920)
Total property, plant and equipment, net	$ 50,403	$ 51,135

Depreciation, depletion and amortization expense related to property, plant and equipment, net was $2,203 and $4,165 for the three and six months ended June 30, 2023, respectively. Depreciation, depletion and amortization expense related to property, plant and equipment, net was $1,590 and $3,785 for the three and six months ended June 30, 2022, respectively.

As of June 30, 2023, Land, Building and improvements, Computer equipment and Machinery and equipment contain finance leases assets, recorded at cost of $12,931, less accumulated depreciation of $2,914. As of December 31, 2022, Computer equipment and Machinery and equipment contains finance leases assets, recorded at cost of $3,128, less accumulated depreciation of $1,123. The increase is in finance lease assets primarily relates to the Sale-Leaseback Transaction.

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8. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities comprised the following:

	June 30, 2023	December 31, 2022
Accrued compensation and benefits	$ 2,574	$ 2,522
Freight, custom and duty accrual	966	1,022
Goods in transit accrual	603	1,172
Income tax accrual	—	451
Other accrued liabilities	5,403	8,041
Total accrued expenses and other current liabilities	$ 9,546	$ 13,208

9. DEBT

Debt is comprised of the following:

	June 30, 2023	December 31, 2022
Term loan - net of unamortized discount and deferred financing costs of $4,704 and $5,142 as of June 30, 2023, and December 31, 2022, respectively	$ 118,421	$ 118,608
Other	295	160
Total debt	$ 118,716	$ 118,768
Current portion of long-term debt	$ 1,450	$ 1,307
Long-term debt - net of unamortized discount and deferred financing costs of $4,704 and $5,142 as of June 30, 2023, and December 31, 2022, respectively	117,266	117,461
Total debt	$ 118,716	$ 118,768

Term Loan

On October 25, 2021, the Company and certain of its direct and indirect subsidiaries (the "Obligors") entered into a Credit and Guaranty Agreement with JPMorgan Chase Bank, N.A., as administrative agent for the lenders, pursuant to which the Company borrowed a $125,000 senior secured term loan (“Term Loan”). The Term Loan was amended by Amendment No. 1 to Credit and Guaranty Agreement (“Amendment No. 1”) effective on June 27, 2023, to replace the LIBOR referenced rates with SOFR referenced rates. Pursuant to Amendment No. 1, any Term Loan that constitutes a Eurodollar Rate Loan that is outstanding as of the Amendment No. 1 closing date shall continue until the end of the applicable interest period for such Eurodollar Rate Loan and the provisions of the Term Loan applicable thereto shall continue and remain in effect (notwithstanding the occurrence of the Amendment No. 1 closing date) until the end of the applicable interest period for such Eurodollar Rate Loan, after which such provisions shall have no further force or effect. Such Eurodollar Rate Loan shall subsequently either be an ABR Loan or a Term Benchmark Loan. The ABR Loans shall bear interest at the Alternate Base Rate (with a 2.0% floor) plus 4.50%, and Term Benchmark Loans shall bear interest at the Adjusted Term SOFR Rate (with a 1.0% floor) plus 5.50%. The ABR Loan and Term Benchmark Loan credit spreads of 4.50% and 5.50%, respectively, within the Amendment No. 1 have not changed from the credit spreads in the original Term Loan. Legal fees associated with Amendment No. 1 were not material, and were included in Other (expense) income, net, on the Condensed Consolidated Statements of Operations during the three and six months ended June 30, 2023. The foregoing description of Amendment No. 1 does not purport to be complete and is qualified in its entirety by reference to the provisions of Amendment No. 1, a copy of which is filed as Exhibit 10.2 to this Form 10-Q and is incorporated herein by reference. Capitalized terms referenced above are defined in the Term Loan.

The Term Loan is subject to a call premium of 1% if called prior to October 25, 2023, and 0% thereafter, and matures on October 25, 2028 ("Maturity Date"). Deferred financing costs are being amortized to interest expense over the term of the loan. For the three months ended June 30, 2023, the effective interest rate was 11.47% and interest expense was $3,529, which

includes amortization of deferred financing costs and discount of $220. For the six months ended June 30, 2023, the effective interest rate was 11.22% and interest expense was $6,876, which includes amortization of deferred financing costs and discount of $438.

The principal amounts of the Term Loan are required to be repaid in consecutive quarterly installments in amounts equal to 0.25% of the original principal amount of the Term Loan, on the last day of each fiscal quarter commencing March 31, 2022, with the balance of the Term Loan payable on the Maturity Date. The Company is also required to make mandatory prepayments in the event of (i) achieving certain excess cash flow criteria, including the achievement and maintenance of a specific leverage ratio, (ii) selling assets that are collateral, or (iii) upon the issuance, offering, or placement of new debt obligations. There were no such mandatory prepayments made since inception of the Term Loan. As of June 30, 2023, and December 31, 2022, the outstanding principal balance on the Term Loan was $123,125 and $123,750, respectively.

The Term Loan requires the Company to maintain certain reporting requirements, affirmative covenants, and negative covenants, and the Company was in compliance with all requirements as of June 30, 2023. The Term Loan is secured by a first lien on the non-working capital assets of the Company and a second lien on the working capital assets of the Company.

Revolving Credit Facility

On March 29, 2021, the Obligors entered into a Senior Secured Revolving Credit Facility (the "Revolving Credit Facility") with JPMorgan Chase Bank, N.A., as administrative agent, issuing bank and swingline lender, and the lenders from time to time party thereto. The Revolving Credit Facility is due on June 30, 2026, or any earlier date on which the revolving commitments are reduced to zero.

The Revolving Credit Facility originally had a borrowing limit of $50,000. On August 31, 2021, the Obligors entered into an amendment (the "First Amendment") to increase their original borrowing limit to $100,000. In connection with the First Amendment, the Company's previously acquired subsidiaries became party to the Revolving Credit Facility as either borrowers or as guarantors. On October 25, 2021, the Company and its subsidiaries entered into a second amendment (the “Second Amendment”), with JPMorgan Chase Bank, N.A., pursuant to which the parties consented to the Term Loan described above, and made certain conforming changes to comport with the Term Loan provisions. The Revolving Credit Facility was further amended by a third amendment and joinder dated August 23, 2022 (the “Third Amendment”), pursuant to which several previously acquired subsidiaries became parties to the Revolving Credit Facility and granted liens on their assets. On December 22, 2022, the Company entered into a fourth amendment (the “Fourth Amendment”) pursuant to which a sale-leaseback transaction was permitted, and certain other changes were made, including a reduction of the maximum commitment amount under the Revolving Credit Facility from $100,000 to $75,000 and transitioning the LIBOR based rates to SOFR based rates. On March 31, 2023, the Company and certain of its subsidiaries entered into an amendment (the “Fifth Amendment”) pursuant to which the maturity date was extended to June 30, 2026, the maximum commitment amount under the Revolving Credit Facility was reduced to $55,000, and the interest rate on borrowings was revised to various spreads, based on the Company's fixed charge coverage ratio.

The unamortized debt discount and deferred financing costs were $623 as of June 30, 2023, and are included in other assets in the condensed consolidated balance sheets. Debt discount and deferred financing costs are being amortized to interest expense over the term of the Revolving Credit Facility.

The Revolving Credit Facility is an asset-based facility that is secured by a first lien on the working capital assets of the Company and a second lien on the non-working capital assets of the Company (including most of the Company’s subsidiaries). The borrowing base is based on a detailed monthly calculation of the sum of (a) a percentage of the Eligible Accounts at such time, plus (b) the lesser of (i) a percentage of the Eligible Inventory, at such time, valued at the lower of cost or market value, determined on a first-in-first-out basis, and (ii) the product of a percentage multiplied by the Net Orderly Liquidation Value percentage identified in the most recent inventory appraisal ordered by the Administrative Agent multiplied by the Eligible Inventory, valued at the lower of cost or market value, determined on a first-in-first-out basis, minus (c) Reserves (each of the defined terms above, as defined in the Revolving Credit Facility documents).

The Company is required to maintain certain reporting requirements, affirmative covenants and negative covenants, pursuant to terms outlined in the agreement. Additionally, if the Company’s Excess Availability (as defined in the Revolving Credit Facility documents) is less than an amount equal to 10% of the Aggregate Revolving Commitment (currently $55,000),

the Company will be required to maintain a minimum fixed charge coverage ratio of 1.1x on a rolling twelve-month basis until the Excess Availability is more than 10% of the Aggregate Revolving Commitment for thirty consecutive days. In order to consummate permitted acquisitions or to make restricted payments, the Company would be required to comply with a higher fixed charge coverage ratio of 1.15x, but no such acquisitions or payments are currently contemplated. As of June 30, 2023, the Company is in compliance with the covenants contained in the Revolving Credit Facility.

The Revolving Credit Facility provides for various interest rate options including the Adjusted Term SOFR Rate, the Adjusted REVSOFR30 Rate, the CB Floating Rate, the Adjusted Daily Simple SOFR, the CBFR, the Canadian Prime Rate, or the CDOR Rate. The rates that use SOFR as the reference rate (Adjusted Term SOFR Rate, the Adjusted REVSOFR30 Rate, the Adjusted Daily Simple SOFR and the CBFR rate) use the Term SOFR Rate plus 1.95%. Each rate has a 0.0% floor. A fee of 0.40% per annum is charged for available but unused borrowings.

As of June 30, 2023, and December 31, 2022, the Company had zero borrowed under the facility. As of June 30, 2023, the Company would be able to borrow approximately $34 million under the Revolving Credit Facility, before the Company would be required to comply with the minimum fixed charge coverage ratio of 1.1x.

Other Debt

Other debt of $295 and $160 as of June 30, 2023, and December 31, 2022, respectively, was primarily comprised of a foreign subsidiary's other debt which constitutes an immaterial revolving line of credit and mortgage.

Aggregate future principal payments

As of June 30, 2023, the aggregate future principal payments under long-term debt are as follows:

		Debt
For the period of July 1, 2023 to December 31, 2023	$	815
Year ending December 31,		
2024		1,269
2025		1,269
2026		1,269
2027		1,270
2028		117,528
Total	$	123,420

10. STOCKHOLDERS’ EQUITY

Common stock

Each holder of common stock is entitled to one vote for each share of common stock. Common stockholders have no pre-emptive rights to acquire additional shares of common stock or other securities. The common stock is not subject to redemption rights and carries no subscription or conversion rights. In the event of liquidation, the stockholders are entitled to share in corporate assets on a pro rata basis after the Company satisfies all liabilities and after provision is made for any class of capital stock having preference over the common stock. Subject to corporate regulations and preferences to preferred stock, if any, dividends are at the discretion of the Board of Directors. As of June 30, 2023, there were 45,540,217 shares outstanding and 300,000,000 shares authorized.

Warrants

On July 19, 2021, the Company completed the redemption ("Redemption") of certain of its outstanding warrants (the "Investor Warrants") that were issued in connection with a private placement of units (the "private placement"), each consisting

of a share of common stock and a warrant to purchase an additional one-half (1/2) shares of common stock. In connection with the private placement, the Company agreed to engage the placement agent (the "Placement Agent") as the Company's warrant solicitation agent in the event the Investor Warrants were called for Redemption. The Company agreed to pay a warrant solicitation fee to the Placement Agent equal to five percent of the amount of net cash proceeds solicited by the Placement Agent upon the exercise of certain Investor Warrants following such call for Redemption. As of June 30, 2023, and December 31, 2022, respectively, there were no Investor Warrants outstanding. In connection with the private placement, the Placement Agent was issued warrants (the “placement agent warrants”) which will expire on December 14, 2023.

As of June 30, 2023, the following table summarizes the outstanding placement agent warrants:

	Number of Warrants	Exercise Price
Placement agent warrants	11,662	$ 8.43
Placement agent warrants	6,007	$ 16.86
Total	**17,669**	**$ 11.30**

As of December 31, 2022, the following table summarizes the outstanding placement agent warrants:

	Number of Warrants	Exercise Price
Placement agent warrants	11,662	$ 8.43
Placement agent warrants	6,007	$ 16.86
Total	**17,669**	**$ 11.30**

11. STOCK-BASED COMPENSATION

Stock-based compensation plan overview

The Company maintains three equity incentive plans: the 2018 Equity Incentive Plan (“2018 Plan”), the 2019 Employee, Director and Consultant Equity Incentive Plan (“2019 Plan”) and the 2020 Employee, Director, and Consultant Equity Incentive Plan (“2020 Plan” and collectively, “Incentive Plans”). The 2020 Plan serves as the successor to the 2019 Plan and 2018 Plan and provides for the issuance of incentive stock options ("ISOs"), stock grants and stock-based awards to employees, directors, and consultants of the Company. No further awards will be issued under the 2018 Plan and 2019 Plan. As of June 30, 2023, a total of 1,533,570 shares are available for grant under the 2020 Plan.

The Incentive Plans are administered by the Company's Board of Directors. Notwithstanding the foregoing, the Board of Directors may delegate concurrent responsibility for administering each plan, including with respect to designated classes of persons eligible to receive an award under each plan, to a committee or committees (which term shall include subcommittees) consisting of one or more members of the Board of Directors (collectively, the “Plan Administrator”), subject to such limitations as the Board of Directors deems appropriate.

In November 2020, the Board of Directors and stockholders approved the 2020 Plan and reserved an aggregate of 2,284,053 shares of common stock for issuance under the 2020 Plan. Pursuant to the 2020 Plan, the number of shares available for issuance under the 2020 Plan may be increased on January 1 of each year, beginning on January 1, 2021, and ending on January 2, 2030, in an amount equal to the lesser of (i) 4% of the outstanding shares of the Company’s common stock on such date or (ii) such number of shares determined by the Plan Administrator.

The 2020 Plan provides for the grant of ISOs, nonqualified stock options, stock grants, and stock-based awards that are based in whole or in part by reference to the Company’s common stock.

- The Plan Administrator may grant options designated as incentive stock options or nonqualified stock options. Options shall be granted with an exercise price per share not less than 100% of the fair market value of the common stock on

the grant date, subject to certain limitations and exceptions as described in the plan agreements. Generally, the maximum term of an option shall be 10 years from the grant date. The Plan Administrator shall establish and set forth in each instrument that evidences an option the time at which, or the installments in which, the option shall vest and become exercisable.

- The Plan Administrator may grant stock grants and stock-based awards, including securities convertible into shares, stock appreciation rights, phantom stock awards or stock units on such terms and conditions which may be based on continuous service with the Company or related company or the achievement of any performance goals, as the Plan Administrator shall determine in its sole discretion, which terms, conditions and restrictions shall be set forth in the instrument evidencing the award.

Restricted Stock Unit ("RSU") Activity

RSUs granted to certain executives, employees and members of the Board of Directors expire 10 years after the grant date. The awards generally have a time-based vesting requirement (based on continuous employment). Upon vesting, the RSUs convert into shares of the Company's common stock. The stock-based compensation expense related to service-based awards is recorded over the requisite service period. During the first quarter of 2023, the Company granted RSU awards that are expected to vest with two equal vesting tranches, which are scheduled to occur on October 31, 2023, and October 31, 2024. During the three months ended June 30, 2023, the Company granted RSU awards to members of the Board of Directors that are expected to vest on the one year anniversary of the grant date.

The award granted to a former member of the Board (the "former Board member") in July 2020, and modified in November 2020, contained a market-based vesting condition based on the traded value of shares of the Company's common stock following the IPO over a specific time frame. For this award, the market condition was factored into its fair value. The fair value of the award, at the modification date, was $3,180, all of which was recorded as stock-based compensation expense upon the IPO. In July 2021, the market-based vesting condition for this award was satisfied and 148,315 RSUs of the former Board member vested. The remaining 111,236 unvested RSUs met the time-based vesting conditions during the year ended December 31, 2022, and vested at that time. No additional awards with market-based conditions have been granted.

The following table summarizes the activity related to the Company's RSUs for the six months ended June 30, 2023. For purposes of this table, vested RSUs represent the shares for which the service condition had been fulfilled during the six months ended June 30, 2023:

	Number of RSUs	Weighted average grant date fair value
Balance, December 31, 2022	**992,633**	**$ 8.57**
Granted	**792,226**	**$ 1.17**
Vested	**(412,433)**	**$ 8.58**
Forfeited	**(43,043)**	**$ 11.10**
Balance, June 30, 2023	**1,329,383**	**$ 4.08**

As of June 30, 2023, total unamortized stock-based compensation cost related to unvested RSUs was $3,939 and the weighted-average period over which the compensation is expected to be recognized is 1.04 years. For the three and six months ended June 30, 2023, the Company recognized $1,427 and $2,428, respectively, of total stock-based compensation expense for RSUs. As of June 30, 2023, there were 6,357 RSUs which had previously vested, but were not yet issued due to the recipients' elections to defer the awards.

Hydrofarm Holdings Group, Inc.
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(dollars in thousands, except share and per share amounts)

Performance Stock Unit ("PSU") Activity

During the first quarter of 2023, the Company granted PSU awards that are subject to a one-year vesting requirement (based on continuous employment) and contain performance conditions based on certain performance metrics. The following table summarizes the activity related to the Company's PSUs for the six months ended June 30, 2023:

	Number of PSUs	Weighted average grant date fair value
Balance, December 31, 2022	**96,246**	**$ 15.74**
Granted	**1,141,543**	**$ 1.77**
Vested	**(25,894)**	**$ 15.74**
Forfeited	**(171,795)**	**$ 7.49**
Balance, June 30, 2023	**1,040,100**	**$ 1.77**

During the six months ended June 30, 2023, the PSU forfeitures were due to employee terminations and performance conditions that were not satisfied, while PSU vests were from awards granted in prior periods. As of June 30, 2023, total unamortized stock-based compensation cost related to unvested PSUs was $980 and the weighted-average period over which the compensation is expected to be recognized is less than one-year. For the three and six months ended June 30, 2023, the Company recognized $319 and $416, respectively, of total stock-based compensation expense for PSUs.

Stock Options

The vesting of stock options is subject to certain change in control provisions as provided in the incentive plan agreements and options may be exercised up to 10 years from the date of issuance.

There were no stock options granted or exercised during the six months ended June 30, 2023. The following table summarizes the stock option activity for the six months ended June 30, 2023:

	Number	Weighted average exercise price	Weighted average grant date fair value	Weighted average remaining contractual term (years)
Outstanding as of December 31, 2022	**670,026**	**$ 9.50**	**$ 2.05**	**5.25**
Cancelled	**(20,062)**	**$ 9.43**	**$ 2.64**	
Forfeited	**(1,446)**	**$ 11.45**	**$ 8.08**	
Outstanding as of June 30, 2023	**648,518**	**$ 9.52**	**$ 2.08**	**4.09**
Options exercisable as of June 30, 2023	**607,484**	**$ 9.16**	**$ 1.58**	**3.92**
Vested and expected to vest as of June 30, 2023	**648,518**	**$ 9.52**	**$ 2.08**	**4.09**

The following table summarizes the unvested stock option activity for the six months ended June 30, 2023:

	Number	Weighted average grar date fair valu
Unvested as of December 31, 2022	**70,587**	**$ 7**
Vested	**(28,107)**	**$ 4**
Forfeited	**(1,446)**	**$ 8**
Unvested as of June 30, 2023	**41,034**	**$ 9**

As of June 30, 2023, total compensation cost related to unvested awards not yet recognized was $284 and the weighted-average period over which the compensation is expected to be recognized is 1.19 years. For the three and six months

ended June 30, 2023, the Company recognized $71 and $155, respectively, of total stock-based compensation expense for stock options.

12. INCOME TAXES

The Company recorded an income tax benefit of $318 and $171 for the three and six months ended June 30, 2023, representing an effective income tax rate of 2.4% and 0.6%, respectively. The Company's effective tax rate for the six months ended June 30, 2023, differs from the federal statutory rate of 21% primarily due to the Company maintaining a full valuation allowance against its net deferred tax assets in the U.S. and most foreign jurisdictions. The tax benefit for the three and six months ended June 30, 2023, was primarily due to a net foreign tax benefit in certain jurisdictions.

The Company recorded an income tax benefit of $6,861 and $12,430 for the three and six months ended June 30, 2022, representing an effective income tax rate of 3.3% and 5.2% for the three and six months ended in June 30, 2022, respectively. The Company's effective tax rate for the six months ended June 30, 2022, differs from the federal statutory rate primarily due to the impairment of goodwill for certain 2021 acquisitions which was not deductible for U.S. tax purposes, increases in the Company's valuation allowance on U.S. deferred tax assets, and the establishment of a valuation allowance for Canadian deferred tax assets. As described in Note 3 – *Goodwill and Intangible Assets, Net*, during the three months ended June 30, 2022, the Company fully impaired the goodwill associated with all 2021 acquisitions. For the six months ended June 30, 2022, the Company recorded discrete income tax benefits of $12,058 relating primarily to measurement period adjustments associated with 2021 acquisitions, and certain tax benefits related to goodwill impairment.

13. COMMITMENTS AND CONTINGENCIES

Purchase commitments

From time to time in the normal course of business, the Company will enter into agreements with suppliers which provide favorable pricing in return for a commitment to purchase minimum amounts of inventory over a defined time period.

Contingencies

In the normal course of business, certain claims have been brought against the Company and, where applicable, its suppliers. While there is inherent difficulty in predicting the outcome of such matters, management has vigorously contested the validity of these claims. Based on available information, management believes the claims are without merit and does not expect that the outcome, individually or in the aggregate, would have a material adverse effect on the consolidated financial positions, results of operations, cash flows or future earnings.

14. FAIR VALUE MEASUREMENTS

Recurring

Contingent consideration, as described under the heading *Business combinations* in Note 2 – *Basis of Presentation and Significant Accounting Policies*, was measured at estimated fair value on a recurring basis and based on Level 3 fair value measurements. The fair value of the contingent consideration for the Heavy 16 and Aurora Innovations acquisitions was $200 and $16,834, respectively, as of December 31, 2021. There was no change in the fair value of the contingent consideration for the Heavy 16 acquisition during fiscal year 2022, and it was paid in April 2022. The change in the fair value of contingent consideration for the Aurora Innovations acquisition was a benefit of $1,560, during the six months ended June 30, 2022, and was recognized in SG&A on the condensed consolidated statements of operations during that period. The value of the contingent consideration was $15,274 as of June 30, 2022, and was subsequently paid in July 2022. As of June 30, 2023, and December 31, 2022, the Company had no remaining unsettled contingent consideration relating to the Company's five acquisitions from 2021.

Nonrecurring

Nonrecurring fair value measurements include the Company's goodwill impairment recognized during the three and six months ended June 30, 2022, as determined based on unobservable Level 3 inputs. Refer to Note 3 – *Goodwill and Intangible Assets, Net*, for further discussion.

The note receivable, as described in Note 2 – *Basis of Presentation and Significant Accounting Policies*, was measured at fair value on a nonrecurring basis. During the six months ended June 30, 2022, the Company measured an impairment on the note receivable based on the estimated fair value of the collateral, which was considered a Level 3 fair value measurement. The carrying value of the note receivable was $3,111 as of December 31, 2021. The Company recorded an impairment loss of zero and $2,636 during the three and six months ended June 30, 2022, recognized in Impairments on the condensed consolidated statements of operations. The carrying value of the note receivable was $475 as of December 31, 2022. As of December 31, 2022, the note receivable was included in other assets on the condensed consolidated balance sheet.

Other Fair Value Measurements

The following table summarizes the fair value of the Company's assets and liabilities which are provided for disclosure purposes:

		June 30, 2023		December 31, 2022	
	Fair Value Hierarchy Level	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets					
Cash and cash equivalents	**Level 1**	**26,682**	**26,682**	**21,291**	**21,291**
Liabilities					
Finance leases	**Level 3**	**10,186**	**10,186**	**1,904**	**1,904**
Term Loan	**Level 2**	**123,125**	**100,963**	**123,750**	**105,188**

Cash and cash equivalents included funds deposited in banks, and the fair values approximated carrying values due to their short-term maturities. The fair values of other current assets and liabilities including accounts receivable, accounts payable, accrued expenses and other current liabilities approximated their carrying value due to their short-term maturities.

The estimated fair value of finance leases approximated its carrying value given the applicable interest rates and the nature of the security interest in the Company's assets, which were considered Level 3 fair value measurements. Finance leases primarily relate to the Sale-Leaseback transaction that was entered into in the first quarter of 2023. The fair value of the Term Loan was estimated based on Level 2 fair value measurements and was based on bank quotes. The carrying amount of the Term Loan reported above excludes unamortized debt discount and deferred financing costs. Refer to Note 6 – *Leases* and Note 9 – *Debt*, for further discussion of the Company's finance leases and Term Loan, respectively.

The Company did not have any transfers between Levels within the fair value hierarchy during the periods presented.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information that we believe is relevant to an assessment and understanding of our results of operations and financial condition. You should read this analysis in conjunction with our audited and unaudited consolidated financial statements and the notes contained elsewhere in this Quarterly Report on Form 10-Q and our 2022 Annual Report. This discussion and analysis contains statements of a forward-looking nature relating to future events or our future financial performance. These statements are only predictions, and actual events or results may differ materially. In evaluating such statements, you should carefully consider the various factors identified in this Quarterly Report on Form 10-Q, which could cause actual results to differ materially from those expressed in, or implied by, any forward-looking statements, including those set forth in "Risk Factors" in our 2022 Annual Report. See "Special Note Regarding Forward-Looking Statements."

Company Overview

We are a leading independent manufacturer and distributor of branded hydroponics equipment and supplies for controlled environment agriculture ("CEA"), including grow lights, climate control solutions, growing media and nutrients, as well as a broad portfolio of innovative and proprietary branded products. We primarily serve the U.S. and Canadian markets, and believe we are one of the leading competitors in these markets in an otherwise highly fragmented industry. For over 40 years, we have helped growers make growing easier and more productive. Our mission is to empower growers, farmers and cultivators with products that enable greater quality, efficiency, consistency, and speed in their grow projects.

Hydroponics is the farming of plants using soilless growing media and often artificial lighting in a controlled indoor or greenhouse environment. Hydroponics is the primary category of CEA and we use the terms CEA and hydroponics interchangeably. Our products are used to grow, farm, and cultivate cannabis, flowers, fruits, plants, vegetables, grains and herbs in controlled environment settings that allow end users to control key farming variables including temperature, humidity, CO_2, light intensity spectrum, nutrient concentration and pH. Through CEA, growers are able to be more efficient with physical space, water and resources, while enjoying year-round and more rapid grow cycles as well as more predictable and abundant grow yields, when compared to other traditional growing methods.

We reach commercial farmers and consumers through a broad and diversified network of over 2,000 wholesale customer accounts, who we connect with primarily through our proprietary online ordering platform. Our products are distributed across the United States and Canada through a diversified range of retailers of commercial and home gardening equipment and supplies. Our customers include specialty hydroponic retailers, commercial resellers and greenhouse builders, garden centers, hardware stores, and e-commerce retailers. Specialty hydroponic retailers can provide growers with specialized merchandise assortments and knowledgeable staff.

Market Conditions

We experienced adverse financial results throughout 2022 which continued into the first half of 2023, which we believe is primarily a result of an agricultural oversupply impacting our market. The extent to which these market conditions will continue to negatively impact our business and results of operations is uncertain and difficult to predict at this time.

In connection with our previously disclosed evaluation of our facility footprint and product and brand portfolio, we initiated a restructuring plan (the "Restructuring Plan") during the three months ended December 31, 2022. In connection with the Restructuring Plan, we have undertaken significant actions to streamline our operations, reduce costs and improve efficiencies during the industry recession. Our major initiatives to date have included (i) narrowing our product and brand portfolio, including removing approximately one-third of all products and one-fifth of all brands relating to our primary product portfolio, which excluded our garden center business in Canada, and (ii) relocating and consolidating certain manufacturing and distribution centers, including headcount reductions and reorganization to drive a solution based approach, focusing commercial sales on competencies and product assortment gained from our recent acquisitions.

During the three and six months ended June 30, 2023, we recorded pre-tax charges of $0.8 million and $2.2 million, respectively, relating primarily to the relocation and termination of certain facilities in Canada, the majority of which were recorded within Cost of goods sold on the consolidated statements of operations. The charges also included non-cash asset dispositions and write-downs. Total costs incurred since the Restructuring Plan commenced in the fourth quarter of 2022 are (i) $6.8 million relating to inventory markdowns and (ii) $3.1 million relating primarily to the relocation and termination of certain facilities in Canada. As of June 30, 2023, we have $0.5 million of certain restructuring liabilities remaining, and we may incur additional charges in connection with the Restructuring Plan in the second half of 2023, as discussed in more detail below.

As a result of the continued adverse market conditions, we may implement a second phase of the Restructuring Plan beginning in the second half of 2023, including potential U.S. manufacturing facility consolidations, in particular with respect to our production of certain durable equipment products. We may incur additional charges associated with product dispositions, footprint reductions, and asset write-downs. Any potential actions may generate significant cash and/or non-cash restructuring costs that could be incurred in future periods. The amounts the Company will ultimately realize or disburse in connection with the Restructuring Plan could differ from our estimates, and we may not be able to realize the full extent of our anticipated cost savings.

As of June 30, 2022, primarily due to a sustained decline in the market value of our common stock and the market conditions described above, we identified a triggering event requiring a test for goodwill impairment. We completed our goodwill impairment testing and recorded an impairment charge of $189.6 million as the test determined that the carrying value of the goodwill reporting units of U.S. and Canada was in excess of the fair value. The recognized impairment reduced the goodwill balance to zero as of June 30, 2022. The impairment was primarily due to a deterioration in customer demand in the U.S. and Canada caused by macroeconomic and industry conditions. We also review intangible assets with finite lives and indefinite lives for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. We did not identify a triggering event requiring a test for impairment during the remainder of 2022, or the six months ended June 30, 2023.

In connection with the goodwill impairment analysis performed as of June 30, 2022, we determined the fair value of the U.S. and Canada reporting units based on an income approach, using the present value of future discounted cash flows, and based on a market approach. The fair values were reconciled to the market value of our common stock to corroborate the estimates used in the interim test for impairment. The fair value determinations were a reflection of sales declines we experienced, which we believe were primarily a result of an agricultural oversupply impacting our market, and a reduction to our profitability and loss from operations. These market conditions continued to negatively impact our business and results of operations during the remainder of 2022, and the six months ended June 30, 2023.

We maintain an allowance for excess and obsolete inventory that is based upon assumptions about future demand and market conditions. While we believe our estimates of charges relating to our restructuring plan, long-lived assets, inventory obsolescence, and accounts receivable allowances are reasonable, it is possible that we may incur additional charges in the future and actual results may differ significantly from these estimates and assumptions. Depending on the length and severity of the industry and market conditions impacting our business, it is possible we may execute additional restructuring plans and incur future associated charges, and we may not be able to realize the full extent of our anticipated cost savings.

Filing Status

As of June 30, 2023, the market capitalization of outstanding shares of our common stock owned by non-affiliates decreased to below $60 million, which triggered the Company being classified as a non-accelerated filer with respect to SEC regulations and filing requirements effective December 31, 2023. As a result, our annual assessment of the effectiveness of our internal control over financial reporting does not require an audit by our external audit firm in compliance with the provisions of Section 404 of the Sarbanes-Oxley Act of 2002 for our next Annual Report on Form 10-K for the year ending December 31, 2023. The Company continues to qualify as a smaller reporting company in accordance with Rule 12b-2 under the Exchange Act and may continue to follow certain of the scaled back disclosure accommodations.

Results of Operations—Comparison of three and six months ended June 30, 2023 and 2022

The following table sets forth our unaudited interim condensed consolidated statements of operations for the three and six months ended June 30, 2023, and 2022, including amounts and percentages of net sales for each period and the period-to-period change in dollars and percent (amounts in thousands):

	Three months ended June 30,					
	2023		2022		Period change	
Net sales	**$ 63,051**	100.0 %	**$ 97,508**	100.0 %	$ (34,457)	-35.3 %
Cost of goods sold	**48,578**	77.0 %	**90,169**	92.5 %	(41,591)	-46.1 %
Gross profit	**14,473**	23.0 %	**7,339**	7.5 %	7,134	97.2 %
Operating expenses:						
Selling, general and administrative	**23,468**	37.2 %	**25,974**	26.6 %	(2,506)	-9.6 %
Impairments	**—**	0.0 %	**189,572**	194.4 %	(189,572)	-100.0
Loss from operations	**(8,995)**	-14.3 %	**(208,207)**	-213.5 %	199,212	95.7 %
Interest expense	**(3,768)**	-6.0 %	**(2,424)**	-2.5 %	(1,344)	-55.4 %
Other (expense) income, net	**(420)**	-0.7 %	**458**	0.5 %	(878)	-191.7 %
Loss before tax	**(13,183)**	-20.9 %	**(210,173)**	-215.5 %	196,990	93.7 %
Income tax benefit	**318**	0.5 %	**6,861**	7.0 %	(6,543)	-95.4 %
Net loss	**$ (12,865)**	-20.4 %	**$ (203,312)**	-208.5 %	$ 190,447	93.7 %

	Six months ended June 30,					
	2023		2022		Period change	
Net sales	**$ 125,229**	100.0 %	**$ 208,885**	100.0 %	$ (83,656)	-40.0 %
Cost of goods sold	**99,375**	79.4 %	**184,940**	88.5 %	(85,565)	-46.3 %
Gross profit	**25,854**	20.6 %	**23,945**	11.5 %	1,909	8.0 %
Operating expenses:						
Selling, general and administrative	**47,899**	38.2 %	**66,221**	31.7 %	(18,322)	-27.7 %
Impairments	**—**	0.0 %	**192,328**	92.1 %	(192,328)	-100.0 %
Loss from operations	**(22,045)**	-17.6 %	**(234,604)**	-112.3 %	212,559	90.6 %
Interest expense	**(7,460)**	-6.0 %	**(4,790)**	-2.3 %	(2,670)	-55.7 %
Other (expense) income, net	**(380)**	-0.3 %	**356**	0.2 %	(736)	-206.7 %
Loss before tax	**(29,885)**	-23.9 %	**(239,038)**	-114.4 %	209,153	87.5 %
Income tax benefit	**171**	0.1 %	**12,430**	6.0 %	(12,259)	-98.6 %
Net loss	**$ (29,714)**	-23.7 %	**$ (226,608)**	-108.5 %	$ 196,894	86.9 %

Net sales

Net sales for the three months ended June 30, 2023, were $63.1 million, a decrease of $34.5 million, or 35.3% compared to the same period in 2022. Net sales for the six months ended June 30, 2023, were $125.2 million, a decrease of $83.7 million, or 40.0% compared to the same period in 2022.

The 35.3% decrease in net sales for the three months ended June 30, 2023, as compared to the same period in 2022, was due to a 32.5% decline in volume of products sold, a 2.3% decrease in price and mix of products sold, and a 0.5% decline from unfavorable foreign exchange rates. The decrease in volume of products sold was primarily related to the aforementioned oversupply in the cannabis industry. The reduction in price was mainly due to lower prices on specific previously reserved lighting products as well as a higher mix of generally lower-priced consumables relative to higher-priced durable products. The decrease in foreign exchange related to strength in the U.S. Dollar relative to the Canadian Dollar.

The 40.0% decrease in net sales for the six months ended June 30, 2023, as compared to the same period in 2022, was due to a 38.3% decline in volume of products sold, a 1.1% decrease in price and mix of products sold, and a 0.6% decline from unfavorable foreign exchange rates. The decrease in volume of products sold was primarily related to the aforementioned

oversupply in the cannabis industry. The reduction in price was mainly due to lower prices on specific previously reserved lighting products. The decrease in foreign exchange related to strength in the U.S. Dollar relative to the Canadian Dollar.

Gross profit

Gross profit for the three months ended June 30, 2023, was $14.5 million, an increase of $7.1 million, or 97.2%, compared to the same period in 2022. Gross profit for the six months ended June 30, 2023, was $25.9 million, an increase of $1.9 million, or 8.0% compared to the same period in 2022.

Gross profit increased $7.1 million for the three months ended June 30, 2023, as compared to the same period in 2022, primarily due to a $9.9 million reduction in inventory provisions from the prior year period. Our gross profit margin percentage (gross profit as a percent of net sales) increased to 23.0% for the three months ended June 30, 2023, from 7.5% in the same period in 2022. The increase in gross profit margin was also due to selling a larger proportion of higher-margin proprietary brand products, lower freight and labor costs, and improved productivity. Our restructuring plan and related cost-saving initiatives contributed to realizing these benefits. The gross profit increase was partially offset by the aforementioned lower net sales and from restructuring costs of $0.7 million in the current period.

Gross profit increased $1.9 million for the six months ended June 30, 2023, as compared to the same period in 2022, primarily due to a $12.5 million reduction in inventory provisions, as well as decreased acquisition and integration expenses. Our gross profit margin percentage increased to 20.6% for the six months ended June 30, 2023, from 11.5% in the same period in 2022. The increase in gross profit margin was also due to selling a larger proportion of higher-margin proprietary brand products and improved productivity. Our restructuring plan and related cost-saving initiatives contributed to realizing these benefits. The gross profit increase was partially offset by the aforementioned lower net sales and from restructuring costs of $2.0 million in the current period.

Selling, general and administrative expenses

Selling, general and administrative ("SG&A") expenses for the three months ended June 30, 2023, were $23.5 million, a decrease of $2.5 million, or 9.6% compared to the same period in 2022. SG&A expenses for the six months ended June 30, 2023, were $47.9 million, a decrease of $18.3 million compared to the same period in 2022.

SG&A expenses decreased $2.5 million for the three months ended June 30, 2023, as compared to the same period in 2022. SG&A expenses decreased in several areas, including as a result of our cost saving and restructuring initiatives: (i) a $0.8 million decrease in acquisition and integration expenses, (ii) a $0.3 million decrease in salaries and benefits, (iii) a $0.3 million decrease in stock-based compensation, (iv) a $0.3 million decrease in costs associated with the relocation of certain of our distribution centers incurred in the prior year, (v) a $0.3 million decrease in professional and outside services, (vi) a $0.3 decrease in amortization and depreciation expenses, and (vii) a $0.2 million decrease in marketing and other expenses.

The $18.3 million decrease in SG&A expenses for the six months ended June 30, 2023, as compared to the same period in 2022, was primarily related to a $8.9 million decline in amortization expenses, as the prior year period included additional amortization expense due to adjustments to the useful lives of intangible assets, as described in Note 2 – *Basis of Presentation and Significant Accounting Policies*. Additionally, SG&A expenses decreased by $9.4 million in the six months ended June 30, 2023, due to lower expenses in several areas, including as a result of our cost saving and restructuring initiatives: (i) a $2.6 million decrease in salaries and benefits, (ii) a $2.1 million decrease in stock-based compensation, (iii) a $1.9 million decrease in acquisition and integration expenses, (iv) a $1.4 million decrease in costs associated with the relocation of certain of our distribution centers incurred last year, (v) a $0.9 million decrease in professional and outside services, and (vi) a $0.5 million decrease in marketing and other expenses.

Impairments

The Company did not record any impairment charges for the three and six months ended June 30, 2023. The Company recorded a goodwill impairment charge of $189.6 million for the three and six months ended June 30, 2022, as we determined that the carrying value of the goodwill reporting units of the U.S. and Canada was in excess of the fair value. The recognized impairment reduced the goodwill balance to zero as of June 30, 2022. The impairment was primarily due to a deterioration in customer demand in the U.S. and Canada caused by macroeconomic and industry conditions. For the six months ended June 30, 2022, the Company also recorded, in the fiscal first quarter, an impairment of a note receivable of $2.6 million. Refer to Note 2 – *Basis of Presentation and Significant Accounting Policies* and Note 14 – *Fair Value Measurements* for further description regarding the note receivable impairment.

Interest expense

Interest expense for the three months ended June 30, 2023, was $3.8 million, an increase of $1.3 million compared to the same period in the prior year. Interest expense for the six months ended June 30, 2023, was $7.5 million, an increase of $2.7 million compared to the same period in the prior year. The increase was primarily due to higher variable interest rates on our Term Loan.

Other (expense) income, net

Other expense, net for the three months ended June 30, 2023, was $0.4 million, an increase of $0.9 million compared to Other income, net of $0.5 million during the same period in the prior year. Other expense, net for the six months ended June 30, 2023, was $0.4 million, an increase of $0.7 million compared to Other income, net of $0.4 million during the same period in the prior year. Other expense, net for the three and six months ended June 30, 2023, was primarily driven by foreign currency exchange rate losses and legal fees associated with the amendment of the Term Loan, partially offset by interest income. Refer to Note 9 – *Debt* for a further description of the Term Loan amendment.

Income tax benefit

We recorded an income tax benefit of $0.3 million and $0.2 million for the three and six months ended June 30, 2023, representing an effective income tax rate of 2.4% and 0.6%, respectively. Our effective tax rate for the six months ended June 30, 2023, differs from the federal statutory rate of 21% primarily due to the Company maintaining a full valuation allowance against its net deferred tax assets in the U.S. and most foreign jurisdictions. The tax benefit for the three and six months ended June 30, 2023, was primarily due to a net foreign tax benefit in certain jurisdictions.

We recorded an income tax benefit of $6.9 million and $12.4 million for the three and six months ended June 30, 2022, representing an effective income tax rate of 3.3% and 5.2%, respectively. Our effective tax rate for the six months ended June 30, 2022, differs from the federal statutory rate primarily due to the impairment of goodwill for certain 2021 acquisitions which was not deductible for U.S. tax purposes, increases in the Company's valuation allowance on U.S. deferred tax assets, and the establishment of a valuation allowance for Canadian deferred tax assets.

Liquidity and Capital Resources

Cash Flow from Operating, Investing, and Financing Activities

Comparison of the six months ended June 30, 2023, and June 30, 2022

The following table summarizes our cash flows for the six months ended June 30, 2023, and 2022 (amounts in thousands):

	Six months ended June 30, 2023	Six months ended June 30, 2022
Net cash from operating activities	$ 961	$ 7,268
Net cash used in investing activities	(3,263)	(4,743)
Net cash from (used in) financing activities	7,447	(3,349)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	246	(115)
Net increase (decrease) in cash, cash equivalents and restricted cash	5,391	(939)
Cash, cash equivalents and restricted cash at beginning of period	21,291	28,384
Cash, cash equivalents and restricted cash at end of period	$ 26,682	$ 27,445

Operating Activities

Net cash from operating activities was $1.0 million for the six months ended June 30, 2023, driven by positive cash from operating activities in the second quarter. The net cash from operating activities was primarily due to a $3.6 million net cash inflow from a reduction in working capital, partially offset by a net loss of $29.7 million less net non-cash items of $27.1 million. The net reduction in working capital was primarily driven by a decrease of $15.4 million in inventories, partially offset by decreases of $4.5 million of lease liabilities, $3.3 million of accrued expenses and other current liabilities, $1.3 million in deferred revenue, and $1.2 million of accounts payable.

Net cash from operating activities was $7.3 million for the six months ended June 30, 2022, primarily due to $7.2 million net cash inflow from a reduction of working capital. This included a decrease of $21.3 million in inventories and a decrease of $6.2 million in accounts receivable, partially offset by decreases of $6.7 million in deferred revenue and $6.4 million in accrued expenses and other current liabilities.

Investing Activities

Net cash used in investing activities was $3.3 million and $4.7 million for the six months ended June 30, 2023, and June 30, 2022, respectively, primarily due to capital expenditures of property, plant and equipment.

Financing Activities

Net cash from financing activities was $7.4 million for the six months ended June 30, 2023, primarily driven by $8.6 million of proceeds from the Sale-Leaseback Transaction. In addition, we paid $0.6 million on the Term Loan relating to required quarterly payments of principal.

Net cash used in financing activities was $3.3 million for the six months ended June 30, 2022. We paid $2.1 million related to employees' withholding tax in connection with the vesting of restricted stock units. In addition, we paid $0.6 million on the Term Loan relating to required quarterly payments of principal.

Availability and Use of Cash

Our ability to make investments in our business, service our debt and maintain liquidity will depend upon our ability to generate excess operating cash flows through our operating subsidiaries. We believe that our cash flows from operating activities, combined with current cash levels and borrowing availability under the Revolving Credit Facility, will be adequate to support our ongoing operations, to fund debt service requirements, capital expenditures, lease obligations and working capital needs through the next twelve months of operations. However, we cannot ensure that our business will generate sufficient cash flow from operating activities or that future borrowings will be available under our borrowing agreements in amounts sufficient to pay indebtedness or fund other working capital needs. Actual results of operations will depend on numerous factors, many of which are beyond our control as further discussed in *Item 1A. Risk Factors* included in this Form 10-Q and in our 2022 Annual Report on Form 10-K.

In January 2023, Gotham Properties LLC, an Oregon limited liability company and our subsidiary (“Seller”), consummated a Purchase and Sale Agreement with J & D Property, LLC, a Nevada limited liability company (“Purchaser”) pursuant to which certain real property located in the City of Eugene, County of Lane, State of Oregon (the “Eugene Property”) was sold to Purchaser for $8.6 million and then leased back by Seller. The new lease has a term of 15 years with annual rent starting at approximately $0.7 million and increases to the final year when annual rent is approximately $1.0 million. The Eugene Property serves as the manufacturing and processing site for certain of our grow media and nutrient brands. We intend to reinvest the net cash proceeds into certain permitted investments, such as capital expenditures. The foregoing description of the reinvestment provisions does not purport to be complete and is qualified in its entirety by reference to the provisions of the Term Loan.

If necessary, we believe that we could supplement our cash position through additional sale-leasebacks, asset sales and equity financing. We believe it is prudent to be prepared if required and, accordingly, continue to be engaged in the process of evaluating and preparing to implement one or more of the aforementioned activities. Any potential such event may be subject to provisions referenced in our Term Loan and Revolving Credit Facility, such as subjecting the Company to making mandatory prepayments.

Term Loan

On October 25, 2021, we and certain of our direct and indirect subsidiaries entered into the Term Loan with JPMorgan Chase Bank, N.A., as administrative agent for the lenders, pursuant to which we borrowed a $125 million senior secured term loan. The Term Loan was amended by Amendment No. 1 effective as of June 27, 2023, to replace the LIBOR referenced rates with SOFR referenced rates. Pursuant to Amendment No. 1, any Term Loan that constitutes a Eurodollar Rate Loan that is outstanding as of the Amendment No. 1 closing date shall continue until the end of the applicable interest period for such Eurodollar Rate Loan and the provisions of the Term Loan applicable thereto shall continue and remain in effect (notwithstanding the occurrence of the Amendment No. 1 closing date) until the end of the applicable interest period for such Eurodollar Rate Loan, after which such provisions shall have no further force or effect. Such Eurodollar Rate Loan shall subsequently either be an ABR Loan or a Term Benchmark Loan. The ABR Loans shall bear interest at the Alternate Base Rate (with a 2.0% floor) plus 4.50%, and Term Benchmark Loans shall bear interest at the Adjusted Term SOFR Rate (with a 1.0%

floor) plus 5.50%. The ABR Loan and Term Benchmark Loan credit spreads of 4.50% and 5.50%, respectively, within the Amendment No. 1 have not changed from the credit spreads in the original Term Loan. The Term Loan matures on October 25, 2028.

The principal amounts of the Term Loan are scheduled to be repaid in consecutive quarterly installments in amounts equal to 0.25% of the original principal amount of the Term Loan on the last day of each fiscal quarter commencing March 31, 2022, with the balance of the Term Loan payable on the Maturity Date of October 25, 2028.

The Term Loan requires us to maintain certain reporting requirements, affirmative covenants, and negative covenants. We were in compliance with all debt covenants as of June 30, 2023. The Term Loan is secured by a first lien on our non-working capital assets and a second lien on our working capital assets.

Revolving Credit Facility

On March 29, 2021, we entered into the Revolving Credit Facility, which provided for a borrowing limit of $50 million. The Revolving Credit Facility was amended by the First Amendment dated August 31, 2021, which increased the revolving line of credit by an additional $50 million for an aggregate borrowing limit of $100 million. The Revolving Credit Facility was further amended by the Second Amendment dated October 25, 2021 which, among other things, permitted the incurrence of the Term Loan and made certain other changes including subordinating its liens on non-working capital assets to the obligations under the Term Loan. The Revolving Credit Facility was further amended by the Third Amendment and Joinder dated August 23, 2022, pursuant to which several previously acquired subsidiaries became parties to the Revolving Credit Facility and granted liens on their assets. On December 22, 2022, the Company entered into the Fourth Amendment pursuant to which a sale-leaseback transaction was permitted, and certain other changes were made, including a reduction of the maximum commitment amount under the Revolving Credit Facility from $100 million to $75 million and transitioning the LIBOR based rates to SOFR based rates. On March 31, 2023, the Company and certain of its subsidiaries entered into the Fifth Amendment, pursuant to which the maturity date was extended to June 30, 2026, the maximum commitment amount under the Revolving Credit Facility was reduced to $55 million, and the interest rate on borrowings was revised to various spreads, based on the Company's fixed charge coverage ratio.

The Revolving Credit Facility provides for various interest rate options including the Adjusted Term SOFR Rate, the Adjusted REVSOFR30 Rate, the CB Floating Rate, the Adjusted Daily Simple SOFR, the CBFR, the Canadian Prime Rate, or the CDOR Rate. The rates that use SOFR as the reference rate (Adjusted Term SOFR Rate, the Adjusted REVSOFR30 Rate, the Adjusted Daily Simple SOFR and the CBFR rate) use the Term SOFR Rate plus 1.95%. Each rate has a 0.0% floor. A fee of 0.40% per annum is charged for available but unused borrowings. Our obligations under the Revolving Credit Facility are secured by a first priority lien (subject to certain permitted liens) in substantially all of our and our subsidiaries' respective personal property assets pursuant to the terms of a U.S. and Canadian Pledge and Security Agreement dated March 29, 2021 and other security documents, as amended to include additional subsidiaries.

The Revolving Credit Facility maintains certain reporting requirements, affirmative covenants, negative covenants and financial covenants. A certain financial covenant becomes applicable in the event that our excess availability under the Revolving Credit Facility is less than an amount equal to 10% of the Aggregate Revolving Commitment (currently $55 million) and would require us to maintain a minimum fixed charge coverage ratio of 1.1x on a rolling twelve-month basis.

In order to consummate permitted acquisitions or to make restricted payments, the Company would be required to comply with a higher fixed charge coverage ratio of 1.15x, but no such acquisitions or payments are currently contemplated.

We were in compliance with all debt covenants as of June 30, 2023. As of June 30, 2023, approximately $34 million was available to borrow under the Revolving Credit Facility, before the Company would be required to comply with the minimum fixed charge coverage ratio of 1.1x.

As of June 30, 2023, and December 31, 2022, the Company had zero borrowed under the Revolving Credit Facility.

Cash and cash equivalents

The cash and cash equivalents balances of $26.7 million and $21.3 million at June 30, 2023, and December 31, 2022, respectively, included $11.6 million and $7.3 million, respectively, held by foreign subsidiaries.

Material Cash Requirements

Our material cash requirements include interest and principal payments on our long-term debt and finance leases, operating lease payments, and purchase obligations to support our operations. Refer to Part I, Item 1, Financial Statements,

Note 9 – *Debt*, Note 6 – *Leases*, and Note 13 – *Commitments and Contingencies* for details relating to our material cash requirements for debt, our leasing arrangements, including future maturities of our operating lease liabilities, and purchase obligations, respectively.

From time to time in the normal course of business, we will enter into agreements with suppliers which provide favorable pricing in return for a commitment to purchase minimum amounts of inventory over a defined time period.

Critical Accounting Policies and Estimates

The preceding discussion and analysis of our consolidated results of operations and financial condition should be read in conjunction with our condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q. Our critical accounting policies and estimates are identified in Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of our most recently filed Form 10-K and include the discussion of estimates used in goodwill and indefinite lived intangible assets, long-lived assets, and inventory valuation. Such accounting policies and estimates require significant judgments and assumptions to be used in the preparation of the Condensed Consolidated Financial Statements included in this Form 10-Q, and actual results could differ materially from the amounts reported.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of economic losses due to adverse changes in financial market prices and rates. Our primary market risk has been interest rate, foreign currency and inflation risk. We do not have material exposure to commodity risk.

Interest Rate Risk

We are exposed to interest rate risk through our variable rate debt. As of June 30, 2023, we had $123.1 million of Term Loan debt that is subject to variable interest rates that are based on Secured Overnight Financing Rate (“SOFR”) or an alternate base rate. Refer to Part I, Item 1, Financial Statements, Note 9 – *Debt* for details relating to the debt. If the rates were to increase by 100 basis points from the rates in effect as of June 30, 2023, our interest expense on the variable-rate debt would increase by an average of $1.1 million annually. There are inherent limitations in the sensitivity analysis presented, primarily due to the assumptions that interest rate changes would be instantaneous, while SOFR changes regularly. We do not currently hedge our interest rate risks, but may determine to do so in the future.

Foreign Currency Risk

The functional currencies of our foreign subsidiary operations are predominantly in the Canadian dollar (“CAD”) and the Euro. For the purposes of presenting these consolidated financial statements, the assets, and liabilities of subsidiaries with CAD or Euro functional currencies are translated into USD using exchange rates prevailing at the end of each reporting period. Income and expense items are translated at the average rate prevailing during the period with exchange differences impacting other comprehensive income (loss) in equity. Therefore, our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, principally the CAD. We are impacted by changes in foreign currency exchange rates when we sell product in currencies different from the currency in which costs were incurred. The functional currencies and our purchasing and sales activities primarily include USD, CAD and Euro. As these currencies fluctuate against each other, and other currencies, we are exposed to foreign currency exchange rate risk on sales, purchasing transactions, and labor. To date, we have not entered into any foreign currency exchange contracts and currently do not expect to enter into foreign currency exchange contracts for trading or speculative purposes.

Impact of Inflation

Our results of operations and financial condition are presented based on historical costs. We cannot provide assurances that our results of operations and financial condition will not be materially impacted by inflation in the future.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation and supervision of our Chief Executive Officer and our Chief Financial Officer, have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, the Company's management, including the Chief Executive Officer and the Chief Financial Officer, concluded that the Company’s disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost benefit relationship of possible controls and procedures.

Changes in Internal Controls over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we may become involved in various lawsuits and legal proceedings, which arise, in the ordinary course of business. We are currently not aware of any legal proceedings or claims that we believe will have a material adverse effect on our business, financial condition or operating results.

ITEM 1A. RISK FACTORS

For a discussion of risk factors, please read Item 1A, "Risk Factors" in our 2022 Annual Report. Such risk factors continue to be relevant to an understanding of our business, financial condition and operating results. As of the date of this Quarterly Report on Form 10-Q, there have been the following material changes with respect to such risk factors.

Failures at financial institutions at which we maintain or deposit funds, or at which parties with whom we conduct business maintain funds, could adversely affect us.

We deposit funds in financial institutions and may, from time to time, maintain cash balances at such financial institutions in excess of the Federal Deposit Insurance Corporation ("FDIC") Limit of $250,000. Recently there has been significant volatility and instability among banks and financial institutions. For example, on March 10, 2023, Silicon Valley Bank, or SVB, was closed by the California Department of Financial Protection and Innovation, which appointed the FDIC as receiver, and for a period of time, customers of the bank did not have access to their funds and there was uncertainty as to when, if at all, customers would have access to funds in excess of the FDIC insured amounts. Should a financial institution at which deposits are maintained fail, there is no guarantee as to the extent that we would recover the funds deposited, whether through FDIC coverage or otherwise, or the timing of any recovery. In addition, if any parties with whom we conduct business are unable to access funds pursuant to arrangements with their financial institution, such parties' ability to pay their obligations to us or to enter into new commercial arrangements requiring additional payments to us could be adversely affected.

Our restructuring activities, including any second phase we may enter into, may increase our expenses and cash expenditures, and may not have the intended effects.

In connection with the Restructuring Plan, we have implemented and may continue to implement a number of restructuring initiatives designed to streamline our operations, reduce costs, and improve efficiencies during the industry recession. See “*Item 2. Management’s Discussion And Analysis Of Financial Condition And Results of Operations – Market Conditions*” above for more information regarding the Restructuring Plan. Restructuring initiatives such as the Restructuring Plan typically result in charges and cash expenditures that may adversely affect financial results for one or more periods, and efforts to minimize or eliminate such expenditures may not be successful. Moreover, restructuring actions can create unanticipated consequences, such as instability or distraction among our workforce or among management.

We cannot assure you that the Restructuring Plan or any other cost-saving initiatives we may undertake will be successful. A variety of factors, many of which are beyond our control, could cause us not to realize expected cost savings, including but not limited to unexpected costs incurred in connection with consolidating and/or closing certain operations or asset write-downs, delays or difficulty terminating leases, unexpected integration challenges, unintended attrition and temporary instability. Any of these factors could hamper our ability to grow and meet customer demand in future periods. If we are unable to structure our operations in the light of evolving market conditions, this could have a material adverse effect on our business, financial condition, results of operations, and cash flows.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

On August 8, 2023, the compensation committee of the Board of Directors approved a $25,000 cash retention bonus and a retention grant of 50,000 RSUs to Mark Parker, Executive Vice President of the Company, under the 2020 Plan. The RSUs will vest annually over three years beginning on the first anniversary of the grant date, subject to his continued service.

ITEM 6. EXHIBITS

(a) Exhibits.

Exhibit	Description
10.1	Fifth Amendment to Credit Agreement, dated March 31, 2023, by and among Hydrofarm Holdings Group, Inc., Hydrofarm, LLC, Field 16, LLC, Innovative Growers Equipment, Inc., Manufacturing & Supply Chain Services, Inc., Hydrofarm Investment Corp., Hydrofarm Holdings LLC, EHH Holdings, LLC, Sunblaster LLC, Hydrofarm Canada, LLC, Sunblaster Holdings ULC, Eddi's Wholesale Garden Supplies Ltd., House & Garden Holdings, LLC, Gotham Properties LLC, Aurora International, LLC, Aurora Peat Products ULC, Greenstar Plant Products Inc., Innovative AG Installation, Inc., Innovative Racking Systems, Inc., Innovative Shipping Solutions, Inc., Innovative Growers Equipment Canada, Inc., JPMorgan Chase Bank, N.A., as lender, and JPMorgan Chase Bank, N.A., as administrative agent (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the SEC on April 6, 2023).
10.2	Amendment No. 1 to Credit and Guaranty Agreement, dated as of June 27, 2023, by and among Hydrofarm Holdings Group, Inc., the subsidiaries of Hydrofarm Holdings Group, Inc. party thereto from time to time, the lenders party thereto and JP Morgan Chase Bank, N.A., as administrative agent and as collateral Agent. (Incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the SEC on July 3, 2023).
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*#	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*#	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101. INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	Inline XBRL Taxonomy Schema Linkbase Document.
101.CAL	Inline XBRL Taxonomy Calculation Linkbase Document.
101.DEF	Inline XBRL Taxonomy Definition Linkbase Document.
101.LAB	Inline XBRL Taxonomy Labels Linkbase Document.
101.PRE	Inline XBRL Taxonomy Presentation Linkbase Document.
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101).

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* Filed herewith.

\# The certifications attached as Exhibits 32.1 and 32.2 accompany this Quarterly Report on Form 10-Q pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed "filed" by the Company for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall they be deemed incorporated by reference into any filing of the registrant under the Securities Act of 1933, as amended, or the Exchange Act, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

Hydrofarm Holdings Group, Inc.

Date: August 9, 2023

/s/ William Toler
William Toler
Chief Executive Officer
(Principal Executive Officer)

Date: August 9, 2023

/s/ B. John Lindeman
B. John Lindeman
Chief Financial Officer
(Principal Financial Officer)

Exhibit 31.1

CERTIFICATIONS UNDER SECTION 302

I, William Toler, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Hydrofarm Holdings Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2023

By: /s/ William Toler
William Toler
Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATIONS UNDER SECTION 302

I, B. John Lindeman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Hydrofarm Holdings Group, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 9, 2023

By: /s/ B. John Lindeman
B. John Lindeman
Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

CERTIFICATIONS UNDER SECTION 906

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Hydrofarm Holdings Group, Inc., a Delaware corporation (the “Company”), does hereby certify, to such officer’s knowledge, that:

The Quarterly Report for the quarter ended June 30, 2023 (the “Form 10-Q”) of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 9, 2023

/s/ William Toler
William Toler
Chief Executive Officer
(Principal Executive Officer)

Exhibit 32.2

CERTIFICATIONS UNDER SECTION 906

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Hydrofarm Holdings Group, Inc., a Delaware corporation (the “Company”), does hereby certify, to such officer’s knowledge, that:

The Quarterly Report for the quarter ended June 30, 2023 (the “Form 10-Q”) of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 9, 2023

/s/ B. John Lindeman
B. John Lindeman
Chief Financial Officer
(Principal Financial Officer)