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

Forward Looking Statements

This Interim Report on Form 10-Q contains, in addition to historical information, certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 ("PLSRA"), Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act") regarding Stem Holdings, Inc. (the "Company" or "Stem", also referred to as "us", "we" or "our"). Forward-looking statements give our current expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historical or current facts. Forward-looking statements involve risks and uncertainties. Forward-looking statements include statements regarding, among other things, (a) our projected sales, profitability, and cash flows, (b) our growth strategies, (c) anticipated trends in our industries, (d) our future financing plans and (e) our anticipated needs for working capital. They are generally identifiable by use of the words "may," "will," "should," "anticipate," "estimate," "plans," "potential," "projects," "continuing," "ongoing," "expects," "management believes," "we believe," "we intend" or the negative of these words or other variations on these words or comparable terminology. These statements may be found under "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Description of Business," as well as in this Form 10-Q generally. In particular, these include statements relating to future actions, prospective products or product approvals, future performance or results of current and anticipated products, sales efforts, expenses, the outcome of contingencies such as legal proceedings, and financial results.

Any or all of our forward-looking statements in this report may turn out to be inaccurate. They can be affected by inaccurate assumptions we might make or by known or unknown risks or uncertainties. Consequently, no forward-looking statement can be guaranteed. Actual future results may vary materially as a result of various factors, including, without limitation, the risks outlined under "Risk Factors" detailed in the Company's Form 10 and S-1 registration statements and matters described in this Form 10-Q generally. In light of these risks and uncertainties, there can be no assurance that the forward-looking statements contained in this filing will in fact occur. You should not place undue reliance on these forward-looking statements. The forward-looking statements speak only as of the date on which they are made, and, except to the extent required by federal securities laws, we undertake no obligation to publicly update any forward-looking statements, whether as the result of new information, future events, or otherwise. We intend that all forward-looking statements be subject to the safe harbor provisions of the PSLRA.

For the three and six months ended March 31, 2021, the financial statements have been prepared by management in accordance with the standards of the Public Company Accounting Oversight Board (United States). For the three and six months ended March 31, 2021, the unaudited interim financial statements have been prepared by management in accordance with the condensing rules of the United States Securities and Exchange Commission.

Results of Operations

	For the Three Months Ended March 31,		Change	
($ in thousands)	**2021**	**2020**	**$**	**%**
Gross Revenue	$ 12,356	$ 2,653	9,703	366%
Discounts and returns	(1,829)	(355)	(1,474)	415%
Cost of goods sold	7,783	1,573	6,210	395%
Consulting fees	1,420	1,398	22	2%
Professional fees	987	884	103	12%
General and administration	3,361	2,068	1,294	63%
Other income (expenses), net	(5,602)	(907)	(4,695)	518%
Loss from equity method investees	-	(243)	243	(100)%
Net loss	**$ (8,626)**	**$ (4,775)**		

Comparison of the results of operations for the three months ended March 31, 2021 compared to the three months ended March 31, 2020

The Company had net revenues during the three months ended March 31, 2021 of $ 10,527 compared with $2,298 for the comparable period of 2020, the increase in revenue was primarily related to the increase due to the acquisitions of both Seven Leaf and Driven and the consolidation of an additional nine related entities.

Cost of goods for the three months ended March 31, 2021 amounted to approximately $7,783 compared to $1,573 in the comparable period of the prior year. These costs include both the cost of finished product purchased for retail and the cost of cultivation and processing for the grow facilities and sold at the wholesale level.

In the three months ended March 31, 2021, we incurred consulting costs of approximately $1,420 compared to approximately $1,398 in the comparable period of the prior year. The increase in consulting fees was attributed to an increase of stock-based expenses for consultants. We expended those fees as we have yet to build up a significant employee base and currently outsource certain tasks to consultants.

In the three months ended March 31, 2021, we incurred professional fees of approximately $987 compared to approximately $884 in the comparable period of the prior year. Those fees are primarily for legal, accounting, and related services that pertains to our being a public company in both the United States and Canada. We expect as we grow our operations these costs will continue to grow.

In the three months ended March 31, 2021, we incurred general and administrative costs of approximately $3,361 compared to approximately $2,068. This increase relates primarily to an increase costs related to the inclusion of certain entities due to their being variable interest entities plus the acquisition of entities and related expenses.

	For the Six Months Ended March 31,		Change	
($ in thousands)	**2021**	**2020**	**$**	**%**
Revenue	$ 18,745	$ 4,204	$ 14,542	346%
Discounts and returns	(2,758)	(585)	(2,174)	371%
Cost of goods sold	11,256	2,642	8,614	326%
Consulting fees	2,164	1,907	257	13%
Professional fees	1,909	1,523	386	25%
General and administration	6,705	4,058	2,647	65%
Other income (expenses), net	(5,858)	(1,324)	(4,534)	343%
Loss from equity method investees	-	(252)	252	(100)%
Net loss	**$ (11,905)**	**$ (8,087)**		

Comparison of the results of operations for the six months ended March 31, 2021 compared to the six months ended March 31, 2020

The Company had net revenues during the six months ended March 31, 2021 of $15,987 compared with $3,619 for the comparable period of 2020, the increase is primarily due to the acquisitions of Driven, Yerba Buena, Seven Leaf and the consolidation of four related entities.

Cost of goods for the six months ended March 31, 2021 amounted to approximately 11,256 compared to $2,642 in the comparable period of the prior year. These costs include both the cost of finished product purchased for retail and the cost of cultivation and processing for the grow facilities and sold at the wholesale level.

In the six months ended March 31, 2021, we incurred consulting costs of $2,164 compared to $1,907 in the comparable period of the prior year. We mitigated our consulting expenses which were stock based the prior year.

In the six months ended March 31, 2021, we incurred professional fees of approximately $1,909 compared to $1,523 in the comparable period of the prior year. Those fees are primarily for legal, accounting and related services relating to our being a public company in both the United States and Canada. We expect as we grow our operations these costs will continue to grow.

In six months ended March 31, 2021, we incurred general and administrative costs of approximately $6,705 compared to $4,058, these costs include payroll, depreciation and amortization, insurance, rent expense and other general costs. We expect that these costs will increase as we increase our operations.

Below is a presentation of Non-Generally Accepted Accounting Principles ("non-GAAP") presentation of Earnings Before Interest Taxes Depreciation and Amortization ("EBITDA") for the three and six months ended March 31, 2021,

Earnings Before Interest Taxes Depreciation and Amortization ("EBITDA"):

	For the Three Months Ended March 31,	
($ in thousands)	**2021**	**2020**
Gross Revenue	$ 12,356	$ 2,653
Discounts and returns	(1,829)	(355)
Cost of goods sold	7,783	1,573
Consulting fees	1,420	1,398
Professional fees	987	884
General and administration	3,361	2,068
Other income (expenses), net	(5,602)	(907)
Loss from equity method investees	-	(243)
Net loss- Generally Accepted Accounting Principles ("GAAP")	**(8,626)**	**(4,775)**
Add Backs:		
Interest	550	863
Taxes	-	-
Depreciation and amortization	1,556	528
EBITDA (non-GAAP)	**(6,520)**	**(3,384)**
Other Add Backs:		
Stock-based compensation	2,061	1,410
Change in fair value of derivative liability	(34)	(121)
Change in fair value of warrant liability	6,278	254
Foreign currency exchange (gain) loss	(22)	(89)
Adjusted EBITDA (non-GAAP)	**$ 1,763**	**$ (1,930)**

Earnings Before Interest Taxes Depreciation and Amortization ("EBITDA)":

	For the Six Months Ended March 31,	
($ in thousands)	**2021**	**2020**
Revenue	$ 18,745	**$ 4,204**
Discounts and returns	(2,758)	**(585)**
Cost of goods sold	11,256	**2,642**
Consulting fees	2,164	**1,907**
Professional fees	1,909	**1,523**
General and administration	6,705	4,058
Other income (expenses), net	(5,858)	(1,324)
Loss from equity method investees	-	(252)
Net loss- Generally Accepted Accounting Principles ("GAAP")	**(11,905)**	**(8,087)**
Add Backs:		
Interest	1,261	1,271
Taxes	-	-
Depreciation and amortization	2,271	1,008
EBITDA (non-GAAP)	**(8,373)**	**(5,808)**
Other Add Backs:		
Stock-based compensation	3,405	1,907
Change in fair value of derivative liability	(242)	(142)
Change in fair value of warrant liability	6,188	215
Foreign currency exchange (gain) loss	21	(21)
Adjusted EBITDA (non-GAAP)	**$ 999**	**$ (3,849)**

LIQUIDITY AND FINANCIAL CONDITION

Liquidity and Capital Resources

The Company had cash of $4,605 as of March 31, 2021. Subsequent to March 31, 2021, the Company raised an additional C$10,309 via an offering consisting of the sale of 16,926,019 Units. Our primary uses of cash have been for salaries, fees paid to third parties for professional services, insurance, general and administrative expenses, and the acquisitions and development of rental properties and their improvement. All funds received have been expended in the furtherance of growing the business. We have received funds from financing activities such as from equity offerings and debt financing as well as the proceeds from advances to be contributed to new ventures. The following trends are reasonably likely to result in changes in our liquidity over the near to long term:

- An increase in working capital requirements to finance our entry into the cultivation, production, and sale of cannabis:
- Acquisition and buildout of rental properties;
- Addition of administrative and sales personnel as the business grows and
- The cost of being a public company.

Subsequent to March 31, 2021, we have not raised any additional funds in our private placements. Our efforts to raise additional capital are ongoing and we expect to continue our efforts in the following quarters.

With respect to the company's investments in the projects pertaining to the equity method investee's and affiliates, we have committed that we need to spend an estimated $2 million in expansion, buildout and improvements potentially in the near term. These capital expenditures are contingent upon several factors including the Company obtaining financing for the development of the properties and the construction of the tenant improvements in such amount and on such terms and provisions as are acceptable to the Company.

The Company has entered into a joint venture in which the Company has extended a $2.5 million line of credit for Community Growth Partners Holdings, Inc. ("CGP"). The Company has funded up to $880k of its obligation to fund the requests of CGP and has currently converted the note into 14% equity in the joint venture. The line of credit has been terminated and is no longer active.

As of December 23, 2019 has entered into a stock purchase agreement with Attollo Capital Holdings A, LLC (the "Purchaser") pursuant to which Stem will issue 11,764,706 shares of preferred stock of the Company (the "Preferred Stock") at a purchase price of US$0.85 per share of Preferred Stock (the "Original Issue Price") for gross proceeds to the Company of approximately US$10,000,000 (the "Investment"). As of the date of this filing, the Company has not yet closed on this transaction.

We have used our available funds to fund our operating expenses, pay our obligations, acquire and develop rental properties, and grow our company. We need to raise significant additional capital or debt financing to acquire new properties, to develop existing properties, and to assure we have sufficient working capital for our ongoing operations and debt obligations. There is no guarantee that such funding will be available to the Company at a viable cost, if at all.

Cash Flow

For the six months ended March 31, 2021 and 2020

Net cash flows used in operating activities was $4,720 for the six months ended March 31,2021 as compared net cash flow used in operating activities to $3,450 for the six months ended March 31, 2020, a change of $1,270.

● Net cash flow used in operating activities for the six months ended March 31, 2021 primarily reflected a net loss of $11,905 adjusted for the add-back of non-cash items consisting of depreciation and amortization of $2,228, stock-based compensation expense of $3,406, non-cash rent and interest $331, amortization of debt discount of $608, and a loss of $105 from equity method investee and the change in foreign currency translation of $20, offset by a gain in sale of equity method investments of $200, a change in the fair value of derivative and warrant liabilities of $5,946, a change in operating assets and liabilities consisting of an increase in accounts payable and accrued expenses of $2,197, an increase in prepaid expenses and other operating assets of $2,336.

● Net cash flow used in investing activities for the six months ended March 31, 2021 amounted to $437 and consisted of $279 used in the purchase of property and equipment. Additionally, a net of $158 was used in investments.

● Net cash provided by financing activities was $7,633 for the six months ended March 31, 2021 as compared to $3,017 for the six months ended March 31, 2020. During the six months ended March 31, 2021, we received proceeds from notes payable and advances of $22 and proceeds of $9,804 for the issuance of common shares. Additionally, an offset of $1,242 of payment on notes payable was incurred and $951 for the forgiveness of debt.

CRITICAL ACCOUNTING POLICIES

Basis of preparation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The condensed financial statements included herein are unaudited. Such financial statements, in the opinion of management, contain all adjustments necessary to present fairly the financial position and results of operations as of and for the periods indicated. All such adjustments are of a normal recurring nature. These interim results are not necessarily indicative of the results to be expected for the year ending September 30, 2021 or for any other period. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission, and because of this, for further information, readers should refer to the financial statements and footnotes included in our Form 10-K for the fiscal year ended September 30, 2020 filed with the Securities and Exchange Commission on December 28, 2020. The Company believes that the disclosures are adequate to make the interim information presented not misleading.

Principles of Consolidation

The Company’s policy is to consolidate all entities that it controls by ownership of a majority of the outstanding voting stock. In addition, the Company consolidates entities that meet the definition of a variable interest entity (“VIE”) for which it is the primary beneficiary. The primary beneficiary is the party who has the power to direct the activities of a VIE that most significantly impact the entity’s economic performance and who has an obligation to absorb losses of the entity or a right to receive benefits from the entity that could potentially be significant to the entity. For consolidated entities that are less than wholly owned, the third party’s holding of equity interest is presented as noncontrolling interests in the Company’s Consolidated Balance Sheets and Consolidated Statements of Changes in Stockholders’ Equity. The portion of net loss attributable to the noncontrolling interests is presented as net loss attributable to noncontrolling interests in the Company’s Consolidated Statements of Operations.

In August 2016, the Company and certain shareholders of the Company entered into a “Multi Party” Agreement, in which the Company became obligated to lease or acquire three separate real estate assets, and separately, if certain events occur, additional real estate assets held by entities related to those shareholders. The Agreement also gives the Company the right of first refusal in regard to certain properties owned by the persons and entities affiliated with the parties of the Agreement so long as certain targets are met. In the quarter ended June 30, 2019, the Company issued 12,500,000 shares of its common stock for the acquisition of Consolidated Ventures of Oregon, LLC (“CVO”) and Opco Holdings, LLC (“Opco”) which comprise the entities within the Multi Party Agreement. On September 6, 2020, the Company received the regulatory approval to transfer all the licenses held under both CVO and Opco. Subsequently, the Company has completed the acquisition and as a result, the Company is no longer engaged primarily in property rental operations but has taken over the operations of its primary renters, which is the cultivation, production and sale of cannabis and related productions. Since CVO and Opco are related to the Company, the acquisition was not accounted for as a business combination at fair value under the codification sections of ASC 805. The assets and liabilities were transferred to the Company at their historical cost and the Company has included the operations of Opco and CVO for all periods presented for this period ended March 31, 2021.

The accompanying condensed consolidated financial statements include the accounts of Stem Holdings, Inc. and its wholly owned subsidiaries, Stem Holdings Oregon, Inc., Stem Holdings IP, Inc., Opco, LLC, Stem Holdings Agri, Inc., Opco Holdings, Inc., 7LV USA Corporation, and Consolidated Ventures of Oregon, Inc., and Driven Deliveries, Inc. In addition, the Company has consolidated YMY Ventures, SAV, LLC; WCV, LLC and NVD RE, Inc. under the variable interest requirements.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. The most significant estimates included in these condensed consolidated financial statements are those associated with the assumptions used to value equity instruments, valuation of its long live assets for impairment testing, valuation of intangible assets, and the valuation of inventory. These estimates and assumptions are based on current facts, historical experience and various other factors believed to be reasonable given the circumstances that exist at the time the financial statements are prepared. Actual results may differ materially and adversely from these estimates. To the extent there are material differences between the estimates and actual results, the Company's future results of operations will be affected.

Revenue recognition

The Company recognizes revenue when its customer obtains control of promised goods or services, in an amount that reflects the consideration which the entity expects to receive in exchange for those goods or services. To determine revenue recognition for arrangements that an entity determines are within the scope of Accounting Standards Codification (ASC) Topic 606, Revenue from Contracts with Customers (Topic 606), the entity performs the following five steps: (i) identify the contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the entity satisfies a performance obligation. The Company only applies the five-step model to contracts when it is probable that the entity will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer. At contract inception, once the contract is determined to be within the scope of Topic 606, the Company assesses the goods or services promised within each contract and determines those that are performance obligations and assesses whether each promised good or service is distinct. The Company then recognizes as revenue the amount of the transaction price that is allocated to the respective performance obligation when (or as) the performance obligation is satisfied.

Revenue for the Company's product sales has not been adjusted for the effects of a financing component as the Company expects, at contract inception, that the period between when the Company's transfers control of the product and when the Company receives payment will be one year or less. Product shipping and handling costs are included in cost of product sales.

Effective October 1, 2019, the Company adopted the requirements of ASU 2014-09 (ASC 606) and related amendments, using the modified retrospective method. The adoption of ASC 606 did not have a significant impact on the Company's revenue recognition policy as revenues related to wholesale and retail revenue are recorded upon transfer of merchandise to the customer, which was the effective policy under ASC 605 previously.

The following policies reflect specific criteria for the various revenue streams of the Company:

Cannabis Dispensary, Cultivation and Production

Revenue is recognized upon transfer of retail merchandise to the customer upon sale transaction, at which time its performance obligation is complete. Revenue is recognized upon delivery of product to the wholesale customer, at which time the Company's performance obligation is complete. Terms are generally between cash of delivery to 30 days for the Company's wholesale customers.

The Company's sales environment is somewhat unique, in that once the product is sold to the customer (retail) or delivered (wholesale) there are essentially no returns allowed or warranty available to the customer under the various state laws.

Delivery

1) *Identify the contract with a customer*

The Company sells retail products directly to customers. In these sales there is no formal contract with the customer. These sales have commercial substance and there are no issues with collectability as the customer pays the cost of the goods at the time of purchase or delivery.

2) *Identify the performance obligations in the contract*

The Company sells its products directly to consumers. In this case these sales represent a performance obligation with the sales and any necessary deliveries of those products.

3) *Determine the transaction price*

The sales that are done directly to the customer have no variable consideration or financing component. The transaction price is the cost that those goods are being sold for plus any additional delivery costs.

4) *Allocate the transaction price to performance obligations in the contract*

For the goods that the Company sells directly to customers, the transaction price is allocated between the cost of the goods and any delivery fees that may be incurred to deliver to the customer.

5) *Recognize revenue when or as the Company satisfies a performance obligation*

For the sales of the Company's own goods the performance obligation is complete once the customer has received the product.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

As noted earlier in Note 1, the Company, engages in a business that constitutes an illegal act under the laws of the United States Federal Government. This raises several possible issues which may impact the Company's overall operations, not the least of which are related to traditional banking and other key operational risks. Since cannabis remains illegal on the federal level, and most traditional banks are federally insured, those financial institutions will not service cannabis businesses. In states where medical or recreational marijuana is legal, dispensary owners, manufacturers, and anybody who "touches the plant," continue to face a host of operational hurdles. While local, state-chartered banks and credit unions now accept cannabis commerce, there remains a reluctance by traditional banks to do business with them. Aside from a huge inconvenience and the need to find creative ways to manage financial flow, payroll logistics, and payment of taxes, this also poses tremendous risks to controls as a result of operating a lucrative business in cash. This lack of access to traditional banking may inhibit industry growth. In the period ended December 31, 2019, the Company's accounts with a major money center bank were closed as the bank would not allow the Company to continue to use its banking network.

Despite the uncertainties surrounding the Federal government's position on legalized marijuana, the Company does not believe these risks will have a substantive impact on its planned operations in the near term.

As of March 31, 2021, the Company has acquired interests in several entities. As part of those interests, the Company has commitments to fund the acquisition of licenses and permits to allow for the cultivation and sale of cannabis and related products in the United States. As of March 31, 2021, Company estimates that its investees will need up to approximately $2 million to complete the acquisition of licenses and permits, to fund the buildout or expansion of facilities to fully operate in their respective cannabis markets, which will encompass several years of development.

OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

(a) ***Disclosure Controls and Procedures***

We are required to maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer (also our principal executive officer) and our chief financial officer (also our principal financial and accounting officer) to allow for timely decisions regarding required disclosure.

Pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 ("Exchange Act"), the Company's management, including the Company's Chief Executive Officer ("CEO") (the Company's principal executive officer) and Chief Financial Officer ("CFO") (the Company's principal financial and accounting officer), has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined under Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were not effective as of March 31, 2021 to ensure that information required to be disclosed by the Company in the reports that the Company files or submits under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Company's CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure. The principal basis for this conclusion is the lack of segregation of duties within our financial function and the lack of an operating Audit Committee.

(b) ***Management's Report on Internal Control over Financial Reporting***

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of, the company's principal executive and principal financial officers and effected by the company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company;

- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and