



ASX RELEASE (2 MAY 2022)

Q1 2022 Quarterly Update & Appendix 4C

Key Points:

- Partnership with The Valens Company (NASDAQ:VLNS) commenced 1 March 2022, with Epsilon receiving operational expenditure reimbursements from Valens;
- Production at the Southport Facility has been ramping up with both Valens and non-Valens customers, with strong order book;
- Q1 2022 cash flows not reflective of post-Valens revenue run rate due to delays in payment receipts from Valens and customers – current receivables balance exceeding \$1 million – and Valens partnership commencing in last month of Q1 2022;
- Targeting strong close to Q2 2022 having regard to cash receipts of receivables, forward production booked through to quarter end;

Epsilon Healthcare Limited (ASX:EPN) (Epsilon or the Company) is pleased to provide an update on its activities and provides its Appendix 4C for the quarter ended 31 March 2022.

Partnership with The Valens Company (NASDAQ:VLNS)

As announced on 3 March 2022, the Company has commenced its partnership with The Valens Company, subject to an initial trial period of three months commencing 1 March 2022.

During this period, Valens has access Epsilon's GMP manufacturing capability at the Southport Facility – the largest cannabis extraction facility in the Southern Hemisphere with TGA and EU GMP capability – in return for Valens funding all mutually budgeted operational and capital expenditures of the Southport Facility on a reimbursement basis.

During the trial period, Epsilon and Valens are working towards the achievement of a A\$2 million sales target of medicinal cannabis products, as well as a number of other performance indicators which are being used to determine the 'success' of the trial. The Company remains confident that this trial period will be successful and look forward to Valens and Epsilon continuing their partnership past the end of May 2022.

Southport Production Ramp Up

Epsilon is pleased to report a continued ramp-up of activities at the Southport Facility for both Valens and non-Valens customers, with a strong order book for the Southport Facility.

In Q1 2022 the Company produced over 20,000 units of tinctures and 5,000 units of dried flower bottles for both Valens and non-Valens customers – a production level reflective of only one month of the Valens partnership. As an indicator of the continued ramp up, in April 2022 alone, a further 6,500 dried flower bottles were packed for release at the Southport Facility.

Q1 2022 cash receipts are not reflective of the true post-Valens run rate due to its commencement in March 2022 as well as delays in receipt of reimbursement payments from Valens and delays in collection from customers, with THC Pharma's total receivables currently exceeding \$1 million.

Tetra Health Clinics Update

Tetra Health's performance continues to lead, with modest growth of ~10% in Q1 2022 in number of doctor consultations and ~25% increase in revenue (unaudited) on the prior quarter, notwithstanding the holiday periods and shorter months in Q1 2022.

Restructuring Canadian Operations

As per the Company's mid quarter update released on 11 March 2022, the restructuring of the Company's Canadian operations continues. Epsilon's hydroponics equipment wholesaling business (Crystal Mountain) is not expected to continue to operate following this restructuring activity, with the Company expecting entities related to that operation to conduct their own insolvency management processes over the coming weeks. Epsilon will provide further updates as these matters progress.

\$1.05 million R&D Tax Incentive Receipt & Reduction of Debt

Epsilon notes that during the quarter, the Company received R&D Tax Incentive refunds totalling \$1.05 million across its two R&D Tax Incentive eligible entities – THC Pharma and Canndeo.

Pursuant to an agreement with Mitchell Asset Management (MAM), the lender of a secured debt facility to the group, the Company has directed the full R&D Tax refund received towards the repayment of the principal amount, reducing total debt to ~\$2.5 million of an original \$4 million debt facility. The Company continues to be in discussions with MAM to consider its ability to redraw funds up to the original facility limit, or otherwise explore secured debt financing opportunities.

Capital Raising

As announced on 2 May 2022, the Company has secured a capital raising of up to \$2.1 million, with a unconditional first tranche of \$600,000 at \$0.034 per share. Subsequent tranches are subject to agreement between the Company and the Investor, and the Company having either sufficient placement capacity under ASX Listing Rule 7.1 or 7.1A or receiving shareholder approval to issue these securities.

The funds raised will be applied towards working capital to support the continued ramp up of operations at the Southport Facility. The Company continues to expect that on the basis of the Company's partnership with The Valens Company (NASDAQ:VLNS) continuing as previously announced, the Southport Facility should become EBITDA positive to the group on a go forward run rate basis.

Additional Disclosure

Receipts from customers in Q1 2022 was an increase over Q4 2021, however as noted above the Company does not consider this to be reflective of the true level of operations at the Southport Facility – particularly from 1 March 2022 onwards. The Company expects Q2 2022 receipts from customers to be materially higher – noting the large receivables balance to date and the strong order book at the Southport Facility through the coming months, as well as the continued Valens operational expenditure reimbursements.

The net cash used in operating activities also includes the receipt of the R&D Tax Incentive noted above, which was applied towards reduction of debt.

The Company also notes that payments to related parties and their associates in the quarter were all remuneration for services as directors in the ordinary course of business.

ENDS

ASX release authorised by the EPN Board of Directors.

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Epsilon Healthcare Limited (ASX: EPN) – epsilonhealthcare.com.au

Epsilon Healthcare (ASX:EPN) is a diversified global healthcare and pharmaceuticals company. EPN owns a number of medicinal cannabis assets including the largest GMP cannabis manufacturing facility in the Southern Hemisphere (the Southport Facility) and the Tetra Health clinic group. EPN has a strategic partnership with The Valens Company (NASDAQ: VLNS), a leading cannabis consumer products company with significant expertise in manufacturing cannabinoid based products, for operation and management of its Southport Facility.

Appendix 4C

Quarterly cash flow report for entities subject to Listing Rule 4.7B

Name of entity

Epsilon Healthcare Limited

ABN

33 614 508 039

Quarter ended ("current quarter")

March 2022

Consolidated statement of cash flows	Current quarter \$A'000	Year to date (3 months) \$A'000
1. Cash flows from operating activities		
1.1 Receipts from customers	555	555
1.2 Payments for		
(a) research and development	(35)	(35)
(b) product manufacturing and operating costs	(344)	(344)
(c) advertising and marketing	(22)	(22)
(d) leased assets	(46)	(46)
(e) staff costs	(728)	(728)
(f) administration and corporate costs	(716)	(716)
1.3 Dividends received (see note 3)	-	-
1.4 Interest received	-	-
1.5 Interest and other costs of finance paid	(146)	(146)
1.6 Income taxes paid	-	-
1.7 Government grants and tax incentives	1,069	1,069
1.8 Deposits refunded	-	-
1.9 Net cash from / (used in) operating activities	(413)	(413)
2. Cash flows from investing activities		
2.1 Payments to acquire or for:		
(a) entities	-	-
(b) businesses	-	-
(c) property, plant and equipment	(55)	(55)
(d) investments	-	-
(e) intellectual property	-	-
(f) other non-current assets	-	-

Consolidated statement of cash flows		Current quarter \$A'000	Year to date (3 months) \$A'000
2.2	Proceeds from disposal of:		
	(a) entities	-	-
	(b) businesses	-	-
	(c) property, plant and equipment	-	-
	(d) investments	-	-
	(e) intellectual property	-	-
	(f) other non-current assets	-	-
2.3	Cash flows from loans to other entities	-	-
2.4	Dividends received (see note 3)	-	-
2.5	Other (provide details if material)	-	-
2.6	Net cash from / (used in) investing activities	(55)	(55)

3.	Cash flows from financing activities		
3.1	Proceeds from issues of equity securities (excluding convertible debt securities)	-	-
3.2	Proceeds from issue of convertible debt securities	-	-
3.3	Proceeds from exercise of options	-	-
3.4	Transaction costs related to issues of equity securities or convertible debt securities	-	-
3.5	Proceeds from borrowings	-	-
3.6	Repayment of borrowings	(1,069)	(1,069)
3.7	Transaction costs related to loans and borrowings	-	-
3.8	Dividends paid	-	-
3.9	Other (provide details if material)	-	-
3.10	Net cash from / (used in) financing activities	(1,069)	(1,069)

Appendix 4C
Quarterly cash flow report for entities subject to Listing Rule 4.7B

4.	Net increase / (decrease) in cash and cash equivalents for the period		
4.1	Cash and cash equivalents at beginning of period	2,335	2,335
4.2	Net cash from / (used in) operating activities (item 1.9 above)	(413)	(413)
4.3	Net cash from / (used in) investing activities (item 2.6 above)	(55)	(55)
4.4	Net cash from / (used in) financing activities (item 3.10 above)	(1,069)	(1,069)
4.5	Effect of movement in exchange rates on cash held	(1)	(1)
4.6	Cash and cash equivalents at end of period	797	797

5.	Reconciliation of cash and cash equivalents at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts	Current quarter \$A'000	Previous quarter \$A'000
5.1	Bank balances	797	2,335
5.2	Call deposits	-	-
5.3	Bank overdrafts	-	-
5.4	Other (provide details)	-	-
5.5	Cash and cash equivalents at end of quarter (should equal item 4.6 above)	797	2,335

6.	Payments to related parties of the entity and their associates	Current quarter \$A'000
6.1	Aggregate amount of payments to related parties and their associates included in item 1	92
6.2	Aggregate amount of payments to related parties and their associates included in item 2	-

Note: if any amounts are shown in items 6.1 or 6.2, your quarterly activity report must include a description of, and an explanation for, such payments.

7.	Financing facilities <i>Note: the term "facility" includes all forms of financing arrangements available to the entity. Add notes as necessary for an understanding of the sources of finance available to the entity.</i>	Total facility amount at quarter end \$A'000	Amount drawn at quarter end \$A'000
7.1	Loan facilities	2,662	2,662
7.2	Credit standby arrangements	-	-
7.3	Other (please specify)	-	-
7.4	Total financing facilities	2,662	2,662
7.5	Unused financing facilities available at quarter end		-
7.6	<p>Include in the box below a description of each facility above, including the lender, interest rate, maturity date and whether it is secured or unsecured. If any additional financing facilities have been entered into or are proposed to be entered into after quarter end, include a note providing details of those facilities as well.</p> <p>On 30 April 2020, the Company entered into a \$4,000,000 secured debt facility. Following an extension agreed and announced on 27 October 2021, the facility is repayable at any time on or before 31 October 2022. The facility attracts interest at 1.25% per calendar month. Please refer to ASX Announcements dated 30 April 2020 and 27 October 2021 for further details including further facility terms.</p> <p>The Company has made repayments against principal totalling \$477,159 in June 2021 and \$1,068,927 in February 2022.</p>		

8.	Estimated cash available for future operating activities	\$A'000
8.1	Net cash from / (used in) operating activities (item 1.9)	(413)
8.2	Cash and cash equivalents at quarter end (item 4.6)	797
8.3	Unused finance facilities available at quarter end (item 7.5)	-
8.4	Total available funding (item 8.2 + item 8.3)	797
8.5	Estimated quarters of funding available (item 8.4 divided by item 8.1)	1.93
	<p><i>Note: if the entity has reported positive net operating cash flows in item 1.9, answer item 8.5 as "N/A". Otherwise, a figure for the estimated quarters of funding available must be included in item 8.5.</i></p>	

8.6 If item 8.5 is less than 2 quarters, please provide answers to the following questions:

8.6.1 Does the entity expect that it will continue to have the current level of net operating cash flows for the time being and, if not, why not?

Answer:

No, the Company does not expect to continue have the current level of net operating cash flows for the time being.

The Company notes:

- (1) The Company has entered into a partnership with The Valens Company (NASDAQ:VLNS) (Valens) effective 1 March 2022 – see ASX announcement 3 March 2022. Pursuant to this agreement, Valens is required to reimburse the Company for its mutually agreed and budgeted operational and capital expenditure at the Southport Facility;
- (2) The current quarter includes ~\$1m+ R&D proceeds which were received during the quarter. These will not be receivable in the coming June quarter, however will be available on a similar run rate basis for the Company to claim in the following September or December quarters;
- (3) Further, Valens and Epsilon are targeting a significant ramp up in production activity at the Southport Facility which should result in a material positive benefit to the net cash used in operating activities; and
- (4) As detailed in the corresponding activities statement for this quarter, the Company currently has a large receivables balance exceeding \$1 million predominantly consisting of payments owed to the Company for recent production activity at the Southport Facility (from both Valens and non-Valens customers) and pending reimbursement of operational expenditure from Valens.

8.6.2 Has the entity taken any steps, or does it propose to take any steps, to raise further cash to fund its operations and, if so, what are those steps and how likely does it believe that they will be successful?

Answer:

The Company refers to its contemporaneous ASX Announcement of 2 May 2022 disclosing that it has secured a capital raising of up to \$2.1 million, with an initial unconditional tranche of \$600,000 to be settled on 4 May 2022. Generally, the Company also notes it has access to a potential redraw of its existing debt facility up to its facility limit, and continues to explore other funding arrangements on an as needed basis. The Company is confident and has proven in that past that it has the ability to raise capital (whether debt or equity) on a timely basis.

8.6.3 Does the entity expect to be able to continue its operations and to meet its business objectives and, if so, on what basis?

Answer:

The Company refers to the items above and is highly confident that it will be able to continue its operations to meet its business objectives on an ongoing basis.

Note: where item 8.5 is less than 2 quarters, all of questions 8.6.1, 8.6.2 and 8.6.3 above must be answered.

Compliance statement

- 1 This statement has been prepared in accordance with accounting standards and policies which comply with Listing Rule 19.11A.
- 2 This statement gives a true and fair view of the matters disclosed.

Date: 2 May 2022

Authorised by: Epsilon Board of Directors
(Name of body or officer authorising release – see note 4)

Notes

1. This quarterly cash flow report and the accompanying activity report provide a basis for informing the market about the entity's activities for the past quarter, how they have been financed and the effect this has had on its cash position. An entity that wishes to disclose additional information over and above the minimum required under the Listing Rules is encouraged to do so.
2. If this quarterly cash flow report has been prepared in accordance with Australian Accounting Standards, the definitions in, and provisions of, *AASB 107: Statement of Cash Flows* apply to this report. If this quarterly cash flow report has been prepared in accordance with other accounting standards agreed by ASX pursuant to Listing Rule 19.11A, the corresponding equivalent standard applies to this report.
3. Dividends received may be classified either as cash flows from operating activities or cash flows from investing activities, depending on the accounting policy of the entity.
4. If this report has been authorised for release to the market by your board of directors, you can insert here: "By the board". If it has been authorised for release to the market by a committee of your board of directors, you can insert here: "By the [name of board committee – eg Audit and Risk Committee]". If it has been authorised for release to the market by a disclosure committee, you can insert here: "By the Disclosure Committee".
5. If this report has been authorised for release to the market by your board of directors and you wish to hold yourself out as complying with recommendation 4.2 of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*, the board should have received a declaration from its CEO and CFO that, in their opinion, the financial records of the entity have been properly maintained, that this report complies with the appropriate accounting standards and gives a true and fair view of the cash flows of the entity, and that their opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.