

Company Announcement
ASX: HPC

DATE: 31/10/2023

Q3 FY23 Quarterly Report and Appendix 4C: Material YoY reduction in cash burn and ongoing revenue growth

KEY HIGHLIGHTS

- Net sales of US\$2.60m achieved in Q3 FY23 – 7% increase on PCP (Q3 FY2022: US\$2.43m) and tenth straight quarter of sales growth on a trailing 12-month basis
- Q3 FY23 is the second highest ever quarterly sales result and consolidates summer month momentum from strong Q2 FY23 net sales
- Gross margin increased 8ppt to 58% on prior quarter (Q2 FY23: 50%) – YoY Gross profit dollars up 23% to a record US\$1.51m from Q3 FY22 (US\$1.23m)
- Net cash used in operating activities down 47% on PCP to US\$1.46m (Q3 FY22: US\$2.78m) and in line with previous quarter – initiatives in place expected to reduce this further
- Marketing costs as a percentage of net revenue down for a third straight quarter to 30% - record low since IPO date, down from 36% in Q2 FY23 and down from 78% in Q4 FY22
- Transition to new broker, LeBeau Excel, expands addressable market for product in Canada and expected to generate 2-3% improvement in customer net margin
- Partnership secured with RooLife Group to market, sell and distribute HydraLyte products in China –expands Company’s global footprint and unlocks additional potential revenue stream
- Amazon Canada subscribers grew from zero to 1,383 during the quarter while Amazon US YoY subscription growth is up 4% from 4,026 same time last year to 4,180 subscribers at end of Q3 FY23, despite a heavy reduction in advertising spend
- Continued execution of stated strategy to reduce expenditure and extend cash reserves through reduced marketing spend following investments in 2022

Hydration solutions company **The Hydration Pharmaceuticals Company Limited (ASX: HPC)** (“HydraLyte North America” or “the Company”) is pleased to provide the following update on its operational and financial performance for the three-month period ended 30 September 2023 (the “quarter”).

Financial overview:

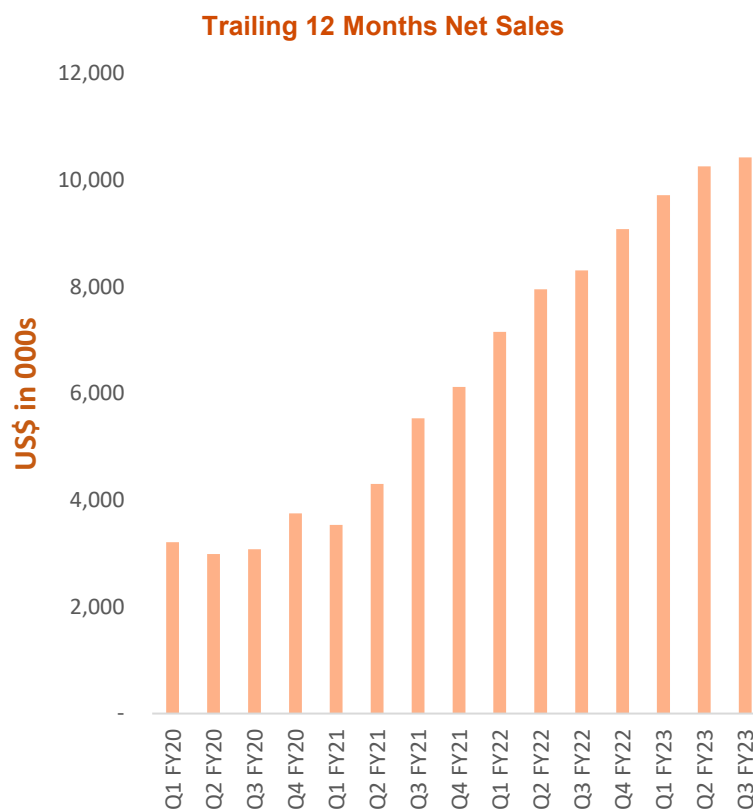
Revenue for the quarter increased 7% on PCP (Q3 FY2022: US\$2.43m) to US\$2.60m, highlighting strong growth and resulting in the second highest quarterly sales result to date.

Quarter on quarter revenue was down slightly, primarily due to the Company's strategic decision to transition to a new sales broker in Canada. This transition was completed during Q3 FY23 and will result in an expected net customer margin improvement of two to three percentage points.

The transition also led to a slight lag in revenue receipts during Q3 FY23. Q3 FY23's strong result takes 12-month trailing revenue to US\$10.43m.

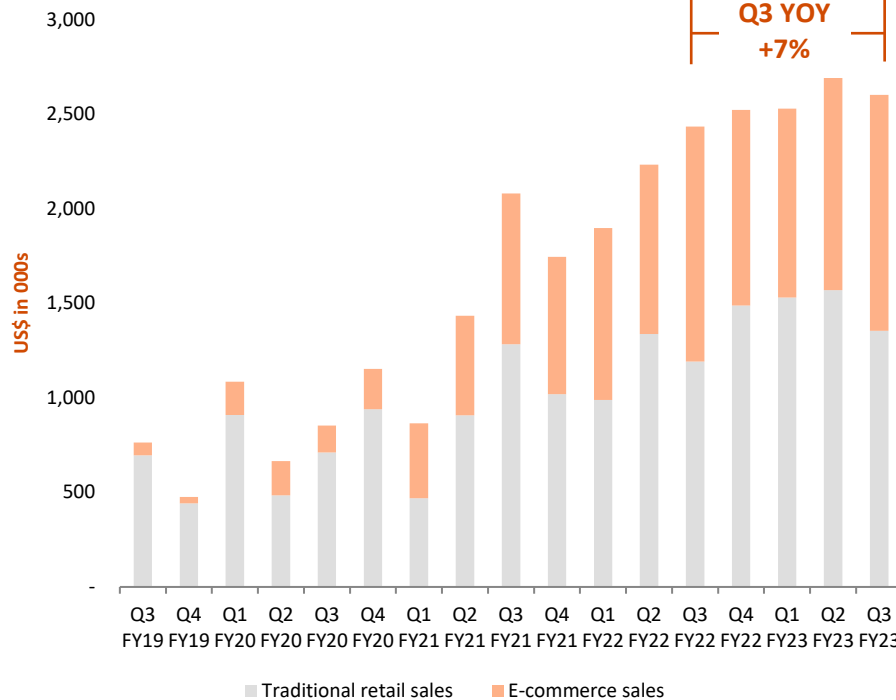
The Q3 FY2023 revenue result was underpinned by continued strong growth through e-commerce channels, highlighted by Amazon Canada quarterly net sales increasing 60% on the PCP to CAD\$0.67m (Q3 FY2022: CAD\$0.42m).

The following chart displays the trailing 12 months net sales for the period ending Q3 FY2023:



Set out below is the growth in YoY sales across e-commerce and traditional retail channels:

Quarterly net revenue - Q3FY19 to Q3FY23



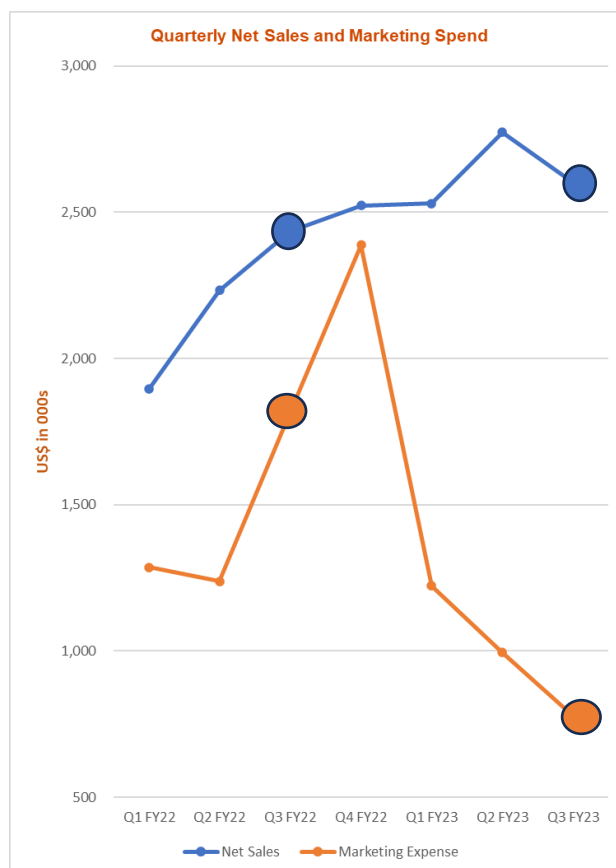
The following table summarises change in revenues and gross margins into Q3 FY2023:

	Q3 FY22	Q2 FY23	Q3 FY23	QoQ change	YoY change
Total net revenue	2,434	2,774	2,602	-6%	7%
<i>E-commerce sales</i>	1,243	1,204	1,248	4%	0%
<i>Traditional retail sales</i>	1,192	1,570	1,354	-14%	14%
Gross Margins	1,234	1,385	1,512	9%	23%
Gross Margin %	51%	50%	58%	8 ppt	7 ppt

US\$0.78m was invested in marketing during the quarter, a 57% decrease on the PCP (Q3 FY22: US\$1.82m) and in line with the Company's cash preservation initiatives.

Marketing costs as a percentage of sales decreased for a third consecutive quarter, down from 36% in Q2 FY23 and 78% in Q4 FY22 to a record low.

The following chart reflects the continued increase in net revenue and significant decrease in marketing spend:



Gross margin dollars hit a record high of US\$1.51m, up 23% on the PCP and gross margin as a percentage of net sales increased 8 percentage points on the PCP to 58% (Q3 FY2022: 51%), and 8 percentage points on the prior quarter (Q2 FY2023: 50%). The increase is attributed to the cost reduction initiatives including the supply chain optimisation.

Commentary on cash flows:

In line with an ongoing focus on cash preservation, net cash used in operating activities decreased slightly on the previous quarter to US\$1.46m (Q2 FY2023: US\$1.48m) and 47% on PCP to US\$1.46 (Q3 FY22: US\$2.78m).

With key marketing investments completed during the previous year, the Company has maintained a focus on reducing operating expenditure to extend cash life through significant reduction in marketing spend, while leveraging its market footprint to maintain revenue growth. The reduced net cash use in FY2023 is a direct result of this ongoing strategy, which is expected to continue over the coming months.

Available funds and PURE arrangements:**Placement and Entitlement Offer to raise A\$4.6m and conversion of PURE warrants:**

During the quarter, the Company raised A\$1.5m (before costs) through the issue of 33.33m new fully paid ordinary shares to new and existing professional, institutional and sophisticated investors at an issue price of \$0.045 per share.

In conjunction with the placement, the Company also completed pro rata non-renounceable entitlement offer of one fully paid share for every 2.27 shares held by eligible shareholders on the record date of 9 August 2023 at the same issue price of the placement.

Upon completion of the entitlement offer and placement of relevant shortfall from the initiative, the Company raised an additional ~A\$2.7m (before costs).

Subsequent to the quarter end, the Company also raised a further ~A\$0.4m via the exercise of Warrants by Pure Asset Management. On 25 October 2023, the Company issued 7,471,261 fully paid ordinary shares in the Company (**Shares**) to Pure Asset Management on exercise of that same number of Warrants. The additional ~\$0.4m is not recognised in the attached Appendix 4C.

Pure Asset Management (“PURE”) arrangements:

In conjunction with the aforementioned capital raising, and as approved by shareholders at the general meeting held on 26 September 2023, the Company and PURE have agreed:

- the availability period of the second tranche of PURE’s debt (A\$5.5m) will be extended from 14 October 2023 to 31 December 2024; and
- the second tranche will be made available if PURE consents (at its discretion) to make it available at the time the Company seeks to draw it down.

PURE has also agreed that the exercise price of the remaining ~14.9m Warrants will have a ‘floor price’ of the adjusted price after this capital raising (in circumstances where the exercise price of the warrants could otherwise decrease in the future in the event of a subsequent dilutive capital raising in accordance with their terms of issue).¹

Use of funds and ongoing focus on reducing net cash used in operating activities:

Capital from the aforementioned placement and entitlement offer will be deployed towards product development and manufacturing, strategic marketing initiatives and ongoing expansion of sales in North America and other territories. These objectives will be undertaken in collaboration with stringent cost management initiatives across other aspects of the business with a strong focus on reduced cash burn through improved return on marketing.

Available funds:

Cash and cash equivalents at the end of the quarter were US\$2.7m. An additional A\$0.4m was received subsequent to quarter end from the exercise of the PURE warrants as mentioned above.

¹ See ASX Announcement ‘Notice of Meeting’ dated 24 August 2023.

In addition to cash on hand, at PURE's discretion, the Company may access the second tranche of PURE's debt equal to A\$5.5m.

Operational overview:

Leading sales broker appointed to expand Canadian market footprint at lower cost:

During the quarter, the Company made the strategic decision to appoint LeBeau Excel ('LeBeau') as its new sales broker. LeBeau is a leading health and wellness products broker with a major footprint in the Canadian market.

Strategically, the agreement allows the Company the ability to significantly expand its addressable market across Canadian bricks & mortar retail channels, broadening its scope from pharmacy and grocery to include store chains in the health & wellness sector such as Whole Foods.

Headquartered in Toronto, LeBeau has a national sales footprint with a dedicated field team of over 15 full-time sales staff visiting stores every day. LeBeau representatives maintain strong relationships with major natural health distributors in Canada and serve an extensive client base of the major retailers including Wholefoods and all major existing HydraLyte North America accounts such as Walmart Canada.

The agreement will complement HydraLyte North America's existing distribution footprint in Canada, which includes Shopper's Drug Mart – one of the largest pharmacy network in the country with 1,300 stores nationally².

As previously advised, Q3 FY23 revenue growth was affected slightly because of the transition, primarily due to the associated warehouse transition.

Partnership agreement with RooLife Group to expand footprint in China:

Highlighting the Company's cost-effective approach to sales expansion, HydraLyte appointed specialist e-commerce company, RooLife Group Limited ("RooLife") (ASX: RLG) to exclusively market, sell and distribute HydraLyte products in China.³

The agreement aligns with HPC's strategy to further expand its global addressable market via a targeted partnership approach which provides cost effective sales expansion through a partner group with an established distribution footprint.

The partnership provides HydraLyte with a unique access point to the China consumer market, which RooLife has built over a long term in line with rigorous compliance standards for imported goods.

RooLife is currently on boarding the Company's products and is in well progressed discussions with a number of ecommerce and bricks & mortar retailers in China to stock HydraLyte products. Additional updates on sales growth will be made as orders materialise.

² <https://corporate.shoppersdrugmart.ca/en/about-our-company>

³ See ASX Announcement 'HPC partners with RLG to expand global distribution in China' dated 22 August 2023

Cancellation of Options:

Subsequent to the end of the quarter, in October FY23, the Company cancelled twenty million options to help optimize and strengthen its capital structure.

Issue of Shares:

Cleansing Statement

The Company hereby gives notice under section 708A(5)(e) of the Corporations Act 2001 (Cth) (Act) that:

1. on 25 October 2023 the Company completed the issue and allotment of 7,471,261 Shares.
2. the Company issued the Shares without disclosure to investors under Part 6D.2 of the Act;
3. as at the date of this notice, the Company has complied with:
 - a. the provisions of Chapter 2M of the Act as they apply to the Company; and
 - b. sections 674 and 674A of the Act; and
4. as at the date of this notice there is no 'excluded information' (as that term is defined in section 708A(7) and (8) of the Act).

Management commentary:

Hydralyte North America CEO Oliver Baker said: *"Hydralyte North America has delivered another solid quarter of net sales, while delivering on its stated strategy to maintain costs, while also generating top-line revenue growth. Pleasingly, the Company has also delivered solid gross margin increases, which is a direct result of our continued optimisation of our supply chain.*

"Further, the Company continued its strong operational performance during the quarter and entered into a number of agreements which should underpin growth over the coming months. This is highlighted by commercial terms being reached with LeBeau - one of the leading sales brokers for health & wellness products in the Canadian market, and RooLife, our new China distributor.

"This agreement followed a period of extensive collaboration between the parties, and we're confident that LeBeau's national market footprint and extensive industry networks offer the ideal launch pad for the next step-change in sales growth for Hydralyte North America products.

"While the transition did effect quarter on quarter growth slightly, we are confident this will be made up during the current quarter and beyond."

ENDS

This announcement was authorised for release by the Board of Hydralyte North America.

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Forward Looking Statements:

This ASX release includes certain forward-looking statements that are based on information and assumptions known to date and are subject to various risks and uncertainties. Forward-looking statements are based on:

- assumptions regarding the Company's financial position, business strategies, plans and objectives of management for future operations and development and the environment in which the Company will operate; and
- current views, expectations, and beliefs as at the date they are expressed, and which are subject to various risks and uncertainties.

Actual results, performance or achievements could be significantly different from those expressed in, or implied by, these forward-looking statements. Such forward-looking statements are not guaranteeing of future performance and involve known and unknown risks, uncertainties, and other factors, many of which are beyond the control of HydraLyte North America. These factors may cause actual results to differ materially from those expressed in the statements contained in this announcement.

The Company disclaims any responsibility for the accuracy or completeness of any forward-looking statement. The Company disclaims any responsibility to update or revise any forward-looking statements to reflect any change in the Company's financial condition, status or affairs or any change in the events, conditions, or circumstances on which a statement is based, except as required by law. The projections or forecasts included in this announcement have not been audited, examined, or otherwise reviewed by the independent auditors of the Company.

You must not place undue reliance on these forward-looking statements.

Appendix 4C

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

Name of entity

The Hydration Pharmaceuticals Company Limited

ABN

83 620 385 677

Quarter ended ("current quarter")

30 September 2023

Consolidated statement of cash flows	Current quarter \$US'000	Year to date (9 months) \$US'000
1. Cash flows from operating activities		
1.1 Receipts from customers	2,284	7,113
1.2 Payments for		
(a) research and development	-	-
(b) product manufacturing and operating costs	(950)	(2,642)
(c) advertising and marketing	(841)	(2,439)
(d) leased assets	-	-
(e) staff costs	(587)	(2,151)
(f) administration and corporate costs	(1,333)	(4,006)
1.3 Dividends received (see note 3)	-	-
1.4 Interest received	-	-
1.5 Interest and other costs of finance paid	(127)	(397)
1.6 Income taxes paid	-	-
1.7 Government grants and tax incentives	-	-
1.8 Other (provide details if material)	90	(12)
1.9 Net cash from / (used in) operating activities	(1,462)	(4,536)
2. Cash flows from investing activities		
2.1 Payments to acquire or for:		
(a) entities		
(b) businesses		
(c) property, plant and equipment		
(d) investments		
(e) intellectual property		
(f) other non-current assets		

Consolidated statement of cash flows		Current quarter \$US'000	Year to date (9 months) \$US'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		

3.	Cash flows from financing activities		
3.1	Proceeds from issues of equity securities (excluding convertible debt securities)	2,704	2,704
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	(236)	(241)
3.5	Proceeds from borrowings		
3.6	Repayment of borrowings		
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	2,468	2,463

4.	Net increase / (decrease) in cash and cash equivalents for the period		
4.1	Cash and cash equivalents at beginning of period	1,739	4,688
4.2	Net cash from / (used in) operating activities (item 1.9 above)	(1,462)	(4,536)
4.3	Net cash from / (used in) investing activities (item 2.6 above)		

Consolidated statement of cash flows		Current quarter \$US'000	Year to date (9 months) \$US'000
4.4	Net cash from / (used in) financing activities (item 3.10 above)	2,468	2,463
4.5	Effect of movement in exchange rates on cash held	(18)	112
4.6	Cash and cash equivalents at end of period	2,727	2,727

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 \$US'000	Previous quarter \$US'000
5.1	Bank balances	2,727	1,739
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)	2,727	1,739

6.	Payments to related parties of the entity and their associates	Current quarter \$US'000
6.1	Aggregate amount of payments to related parties and their associates included in item 1	
6.2	Aggregate amount of payments to related parties and their associates included in item 2	
<i>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.</i>		

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 \$US'000	Amount drawn at quarter end \$US'000
7.1	Loan facilities	4,388	4,388
7.2	Credit standby arrangements		-
7.3	Other (please specify)	-	-
7.4	Total financing facilities	4,388	4,388
7.5	Unused financing facilities available at quarter end*		-
7.6	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.		

8.	Estimated cash available for future operating activities	\$US'000
8.1	Net cash from / (used in) operating activities (item 1.9)	(1,462)
8.2	Cash and cash equivalents at quarter end (item 4.6)	2,727
8.3	Unused finance facilities available at quarter end (item 7.5)*	-
8.4	Total available funding (item 8.2 + item 8.3)	2,727
8.5	Estimated quarters of funding available (item 8.4 divided by item 8.1)	1.86
	<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>	
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: Yes the company expects to maintain a similar level of net operating cash flows for the time being, with those cash flows expected to improve with growth and continued cost management.	
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: Yes the company has consistently raised cash to meet the requirements of the company and expect to continue to do so. The company also has a facility in place with Pure Asset Management wherein the company has access, at the discretion of Pure Asset Management, of A\$5.5m.	

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: Yes the company believes it will be able to continue its operations and meet its business objectives based on the above comments.

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: 31 October 2023

Authorised by: By the board
(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.
- * The company has gone into a trading halt on 31 July 2023 to release the news of a capital raise. As part of the raise, The Hydration Pharmaceuticals Company has conditionally agreed with the debt provider, Pure Asset Management, to release the obligation of providing the second tranche of the debt facility as it is listed in this document with the intention that the capital raise will replace additional debt. The Hydration Pharmaceuticals Company Limited has the right under ASX rule 7.1 to access the second tranche, but the right to access will expire on August 5th without further shareholder approval.