9255 Towne Center Drive, Suite 930
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Company Announcement
ASX: HPC

DATE: 31/08/2023

All amounts in $US and unaudited unless otherwise specified.

1H FY23 Half Year Report and Appendix 4D: Hydralyte North America Achieves Record Revenue and Gross Profit

KEY HIGHLIGHTS

- **Record net revenue achieved for the half of US$5.3m, representing 28% growth on prior corresponding period ('PCP') (1H FY2022: US$4.1m)**
- **Strong half year revenue result underpinned by monthly net sales of US$1.09m in June - demonstrating strong traction ahead of North American summer months**
- **Loss from ordinary activities improved 17% following ongoing review of cost base and implementation of initiatives to reduce capital expenditure**
- **Gross margin remains stable at 49% or US$2.6m, representing a 1% decrease from the last half (2H FY2022: 49%)**
- **Continued execution of strategy to decrease expenditure and extend cash reserves through significant reduction in marketing costs following heavy brand investments in FY2022**
- **6 new product launches well progressed – One new product shipped in Q2 and more launching in Q3 to underpin ongoing sales growth**

Hydration solutions company **The Hydration Pharmaceuticals Company Limited (ASX: HPC) ("Hydralyte North America" or "the Company")** is pleased to provide its half year activities report and Appendix 4D for the six month period ended 30 June 2023 (the "half year" or "1H FY2023").

Financial overview:

Revenue for the half year increased 28% on PCP (1H FY2022: US$4.1m) and 7% on the previous half (2H FY2022: US$5.0m) resulting in record of US$5.3m. The rise in revenues is attributed to higher shipments into new and existing North American retailers driven by record retail shelf sell-through, new product launches and ongoing sales to retail customers through eCommerce channels.

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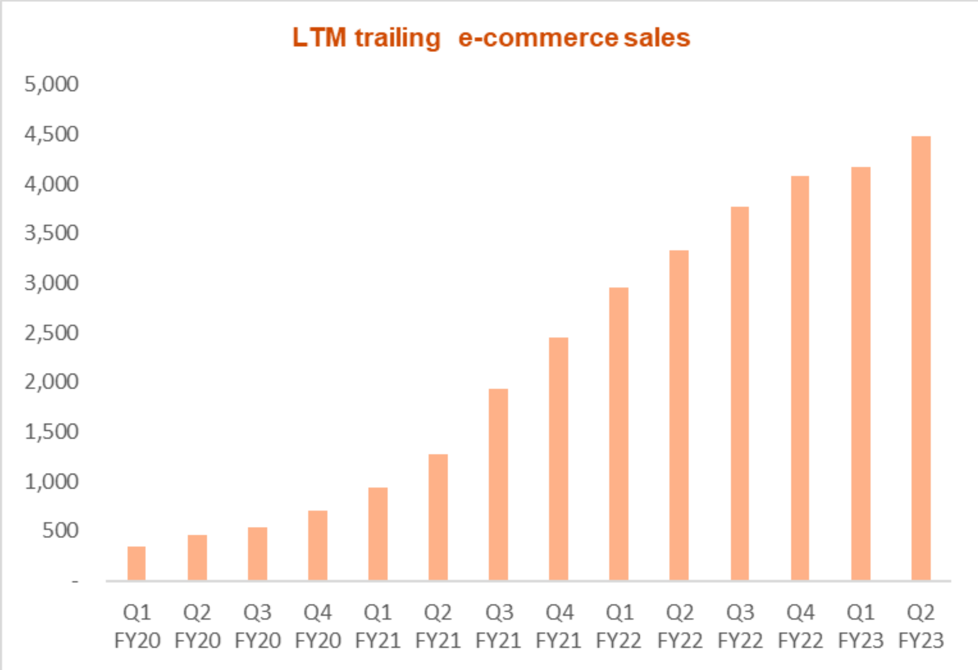
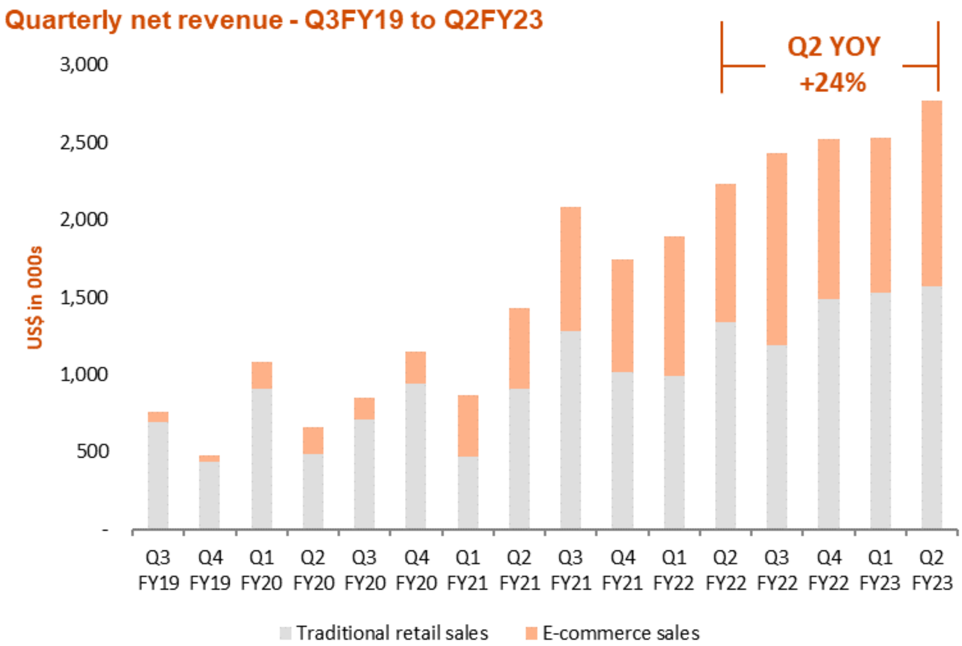
The following chart displays the eCommerce trailing 4-quarter growth through Q2 FY2023:



The following chart displays the strong YoY growth (Q2 FY2023 beat seasonally highest Q3 FY2022):



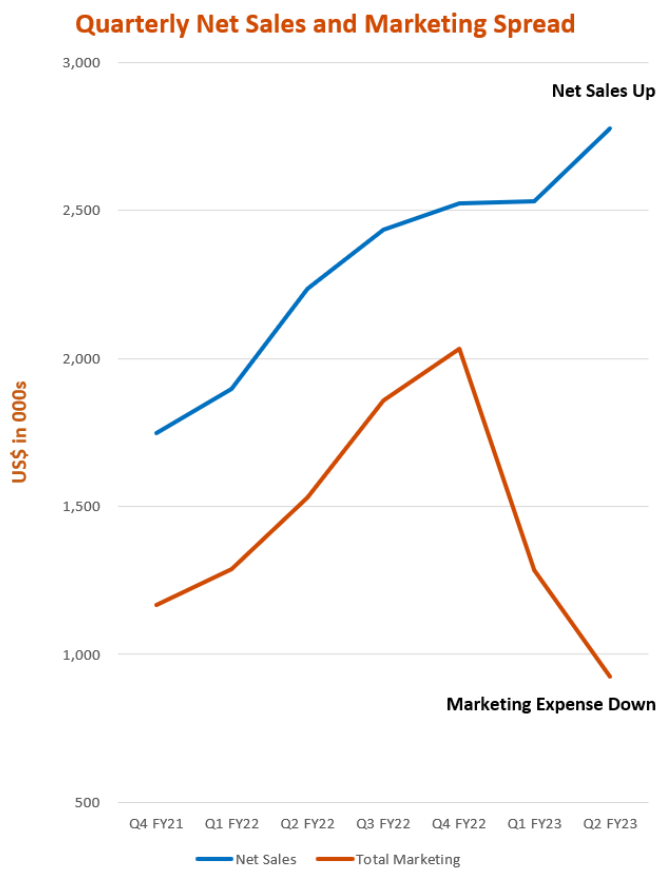
Alongside a material increase in revenue, the Company considerably reduced sales and marketing spend for the half to US$3.7m, down from US$5.3m in 2H FY2022, while sales and marketing as a percentage of net sales decreased from 107% in 2H FY22 to 70% in 1H FY23. Digital Advertising spend was reduced to US$1.0m down from US$1.7m in 2H FY2022. Influencer related spend was reduced to US$0.6m down from US$0.9m. Below, is a table summarising the sales and marking spend movements:

Sales and Marketing Spend Movement	2H FY2022	1H 2023	Variance
Digital Advertising	1,723	977	(746)
Influencer	935	559	(376)
Other	644	443	(201)
Consumer	263	85	(177)
Asset Development	120	9	(110)
Website Development	108	21	(87)
Selling Related Costs	1,502	1,634	131
Total	**5,294**	**3,729**	**(1,566)**

A $250,000 non-cash payment in the form of equity was granted last year to prominent actress, entrepreneur and brand ambassador Ms Shay Mitchell, is included in the marketing expense. Hydralyte recognised SBP costs of US$0.1m in 1H FY2023 related to the equity grant.

The decrease in marketing spend and increased revenue generation highlights the Company's ability to achieve its stated strategy to convert its existing brand awareness in North America into consistent sales while lowering expenses and driving growth in net earnings. The Board and management remain focused on stringent capital management.

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



To further prioritise revenue growth and net cashflow, the Company has modified its product profile to eliminate the lowest performing products. HPC is selling these low performing products off through discount channels to generate sales from its strongest selling inventory and was therefore left with temporarily repressed margin from this process. Although the percentage margin decreased slightly from the PCP, the total margin dollars increased by 15% with the increase in net revenues.

EBITDA loss decreased on the last half by US$1.6m to US$3.6m (2H FY2022 loss US$5.2m). The EBITDA increase was driven by a US$0.1m increase to gross profit dollars, and the aforementioned US$1.6m decrease to sales and marketing related expenses. These improvements were partially offset by a US$0.1m increase to administrative expenses.

On the prior half, EBITDA as a percentage of net sales improved 30% (2H FY2022 US$5.2m). Cash expenditures for the half, compared to 2H FY2022, decreased US$2.3m mainly due to sales and marketing cash expenditures dropping US$2.3m to US$3.3m (2H FY2022 US$5.6m), a US$0.9m expenditure decrease in inventory value, partially offset by US$0.5m increase in cash expenditures for prepaids, US$0.3m increase in finance expenses and US$0.2m increase in employee benefits expense, and US$0.3m increase for administration expenses.

Cash Expenditure Categories	HoH Variance $
Sales and Marketing	2,315
Inventory	942
Trade and Other Payables	393
Other	(1)
Receipts from customers	(67)
Employee Benefits	(219)
Administration	(287)
Finance Expenses	(288)
Prepaids	(478)
Total	**2,311**

Gross margin as a percentage of sales remained steady at 49%, down slightly on the last half (2H FY2022: 49%). Gross Margin dollars at US$2.6m increased 5% on the last half (2H FY2022: US$2.4m)

The following table summarises change in revenues and gross margins into Q2 FY2022:

	1H FY22	2H FY22	1H FY23	HoH change	YoY change
Total Unaudited Net Revenue	4,131	4,957	5,304	7%	28%
E-commerce sales	1,804	2,278	2,204	-3%	22%
Traditional retail sales	2,327	2,679	3,100	16%	33%
Gross Margins	2,246	2,450	2,581	5%	15%
Gross Margin %	54.4%	49.3%	48.6%	(6)ppt	(1)ppt
EBITDA	(3,786)	(5,206)	(3,645)	-30%	-4%

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Operational overview:

Hydralyte announced a Placement and Entitlement Offer to raise up to ~4.8m

During the period, Hydralyte North America announced that it will undertake a share placement to raise A$1.5m (before costs) and a non-renounceable partially underwritten Entitlement Offer to raise up to an additional A$3.3m at an offer price of A$0.045 per share. The Company has subsequently completed the placement of A$1.5m with the Entitlement Offer progressing with expected completion in September.

- **Placement**
  During the period, the Company received firm commitments to raise A$1.5m (before costs) through the issue of 33.33 million new fully paid ordinary shares to new and existing professional and sophisticated investors at an issue price of A$0.045 per share. These funds were received subsequently to the first-half, in August 2023.

- **Entitlement Offer**
  In conjunction with the Placement, the company will undertake a pro rata, non-renounceable entitlement offer of one new Share for every 2.27 existing Share held by eligible shareholders at 7:00pm (Melbourne time) on Wednesday, 9 August 2023. The Entitlement Offer will raise up to approximately A$3.3m (before costs) at the Offer Price by the issue of up to approximately 72.4m Shares (depending on the level of take-up by shareholders).

  The Entitlement Offer is open to eligible shareholders, which are Hydralyte North America shareholders as at 7:00pm (AEST time) on Wednesday, 9 August who have a registered address in Australia or New Zealand (or any other jurisdiction determined by the Board). The Entitlement Offer is non-renounceable which means that entitlements are not transferable and cannot be traded on the ASX (or any other exchange) or transferred privately.

- **Options**
  Participants in the Placement and Entitlement Offer will be offered one attaching option for every two new Shares issued. Each option will be exercisable at A$0.07, on or before 31 December 2025.

  The issue of Options to Placement participants will be conditional on shareholder approval at an EGM to be held in mid-September 2023.

Pure Asset Management (“PURE”) Arrangements

In conjunction with the capital raising, the Company and PURE have agreed that (conditional on completion of the capital raising):

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

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In addition, PURE has committed to exercise approximately 7.5 million of the Warrants granted to it on completion of the capital raising at the 'adjusted price' (refer to the Notice of Annual General Meeting dated 4 April 2023 for further details) for expected total proceeds of approximately A$0.4m. PURE has also agreed, subject to successful exercise of the Warrants and shareholder approval, 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).

PURE has also agreed to sub-underwrite approximately A$0.6m worth of shortfall Shares under the Entitlement Offer.

Additional marketing and growth initiatives:

The Company launched a time square billboard ad campaign with accompanying high-profile influencers to a video format displayed in New York. The promotion will run through to the end of December and is expected to increase brand awareness. The billboard ad campaign will run in conjunction with various social media platform posts.

Streamlined Canadian manufacturing:

During the half year, the Company began manufacturing powder sticks at its new Canadian-based contract manufacturer for the Canadian market. This is viewed as a strategic priority and optimises HPC's manufacturing process from a North American facility, allowing the Company to capitalise on its existing North American distribution channels.

The manufacturing change is expected to lead to a reduction in cost of goods sold, cheaper freights and an increase to gross margins on the powder stick range.

In Q1 FY2023, the company has begun manufacturing liquids at its US-based contract manufacturer for the Canadian market. This is viewed as a strategic priority and optimises HPC's manufacturing process from a centralised production hub, allowing the Company to capitalise on its existing North American distribution channels.

The manufacturing change is expected to lead to a reduction in costs of goods sold, cheaper freights and an increase in gross margin on the liquid range.

New product development and recent launches:

Further product development initiatives and launches remain a focus. The Company successfully launched 2 new products, Hydralyte+ Apple Cider Vinnegar and Hydration plus Liver Support Tub during the half and July subsequent to the activity period covered in this report. The new stock keeping units (SKUs) are currently being shipped to retailers in the US.

Hydralyte North America is also progressing 6 new products for launch into the US and Canadian market, with the majority set to debut by years' end, providing potential increased uptake and enhanced sales. The proposed launches will include new flavours, larger serving sizes, and increased Hydralyte+ products.

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Comments on Cash Flows:

Net cash used in operating activities was US$2.9m, which included a US$2.3m reduction of sales and marketing related expenses on the prior half (2H FY2022) as the Company has increased focus on reducing operating expenditure to extend cash life through significant reduction in marketing spend, while leveraging its market footprint to maintain record revenue growth.

Non-cash working capital is expected to decrease as the company is focused on improving its product portfolio by continuously reviewing and creating new innovative products to drive sales. The company will also continue to leverage the new supply chain to improve lead times, and improve margins.

As at 30 June, Hydralyte North America had cash and cash equivalents of US$1.7m. In addition, at the discretion of PURE Asset Management, the Company may draw the second tranche of A$5.5m as outlined above. Additionally, as outlined above, subsequent to the end of the first-half, the company has successfully completed a A$1.5m placement offer and is progressing an additional entitlement offer of up to approximately A$3.3m. The directors believe that the Group will be successful in growing the business to a breakeven point and eventually profitability.

Management commentary:

Hydralyte North America CEO Oliver Baker said: *"The Company has delivered very strong first half results, which show continued growth in revenue and a material reduction in marketing spend. This further highlights Hydralyte North America's ability to deliver on its strategy, which aims to convert our leading market footprint into consistent sales on a decreased cost base to drive net earnings.*

"The Board and management remain increasingly focused on cash preservation, while pursuing a number of high margin growth opportunities. This includes a number of new product introductions scheduled for the second half, increased sales into new countries and potential expansion into new verticals. We look forward to providing additional updates as these developments materialise."

ENDS

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

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