

## HILL STREET BEVERAGE COMPANY INC.

### MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE-MONTH AND NINE-MONTH PERIODS ENDING MARCH 31, 2022

The following management's discussion and analysis ("MD&A") provides a review of the activities, results of operations and financial condition of Hill Street Beverage Company Inc. (the "**Company**" or "**Hill Street**") for the three months and nine months ended March 31, 2022, in comparison with the three months and nine months ended March 31, 2021. These comments should be read in conjunction with the audited financial statements for the years ended June 30, 2021, and June 30, 2020, and accompanying notes included therein, which have been prepared in accordance with International Financial Reporting Standards ("**IFRS**"). This MD&A has been prepared as of May 30, 2022. Additional information relating to Hill Street is available on SEDAR.

All amounts are stated in Canadian dollars unless otherwise identified.

#### **FORWARD-LOOKING STATEMENTS**

Except for the historical information contained herein, the discussion in this MD&A contains certain forward-looking statements that involve risks and uncertainties, such as statements of Hill Street's plans, objectives, strategies, expectations and intentions. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may", "will", "expect", "intend", "anticipate", "seek", "plan", "believe" or "continue" or the negatives of these terms or variations of them or similar terminology. Although Hill Street believes that the expectations and assumptions reflected in these forward-looking statements are reasonable, undue reliance should not be placed on these forward-looking statements. These forward-looking statements are not guarantees and reflect Hill Street's views as of May 30, 2022 with respect to future events. Future events are subject to certain risks, uncertainties and assumptions, which may cause actual performance and financial results to differ materially from such forward-looking statements. The forward-looking statements, including the statements regarding expected volumes, operating efficiencies, and costs are based on, among other things, the following material factors and assumptions: sales volumes in the quarter will increase; no material changes in consumer preferences; brewing, blending, and packaging efficiencies will improve; the cost of input materials for brewing and blending will increase; competitive activity from other manufacturers will continue; foreign currency exchange rates will change; no material change to the regulatory environment in which Hill Street operates and no material supply, cost or quality control issues with vendors. Readers are urged to consider the foregoing factors and assumptions when reading the forward-looking statements and for more information regarding the risks, uncertainties and assumptions that could cause Hill Street's actual financial results to differ from the forward-looking statements, to also refer to the remainder of the discussion in this MD&A, Hill Street's various other public filings as and when released by Hill Street. The forward-looking statements included in this MD&A are made only as of May 30, 2022, and, except as required by applicable securities laws, Hill Street does not undertake to publicly update such forward-looking statements to reflect new information, future events or otherwise.

## DESCRIPTION OF THE BUSINESS

**Hill Street** is a progressive non-alcoholic beverage and cannabis infusion technology solutions company that is fundamentally transforming its legacy business model to embrace a more profitable and more scalable global growth agenda. We are pioneering the space where craft consumer products meet bioscience by combining our deep CPG expertise and brands with our rights to use **Lexaria Bioscience Corp's** ground-breaking **DehydraTECH™** patent portfolio for product development, licensing and B2B or B2C sales of cannabis ingredients or products on a global scale.

The Company currently has three lines of business:

### 1. Hill Street Alcohol-Free Beverages

This line represents the legacy consumer beverage marketing and distribution business. It includes Vin(Zero) alcohol-free wine in Canada, and on a smaller scale, in the United States and Australia. It is sold in retail chain stores through Canadian distributors, exported outside of Canada through foreign distributors and offered direct to consumers online at [www.hillstreetbeverages.com](http://www.hillstreetbeverages.com).

### 2. Hill Avenue Cannabis Brands

Hill Avenue Cannabis Brands focuses on business-to-consumer (B2C) cannabis edibles products for a growing global market. At present, this line is focused on cannabis-infused (V)ia Regal consumer beverages that were launched in Canada in May of 2021, including (V)ia Regal Pink and White Grape Sparklers.

### 3. Hill Avenue Cannabis Technologies

Hill Avenue Cannabis Technologies' business provides DehydraTECH™-enabled business-to-business (B2B) solutions for both extractors/ingredient suppliers and consumer packaged goods (CPG) manufacturers whose products are infused with cannabis and or hemp extracts. This B2B business line licenses global usage rights for DehydraTECH™ patented intellectual property acquired from Lexaria CanPharm ULC, a subsidiary of Lexaria Bioscience Corp. (together, with Lexaria CanPharm ULC, "**Lexaria**") in December 2020.

DehydraTECH™ is one of the world's newest technologies specifically designed to improve the efficacy of orally administered bioactive molecules, including cannabinoids. DehydraTECH™ improves the way active pharmaceutical ingredients (APIs), such as those found in cannabis, enter the bloodstream by promoting healthier delivery methods and increasing the effectiveness of fat-soluble active molecules in product forms such as the many forms of cannabis-infused edibles and topicals.

Findings from extensive scientific studies on the DehydraTECH™ technology performed by its creator Lexaria include:

- **Increased bioavailability up to 5-10x** – to equate to blood absorption by inhalational delivery
- **Increased brain permeation up to 19x** – as demonstrated in animal studies
- **Avoids first-pass liver metabolism** - mitigating unwanted side effects
- **Reduced time of onset** – effects are felt within 15-20 minutes vs. 60-120 minutes
- **Masks unwanted tastes** – eliminating the need for sugar-filled edibles

The evolution of Hill Avenue Cannabis Technologies has fundamentally changed the Hill Street business model in several significant ways – financially, geographically, and operationally.

**1. Financial Impact**

The overall financial efficiency of the DehydraTECH™ technology licensing business is superior to the legacy beverage business, bringing significantly higher margins and avoiding the requirements for finished product inventory and working capital investment that are required in the beverage businesses.

**2. Geographical Impact**

With the acquisition of the global rights to the DehydraTECH™ patents for use in the production of products containing 0.3% or greater THC which acquisition included pre-existing DehydraTECH™ licensing agreements with certain US LPs, Hill Avenue immediately entered the U.S. cannabis market, generating revenues from licensing partners already operating across multiple U.S. states.

Because of the nature of the DehydraTECH™ licensing business, the ability to expand into global markets is facilitated by a licensing model in which we can easily expand our footprint without major capital or operating expenses.

**3. Operational Impact**

The DehydraTECH™ licensing business is a B2B business model that utilizes the Company's prior CPG product development and marketing knowledge along with its retail experience, to accelerate its agenda of becoming a premium cannabis infusion technology / ingredient solutions provider to companies looking to market premium cannabis edibles.

By combining Hill Street's strengths with those of DehydraTECH™ creator Lexaria's and Hill Street's downstream DehydraTECH™ licensees, the Company has created an ecosystem with robust capabilities in bioscience, food science, new product format and recipe development.

**Q3 HIGHLIGHTS**

Fiscal Year Q3 was another very successful quarter for Hill Street across a wide range of financial and operating results for all three verticals of the Company's multi-business-line model.

**Q3 consolidated net revenues grew a strong 34% versus same quarter of the previous year.**

Solid revenue growth was delivered across all three business units as outlined below:

**1. Hill Avenue Cannabis Technologies revenue grew 65% year-on-year through the footprint and product expansion of existing U.S. DehydraTECH™ licensees and the early impact of the Hill Street & Dehydr8 pilot launch in Michigan.**

- The FY22 Q1 launch of DehydraTECH™ licensee Cannadips' new fast-acting THC-infused line of its top-selling CBD dip pouch products in California and the FY22 Q2 expansion of DehydraTECH™ licensee's popular "Nuka 1906" products into Arizona added to the the Company's organic growth with existing licensees.
- The first early revenues from the Company's pilot launch with its US commercialization partner Dehydr8, LLC ("**Dehydr8**") in Michigan were recognized in the quarter, with licensing revenues expected from the major DehydraTECH™ licensing deal announced March 29, 2022 with Lume Cannabis Co. ("**Lume**") not even yet impacting reported revenues this quarter. Lume is the top

vertically integrated cannabis operator in Michigan and the largest single-state cannabis operator in the U.S.<sup>1</sup>

- New DehydraTECH™ licensing agreements for the expansion of Dehydr8's rights into Illinois and Massachusetts for potential B2B and B2C applications were announced March 1, 2022 and are also not yet impacting revenues.

**2. Hill Avenue Cannabis Brands' (V)ia Regal cannabis beverages, which were launched after Q3 FY21 and first shipped in Q4 FY21, provided new incremental revenues which were not present a year ago.**

- (V)ia Regal cannabis beverage revenues continued to grow in Q3 as we worked with our Health Canada-licensed manufacturing and sales partner Molecule Inc. to increase sales in current geographies as well as push distribution in additional Canadian provinces.

**3. Hill Street Brands revenue increased as alcohol-free beverage sales returned to a growth trend, delivering a 19% increase in net revenues versus the same quarter a year ago.**

- Q3 was a strong quarter for the Company's alcohol-free beverage business as we worked closely with our full commercial ecosystem, from supply chain to distribution and retail, to drive improved business results and efficiencies. As discussed in the Q2 FY22 MD&A, the operational cycles and timing of our purchasing, production, product shipment, and product sales have a significant impact on the quarterly results of this line of business, and therefore, we believe that looking at the longer-term patterns of this business provides a more accurate view of its health than simply viewing quarterly fluctuations. The Q3 revenue growth of our alcohol-free wines brought the year-to-date total net revenue steady compared to a year ago, despite the loss of the discontinued alcohol-free beer revenues that were present a year ago.

**Q3 consolidated gross profit grew even more dramatically than revenues, increasing a full 40% vs. the same quarter of the previous year**

We continue to see the positive impact of the DehydraTECH™ licensing business on the Company's margins. In addition to driving higher gross profit dollar growth, gross profit as a percentage of gross revenue increased to 48% in Q3 from 44% in the prior year. This increase in gross profit margin was achieved despite significant increases in freight costs related to the global supply chain problems.

**Hill Avenue Cannabis Technologies**

**The Company continued actively building its Hill Avenue Cannabis Technologies DehydraTECH™ licensing line of business**

The Company continued executing on building its B2B DehydraTECH™ licensing business which is focused on:

1. licensing usage rights for DehydraTECH™ patented global intellectual property to licensed cannabis CPG companies and brands for application in their cannabis-infused consumer products; and
2. licensing usage rights to extractors for converting cannabis oil into DehydraTECH™ powder to preserve cannabinoid potency and extend shelf life in the supply chain for cannabis-infused CPG brands and products.

During the fiscal year Q3, the Company worked aggressively on expanding licensing relationships for DehydraTECH™ intellectual property with companies operating commercially in the United States in Arizona, California, Colorado,

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<sup>1</sup> <https://www.wxyz.com/news/community-connection/an-inside-look-at-lume-cannabis-co-the-top-marijuana-producer-in-michigan-and-the-country>

Illinois, Massachusetts, Michigan, and Oklahoma. Additional expansion markets were also a focus of the Company for the quarter, including the expansion of license rights to our US commercialization partner DeHydr8 into Oregon, which expansion was announced on May 24, 2022. This addition added a state with \$1.1B in total addressable market cannabis sales to our operating footprint<sup>2</sup>. As noted earlier, the financial impact of the expansion efforts in Illinois, Massachusetts and Oregon are not yet reflected in the reported revenue results and we expect that they will have significant positive impact in future quarters.

As of May 30, 2022, we now have licensing arrangements in states that represented approximately \$15.89B in total addressable market cannabis sales in 2021<sup>3</sup>.

The total US addressable market is projected by BDS Analytics to reach \$28B in sales in 2022 and to grow to \$48B by 2026<sup>4</sup>

### **A major new licensee was signed in the Michigan pilot market to bring Michigan consumers more products powered by DehydraTECH™**

During the quarter, the Company's US commercialization partner Dehydr8 also signed a major new licensing deal in the Michigan market with Lume Cannabis Co., the top vertically integrated cannabis operator in Michigan and the largest single-state cannabis operator in the U.S. The deal involves multi-year licensing of the DehydraTECH™ technology by Lume and related services to be provided by Dehydr8, to power a range of THC-infused consumer products by Lume utilizing the patented DehydraTECH™ process. Lume has thirty-one (31) dispensaries operating in the state. Like the recent Dehydr8 state expansions, the impact of this major new sublicensee in Michigan is not reflected in the Q3 financial results and is expected to contribute significant positive impact in future quarters.

### **Expanded DehydraTECH™ licensing relationship with DeHydr8 to enter into new markets and to drive broader consumer product formats and further the commercialization of the B2B and B2C DehydraTECH™ businesses**

Based on the success of D8's team since acquiring DehydraTECH™ rights from the Company in Michigan in signing top-quality Michigan licensed producers to produce THC products powered by DehydraTECH™, in Q3, the Company expanded the reach of D8's DehydraTECH™ rights to add the new states of Illinois and Massachusetts. Granting DehydraTECH™ rights to D8 in Illinois and Massachusetts represent further steps that the Company is taking to rapidly mobilize and monetize the patented DehydraTECH™ technology by deploying a state-by-state US rollout model to continue to accelerate the Company's financial and operational progress. Hill Street and Dehydr8 have used their joint experiences gained in Michigan to create a scalable operating model for state-by-state expansion of the DehydraTECH™ licensing business.

### **Important R&D and product innovation efforts advanced in Michigan pilot market**

One of the important initial drivers of the Company's decision to launch a pilot program with Dehydr8 in Michigan was to quickly gain access to licensed, experienced individuals and entities who could work directly with the DehydraTECH™ process. The Hill Street team, together with the team that has been assembled in Michigan, collectively have extensive experience in developing innovative and differentiated consumer products and product

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<sup>2</sup> "Oregon Cannabis Ekes Out Modest 2021 Sales Again, Hits Another High Mark", Portland Business Journal, January 3, 2022,

<https://www.bizjournals.com/portland/news/2022/01/03/oregon-cannabis-grew-in-2021-but-slower-than-ever.html>

<sup>3</sup> <https://azdor.gov/reports-statistics-and-legal-research/marijuana-tax-collection>,

<https://www.cdtfa.ca.gov/dataportal/charts.htm?url=CannabisTaxRevenues>, <https://cdor.colorado.gov/data-and-reports/marijuana-data/marijuana-sales-reports>, <https://www.idfpr.com/profs/adultusecan.asp>,

[https://www2.illinois.gov/sites/mcpp/Pages/update01032022\\_mcpp.aspx](https://www2.illinois.gov/sites/mcpp/Pages/update01032022_mcpp.aspx), <https://www.wbjournal.com/article/mass-doubled-its-all-time-adult-use-cannabis-sales-in-2021>, <https://mjbizdaily.com/oklahoma-medical-marijuana-businesses-demand-steps-to-combat-illicit-grows/>,

<https://www.bizjournals.com/portland/news/2022/01/03/oregon-cannabis-grew-in-2021-but-slower-than-ever.html>

<sup>4</sup> "It Isn't Magic, It's Data – Successfully Expand Your Cannabis Business", BDS Analytics, [https://bdsa.com/wp-content/uploads/2022/05/BDSA-It-Isnt-Magic-Its-Data\\_Successfully-Expand-Your-Cannabis-Business.pdf](https://bdsa.com/wp-content/uploads/2022/05/BDSA-It-Isnt-Magic-Its-Data_Successfully-Expand-Your-Cannabis-Business.pdf)

formats to meet a wide range of consumer needs, from edible products to topicals, and have been using that experience to develop and test new THC consumer products and product formats that are now, for the first time, made possible through the use of DehydraTECH™ technology.

The science team in Michigan continues to work on developing a wide portfolio of consumer products, many of which are spurring early interest among potential new customers who are looking for differentiation and innovation in their markets. The Company believes that having an extensive and differentiated product portfolio that can be licensed and brought to market by DehydraTECH™ licensees adds potential depth and breadth to our offerings as we expand our US state footprint.

### **Hill Avenue Cannabis Brands**

#### **The Company continued to work closely with Molecule Inc. to advance Hill Avenue Cannabis Brands' (V)ia Regal business**

The Company continues to work through its Health Canada-licensed co-packing partner Molecule Inc. to further drive sales velocity on Hill Avenue's first cannabis-infused beverages, (V)ia Regal Pink Grape Sparkler and (V)ia Regal White Grape Sparkler, both premium sparklers made from grapes imported from European vineyards.

During the quarter, advances were made on retail support for the brand including efforts by Molecule. In May 2022, it was announced that Molecule had engaged the sales agency Humble + Cannabis Solutions Inc. ("**Humble**") to drive retail support of its brands, including of the Company's (V)ia Regal products. The Company expects that Humble's national sales force of experienced cannabis professionals will help to unlock the opportunity for (V)ia Regal to be represented from coast-to-coast.

Additionally, the decision was made together with the Ontario Cannabis Store to lower the retail price of (V)ia Regal products in Q4 in order to encourage broader consumer trial. While the Company's (V)ia Regal products are made with high-quality premium ingredients producing a superior product, the Company felt that a price reduction was warranted given that consumers in this early-stage Canadian cannabis beverage market are still quite price sensitive in their trial choices in this new category, and there are significant regulatory and legal limitations in the Company's ability to effectively market the brand's premium ingredients in Canada.

#### **Preparations continued on securing cannabis licenses for Hill Avenue's Lucknow facility**

In FY22 Q2, the Company submitted its application for a Health Canada R&D license for its Lucknow cannabis facility in Mississauga, Ontario. The Company believes that it is in final stages of the R&D licensing application process.

The Company also continued preparations for obtaining the Health Canada Standard Processor License for the Lucknow facility, which will enable the production of DehydraTECH™ fast-acting cannabinoid powder for potential B2B and B2C sales in Canada. The Company has begun construction at the facility, but continued and significant delays related to municipal permits for the build-out are impacting the timing for submission of that Standard Processor License application to Health Canada.

Those municipal delays, as well as our continued prioritization of cash resources towards the highest and most immediate returns, are why, as we progress on Lucknow licensing and construction, we continue to work on securing a relationship with a licensed processor partner in Canada who we can start to develop our DehydraTECH™ business within Canada in the near future.

#### **The Company changed its ticker symbol from "BEER" to "HILL"**

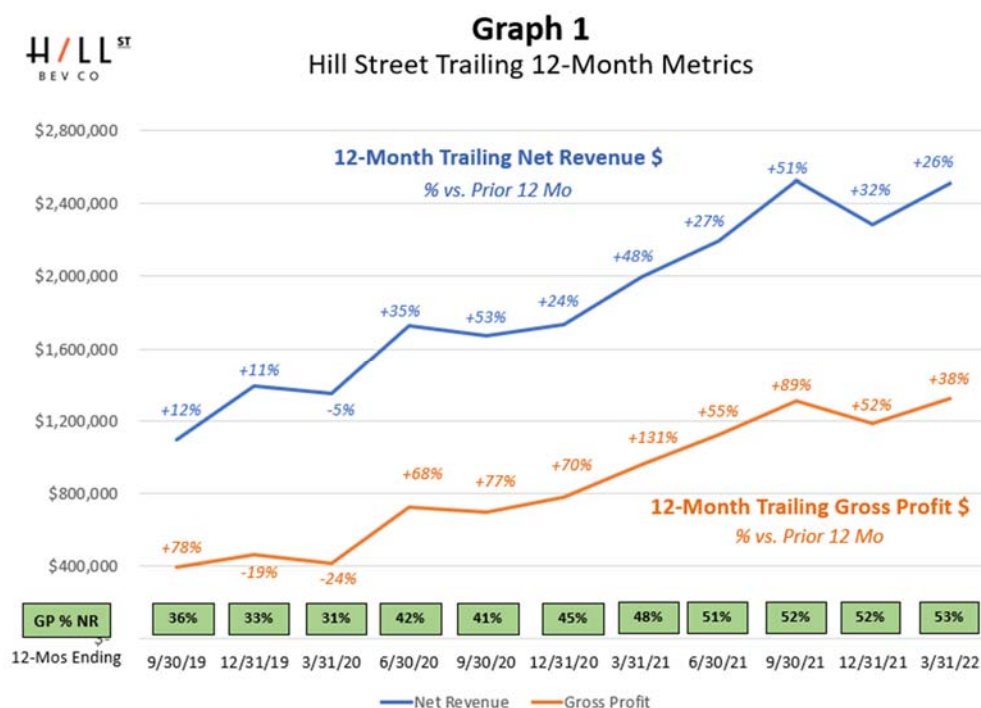
The Company originally obtained the "BEER" ticker symbol on the TSX Venture Exchange when it completed its reverse takeover transaction in 2018 and the choice of ticker symbol at that time reflected the nature of the business

and its focus at that time. Given the significant evolution of the Company’s business model and focus, the ticker symbol was changed to “HILL” on March 3, 2022. The “HILL” ticker symbol better reflects the Company's growth beyond the domestic beverage business towards building a global, multi-business company, pioneering the space where premium crafted consumer products meet bioscience.

### LONGER TERM PERFORMANCE UPDATE

As presented in the April 5, 2022 CEO Update to Investors (the “Update Letter”), the Company has been delivering a compelling long-term growth story and the strong Q3 results continue that trend.

The Update Letter introduced the analysis of the consolidated quarterly trailing 12-month figures (TTM) as a key metric to assess the performance and trend of the business. Graph 1 below adds the FY22 Q3 results to the graph that was presented in the update letter. The graph shows the consolidated quarterly trailing 12-month figures (TTM) for net revenue and gross profit from September 2019 to March 2022, which represents the period from Q1 FY 2020 through Q3 FY 2022. The figures above each line represent the change vs. prior year for that metric. Additionally, the figures in the green boxes represent the gross profit margin expressed as a % of net revenue.



As the graph shows, the financial results for Hill Street have been solid now for a full eight quarters. TTM net revenues have been continuously increasing between 24% - 53% vs. the prior year and gross profit has been even stronger at +38% to +131%. In fact, the key gross profit figures show that TTM gross profit dollars have more than tripled for the FY22 Q3 period vs. just two years ago for the FY20 Q3 period. As we've noted, the dramatic growth in gross profit dollars is accompanied by a significant improvement in our gross profit margins - which have increased as a percentage of net revenue from a low of 31% in fiscal year 2020 to over 50% in each of the past four quarters. As noted earlier, this significant improvement in gross profit dollars and gross profit margins do not yet show the impact of the DehydraTECH™ licensing deals announced with Lume in Michigan or the expansion of Dehydr8's commercialization efforts into Illinois, Massachusetts or Oregon.

## CFO Search Update

The Company has retained an executive search firm to find a replacement CFO and are progressing along with that search. Concurrently, as the CFO job market is quite competitive and as we want to find the right person to lead our finance initiatives given our aggressive growth profile and expanding global operations, we are in the process of engaging a fractional CFO resource to overlap with our outgoing CFO prior to her departure and for a period after a replacement CFO is onboarded, to ensure continuity in our finance function. We also have significant financial competency in other members of our team, as we have just hired a new controller and leading our Corporate Development team is another CPA and experienced finance professional.

## SELECTED QUARTERLY FINANCIAL INFORMATION

### RESULTS OF OPERATIONS

The following table summarizes certain financial information of the Company for the three months and nine months ended March 31, 2022, and the three months and nine months ended March 31, 2021.

Results for the Period Ended	Quarter Ended March 31, 2022	Quarter Ended March 31, 2021	Nine Months Ended March 31, 2022	Nine Months Ended March 31, 2021
Gross Revenue	\$988,549	\$774,747	\$2,225,654	\$2,034,726
Chargebacks, finance fees, and listing fees	-\$107,606	-\$119,488	-\$231,235	-\$359,006
Net Revenue	\$880,943	\$655,259	\$1,994,419	\$1,675,720
Direct Costs	-\$406,183	-\$317,155	-\$928,780	-\$809,701
Gross profit	\$474,760	\$338,104	\$1,065,639	\$866,019
Operating Expenses (excl. One-time & non-Cash)	\$732,113	\$835,460	\$2,177,067	\$2,092,925
Other One-time Expenses	\$9,500	\$47,643	\$25,646	\$71,479
Non-Cash Expenses	\$217,790	\$195,477	\$624,383	\$401,711
Loss before other Income (Expense)	-\$484,643	-\$740,476	-\$1,761,457	-\$1,700,096
<b>Other income (Expenses)</b>				
Gain (Loss) on Foreign Exchange	-\$1,744	\$15,463	\$7,370	-\$13,483
Gain (Loss) on favourable interest rate	\$0	\$6,541	\$0	\$6,541
Gain (Loss) on Settlement of liability	\$3,878	\$59,253	\$1,158	\$65,983
Gain (Loss) on fair value of consideration	\$62,834	\$0	\$48,363	\$0
Loss on Settlement of Debt	\$0	-\$1,168	\$0	-\$1,168
Write-off of Equipment	-\$16,638	\$0	-\$16,638	\$0
Write-off of inventory	\$0	\$0	-\$20,579	-\$1,535
Other Income	\$2,620	\$0	\$9,054	\$30
Loss and comprehensive loss for the period	\$433,693	\$660,387	\$1,732,729	\$1,616,762
Basic and diluted loss per common share	(\$0.00)	(\$0.00)	(\$0.01)	(\$0.01)
Weighted average number of common shares outstanding	214,948,996	141,905,150	212,060,433	125,375,081



## **REVENUES**

During the three months ended March 31, 2022, gross revenues were \$988,549 compared to \$774,747 for the three months ended March 31, 2021. The increase of \$213,802 or 28% compared to March 31, 2021, was due to an increase in cannabis revenues, which grew by 139% compared to the same quarter of prior year as well as a 14% gross revenue increase in alcohol-free beverages. Increased wine volume was offset by the Company's decision to discontinue the alcohol-free beer business in the face of supply chain issues and retailer fines and fees.

Net revenues for the three months ended March 31, 2022, were \$880,943 compared to \$655,259 for the three months ended March 31, 2021, representing an increase of 34% which was mainly driven by the increase in gross revenue and lower chargebacks as a percentage of gross revenue. For the three months ended March 31, 2022, chargebacks represented 11% of gross revenues compared to 15% for the three months ended March 31, 2021. Chargebacks are fees charged by retailers and distributors for program money and discounts. Listing fees were nil for the three months ended March 31, 2022, and nil for the three months ended March 31, 2021. Net revenues for the nine months ended March 31, 2022, were \$1,994,419 compared to \$1,675,720 for the nine months ended March 31, 2021, representing an increase of 19%.

## **COST OF SALES/DIRECT COSTS**

Direct costs were \$406,183 or 41% of gross revenue for the three months ended March 31, 2022, and \$317,155 or 41% of gross revenue for the three months ended March 31, 2021. The flat percentage of gross revenue over the three months ended March 31, 2021, compared to year ago was mainly driven by the alcohol-free beverage business, with favorable inventory adjustments for the recovery of costs for damaged product offset by higher freight costs and unfavorable product mix.

## **GROSS PROFIT**

During the three months ended March 31, 2022, gross profit increased to \$474,760 compared to \$338,104 for the three months ended March 31, 2021, an increase of 40%. Gross profit as a percentage of revenue increased to 48% compared to 44% in the prior year. The increase of 4 percentage points is primarily driven from the addition of the higher margin cannabis technology licensing business offset by alcohol free cost drivers above. For the nine months ended March 31, 2022, gross profit increased to \$1,065,639 compared to \$866,019 or 23% from the nine months ended March 31, 2021. The primary driver was higher cannabis licensing revenues offset to a degree by lower alcohol-free revenues mainly due to the discontinued beer revenues.

## **OPERATING EXPENSES – ORDINARY**

Ordinary operating expenses include selling and marketing expenses, employee expenses, donations, dues and licenses, professional fees, and other general and administrative expenses. For the three months ended March 31, 2022, operating expenses totaled \$732,113 compared to \$835,460 for the three months ended March 31, 2021. The principal drivers of the \$103,347 decrease in operating expenses were lower professional fees of \$152,120 for legal and accounting, management fees of \$55,250, consulting expenses of \$35,539, interest on the convertible debt of \$14,949, selling and delivery of \$26,930, and filing fees of \$9,352. These decreases were offset by higher expenses in salaries and wages of \$142,714, marketing expenses of \$41,985, insurance expenses of \$5,207 due to cannabis exposure, and office and miscellaneous of \$3,516. Convertible debentures outstanding were converted into common shares of the Company during the fourth quarter of the prior fiscal year.

The Company experienced significant increases in audit and insurance expenses versus prior year due to requirements relating to its entry into the cannabis business. The Company does not expect that these expenses will increase at the same rate in future periods, even at higher cannabis revenue levels.

### **OPERATING EXPENSES – ONE TIME**

For the three months ended March 31, 2022, one-time expenses were \$9,500 for expenses incurred for incorporation of a US legal entity to support the continued expansion of our business resources and efforts in the U.S. For the three months ended March 31, 2021, one-time expenses were \$47,643 relating to \$71,749 for severance costs offset by a recovery of costs from a supplier.

### **OPERATING EXPENSES - NON-CASH**

For the three months ended March 31, 2022, the Company incurred non-cash expenses totaling \$217,789, which include expenses related to stock options, restricted share units, depreciation, accretion expense for an interest-free CEBA loan, lease interest expenses, and accrued interest on a promissory note. For the three months ended March 31, 2021, the company incurred non-cash operating expenses of \$195,477 which included expenses related to stock options, depreciation, the expense of warrants issued in exchange for marketing services, accretion expense on convertible debentures, lease interest expense and promissory note interest expense.

### **OTHER EXPENSES**

For the three months ended March 31, 2022, the Company incurred other expenses totaling \$50,950. This included a gain on fair value of consideration of \$62,834, gain on settlement of liabilities for \$3,878, and other income of \$2,620. These gains were offset by a foreign exchange loss of \$1,744 and an equipment write off of \$16,638. For the three months ended March 31, 2021, the Company incurred other income and expenses totaling \$80,089. This included a gain on foreign exchange of \$15,463, a gain on favourable interest rate of \$6,541, a gain on settlement of liabilities of \$59,253, and a loss on debt conversion of \$1,168.

### **NET EARNINGS**

The Company recorded a net loss of \$433,693 for the three months ended March 31, 2022, compared to a loss of \$660,387 for the three months ended March 31, 2021. The increase in net earnings of 34% was primarily driven by an increase in gross profit along with decreases in ordinary operating expenses.

The basic and diluted loss per share for the three months ended March 31, 2022, was \$0.00 per share. The basic and diluted loss per share for the three months ended March 31, 2021, was \$0.00 per share.

## SELECTED QUARTERLY INFORMATION

The following table summarizes certain financial information of the Company for the quarters indicated below:

	Mar 31, 2022	Dec 31, 2021	Sep 30, 2021	June 30, 2021	Mar 31, 2021	Dec 31, 2020	Sept 30, 2020	June 30, 2020
Gross Revenue	\$988,549	\$576,622	\$660,483	\$718,755	\$774,747	\$875,529	\$384,450	\$623,450
Net Revenue	\$880,943	\$508,737	\$604,739	\$519,194	\$655,259	\$745,749	\$274,712	\$323,604
Direct Costs	\$406,183	\$252,280	\$270,317	\$261,583	\$317,155	\$363,840	\$128,706	\$231,176
Gross Profit	\$474,760	\$256,457	\$334,422	\$257,611	\$338,104	\$381,909	\$146,006	\$92,428
Net Loss (gain)	\$433,693	\$699,476	\$599,560	\$1,469,469	\$660,387	\$480,522	\$475,853	\$456,685
Total Assets	\$6,504,174	\$6,551,448	\$7,125,001	\$7,609,334	\$5,935,113	\$6,438,534	\$1,368,840	\$2,016,673
Total Liabilities	\$3,225,247	\$3,241,881	\$3,161,015	\$3,632,174	\$5,031,004	\$4,941,526	\$1,600,388	\$1,831,246
Shareholder Equity	\$3,278,927	\$3,309,567	\$3,963,986	\$3,977,160	\$904,109	\$1,497,008	(\$231,548)	\$185,427

\*Certain contractual changes and their associated accounting treatment impact gross revenue comparability over quarters. However, these changes do not similarly impact net revenue and therefore, net revenue of the Company provides better comparability over quarters.

## LIQUIDITY AND CAPITAL RESOURCES

### FINANCIAL POSITION

The Company's principal capital needs are for operating expenses related to alcohol-free beverage inventory, employee and marketing expenses. Additional investments are being made to support the Company's cannabis-infused product line of business and the build-out of the Company's facility to obtain Health Canada's Standard Processing License for cannabis. Since its formation, the Company has financed its additional cash requirements through revenues generated from operations, issuance of securities and borrowing from shareholders and other lenders.

The Company has positive working capital and will continue to focus on cost management and revenue growth.

### WORKING CAPITAL

Working capital represents current assets less current liabilities. As of March 31, 2022, the Company had a positive working capital of \$1,736,328 compared to negative working capital of \$237,323 for the three months ended March 31, 2021.

As the Company shifts its focus from the alcohol-free beverage business with higher asset requirements and relatively lower margins, to growing its cannabis technology licensing revenues through a high-margin business requiring little to no inventory capital, the Company expects that the inventory working capital in future periods will decrease as a percentage of its sales.

## CASH FLOWS

During the nine months ended March 31, 2022, Hill Street had negative cash flows from operations of \$1,442,581 compared to negative cash flows of \$1,424,175 during the nine months ended March 31, 2021. The amount of cash (used) in investing activities in the nine months ended March 31, 2022, was \$149,364 primarily for investment in the standard processing licensed facility. This compared to \$370,977 in the nine months ended March 31, 2021, which included a cash investment in the Lexaria assets. The amount of cash generated from financing activities during the nine months ended March 31, 2022, was \$292,966 compared to cash used of \$1,419,447 in the nine months ended March 31, 2021.

## CONTRACTUAL OBLIGATIONS

A summary of the Corporation's contractual obligations for future periods is as follows:

Contractual Obligations	Payments due by Period					Total
	FY2022	FY2023	FY2024	FY2025	FY2026	
Operating Leases and TMI	\$23,238	\$0	\$0	\$0	\$0	\$23,238
Purchase Obligations	\$538,953	\$103,815	\$0	\$0	\$0	\$642,768
<i>Total</i>	\$562,191	\$103,815	\$0	\$0	\$0	\$666,006

## SHARE CAPITAL

The Company is authorized to issue an unlimited number of common shares of which 222,940,400 common Shares are issued and outstanding as of the date hereof.

Security Designation	Number issued and outstanding
Common shares	222,940,400
Warrants to purchase common shares	62,119,544
Incentive Stock Options	13,810,620
Restricted Share Units	11,671,223
<b>Maximum Fully Diluted</b>	<b>310,541,787</b>

## CAPITAL RESOURCES

As of March 31, 2022, the Company has capital investments in fiscal year 2022 for leasehold improvements at the Lucknow facility for DehydraTECH™ powder product research and production.

## OFF BALANCE SHEET ARRANGEMENTS

Hill Street does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the financial performance or financial condition of the Company.

## TRANSACTIONS WITH RELATED PARTIES

The Company considers its executive officers and directors to be key management personnel. The Company incurred the following amounts to related parties during the respective periods for key management personnel compensation.

<b>During three-month period ended March 31,</b>	<b>2022</b>	<b>2021</b>
Total salaries, benefits and management fees	\$933,978	\$737,370
Stock-based compensation	\$163,195	\$92,942
Management and director compensation	\$1,097,173	\$830,312

Included in accounts payable as of March 31, 2022, is \$458,387 (compared to \$294,287 as of June 30, 2021) payable to directors and officers of the Company for management compensation.

On April 9, 2021, certain members of management and board members participated in a non-brokered private placement financing of units ("**April 2021 Units**") for gross proceeds of \$310,825 at a price of \$0.08 per April 2021 Unit. Each April 2021 Unit consists of one common share and one warrant, with each warrant entitling the holder thereof to purchase one common share in the capital of the Company at a price of \$0.11 per share for a period of three years from closing, subject to acceleration on certain terms.

During the year ended June 30, 2021, the principal amount of \$1,022,500 of a convertible debentures payable by the Company was converted into 20,450,000 common shares at conversion price of \$0.05 per share.

### **CRITICAL ACCOUNTING ESTIMATES**

The determination of income tax is inherently complex and requires making certain estimates and assumptions about future events. While income tax filings are subject to audits and reassessments, the Company has adequately provided for all income tax obligations. However, changes in facts and circumstances as a result of income tax audits, reassessments, jurisprudence and any new legislation may result in an increase or decrease in our provision for income taxes.

Calculation of the net book value of machinery and equipment requires management to make estimates of the useful economic life of the assets, residual value at the end of the asset's useful economic life, method of depreciation and whether impairment in value has occurred. Residual values of the assets estimated useful lives and depreciation methodologies are reviewed annually with prospective application of any changes, if deemed appropriate. Changes to estimates could be caused by a variety of factors, including changes to the useful life of the assets. A change in any of the estimates would result in a change in the amount of depreciation and, as a result, a charge to net income recorded in the period in which the change occurs, with a similar change in the carrying value of the asset on the balance sheet.

The amortization of the Company's intangible assets involves estimates of their useful lives. Such estimates may change as more experience is obtained or as general market conditions change, thereby impacting the value of the Company's intangible assets.

When valuing options, management uses judgment to determine the inputs to the Black-Scholes option pricing model including the expected plan lives, underlying share price volatility and forfeiture rates. Volatility is estimated by considering peer companies historic share price volatility over similar periods to the expected life of the awards under consideration. Changes in these assumptions will impact the calculation of fair value and the amount of compensation expense recognized in the consolidated statements of loss and comprehensive loss.

When valuing warrants, similar to other stock-based compensation, management uses judgment to determine the inputs to the Black-Scholes option pricing model including the expected life, and underlying share price volatility. Volatility is estimated by considering peer companies historic share price volatility over similar periods to the expected life of the warrants. Changes in these assumptions will impact the calculation of fair value and the value attributed to the warrants.

When the Company enters into leases as a lessee and where the interest rate implicit in a lease cannot be readily determined, the Company determines its incremental borrowing rate in order to measure its lease liability. The incremental borrowing rate is the rate of interest that a lessee would have to pay to borrow over a similar term, and with similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. In estimating its incremental borrowing rate, the Company considers the term of the lease, the nature of the leased asset, and its level of indebtedness with reference to market risk-free interest rates.

When determining the discount rate used to estimate the fair value of the debt component of the convertible debenture and the fair value of the CEBA loan, the Company considers market conditions and other internal and external factors. The Company estimates its credit rating and benchmarks the discount rate to certain fixed income indices.

In some contracts, the Company transfers control of a product to distributors and grants the distributors the right to return the product for a full or partial refund in the scenario that products are to expire in the hands of the distributor. To account for the transfer of products with a right of return, the Company recognises revenue for the transferred products in the amount of consideration to which the Company expects to be entitled to (therefore, revenue would not be recognised for the products expected to be returned). The expected consideration to be received is determined based on a combination of historical, current and forecasted information available to the entity at the end of each reporting period.