



ABN 27 621 105 824
ACN 621 105 824

18 September 2019

Lisa Banh
Senior Adviser, Listings Compliance (Sydney)
ASX Compliance Pty Ltd
20 Bridge Street
Sydney, NSW 2000

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Dear Lisa

Response to Aware Query

Smiles Inclusive Limited (ASX: **SIL**) (**Company**) refers to your letter dated 16 September 2019 regarding the Company's financial condition.

The Company provides the following responses to your questions:

- 1. Please provide a breakdown of the components making up the "positive EBITDA" recorded in SIL's management accounts for the month of July 2019.**

The Company confirms its income for July 2019 exceeded its income for June 2019 by \$550,451.

The July 2019 EBITDA breakdown is as follows:

Gross practice revenue	\$4,525,170
Net practice EBITDA after profit share	\$538,030
Corporate costs	\$502,011
EBITDA	\$36,019

- 2. Please advise:**

- a. as to the quantum of SIL's cash and cash equivalents balance at Friday 13 September 2019; and**

The Company's cash and cash equivalents balance at the end Friday 13 September 2019 was \$323,344 (plus \$1.191 million Bartercard Trade dollars).

- b. whether SIL has sufficient cash to meet its current liabilities to staff and other creditors for the month of September 2019**

The Company confirms that payments to staff were made on time in its most recent payroll run, and there were no employee arrears as at 10 September 2019. The Company continues to manage its relationships with creditors (including independent contractors) and expects to have sufficient cash to meet its current liabilities to staff and other creditors for the month of September 2019.

- 3. Please advise whether SIL's auditor has yet formed a view as to the quantum of the impairment to be recognised by SIL for FY19**

The auditor has not yet formed a view as to the quantum of the impairment recognised by the Company for FY19. The Company remains in discussions with the auditor, which are ongoing and productive.

4. Does SIL expect that it will continue to have negative operating cash flows for the time being and, if not, why not?

The Company is implementing a turnaround plan, which consists of several discrete initiatives that vary in complexity and will be executed in the immediate, medium and long terms. Early indications are positive. While every effort is being made to improve performance as soon as possible, the Company expects its cash flows to fluctuate, particularly when taking into consideration the ordinary and seasonal business cycle. The Company expects improvements in cash flows over the medium to long term, though the likelihood of negative operating cash flows for the time being remains relatively high.

5. Has SIL 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?

The Company is actively considering all funding avenues open to it, including debt and equity.

The Company is in productive discussions with its primary lenders to ensure it continues to meet its immediate working capital requirements.

The Company raised funds via existing shareholders (sophisticated investors) through a placement on 21 June 2019. The Company continues to actively consider all options available to it as an ASX listed entity, and remains confident it would be successful should it elect to raise further funds via equity capital markets.

6. Does SIL expect to be able to continue its operations and to meet its business objectives and, if so, on what basis?

The Company continues to believe in its underlying business model and the Company's current board and management remain committed to the objectives set out in the Company's prospectus and market announcements, including focusing on implementing its turnaround plan, improving business performance and providing reliable dental services.

The Company expects to be able to continue its operations and to meet its business objectives on the basis that it continues to have the support of its primary lenders, stakeholders and that it is seeing positive tangible change within the business as a result of the implementation of its turnaround plan.

7. Does SIL consider that its financial condition is sufficient to warrant continued listing on ASX as required under listing rule 12.2? In answering this question, please also explain the basis for this conclusion.

The Company considers that its financial condition is sufficient to warrant continued listing on ASX.

As a business in turnaround mode, the current cash flows are not reflective of management's expected cash flows for the period leading to and following the time the turnaround is complete. As disclosed on several occasions, implementation of the turnaround plan is in its early stages, with performance improvements expected to be realised over the next 12 months.

Recent announcements in respect of the Company's Balance Sheet have focused on the required impairment of its Goodwill asset, and its impact on the Net Assets of the Company.

Under current accounting standards, the assessment of the carrying value of goodwill is required to be considered by the Company at least annually. AASB136, requires the Company to consider (amongst other factors) the most recent cash flows of the business, and does not permit consideration of those cashflows expected following the substantial operational restructure currently underway.

The amount of the impairment charge incurred by the business as at 30 June 2019 is a product of the poor decisions of previous management which are in the process of being, unwound and reset with appropriate commercially-focused arrangements. The expectations are that these arrangements will substantially improve operational performance of the Company and shareholder value.

Accordingly, management do not consider that the most recent cash flows of the business, and any valuation of the entity as a result of those cash flows, are necessarily representative of the likely future performance of the business and its corresponding value.

Despite disappointing historical cash flows, and the recent impairment recognised by the Company, the Company continues to have the support of its primary lenders, who are working closely with the Company to manage immediate working capital requirements.

SIL therefore believes it's continued ASX listing is appropriate

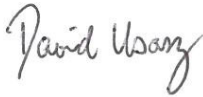
- 8. Please confirm that SIL is complying with listing rule 3.1 and that there is no information that should be given to ASX about its financial condition under that rule that has not already been released to the market.**

The Company considers that it is complying with listing rule 3.1 and there is no information that should be given to ASX about its financial condition that has not already been released to the market.

- 9. Please confirm that SIL's responses to the questions above have been authorised and approved in accordance with its published continuous disclosure policy or otherwise by its board or an officer of SIL with delegated authority from the board to respond to ASX on disclosure matters.**

Confirmed.

Yours faithfully



David Usasz
Chairman

16 September 2019

Reference: 06511

Ms Emma Corcoran
Company Secretary / CFO
Smiles Inclusive Limited
PO Box 382
West Burleigh, QLD 4219

By email

Dear Ms Cocoran

Smiles Inclusive Limited ('SIL'): Query Letter

ASX refers to the following matters:

Background

- A. On 28 February 2019, SIL released an Appendix 4D Half Year Report (the "Appendix 4D") on MAP which disclosed results for the six months ended 31 December 2018, including:
 - i. Revenue from ordinary activities = \$16,132,000; and
 - ii. Net profit / (loss) attributable to members = (\$1,592,000).
- B. On 31 July 2019, SIL released an Appendix 4C for the three months ended 30 June 2019 which disclosed:
 - i. Net cash from / (used in) operating activities = (\$537,000), comprising:
 - a. receipts from customers = \$12,247,000;
 - b. manufacturing and operating costs = \$5,695,000;
 - c. advertising and market costs = \$100,000;
 - d. staff costs = \$5,839,000;
 - e. administration and corporate costs = \$785,000; and
 - f. costs of finance = \$365,000.
 - ii. Net cash from / (used in) financing activities = \$1,751,000, including:
 - a. Proceeds from issues of shares = \$1,217,000; and
 - b. Proceeds from borrowings = \$874,000.
 - iii. Cash / cash equivalents at the end of the quarter = \$1,595,000.
 - iv. Financing arrangements as follows:

8. Financing facilities available

Add notes as necessary for an understanding of the position

	Total facility amount at quarter end \$A'000	Amount drawn at quarter end \$A'000
8.1 Loan facilities	19,608	19,608
8.2 Credit standby arrangements	-	-
8.3 Other	5,952	4,429

8.4 Include below a description of each facility above, including the lender, interest rate and whether it is secured or unsecured. If any additional facilities have been entered into or are proposed to be entered into after quarter end, include details of those facilities as well.

Loan facilities in 8.1 include the NAB senior debt and acquisition facility of \$14,708,000 (secured), and the working capital facility of \$4,000,000 (secured) and 3rd party loans of \$900,000 (unsecured). The weighted average interest rate on financing facilities at 30 June 2019 was 4.92%. The business is currently in a consolidation phase and as a result the NAB acquisition facility of \$30 million was reduced to the amount drawn of \$14,708,000.

Other facilities includes the following:

- Ancillary facilities of \$2,000,000 (secured) \$477,000 (drawn).
- Equipment lease facility of \$3,952,000 (secured and drawn).

- v. estimated cash outflows for the three months ended 30 September 2019 of \$13,000,000, comprising:
 - a. Manufacturing and operating costs = \$6,500,000;
 - b. Advertising and marketing = (\$300,000);
 - c. Staff costs = \$5,500,000; and
 - d. Administration and corporate costs = \$700,000.
- C. On 30 August 2019, SIL released an Appendix 4E Preliminary Final Report (the 'Appendix 4E') on MAP. The Appendix 4E disclosed for the 12 months ended 30 June 2019:
 - i. net profit/(loss) attributable to members = (\$18,878,000);
 - ii. a net goodwill impairment of \$13,700,000;
 - iii. a "small profit at an EBITDA level" recorded in SIL management accounts for July 2019;
 - iv. cash and cash equivalents of \$1,595,000.
- D. On 5 September 2019, ASX released its query SIL relating to the Appendix 4E, and SIL's response, released on MAP. SIL's response disclosed that:
 - i. It did not consider its net loss of \$18.9 million to be information which is material to the price or value of its securities within the meaning of listing rule 3.1.
 - ii. It became aware of that its goodwill would be subject to an impairment of \$13.7 million after close of trade on 30 August 2019, and that its auditor is yet to express a "definitive view on impairment".
 - iii. It had reclassified certain matters that had previously been reported for "significant business / practice events" following its subsequent banking covenant assessment, at which time these matters were "deemed not to be significant practice events."
- E. Listing rule 12.1, which states:

12.1 *The level of an entity's operations must, in ASX's opinion, be sufficient to warrant the continued quotation of the entity's securities and its continued listing.*

F. Listing rule 12.2, which states:

12.2 An entity's financial condition (including operating results) must, in ASX's opinion, be adequate to warrant the continued quotation of its securities and its continued listing.

G. Listing rule 3.1, which applied at all relevant times, and requires a listed entity to immediately give ASX any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity's securities.

Questions and Request for Information

Having regard to the above, ASX asks SIL to respond separately to each of the following questions and requests for information:

1. ASX has received market intelligence to suggest that SIL's income for July 2019 is comparable to that received in June 2019.

Please provide a breakdown of the components making up the "positive EBITDA" recorded in SIL's management accounts for the month of July 2019.

2. If SIL's income for the three months ended 30 September 2019 is comparable to that in the previous quarter (see paragraph B above), then, observing that:

- SIL's forecast cash outflows for this quarter were \$13 million (which would suggest similar outgoings to those reported for June 2019 quarter);
- SIL reported for the June 2019 quarter cash and cash equivalents of \$1,595,000, comprising:
 - Cash and cash equivalents at the beginning of the quarter of \$641,000
 - Net cash from operating activities of (\$537,000)
 - Net cash from investing of (\$260,000)
 - Net cash from financing activities of \$1,751,000
- For the June 2019 quarter, SIL reported that its loan facility of \$19,608,000 was fully drawn, and that it had "other" facilities with around \$1.5 million yet-to-draw,

it is reasonable to conclude that there is some possibility that, without further funding, SIL will run out of cash in the September 2019 quarter. Further to ASX's concerns in this regard, it has also received market intelligence to indicate that payments to a number of SIL staff are currently in arrears as at 10 September 2019.

Please advise:

- i. as to the quantum of SIL's cash and cash equivalents balance at Friday 13 September 2019; and
 - ii. whether SIL has sufficient cash to meet its current liabilities to staff and other creditors for the month of September 2019.
3. Please advise whether SIL's auditor has yet formed a view as to the quantum of the impairment to be recognised by SIL for FY19.
4. Does SIL expect that it will continue to have negative operating cash flows for the time being and, if not, why not?
5. Has SIL 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?

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6. Does SIL expect to be able to continue its operations and to meet its business objectives and, if so, on what basis?
 7. Does SIL consider that its financial condition is sufficient to warrant continued listing on ASX as required under listing rule 12.2? In answering this question, please also explain the basis for this conclusion.
 8. Please confirm that SIL is complying with listing rule 3.1 and that there is no information that should be given to ASX about its financial condition under that rule that has not already been released to the market.
 9. Please confirm that SIL's responses to the questions above have been authorised and approved in accordance with its published continuous disclosure policy or otherwise by its board or an officer of SIL with delegated authority from the board to respond to ASX on disclosure matters.

When and where to send your response

This request is made under listing rule 18.7. Your response is required as soon as reasonably possible and, in any event, by no later than **5:00 pm AEST on Wednesday, 18 September 2019**.

You should note that if the information requested by this letter is information required to be given to ASX under listing rule 3.1 and it does not fall within the exceptions mentioned in listing rule 3.1A, SIL's obligation is to disclose the information 'immediately'. This may require the information to be disclosed before the deadline set out in the previous paragraph.

For the purpose of preparing its answers to the above questions concerning when it was aware of particular matters, ASX also directs SIL to the following definition in chapter 19 of the listing rules¹:

aware *an entity becomes aware of information if, and as soon as, an officer of the entity (or, in the case of a trust, an officer of the responsible entity) has, or ought reasonably to have, come into possession of the information in the course of the performance of their duties as an officer of that entity.*

ASX reserves the right to release a copy of this letter and your response on MAP under listing rule 18.7A.

Accordingly, your response should be in a form suitable for release to the market. Your response should be sent to me by e-mail. It should not be sent directly to the ASX Market Announcements Office. This is to allow me to review your response to confirm that it is in a form appropriate for release to the market, before it is published on the ASX Market Announcements Platform.

Enquiries

If you have any queries or concerns about any of the above, please contact me immediately.

Yours sincerely,

Lisa Banh
Adviser, Listings Compliance (Sydney)

¹ Refer also to the commentary at section 4.4 in Guidance Note 8.