McGrath

# ASX ANNOUNCEMENT

# McGrath Limited 2018 Annual General Meeting
# Friday 23 November 2018
# Chair and Chief Executive Officer's Address

**Chair's Address**

The 2018 financial year was one of significant change in our business. Over the past 12 months a new Management team, CEO, Chair and Board have been appointed.

This year, McGrath celebrates its 30th year of operations and the fundamentals of our business remain strong. We are indebted to our founder John McGrath for establishing such a strong brand from the earliest of days which has provided a much needed platform during the very challenging last financial year. Due to a range of internal and external factors, the company's financial performance has been disappointing, but we do retain a leading sales agent team, brand name, and network reach which will underpin the company's return to sustainable profitable growth over the medium term.

With offices across New South Wales, Queensland, Victoria and the ACT, we have an extensive presence and understanding of the East Coast markets. This enables us to offer a premium level of service to deliver outstanding results for clients.

***Strategic investment by Aqualand***

In June 2018 we formed a strategic relationship with Aqualand, one of Australia's premier residential property development and investment groups. Aqualand has a significant property development portfolio with gross development values in the billions and recently established AL Capital with Wayne Mo as CEO to pursue opportunities in adjacent and other spaces.

Aqualand invested $10.7 million for a 15% shareholding in McGrath. As McGrath's second largest shareholder, Aqualand nominated Wayne Mo for appointment to the Board, a move welcomed by all directors.

This significant stake achieves strategic commercial alignment between McGrath and Aqualand.

Importantly this also provides us with financial security during a period of industry weakness and the capacity to make strategic moves as opportunities become available.

The 2019 Financial Year will be focussed on stabilising the business and returning it to growth. Challenging market conditions are expected to continue, but we believe that McGrath has the quality brand, skills, experience and now financial capacity that positions us well in our industry.

The Management team are developing a strategic plan for future organic growth with the FY19 key priorities being:

- Learning and development initiatives
- Data technology improvements to enhance the agent and vendor experience
- Growth in the annuity businesses in Property Management, Franchise and Oxygen
- Enhancing the agent network through agent productivity, retention of high performing agents and converting a strong agent recruitment pipeline
- Developing scale in Project Marketing business

All of those should drive share growth in key markets and we believe that our Board and Management team have the necessary skills and experience to execute those priorities.

In closing, I would like to publicly acknowledge my fellow Directors and Management team for their dedication and contributions in what has been a challenging year across both our sector and for our business. I would also like to thank our magnificent team of agents and employees - whether franchised or company owned - for their efforts and professionalism in a very difficult time. Finally, to you our shareholders, thank you for your ongoing support and patience.

I will now ask Geoff Lucas, our CEO, to present the FY18 financial results and specific initiatives.

**Chief Executive Officer's Address**

Good afternoon ladies and gentlemen and thank you Peter for your introduction. My brief presentation this afternoon will have three parts:

- A recap of the 2018 financial year.
- A review of our most recent trading update issued in October 2018
- Key Priorities and Outlook.

Before I start the recap of the 2018 financial year, I would like to thank you our shareholders for your patience and commitment in supporting our new board, the management team and myself as CEO as we have stabilised the business and focused on turning the performance of your company around. It is a responsibility we do not take lightly, and speaking personally, a challenge and responsibility that I am embracing with enormous energy, enthusiasm and pride. Together, we thank you for your continued support.

The 2018 financial year saw a combination of difficult market conditions, lower sales volumes and the departure of a number of sales agents and franchisees impacted revenues with a 23% reduction over the prior year, resulting in an underlying EBITDA of $5 million, which is 67% below the prior year.

On a statutory basis, the net loss after tax of $63 million was impacted by a $59 million impairment related primarily to the company owned office network.

On a segment basis, it's clear from the chart the biggest impact of the reduced performance has been the performance of our Company Owned business with EBITDA reducing to $4.2 million from $15.5 million in FY17. This was the direct result of a sharp reduction in agent numbers in our company owned offices. This also led to a small reduction in our Property Management business.

Challenging market conditions resulted in a reduction in the number of franchise offices, with a net reduction of 5 franchise offices during the 2018 financial year. A lower number of offices and associated franchise revenue reduced the earnings slightly in this segment.

Our other Businesses of Oxygen, Auctions and Training suffered relatively smaller falls, however were also affected by reduced transaction numbers.

You will see that Corporate Overheads were reduced through the year by $2 million reflecting the benefits of a restructure. We have continued the reduction in overheads in the current year. Whilst the expenditure reductions have been material and reflective of a lower revenue environment, we have been careful not to make cuts that directly impact revenue or the ability to grow our business.

After sustaining a significant reduction in sales agent numbers in the first 9 months of the 2018 financial year, we stabilised the agent team by stemming losses and achieving a small growth in company owned agents in the fourth quarter. The impact of large numbers of agents leaving the business generates a revenue lag effect that has been carried over into the beginning of the 2019 financial year. This is a business that takes some time to turn around, especially from a loss in agent numbers the quantum of which this business experienced. I am pleased to report that by the end of October 2018, our company-owned residential sales business has seen agent numbers grow by 9 agents.

The quality of our agent team is of primary importance to McGrath and also our clients. We pride ourselves on the provision of excellent customer service and results. And we place the customer experience and importantly sales results at the forefront of our business. We remain committed to ensuring our agents remain the best in the market. This sets us apart and for this reason we are highly focused on talent identification and developing and retaining high performing quality agents.

On 23 October 2018, and in response to a continually worsening residential sales market, the company released a trading update announcing a $1.9 million EBITDA loss for the first quarter, with an expectation that the second quarter would see a materially lower loss. Further improvements were expected to result in a full year EBITDA result of at least break even. We maintain that expectation.

Whilst improvements in the business have been made, with agent losses stemmed, and small increases in numbers being achieved, the impact of these factors along with a continually challenging real estate market had a marked effect on trading performance in the first quarter.

We have seen a number of factors contributing to a deteriorating residential sales market. These include a significant reduction in credit availability, a downturn in Sydney and Melbourne dwelling values, reduced auction clearance rates and a lower number of new listings as vendors adjust their value expectations.

As you can see in the displayed chart, the monthly national transaction numbers are now approaching a two decade low, and specifically the number of settled sales for Sydney, Melbourne, and Brisbane are down on the prior year by 16.7%, 14.4% and 8.4% respectively.

Moving from transaction Volume to Value, this chart shows a national decline in values over the 12 months to October 2018 of 3.5%. Our key markets of Sydney and Melbourne have seen falls far greater with 7.4% and 4.7% respectively. Brisbane, a key emerging market for McGrath, in contrast has seen a small 0.4% gain over the 12 month period. You will also see from the chart the national falls for combined capital cities is approaching a historical low.

We believe the challenging market conditions will present opportunities for McGrath to build market share across our markets.

Our management team is operating in some of the most challenging real estate market conditions in several decades. We believe however that the environment will present opportunities to build a stronger business and generate sustainable market share gains. Throughout this period, we will not compromise on our highly valued levels of customer service and sales results.

For the balance of FY19 we expect challenging market conditions to continue with a small deterioration of dwelling values and tightened credit approvals. We believe that in a tightening cycle customers will continue to be attracted to a premium brand, represented by highly skilled and experienced agents.

**Key Priorities**

We have stabilised our agent base and now paved the way for steady growth in both agent numbers and offices. The majority of our growth over the next three years will be franchised offices in our key eastern seaboard markets.

Whilst the project marketing environment remains challenging at present, we believe this market will return to strength within the next two years. We are in the process of building a high calibre Project Marketing team to maximise the opportunities available to us through our strategic partnership with Aqualand and other world class developers.

The balance of this financial year will see the continued development of our technology systems to drive efficiencies in our business.

We're proud of the quality of agents at McGrath and that's by design rather than chance. This doesn't come without investment, and we will continue to invest in market leading Learning and Development programs ensuring our team are well equipped to provide exceptional service and results in all markets

As we've seen, the sales market can be volatile. We've taken care to establish and grow our annuity businesses that include Oxygen, our Franchise business and also both Company Owned and Franchise network property management growth.

Increasingly we are seeing real estate business owners seeking to return to a role of real estate sales agent without the attendant issues of running a business in a difficult environment. As a result an increasing number of rent rolls with sales businesses attached are beginning to come to market.

By virtue of our recent 15% placement to our strategic partner Aqualand, McGrath is uniquely placed to take advantage of a weakening market place. With currently $16 million in cash and one of Australia's largest rent rolls that would typically be valued at between $45 and $55 million and zero debt, we're well placed to make prudent and strategic acquisitions.

We are pleased to announce that we have made two small rent roll acquisitions consistent with the trend I've described. Although small, they are indicative of what we expect will become more frequent in the short to medium term.

We will continue to assess opportunities to acquire strategically beneficial businesses.

We remain on track with our latest Trading Update and will be using the balance of this financial year to reinforce McGrath's position as the leader in premium residential sales and service in Australia.

Thank you again, I will now hand back to our Chairman Peter Lewis.