AVJennings

FY19 Results Presentation Speaker Notes – 20 August 2019

Chief Executive Officer & Managing Director – Mr Peter Summers

Welcome everyone to this Investor Briefing Teleconference for the AVJennings Limited 30 June 2019 results. With me today are our Chief Financial Officer, Mr. Larry Mahaffy and our Company Secretary, Mr. Carl Thompson.

As usual we will be following the format of the Investor Briefing document we released to the ASX earlier this morning. There will be three parts to this presentation,

- Larry will take us through the financial outcomes for FY19;
- I will then look beyond FY19; and
- We will finish with a period for questions.

If I could now ask Larry to take us through the financial outcomes which begin on Slide 6.

Chief Financial Officer – Mr Larry Mahaffy

Thank you, Peter.

Turning to Slide 6, we see that revenue and statutory profit, both before and after tax, were down on the prior corresponding period, but were nevertheless ahead of internal expectations. The decrease is fundamentally due to slower market conditions that adversely affected the volume of land sold and settled during the year. 970 lots were settled or revenue-recognised in FY19, down about 25% on the preceding year 1,292 lots.

The full year result was reliant, to a greater extent than usual, upon the settlement of sales made in earlier periods, particularly those with good margins at Lyndarum North and 'Waterline Place' (GEM Apartments) in Victoria, together with settlements at 'Arcadian Hills' Cobbitty, 'Argyle' Elderslie, Spring Farm and 'Magnolia' Hamlyn Terrace in NSW.

Pleasingly, the rate of settlement completion experienced by the Company remained close to 100%, although a small number of customers did require a short extension to their contracted settlement period in order to obtain mortgage finance.

Average gross margin rose half a percentage point to 24.5%, reflecting the mix of product settled, which included relatively more higher margin land sale contracts (notwithstanding the fact that land settlements overall, were lower than the previous year).

I will comment upon the declared dividend later.

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Slide 8 analyses revenue by product type. The year-on-year reduction in revenue from both land-only and housing product, highlights the effect of the slower market on contract signings, while the increase in revenue from apartments is attributable to settlement of the bulk of sales made in the GEM Apartments building at Waterline Place in Victoria.

Slide 9 demonstrates that the average value of contracts signed during the year continues to rise as the product mix skews further towards built form over land-only.

Slide 10 shows that the balance sheet remains strong, with net assets of $396 million. This was down nominally from the prior year due to the impact upon retained earnings of the adoption of the new revenue accounting standard AASB15, which saw the reversal of around $12 million in margin on unconditional contracts with builders in Australia that was recognised under the prior accounting standard, but where control of the land had not passed to the builders as at 30 June 2018, as required by the new standard. The approach adopted in transitioning to the new accounting standard is also responsible for the significant drop in receivables since FY18. Net Tangible Assets of 97 cents per share is down about 3 cents per share since 30 June 2018, which in addition to the effect of adopting the new accounting standard, is also a function of the issue of new shares under the DRP that was operative at 30 June 2018. For those who are interested, the position is set out in detail in the Appendix 4E.

Slides 11 and 12 show that gearing remains well within the Company's target range of 15-35% and continues to follow the traditional pattern of rising with production in the first half, before declining with stronger settlements in the second. The increase in net debt year-on-year is attributable to the net effect of settlement of our exciting new flagship project 'Ara Hills', located at Orewa, some 30 Kilometres north of the Auckland CBD, together with the acquisition of the remaining 50% of 'Riverton' in Jimboomba Queensland, over some tapering of new production commitments in response to market conditions.

Slide 13 is the summary Cash Flow Statement, the most significant aspect of which is the movement in net cash from operations between the years. When considering this, it is important to bear in mind that approximately $62.8 million was invested in the acquisition and first stage of development of Ara Hills, which is expected to contribute to earnings in 2021. Cash generation from the balance of operations was therefore positive at approximately $17 million, notwithstanding the softer market conditions experienced during the year.

Slide 14 shows that earnings per share and declared dividends reduced in line with reported profit. The final, fully franked dividend declared of 1.5 cents per share, brings total fully franked dividends declared for the year to 2.5 cents per share, equating to a fully franked, grossed up yield in excess of 6% per share based upon the current stock price.

Further information is contained within the Appendices.

I will now hand back to Peter.

Thanks Larry.

On Slide 15 we have identified 4 areas which I will take you through which collectively will be the main drivers for results going forward.

I will begin with market conditions which I am pleased to say are on the improve, certainly compared to FY19.

Slide 16 starts by addressing the improving market sentiment. In our FY18 results announcement, and certainly at our 2018 AGM, we called out the risks associated with having 3 significant elections in front of us. It is fair to say confidence in Australian politics was low through FY19, a period where we saw another change in Prime Minister. The lead up to the Federal Election, in particular, was turbulent and had a considerable impact on consumer confidence.

The period since the Federal election has been different and we have seen that reflected in increasing confidence levels.

Recent months have also seen positive changes in relation to mortgage lending and the cost of finance. The Banking Royal Commission had a significant impact on FY19 with lending practices making it much more difficult to obtain mortgage finance lengthening the time it took to get finance. It also had a negative impact on consumer confidence as confidence in financial institutions dropped.

But with changes such as APRA's recent change to the minimum mandatory servicing requirement to be used by banks when assessing home loan applications, as well as reductions in the official cash rate, the environment for our customers seeking finance is improving, but there is still some way to go.

Before I leave the point in relation to finance, I would like to emphasise the point Larry made earlier that whilst this difficult lending environment impacted on consumer confidence to buy, we saw very few cancellations in relation to pre-sales or even new sales made. What we did see was a small number of customers requiring time extensions to meet the longer timeframe of banks in approving loans.

It is also important to remember that there have been reductions in house and land prices, especially in Melbourne and Sydney, which has reset the affordability equation.

All of this is playing out tangibly in a number of ways. We are seeing much more positive, or at least balanced, media commentary around residential property.

We are seeing improving auction clearance rates. This is not only an important indicator of improving sentiment but an important factor for some of our customers who need to first sell their existing home before buying a new home. Improved confidence is also supported by new tax offsets and future tax cuts announced, and in the case of first home buyers by continued support through Government grants and stamp duty relief.

Slide 17 also shows the way this has played out in terms of our recent experience in enquiry levels and contract signings.

Throughout FY19, whilst open in our conversations about downside risks to the market, we also openly expressed our view market fundamentals remained sound.

As set out Slide 18, other than in relation to high rise apartments, the sectors in which we operate continued to be steady. In particular, the supply/demand balance remained positive in that we continued to see an under supply of traditional housing.

Population growth, employment, GDP, interest rates and wages growth all continued to be either strong, trending more positively than in recent years, or at least stable, as set out on Slide 19.

The second factor that will impact on our results going forward is our land bank, in terms of quantity, quality and status.

As can be seen on Slide 20, FY19 did see a reduction in the level of work in progress, which you would expect in more challenging market conditions. However, it remains at historically strong levels and is located in those areas you would want to see it.

Slide 21 also shows our Net Funds Employed levels and geographic diversity to be strong, with growth occurring in Auckland with the settlement and development commencement of our Ara Hills project.

As set out on slide 22 we have maintained a similar level of land bank. We have remained active in looking at new opportunities but prices have, in general, tended to remain above levels we consider as true value. We were successful in acquiring a project at Mernda in Melbourne's north, and whilst not adding to the number of lots we have under control, the acquisition of the remaining 50% of our Riverton, Jimboomba, project increases the value of the land bank and will increase results from that project going forward.

Since 30 June, 2019, we have also entered into a binding Heads of Agreement for about 3,500 lots in relation to a large project in Caboolture, north of Brisbane. At an estimated 8,500 lots in total, this project will take some time to get through the planning process but will form a significant platform for our Queensland operations for many years to come. These types of projects are valuable just as Hobsonville Point, Auckland has been for our New Zealand operations over more than a decade, and as Ara Hills will be going forward.

In Victoria, Lyndarum North, replaced our Lyndarum project. Together they have and will provide a key platform for our Victorian operations for well over 20 years.

Slide 23 is included to provide information in relation to the status of our significant projects. At the start of FY19 we had much in front of us. Lyndarum North had significant pre-sales but we had not completed or settled any stages as we entered FY19. In the second half of FY19 we completed stages 1 to 6 and settled on 287 pre-sales. We will complete stage 7 soon and stages 8 and 9 are under development.

In Queensland our Riverton, Jimboomba, joint venture project was stalled. During FY19 we acquired the remaining 50% interest in that project and we have recommenced both development and sales on that project. Arbor, Rochedale, also commenced in FY19 and 52 pre-sales were made. These will all contribute to profit in FY20. A number of other Queensland projects have also made significant steps forward in terms of achieving important milestones.

In New Zealand, the acquisition of Ara Hills, which had been held up in a lengthy approval process, was finalised and considerable development work has been achieved. Builder pre-sales have commenced and a retail launch is planned for around November this year.

Whilst you would expect projects to be advanced as normal business, this has been an exceptional year for such progress and gives us considerably more momentum moving into FY20 and beyond.

For the sake of time I won't talk specifically to slides 24 to 28. However, I would like to highlight the comment on slide 27 in relation to pre-sales held for the Buckley B precinct at Hobsonville Point. Profit recognition is awaiting the normal Council sign off process which is expected in the first half of FY20. To date almost all of our New Zealand business has been B2B and very lumpy. This has resulted in a skewed FY19 result as the timing of profit recognition for Buckley B has fallen into FY20 despite sales and development all occurring in FY19 or earlier.

The third factor in terms of our future performance relates more specifically to our capabilities. During FY19 we undertook a significant review of our operational structure and capabilities. The first outcome was the appointment of a Chief Operating Officer in September 2018. This was followed by a restructuring of the business along discipline lines rather than geographically, with a strong emphasis on projects. This has given us a stronger national approach with a clearer line of sight to issues to be resolved and opportunities to take. The early outcomes have been very positive and I am sure will be an important contributing factor to our performance going forward.

And in terms of capability we are always aware of the strength of our AVJennings brand. There have been some issues in relation to high profile high-rise apartments in recent months. As consumers move from a position of lacking in confidence to looking to acquire property, we know they rate more than ever the importance of trust in who they are dealing with.

To that end we were proud to achieve the Readers Digest Commendation as a Trusted Brand during the year.

This ties in nicely with the final part of the equation which is Social Licence. Consumers are demanding more and more of those they transact with. They want to know that the businesses they deal with operate the right way and do the right thing. It is the same internally, with the relationship between employee and employer much more equal than has been the norm in the past.

We continue to invest in our people, in safety, and in the community. We continue to focus on innovation and quality and ensuring we deliver high quality, affordable choice to our customers.

These are things we have believed for many years. Slides 35 to 37 look at some of those areas in more detail and whilst I won't speak to those now, I encourage you to look at those later.

To conclude this part of the presentation I ask that you turn to slide 31.

FY19 was a challenging year, and one of the most challenging aspects was dealing with very poor sentiment levels towards residential property. For reasons stated earlier we believe sentiment is improving and will continue in that direction. This will be supported by continuing positive market fundamentals.

From an AVJennings specific aspect, our portfolio has seen considerable advancement through FY19 and this has continued since the end of the year. It places us in a better position to capitalise on improved market conditions.

We have continued to challenge ourselves to find better ways to do things and this has led to change during the year. I am pleased with how this has played out to date and am confident it will be a strong contributor to our performance going forward.

And finally, we continue to focus on those matters that are important to our people, to our customers and to the community. It is largely on those values that the legacy of AVJennings has been built over 87 years.

We believe that maintaining a diversified portfolio, continuous improvement of our operational performance and focusing on the needs of our stakeholders will drive better returns for shareholders going forward.

Before I hand back to Rochelle to invite questions, can I thank my executive team and all staff of AVJennings for their enormous efforts during a challenging year. I am sure we are all looking forward to seeing the results of those efforts moving forward.

I also thank the Board, all our business partners and our shareholders for their support over the past 12 months.

ENDS…

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