Mayfield Childcare Limited (ASX:MFD) - CY 2019 Full Year Results

31 January 2020

MAYFIELD
CHILDCARE LIMITED

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Contents

01 2019 Highlights

- **Business strength delivers solid performance**
  - Continued positive growth across all financial and operating measures
  - Revenue growth of 13.9% on the back of 2018 and 1H 2019 acquisitions, slightly improved pricing and occupancy growth
  - Easing trading conditions saw occupancy grow by 0.5%
  - Tight operational management delivered excellent centre based EBITDA margin growth of 2.8% to 23.0%
  - Solid EBIT growth of 12.6%, fell marginally short of guidance, due to higher wage oncost provisions and depreciation charges

- **Attractive earnings and dividends**
  - Underlying NPAT of $3.8m up 11.8%
  - Fully franked dividend for CY 2019 of 7.71cps

- **Increased investment in business assets and operations**
  - Capital improvement program continues across the centres, with a focus this year on external play environments
  - Completion of centre based Website development and integration with Social Media portals
  - Creation of Business Operations and Service Delivery Management functions
  - Ongoing investment in centre resources and professional development of staff

- **Acquisitions**
  - The single acquisition for 2019 was a great pick up for the business, though the lack of suitable acquisitions targets has been frustrating
  - The company has pursued a number of significant acquisition opportunities, though at this stage has been unable to agree acceptable terms
  - More broadly the business is considering expansion into other states, should an opportunity for a cluster of centres present itself

01 2019 Highlights

- **Quality recognition**
  - Our Quality Improvement Program continues to deliver great results for the business
  - Initiatives focused on Centre Presentation, Educator Development and Educational Programs
  - Despite acquiring a Working Towards centre during 2019, 86% of the portfolio is now rated Meeting or Exceeding the National Quality Standard

- **Focused cash management**
  - Restructured debt facility, extending the terms of the individual loans by 5yrs, securing attractive rates along with greater redraw flexibility
  - Prudent cash management strategies alleviating financing costs
  - Available debt of $6.55m for acquisitions and working capital

- **Improving trading conditions**
  - Sector challenges of the past few years are moderating
  - Supply for the most part in Victoria has eased, with reduced supply growth at least evident in the geographical areas that Mayfield operates
  - With the new CCS system now past it first anniversary, parents feedback indicates they now understand he system and benefits to be derived
  - CCS will continue to slowly stimulate demand

02 **Financial performance:**

AASB 16 *Leases*

Operating performance

Balance Sheet

Cash flows

Dividend

02 AASB 16 *Leases* Standard

- As previously advised, 1 January 2019 saw the implementation of the new Accounting Standard, AASB 16 *Leases*. With the exception of short-term and low-value asset leases, all leases are now recognised on the balance sheet, with the following implications:
  - Lease liabilities (current and non-current) matched by corresponding right-of-use assets (non-current) upon implementation;
  - Right-of-use asset depreciated on a straight line basis over the life of the lease; and
  - Lease payments apportioned between principal (repayment of liability B/S) and interest (P&L) components resulting in lower profits in the early years and higher profits in the later years of each lease.

- In keeping with the sector, Mayfield is reporting the reversal of AASB 16 *Leases* to highlight its underlying business, the economics of which remain unchanged.
  - CY 2019 Full Year NPAT impact of $431K

- The table below highlights the key financial statutory metrics impacted by AASB 16 and the underlying business result:

	CY 2019 Statutory	CY 2019 Underlying	Fav / (Unfav) Movement		CY 2019 Statutory	CY 2019 Underlying	Fav / (Unfav) Movement
Performance				**Balance Sheet**			
Earnings before interest & tax	5,906	5,734	(173)	Working Capital Ratio	30%	55%	25%
NPAT from continuing operations	3,347	3,778	431	Debt to Equity Ratio	45%	44%	1%
Earnings per share (EPS) - cents	10.58	11.94	1.36	Gearing Ratio	29.8%	29.6%	0.2%
EBIT Interest cover	4.1x	8.7x	4.6x	Net Tangible Assets - cents	(116.4)	(35.3)	81.1

02 Operating Performance

$000's	CY 2019 Statutory	AASB 16 *Leases*	CY 2019 Underlying	CY 2018 Underlying	Var %
Revenue	35,866		35,866	31,489	13.9
Labour costs	20,186		20,186	17,749	(13.7)
Operating expenses	2,494		2,494	2,320	(7.5)
Facilities costs	1,131	3,818	4,949	4,385	(12.9)
Centre EBITDA	**12,055**	**(3,818)**	**8,237**	**7,035**	**17.1**
HO Staff & related costs	1,363		1,363	1,073	(27.0)
Other corporate overheads	712	59	771	692	(11.4)
Group EBITDA	**9,980**	**(3,877)**	**6,103**	**5,270**	**15.8**
Depreciation	4,073	(3,704)	369	179	(100.0+)
Group EBIT	**5,906**	**(173)**	**5,734**	**5,091**	**12.6**
Interest	1,428	(767)	661	562	(17.6)
PBIT	4,478	595	5,073	4,529	12.0
Tax	1,131	164	1,295	1,151	(12.5)
NPAT from Continuing Operations	**3,347**	**431**	**3,778**	**3,378**	**11.8**
Earning per share (EPS)			11.94c	10.99c	8.6
Centre EBITDA margin			23.0%	22.3%	2.8
Wages to Revenue %			56.3%	56.4%	0.1

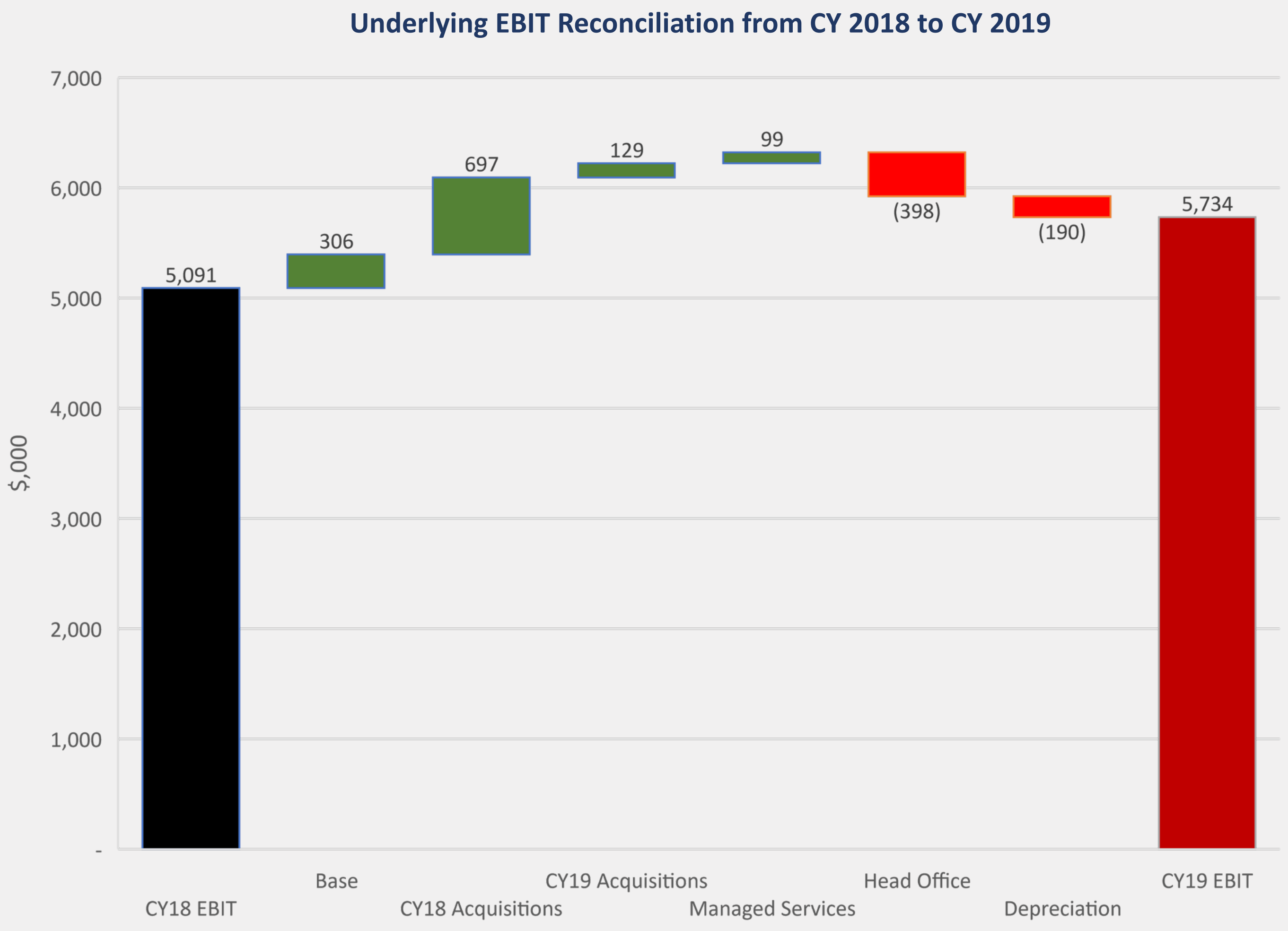
The operating performance for CY 2019 reflects the following

- Revenues up 13.9% on the back of 2018 and 1H 2019 acquisitions, improved pricing and occupancy growth
- Total centre expenses up 13.0%, allowing for acquisitions and disposals, underlying expenses up 3.1%,
- Wages to revenue have held at 2018 levels of 56.3%
- Centre operating margins strengthened 2.8% to 23.0%
- Corporate increases reflect expanded Operations and Area Management functions,
- Depreciation driven by increased investment in centre refurbishment program and Website development. Annualised Capex of $1.0m
- Movements in finance costs reflects full year effect of increased borrowings to fund 2018 & 2019 acquisitions
- Underlying NPAT of $3.8m - up 11.8%

Note: Statutory Reports have been adjusted to reverse the impact of AASB 16 Leases

02 Group EBIT Reconciliation

- The initial IPO portfolio and 2017 acquisitions generated additional EBIT of $0.3m
- Though slightly behind expectations, CY 2018 acquisitions have responded to our investment in centre improvements and quality programs delivering EBITDA growth $0.7m
- Our 2019 acquisition has performed well to deliver EBITDA of $0.13m for the 6mths of trading
- Managed services marginally up $0.1m
- Head Office expenses up $0.4m recognising a full year of structural expenses and growth of the business
- Depreciation up $0.2m reflects increased investment in centres and Website development.



02 Balance Sheet

$000's	31 Dec 19 Statutory	AASB 16 *Leases*	31 Dec 19 Underlying	31 Dec 18 Underlying	Var
Cash & cash equivalents	649		649	880	(231)
Trade & other receivables	1,572		1,572	1,256	316
Current Assets	**2,221**		**2,221**	**2,136**	**85**
Plant & equipment	2,151	55	2,206	1,324	882
Deferred tax	652	(164)	488	396	92
Right of use assets	25,232	(25,232)	-		-
Intangibles	39,741		39,741	38,856	885
Non-current assets	**67,776**	**(25,431)**	**42,435**	**40,576**	**1,859**
Assets	**69,997**	**(25,341)**	**44,656**	**42,712**	**1,944**
Trade & other payables	1,544		1,544	1,317	227
Borrowings	1,295	33	1,328	-	1,328
Leases	3,360	(3,360)	-	-	-
Tax liabilities	53		53	765	(712)
Provisions	1,137		1,137	933	204
Current liabilities	**7,389**	**(3,327)**	**4,062**	**3,015**	**1,047**
Borrowings	11,493	33	11,526	13,300	(1,774)
Leases	22,478	(22,478)	-	-	-
Provisions	79		79	142	(63)
Non-current liabilities	**34,050**	**(22,445)**	**11,605**	**13,442**	**(1,837)**
Liabilities	**41,439**	**(25,772)**	**15,667**	**16,457**	**(790)**
Net Assets	**28,558**	**431**	**28,989**	**26,255**	**2,734**

- Lower cash position from partial funding of acquisitions, and tighter cash management strategies to offset financing costs.
- P&E increases reflect ongoing centre refurbishment programs
- Intangibles up $0.9m following latest centre acquisition
- Commencing debt repayments in Jan 2020
- Tax movement reflects final payment of 2018 tax and timing on 2019 obligations
- Overall reduction in borrowings reflects cash management to offset financing costs
- Net assets of $29.0m up 10.4%

Note: Statutory reports have been adjusted to reverse the impact of AASB 16 Leases

02 Cash flows

$000's	CY19 1H Statutory	AASB 16 *Leases*	CY19 1H Underlying	CY 2018 Underlying
Operating cash flows				
Customer receipts	35,596	-	35,596	31,465
Operating expenses	(25,252)	(3,877)	(29,129)	(26,262)
Net interest paid	(660)	(3)	(663)	(523)
Other	17	-	17	51
Income tax paid	(2,099)	-	(2,099)	(1,783)
Net operating cash flows	**7,602**	**(3,880)**	**3,722**	**2,948**
Investing cash flows				
Plant & equipment	(1,248)	-	(1,248)	(1,087)
Centre acquisitions	(902)	-	(902)	(7,041)
Other	6	-	6	9
Net investing cash flows	**(2,144)**		**(2,144)**	**(8,119)**
Financing cash flows				
Borrowings (net)	(750)	(17)	(767)	5,852
Repayment of Leases	(3,127)	3,127	-	-
Interest paid on Leases	(770)	770	-	-
Dividends paid	(1,934)	-	(1,934)	(1,279)
Other	(5)	-	(5)	(61)
Net financing cash flows	**(6,586)**	**3,880**	**(2,706)**	**4,512**
Net increase / (decrease)	(1,128)	-	(1,128)	(659)
Cash & cash equivalents	**649**	**-**	**649**	**880**

- Positive net operating cash flows in line with business performance
- Net Investing cashflows, reflect ongoing investment in centre upgrades and resources along with acquisition growth
- Overall reduction in borrowings reflects cash management to offset financing costs

Note: Statutory reports have been adjusted to reverse the impact of AASB 16 Leases

02 Dividend

- In March of 2019, Mayfield paid its annual fully franked dividend of $2.8m or 8.97 cps for the year ended 31 December 2018
  - Dividend payment was made up of $1.9m in cash and 869,647 ordinary shares issued under the DRP at $0.97/share

- The Board announces for the 12 months ending 31 December 2019, Mayfield will pay a fully franked divided of 7.71cps
  - Payable in March 2020

- The Board recommends consideration of the Dividend Reinvestment Plan (DRP).
  - Shareholders who elect to take shares instead of cash under the DRP will receive shares at a discount of 5% to the VWAP share price over the pricing period

- Commencing in CY 2020, it is the intention of the Company to transition to an Interim and Final Dividend structure, while taking the opportunity to review the quantum of the dividend in order to better facilitate capital growth from acquisitions

03 Operational performance:

Centre based metrics

Occupancy & revenue

Operational metrics

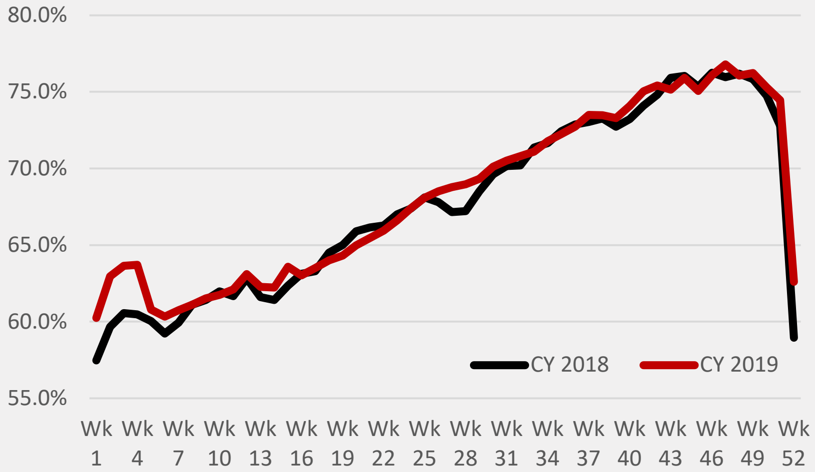
03 Centre Based Metrics

- Average fees are $115, following a 3.9% price increase
  - In real terms, price increases reflect a $4-5/day fee increase
  - Excluding the 2 highest priced centres (+$140/day), underlying average daily fee is $111
- Wages as a percentage of revenue has been held at 2018 levels of 56.3% allowing for an Award rate increase of 3.0%
- Healthy average lease term across the business of 21.7 years and well below market rental rates per child at $2,160
- Leasehold rental increases of 2.7% is a mixture of CPI, and fixed rates increases, along with planned market reviews.
  - The decline over the 2018 year reflects low CPI levels

Key Metrics	CY 2017	CY 2018	CY 2019
Number of centres	19	20	21
Number of registered places	1,588	1,693	1,771
Average centre size	84	85	84
Average fees per day	$105	$111	$115
Average daily fee increase	5.9%	3.5%	3.9%
Number of educators	423	445	490
Wages to revenue ratio	55.6%	56.4%	56.3%
Average award wage increase	3.3%	3.5%	3.0%
Average lease term	22.2 yrs	22.4 yrs	21.7 yrs
Average rent per registered place	$1,933	$2,119	$2,160
Average rent increase	2.7%	3.1%	2.7%

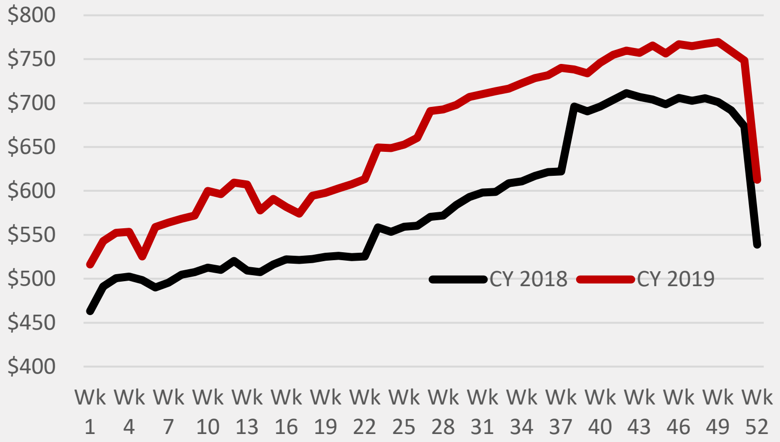
03 Occupancy, Revenue & Wage Performance

Weekly Occupancy %



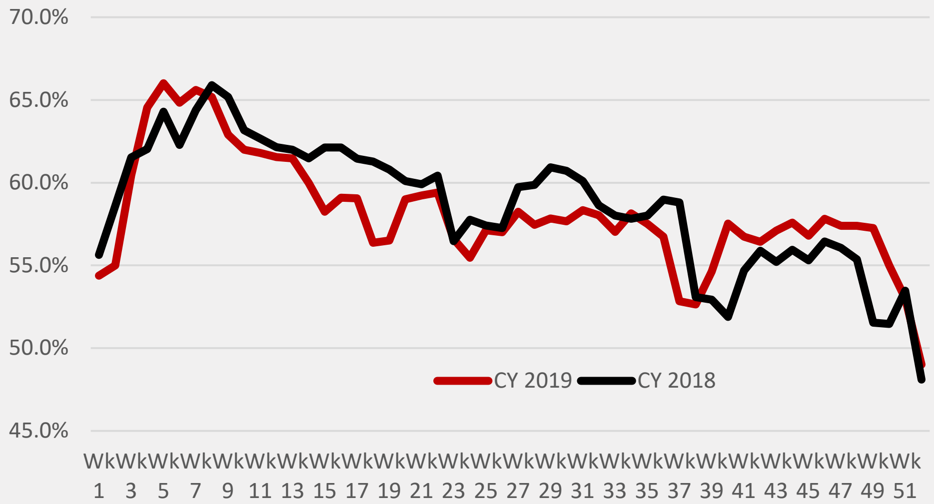
Occupancy gains were mixed throughout the year, with centres in the Western Suburbs struggling with overall results up 0.5% to 69.5%

Weekly Revenue A$ 000's



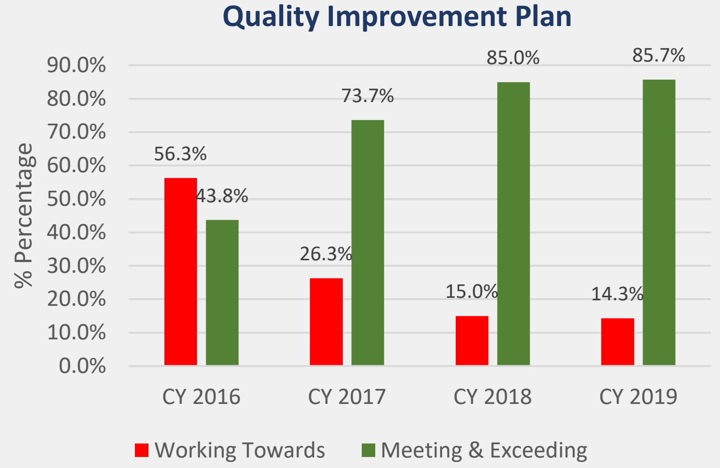
Revenue performance tracked in line with occupancy performance and pricing. The step change in 3rd Qtr 2018, represents 2018 acquisitions

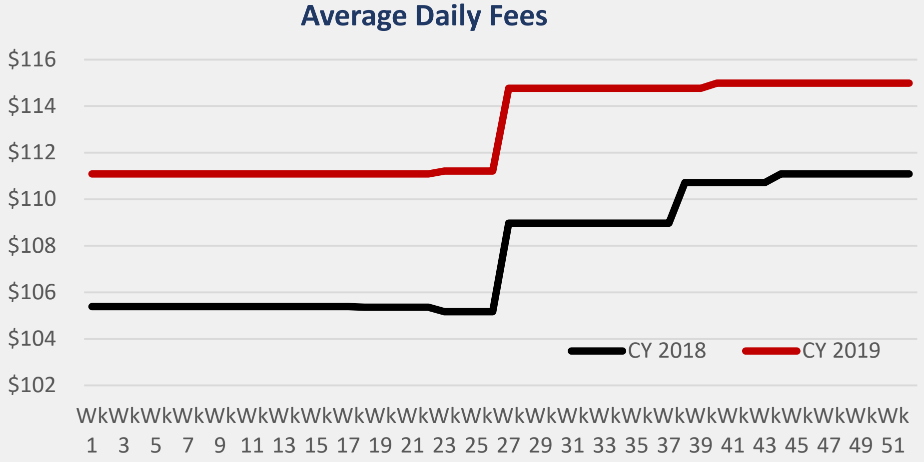
Wages % of Revenue



Wage performance was very pleasing throughout the year, essentially holding at 2018 levels at 56.3%

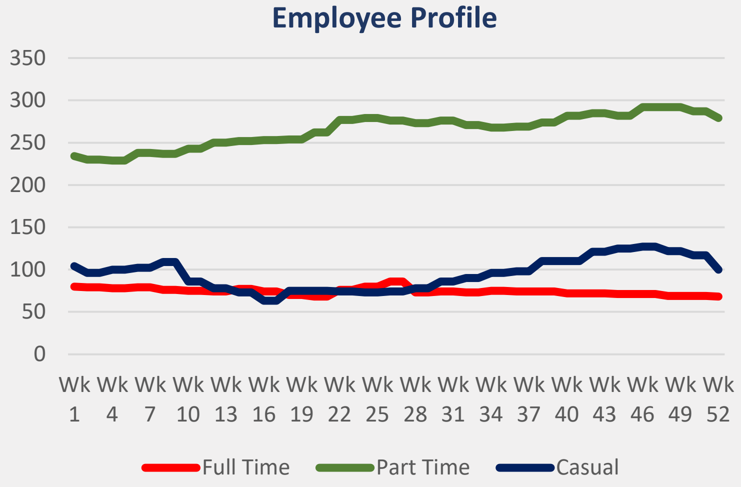
03 Operational Metrics





Our Quality Improvement continues to deliver great results for the business.
Note: a Working Towards centre was purchased in 2019

Average daily fees sit at a comfortable level of $115/day following the price increase of 3.9% - this equated to $4 or $5/day increase depending on the centre



Total centre staff of 490. Senior centre based staff (Centre Mgr, ECT and Education Leaders) have remained stable, though increases in casual staff in qtr 4, did challenge wage levels

04 Acquisitions:

04 Centre Acquisitions

20 **No of centres as at Dec 2018**

1 **Centre acquired in July**

0 **Centres disposals**

21 **Total centres**

Key Metrics	Acquisitions
Number of centres	1
Registered places	76
EBITDA CY 2019	$0.12m
Average Daily Fees	$119
Rent per place	$3,500
Purchase price	$0.9m
Funding source	Debt / Cash

- While the single acquisition for 2019 was a great pick up for the business, the lack of suitable acquisitions targets has been frustrating. Much of the available stock appears to be
  - Small (<50places), home conversions that present poorly
  - High performing though over priced centes, with questionable vendor metrics
  - Regionally based centres that don't fit with a our Management structure
- The business is currently pursuing a significant acquisition opportunity, though its unclear at this stage if we will agree acceptable terms.
- More broadly the business is considering expansion into other states, though only if a cluster of centres are available, in order to replicate our central management structure and contain our cost to serve

05 Industry:

05 Industry

- **Victorian childcare supply**
  - In the context of Victoria, we have seen supply numbers progressively decrease quarter on quarter which has been encouraging
  - The in-market perspective in geographical areas that Mayfield operates, is that supply growth has eased
  - Though supply in the December quarter increased in sharp contrast
  - Also of note, is that new centres being built are typically larger (+100 places) than that of the other States and Territories
  - Mayfield’s view is such
    - Supply will steadily increase albeit at slower rates than in past years
    - Inner suburban areas will always be sought after – greater potential for higher fee / higher margin businesses
    - New housing developments will continue to attract developers, though Council’s are more attuned to assessing the merits of new developments
    - There will be gradual rationalisation of the smaller house-conversion centres
    - As Mayfield already operates in highly competitive areas, our success has, and will continue to be, driven by a focus on quality through continuous investment in our centres, our educational programs and our teams, which cant be matched by the broader independent childcare operator

- **Child Care Subsidy**
  - 18 months on from the introduction of the CCS, parents appear to understand the system, they’ve managed their way through the year-end rebate process, and now for the most part its business as usual.
  - The introduction of sessional hours has been essential in supporting families to maximise their eligible hours
  - Moving forward, Mayfield views the CCS as a slow but progressive stimulus to the childcare sector

06 2020 Outlook:

06 2020 Outlook

- The Mayfield Board and Management team look forward to a more robust year in 2020.
- Key areas of focus
  - Drive Business Growth
    - Generate Underlying EBIT growth of 10% excluding any new acquisitions
    - Aggressively seek acquisition growth in Victoria, while exploring interstate expansion in keeping with company operating structure
    - Foster emerging Managed Services business
  - Operations Management
    - Deliver operational efficiencies through enhanced service delivery
    - Focused workforce planning to contain wage costs
    - Competitive pricing
  - Continued investment in Quality Platform
    - Maintain investment in our people, our programs and our resources
    - Ongoing capital program to enhance centre offering and presentation
  - Increase Shareholder value
    - Move to Interim and Final dividend structure

Thankyou

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