Release to the Australian Securities Exchange

Adairs Limited
Results for first half of FY23
Record Group sales with 24% increase in NPAT

20 February 2023

Adairs Limited (ASX: ADH)

Adairs Limited today released its results for the 26 weeks to 25 December 2022 (1H FY23).

The Group achieved record sales in 1H FY23 with strong growth coming from the Adairs and Focus on Furniture ('Focus') brands.

1H FY23 financial summary (compared to prior corresponding periods)

- Group sales +34.1% to $324.2 million
- Underlying[1] Group EBIT +7.9% to $35.5 million
- Statutory NPAT of $21.8 million (+23.9%) and EPS 12.7 cps (+22.2%)
- Group net debt $81.0 million, $12.2 million lower than June 2022
- Interim dividend of 8.0 cents per share (fully franked) declared and DRP remains active

1H FY23 non-financial summary

- Adairs store floorspace increased +2.4%
- New Adairs brand website launched with an enhanced customer experience
- Focus continues to perform well with a strong value proposition, quality product range, outstanding service, high stock availability and short lead times
- Operational outcomes at the Adairs National Distribution Centre ('NDC'), while improving, continue to be below expectations and remain a priority for management and DHL
- Mocka's operational platform has been restored, improving its customer experience

Brand performance[2]

Adairs

The Adairs brand delivered a record sales result in 1H FY23, up 13.1% to $220.4 million. Adairs store sales were up +22.9% with no COVID-related closures (31% of trading days were lost in 1H FY22) while online sales were down -7.4% to $58.5 million (26.5% of total sales) as customers returned to stores.

As anticipated, gross profit margin softened in 1H FY23 against 1H FY22 (-330 bps) because of higher inbound container rates and industry-wide increases in delivery charges by local carriers. Gross margin will benefit going forward from significantly lower inbound freight costs and minimal exposure to the USD with 2H FY23 hedged at 72.5 cents.

---

[1] See Appendix 6 of the Investor Presentation for a reconciliation of statutory and underlying results.

[2] All comparative measures are against the prior corresponding period unless otherwise stated.

A new Adairs brand website was launched in November. The new website provides an improved customer experience (simpler navigation, better product showcasing, faster page speeds) and importantly provides the foundations and capability for future online business initiatives, a number of which are in development.

Two new stores were opened, and four stores were upsized driving a +2.4% increase in gross lettable area (GLA) during the half and a +5.5% increase over the last 12 months. A further 2-4 new stores are expected to be opened in 2H FY23.

The DHL-operated NDC became fully operational in July 2022. Since commencement, operational outcomes have been below expectations which has adversely affected customer experiences and resulted in significantly higher cost of operations. Adairs and DHL management continue to work collaboratively to resolve these issues with early signs that operational outcomes are improving. As part of an updated agreement a new pricing model became effective in January 2023 which will see average variable costs per unit dispatched reduce by approximately 20% over 1H FY23 levels.

Adairs' cost of doing business (CODB) as a percentage of sales increased by 110bps in 1H FY23 reflecting the return to a fully operating store network combined with the inflated supply chain costs associated with the NDC, including temporary warehousing requirements. Management estimates that the warehousing cost impact of this to be c.+$5 million on 1H FY22.

Adairs underlying EBIT declined -23.4% to $18.7 million.

Focus on Furniture[3]

Focus delivered a strong 1H FY23 performance with sales +20.1% to $78.6 million. Store sales increased +28.8% to $73.7 million and online sales reduced $3.3 million to $5.0 million (6.3% of total sales) with all stores open throughout the half.

High levels of product availability, short lead times, quality product ranges and a disciplined pricing strategy delivered gross margin % gains in 1H FY23 (+40bps) despite the industry-wide supply chain headwinds.

The strong sales and margin growth delivered EBIT growth of +27.2% to $16.6 million.

One new store is expected to open in 2H FY23 and one existing store will be refurbished. New store openings remain a priority with a pipeline of opportunities being built despite the tight market for space in Homemaker centres.

Mocka

Mocka sales fell -26.8% to $25.1 million as the brand resolved the operational issues of 2H FY22 and cleared excess inventory. The impact of customers returning to stores has been felt by most pure play online businesses with the impact on Mocka amplified by its operational issues in 2H FY22. Website traffic and search activity across Mocka's sites is more than 10% higher than pre-COVID levels[4].

[3] Focus' 1H FY23 performance has been measured against the full 26 weeks of 1H FY22 to enable a true like-for-like comparison. Adairs ownership commenced on 1 December 2021, with Focus contributing 4 weeks only to the Group's 1H FY22 result.

[4] Compared to website traffic level in 1H FY19 and 1H FY20

Gross profit was impacted by extensive clearance activities of discontinued ranges in Q1, higher delivery costs following a change of the Australian domestic delivery partner (after the disruptions experienced in FY22), and higher inbound shipping costs. Inbound shipping costs are now materially lower which will benefit gross profit in 2H FY23 and beyond.

Mocka finished 1H FY23 with an underlying EBIT of $0.3 million.

Management's focus on stabilising the operating platform, restoring customer confidence, growing GM% and reducing the inventory range is progressing. Whilst the operational issues of 2H FY22 continued to impact Q1 FY23, the work done on resolving the issues and delivering great product has seen margin improve in Q2 FY23 and into early 2H FY23 which will form the basis for improved profitability moving forward.

Cash flow and balance sheet

Cash flow improved through the half with stronger sales and offshore supply chains stabilising leading to improved stock turns. Group net debt fell by $12.2 million over the half to close at $81.0 million. The Group has total finance facilities of $135 million available until January 2025 ($45 million) and January 2026 ($90 million) with substantial covenant headroom.

Inventory closed in line with expectations, noting Boxing Day was in 2H FY23 but 1H in FY22 and Chinese New Year is a week earlier in FY23. Mocka reduced its previously elevated inventory holdings by c.20% over 1H FY23 with excess and underperforming inventory cleared.

Supply chain volatility has reduced however the Group has retained inventory buffers to manage the risk of unforeseen interruptions. The majority of inventory across all three brands is in core category lines with lower fashion/seasonal risk. Subject to the continued stability in offshore supply chains, inventory levels are expected to reduce across 2H FY23.

Trading update and outlook

The first week of 2H FY23 saw record Boxing Day sales for both the Adairs and Focus brands. Mocka sales for the first seven weeks were in line with expectations with margins 570bps above the prior corresponding period and 280bps above 1H FY23.

Unaudited Sales (first 7 weeks of 2H FY23)	v 2H FY22
Group	+1.8%
Adairs	+3.1%
Focus	+14.4%
Mocka	-(31.7)%

Note: First seven weeks is comparable with the previous corresponding period with all stores open and trading.

Cost-out programs have been initiated across the Group to manage the potential impact of a weaker economic environment. Inbound freight costs are reducing, while the Group's hedging strategy has mitigated AUD weakness with USD purchases in 2H FY23 fully hedged at 72.5c.

Productivity at the NDC has improved over the last 5 weeks delivering better cost and customer outcomes. The new pricing agreement with DHL will see average variable costs per unit despatched through the Adairs NDC reduce by approximately 20% from January 2023 compared to 1H FY23 levels.

adairs

Commenting on the result and outlook for the balance of the year Managing Director and CEO, Mark Ronan, said:

"The first half of FY23 delivered strong sales growth for the Group with customers across our brands preferring to shop in store. The continued Group sales growth highlights the strength of our brands, the critical role of our exclusive product, and the resilience we have seen with the Australian consumer. Across the brands we are focussed on our operational execution, continued development of exclusive on-trend product and growing our membership bases, putting us in a good position to manage what is likely to be a more challenging trading environment in the second half."

Guidance

Current trading conditions are broadly in line with plan and as a result the existing FY23 sales guidance is retained. Elevated supply chain costs in 1H FY23, some of which will continue into 2H FY23, mean that EBIT guidance has been updated as follows:

	FY23 Guidance	Previous
Group Sales ($m)	625 – 665	625 – 665
Group EBIT ($m)	70 – 80	75 – 85
Capital investment ($m)	12 – 15	12 – 15

Interim Dividend and DRP

Given the underlying NPAT achieved in 1H FY23 and having regard to the prevailing trading environment and a desire to focus on debt reduction, the Board has declared an interim fully franked dividend of 8.0 cents per share (8.0 cents in 1H FY22). The Record Date for the dividend will be 21 March 2023 with payment on 6 April 2023.

The Board has determined that the Dividend Reinvestment Plan (DRP) will remain active for the FY23 interim dividend and that the key features will remain unchanged:

- the Pricing Period used to determine the DRP Allocation Price shall be the 5 trading days commencing on the second Business Day immediately following the Dividend Record Date (23-29 March 2023, inclusive);
- a 1.5% discount to the Average Market Price will apply in setting the DRP Allocation Price; and
- DRP shares will be sourced via an issue of new ordinary shares by Adairs Limited.

DRP elections must be received by no later than 5pm (Melbourne time) on 22 March 2023 to be effective for the FY23 interim dividend.

Conference Call

As previously announced, a conference call for investors and analysts to discuss this announcement, hosted by Mark Ronan (Managing Director and Chief Executive Officer) and Ashley Gardner (Chief Financial Officer), will be held at 11.00am (Melbourne time) today.

Anyone wishing to listen to the call are required to pre-register which can be done by clicking on the link below. You will be given a unique pin number to enter when you call which will bypass the operator and give you immediate access to the briefing.

Pre-register for call (click here)

This call will be recorded and made subsequently available on the Adairs Investor Relations website (http://investors.adairs.com.au/investors/).

ENDS

This announcement has been approved by the Board of Adairs Limited.

Contact:
Jamie Adamson
Head of Investor Relations
P: +61-3 8888 4500
M: +61 (0) 437 449 935
E: ***jadamson@adairs.com.au***

About Adairs Limited
Adairs Limited is Australia's largest omni channel specialty retailer of home furnishings, home furniture and home decoration products. We own and operate three vertically integrated brands in the Home category – Adairs, Mocka and Focus on Furniture. All brands are design led, customer focused, and sell quality in-house designed product direct to customers through our own channels in Australia and New Zealand.

Adairs Limited's head office is in Melbourne, Australia.

For further information visit our investor relations website ***www.investors.adairs.com.au***