Arvida

NZX RELEASE
CHAIR'S ADDRESS TO THE ANNUAL MEETING OF SHAREHOLDERS

21 July 2023

"It is my pleasure to address you today, with this being my 9th year as a director and second as your Chair.

The business has become a considerably larger entity than when first listed with 18 villages in 2014. We have quickly become a leading provider of retirement living and aged care services and as you know, now operate 36 villages nationally providing services to more than 6,750 residents – and we are well positioned to continue to grow and deliver on our strategic goals.

Notwithstanding, 2023 again presented a number of difficult challenges for the business.

Performance through the first part of the year was heavily impacted by New Zealand's Omicron outbreak. While a recent experience – and hopefully not one that will repeat in the near term – we should not underestimate the impact of the pandemic on aged care worldwide.

Our older residents and those with comorbidities were the most at risk of serious health outcomes from infection and our primary focus was on keeping Covid out.

Our approach continued to prioritise resident and team wellbeing and we again implemented a range of precautions, but these came at considerable cost. Few subsidies were provided by the government to support our response.

The result was lower care profitability as admissions were restricted in an environment of higher operating costs. Once through the worst of the Omicron outbreak, we saw an improvement in care occupancy and revenue performance as settings began normalising.

As a Board, we consider our strategy during the pandemic was the right one and entirely aligned with our purpose, our values and our priority in focusing on and investing in our people - we received very positive feedback from residents and family on the approach we took.

Through this period the residential property market also faced its own challenges with a material reduction in buyer demand. The number of days to sell a house increased, and pricing and volumes continued to decline. This had a material impact on general market liquidity as buyers paused waiting for more favourable purchase conditions. While our village unit prices remained quite resilient over this period, the impact on us was an increase in settlement timeframes and an associated increase in working capital.

Operating performance and cash flows were also impacted by rapid cost inflation, particularly in wages and construction costs, as well as severe weather events in January and February of this calendar year.

In this environment, with a number of factors negatively impacting performance, we were very pleased to report a resilient set of financial results.

For the 12 months ending 31 March 2023 our underlying profit was $88 million, up a significant 20% on the prior year.

So facing the challenges of a global pandemic and a deteriorating residential property market, we focused hard on aspects of the business we had a level of control over, with an imperative of making sure we were offering our residents and the market an outstanding, market leading village living and care experience.

We believe that this was a key contributor to our sales performance. In a weak property market, demand, and pricing for Arvida units remained strong. The level of sales and continued momentum reflects positively on the relative appeal of our product, our underlying business culture and our residential living and care offering.

Embedded value now represents an estimated $1.1 billion of future cash flow.

New Zealand's ageing population will continue to drive demand for aged care services and retirement living options. At the same time, continued underfunding of the sector by the government is accelerating retirement living demand as older New Zealanders look to lock in their care options early.

Provision of care will remain a core part of our strategy as we believe a continuum of care offering is an essential part of our business.

However, we continue to be very concerned about government underfunding in the wider aged care sector. Arvida is part of a group called Aged Care Matters that spent much of the year lobbying government about the serious risks facing the sector from underfunding.

More than 1,200 aged care beds closed in New Zealand in 2022 and a number of key providers have recently advised that they intend to reduce the care component of their business, this having the obvious outcome of progressively reducing care capacity across the country. With nowhere else to go, the public health system becomes the only option for many older people to obtain care. With the number of New Zealanders aged over 75 years expected to grow by more than 75% over the next 15 years, this becomes unsustainable.

Supply of aged care beds cannot be turned on overnight. It takes around three years to plan, build and commission a new 60 bed care centre. This suggests access to quality aged care will likely be at a premium in years to come.

While future demand remains clear, building material shortages and elevated build costs have meant that we have taken a more cautious approach to the type and volume of projects we are currently undertaking.

Development capital expenditure has been tapered, with our annual build rate now closer to 200 units – which is considerably lower than the 300 units we had anticipated to be building at this stage.

We have reduced our capital expenditure commitments to ensure our capital position remains robust and appropriate for the current risk and opportunities, and our balance sheet remains strong.

You will be aware that during the year, the market increased its focus on the sector's capital capacity and management, this driven by increased funding costs and by capital constraints faced by some of our competitors. The Board and senior executive team spent considerable time re-examining and ratifying our capital management framework to ensure we were closely monitoring our capital sources and supply and matching our capital capacity to our commitments.

Gearing at 31% was the lowest in the sector at balance date, and within the Board's target range of 25% to 35%. Maintaining a conservatively geared balance sheet in the current environment is critically important to the Company. The imperative here is to make sure our capital position is not only strong defensively in the event the market remains difficult for longer, but also to have capital capacity to capture suitable opportunities to continue to develop and enhance the portfolio as appropriate.

Dividend policy is a key part of our capital management framework.

Our challenge, as we have grown, has been to set a sustainable dividend policy which aims for dividend payments to be funded from free cash flows derived from operations.

Market events have resulted in significant cash flow volatility over the past couple of years. Through this period, we have maintained a dividend stream as we recognise a large number of our shareholders value regular dividend payments.

However, in balancing the payment of dividends against the capital requirements of the Company, including the requirement to fund the growth of our portfolio, the Board has adopted a lower distribution range of 30% to 50% of full year underlying profit going forward. Dividends are expected to be at the bottom end of this revised payout range until operating conditions improve and business cash flows mature.

Over time we would expect to see a significant uplift in resale gains and the realisation of deferred management fees, along with increases in care and village fees. This will improve the cash flow performance of our operations.

In terms of governance, with Arvida having been operating since 2014, the board is comprised of directors that were appointed around the time of our listing, which means that Arvida has the slightly unusual situation of the majority of its directors having similar board tenure. Given this, our board composition and succession plan now have an increased concentration on director rotation, with this process focused on the careful selection and appointment of new directors with the skills and experience required by the board and company at the time, balanced against the requirement to preserve board stability, company and sector knowledge and overall performance.

We anticipate that we will add another director to the board this year to facilitate director rotation, and with the focus of regulators and the broader market intensifying in the areas of audit compliance and reporting, particularly in the expanding areas of sustainability, environmental and risk management and disclosure, at this stage the focus is likely to be on introducing a director with strong capability and experience in these areas.

Any changes to the board will of course be announced to shareholders and the market as appropriate.

I would like to mention the separate sector reviews being undertaken by the Commerce Commission and Ministry of Housing and Urban Development. Both are scrutinising different aspects of the retirement sector.

There are some 200 operators involved in the sector. While practices will vary across the operators, all are governed by legislation that requires occupational right agreements to be signed off only after appropriate legal advice has been obtained by the resident.

Considerable effort has been made to ensure our occupational right agreements are written in plain English and adopt best practice terms. Feedback on the resident experience is obtained every year through our resident survey with the sales and contracting experience forming part of this survey.

However, improvements to the residents' quality of experience will always be welcomed. We look forward to keeping you updated on progress with these reviews.

Looking forward, Covid is expected to have a lesser impact on business performance as transmission rates decline. We are also seeing early signs of improved liquidity in the residential property market which is flowing through to sales activity. However, the general election in the third quarter is likely to result in a period of uncertainty for the market, this expected to have an impact on New Zealand's economic activity.

Acknowledging the uncertainties around economic and market conditions, we believe Arvida is well positioned to continue to progress and deliver shareholder value. We are rebalancing our focus across residents, teams and shareholders as we move out of the Covid environment and hopefully transition into a stronger residential market.

In concluding ladies and gentlemen, I would note that while market conditions remain challenging, the business is in good shape. We have an outstanding living and aged care offering and our aspiration is for this to lead the market, our product is well positioned, and we have achieved very strong sales in a difficult sales environment, our balance sheet is strong and we remain well positioned to continue to grow the portfolio in target markets, albeit that we are taking a more cautious approach to capital commitments at this stage.

Before I hand over to Jeremy I would like to acknowledge and thank the wider Arvida team for an outstanding effort and contribution to the business during the year. This was not an easy operating environment and its fantastic to see the approach taken by the team and the result that was achieved. I would particularly acknowledge the effort of the team during the Auckland flood crisis earlier in the year, which saw our villages in one case quite badly damaged, but with our residents and team members safe and sound.

– ENDS –

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About Arvida:
Arvida is one of New Zealand's largest aged care providers owning and operating 36 retirement villages located nationally with over 6,750 residents. Each village operates independently under a corporate structure that supports village operations to ensure quality and consistency of service. Arvida provides a continuum of care that extends from independent living to full rest home, hospital and dementia-level care.

Arvida's growth strategy includes the targeted development of new villages in areas that are supported by a strong demographic and economic profile and acquisition of quality villages that meet strict acquisition criteria as well as the development of additional facilities at existing villages.

Arvida is listed on the NZX (NZX: ARV). Website: **www.arvida.co.nz**