TRANSCRIPTION

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[START OF TRANSCRIPT]

Gary Carrol: Good afternoon, everyone and thanks for joining us today. My name is Gary Carroll. I'm the CEO of G8 Education. I'm joined today by Sharyn Williams, our group's CFO, Robert Dawkins, our Chief Property Officer and John O'Meara, our General Manager of Strategy. By way of background, given the revised approach to Greenfield Investments and the transition to reporting on a statutory basis, we'd flagged at our recent AGM that an update would be delivered to give investors and analysts further visibility on how performance of the Greenfield portfolio will be reported. Today, we'll walk through the Greenfield approach and reporting presentation that was posted on the ASX earlier today and then provide time for questions. This presentation will cover a review of the historical Greenfield Centre's performance, the revised approach to the Greenfield portfolio and the rationale for that change, as well as the resulting impact on how we will report the performance of Greenfield Centres going forth. An element of the group strategy to deliver sustainable, profitable growth is the measured rollout of new Greenfield Centres.

Gary Carrol: And here we define a Greenfield Centre as a newly constructed Centre that will be open for the first time, as opposed to a Brownfield Centre, which is an existing, already occupied and operational centre. The Legacy Greenfield programme has informed a refreshed Greenfield approach, designed to progressively enhance the network and realise measured profitable growth. Encouragingly, 70% of the Legacy Greenfield Centres have reached, or expected to reach a return on investment of over 20%. Under the refreshed approach, a deliberate number of new Greenfield Centres will be opened each year in attractive and targeted locations, with partners with quality developed partnerships with quality developers in a capital like manner. Opening new centres involves engagement with quality property development partners in the preferred locations and property design. A small group of dedicated G8 team members focus on fitting out the in-centre educational resources for creating the new team, marketing potential new families and welcoming these families and their children when the centre opens.

Gary Carrol: Properly executed, Greenfield growth improves the operational quality and financial returns from our centre network. The benefits include the ability to select an ideal location, design a centre that it's both appealing and functional and negotiate appropriate commercial lease arrangements. Clearly the flip side to this is that we have to recruit and train a new team ahead of the centre opening and build family bookings from a zero base. This means that the centre will incur startup losses until it builds sufficient occupancy and revenue. Now, this concept of Greenfield Centres is not new to the group, with a pipeline of 44 Greenfield Centres undertaken from 2016 and completed in 2020, at a capital cost of circa $145 million. With this capital outlay being determined on a multiple of forecast earnings. Reviewing the performance of this prime cohort of centres was a critical part of forming a future approach to our Greenfield Centres.

Gary Carrol: So that ends slide six of your pack, outlines the performance of these 44 centres from an occupancy EBIT and return on investment perspective. The table to the left on slide six, outlines the number of centres by cohort year, the average occupancy, the CY-20 E-fit on a pre AASB 16 basis and the ROI based on the acquisition price for those Centres. The 13 Greenfield Centres that were impaired during the 2020 year, are identified as a separate cohort. As a broad overview, as I'd mentioned, 70% of the Greenfield Centres had performed very well, with the 2017 and 2018 centres at occupancy levels above the target of 80% and delivering returns on capital of 21% and 30% respectively. The 2019 team which have been opened for over 18 months and are profitable with an average occupancy of 74% and a maturing ROI of seven percent. The 2020 centres, given their shorter trading period to date, with most of this time being impacted by COVID, are at an occupancy of 40% and have incurred startup losses of one and a half million dollars.

Gary Carrol: Pleasingly, despite this, these centres are operating near the trend line to their age and are considered to be on track with expectations, given the operating environment over the past 12 months. The graph to the right on slide six, is a view of occupancy for the 44 centres for the year ended 31 December 2020, with an occupancy trend line for the group of centres. As you can see it's the number of months since opening increases, theoretically so should the occupancy is [inaudible] . The centres the have been impaired or either situated in challenging locations, such as industrial business parks, or were very large centres. Over 180 places which proved challenging to achieve the occupancy necessary, to achieve an acceptable margin on the fixed operating costs including rental. The 13 impaired centres are the red dots on the chart. The under performance of these centres is reflected in below trend occupancy levels, resulting in under-performance from an earnings perspective.

Gary Carrol: Now they've been a number of learnings from the pipeline that the current leadership team inherited from 2016. These have informed and guided the revised Greenfield approach, which is outlined on slide seven. The objective of the Greenfield Centre approach is to support measured and profitable growth of the centre network by working with high quality partners to develop a deliberate number of centres each year, in attractive locations in a capital like manner. And there are three key priorities to support this process, including firstly, a robust assessment of location, secondly, an optimal new centre opening process, and lastly strong support to the centre, at and after opening. Sending to the robust assessment of location, that this involves a review of market demand elements from a myriad of angles to ensure that forecast supply-demand picture for the catchment area is positive and that the demographics are attractive, for example, the usage of early education and workforce participation being at an appropriate level. An enhancement to the previous process has been the extensive analysis of relative location within the market.

Gary Carrol: The location appeal within a catchment is very important in specifically how that location compares in terms of relative competitors from a street appeal perspective, as well as proximity to convenience related practise, such as schools and public transport. Rob Dawkins, our Chief Property Officer and his team have deep experience in this area, gathered from someone that looks so young, but many years working in large distributed networks and I've had firsthand experience with working with Rob for over 10 years, and can certainly speak to his track record. Development of the approvals for identified new sites incorporates input from relevant areas across the group, including the operations team, all mentored by independent needs assessments from an external demographics consultant. The draught approvals are then considered by a working group of directors, before being formally submitted to the full board for approval. G8's location analysis has clearly determined that there are still pockets of attractive locations for new Greenfield Centres, providing a compelling opportunity for measured growth.

Gary Carrol: The Greenfield growth programme will be balanced, so as to not distract from the group's absolute priority to drive improved performance from the core centre network. Part of the assessment process is providing material input into the design of the centre. Further, it involves negotiating the lease arrangement, the contractual arrangements relating to the delivery schedule and the capital contribution by G8. And this is the area of the Greenfield strategy that's seen very significant change. In the prior approach, a multiple of forecast earnings would be paid to the developer and a lease would be entered into with the landlord. Now, G8 contributes a modest amount of capital, approximately $4,000, the licenced place. Covering in-room educational resources and equipment and at times, a minor contribution to the fit-outs such as the playground. This new approach results in the fiscal assets being recorded on the balance sheet, in the form of a right of use asset relating to the lease, importantly, there is no goodwill being paid for the Greenfield Centres under the revised approach.

Gary Carrol: By way of comparison, the capital for the 44 Legacy Greenfield Centres, under our new model, would have been $18 million to $22 million. A significantly lower capital contribution, meaning ROI hurdles are able to be met at lower occupancy levels. In addition because the expected earnings from the Greenfield Centres haven't changed, this leads to the higher returns on capital invested in the centres. Robust assessments the first priority area and provides the Greenfield centres with the best opportunity to be successful. The second key priority area for success is optimising the new centre opening process. This includes management of the delivery schedule of the centre, executing a structured workforce planning approach to ensure that team has the right people in the right place at the right time and engaging the community in the market catchments, make them aware of and engage with the new centre.

Gary Carrol: The third key priority area, driven from our previous learnings, relates to the level of support a new centre requires at and after opening. An important part of welcoming families to the new centre, is having a centre manager and team that are inducted well and trained in the G8 way, prior to opening and knowing what to do expect as occupancy builds. Our learnings have shown this is fundamental to retaining and attracting great team members as the centre grows. The support model includes a dedicated recruitment officer, which from a team perspective is even more important in the current type labour market that exists in this sector. As well as a family liaison officer, to ensure families experiences are excellent at all stages of the process, from enquiry to settling into the centre. This direct operational support continues for up to 12 months, as the centre to works through the occupancy ramp up, the first enrollment and transition period, and potentially the first assessment and rating process.

Gary Carrol: And we use key metrics to objectively measure and optimise performance. These supporting roles manage multiple Greenfield Centres at the one time to ensure the approach is cost efficient, as well as being consistent across the portfolio of Greenfield Centres. Further, this structure allows for the quick capture in sharing of key learnings, so that we can continuously improve the support provided to future new Greenfield Centres. I'll now hand over to Sharyn to provide an overview of the changes will be implemented in relation to performance reporting for the group, including the measurement of Greenfield portfolio performance.

Sharyn Williams: Turning now to slide eight where the Greenfield portfolio objectives and parameters are explored. The key objective is to provide transparency on the performance of Greenfield Centres, that are still maturing, by separating these from the core portfolio of mature centres. As the Greenfield centre reaches maturity, they are moved to the core and provide an additional element of measured growth for the group.

Sharyn Williams: The refreshed Greenfield portfolio approach is expected to realise on average, a broadly neutral earnings outcome. This reflects the dynamics of the growing earnings stream from centres approaching maturity, funding the startup losses from newly opened centres. The Greenfield portfolio earnings position may fluctuate between a modest profit or loss year by year, depending on the volume of new Greenfields opened during a particular year. Containing the ramp up performance in the Greenfield portfolio, quarantines this impact from the core portfolio. The Greenfield portfolio will help all centres that are in the development phase. This enables investors to identify those centres that are maturing. It also supports an internal operating framework of additional support and focus for these centres. The assessment of maturity will be based on centres that have reached an occupancy of 80% or above. When they are deemed mature, they are transferred to the core, so the focus remains on those centres that are still in the maturation phase.

Sharyn Williams: Based on past experience, it is anticipated that Greenfield Centres should be matured by year three. In some situations, this can be much earlier. If the Greenfield Centre has not reached the occupancy hurdle by the end of year three, it will be assessed at that time for further opportunities to improve performance or potentially an exit may be explored. The graphs on the right outlines this concept relating to the 231 Greenfield Centres that are operating. Most of these centres in year three have reached over 80% occupancy and two centres have not. So, an assessment of this was done under this new methodology. Turning to slide 10, the results are 16 centres being transferred to the core, shown in grey on slide eight. These centres are delivering EBIT on a pre AASB16 basis of 10.6 million and return on the investment of greater than 30%. Of these centres,

Sharyn Williams: 14 have reached maturity and are over 80%, and two have aged out, reflected on the graph as the two dots on the lower right. These two centres still generate profits of over $200,000 each despite lower than 80% occupancy and have been assessed to join the core, resulting in all 2017 Greenfield centres graduating from the Greenfield portfolio. This leaves the remaining 15 centres, which are comprised of two 2018 centres, and all of the 2019 and 2020 centres. These are maturing as expected. This portfolio is breaking even with an occupancy of circa 60% and a positive ROI measured on a pre-AASB16 basis. The statutory net profit before tax of these centres is lower at a $2 million loss, reflecting the very early stage of the lease life of these Greenfield centres, and I will cover this in more detail in the following slides.

Sharyn Williams: During the 2021 year, new Greenfield centres will be added to this cohort, and the group has signed agreements for eight new Greenfield centres. Our current visibility suggests that G8 will take possession of four Greenfield centres by the end of the year, with one expected to open by year-end and three in early calendar year 2022, following completion of their fit-out and obtaining service approvals. The expected capital outflow per centre is 400,000 to $500,000, and consistent with our turnaround programme strategy, any savings on the previously projected $4 million of ramp-up losses will be reinvested in 2021 to drive quality across the core centre network.

Sharyn Williams: We've also enhanced our reporting in relation to the performance of our Greenfield portfolio, reflected on slides 11 and 12. Slide 11 outlines the approach to reporting occupancy for the Greenfield centres, where each Greenfield center's occupancy will be shown along with metrics relating to the portfolio. This slide outlines the current 15 Greenfield centres on the left and the core group occupancy on the right, which will be provided in lieu of like-for-like occupancy. Further occupancy tables will be provided relating to the core that investors are familiar with.

Sharyn Williams: From a financial reporting point of view, changes to the prior format of presenting operating performance have been made to enhance disclosure. Slide 12 outlines the approach to the refreshed view of reporting on operating performance. There are two drivers of this change.

Sharyn Williams: Firstly, the move from organic annual cohorts of Greenfield centres, divested, and impaired centres, to a core and Greenfield portfolio approach. The 472 centres currently reflected across these cohorts in the calendar year 2020 reporting are reclassified to core or Greenfield as shown on slide 13, and greater disclosure on licenced places and centre numbers is provided. The previously impaired centres will form part of the core, with additional information disclosed separately on a pre-

AASB16 basis to provide visibility of the run-off profile of this portfolio compared to the calendar year 2019 loss profile. In the prior reporting approach, the prior years numbers were restated each reporting period, based on movements of centres across cohorts. We appreciate that this caused challenges for modelling, so the new approach will freeze the cohorts at that point in time and prior year numbers will remain static.

Sharyn Williams: The second driver of the reporting change is the conversion from reporting operating performance on a pre-AASB16 basis to a post basis, following two years of reporting both to allow investors time to transition their thinking and understanding of the leasing accounting standard. The impact of converting the reporting to a statutory or post-AASB16 approach relates predominantly to the rental expense line for the group.

Sharyn Williams: You will recall that prior to the AASB16 implementation G8, like other businesses with large networks, had numerous operating leases that were not reflected on the balance sheet, and were simply disclosed as lease expenses in the occupancy and other expenses line of the P&L. Under AASB16, this traditional rent expense is replaced by a depreciation expense of the right of use assets, and an interest expense calculated on the outstanding lease liability. The sum of the prior rental expense, and the depreciation and interest that replaced this expense, equal each other over time. However, depending on where a group is at in its lease profile, the timing of these expenses may change. This timing impact is driven by interest expense being higher in the earlier years of the lease and reducing over time, and also the number of options now recognised and spread over the early years of the lease. This impact varies centre by centre.

Sharyn Williams: These changes result in higher EBIT, because the rental expense is removed and replaced by only the depreciation portion. For this reason, the operating performance table will now focus on net profit before tax for centres rather than EBIT, to ensure we capture all lease expense related costs. In order to aid understanding and comparison, the depreciation and interest relating to leases, along with variable rentals, rental loan costs and modifications, will be combined to form a proxy for a rental expense line. The centres themselves do not bear debt financing costs, so effectively for the centres net profit before tax is equivalent to EBIT, besides the impact AASB16 has on the timing of recognising rental expenses.

Sharyn Williams: The resulting estimated impact on the operating performance table is outlined in slide 13, where we have provided the existing approach, a reclassified version with the core and Greenfield cohort, and then the conversion from pre-AASB16 to the new format for statutory reporting, to allow investors and analysts to revise modelling approaches to this refreshed approach. You will note from a centre net profit before tax perspective, there was a reduction in 2020 calendar year of $4 million due to the impact of AASB16, driven by rental expenses being brought forward. In 2021, this AASB impact is expected to be broadly neutral at the net profit line.

Sharyn Williams: We'll now take questions from people on the call.

Operator: Thank you. If you wish to ask a question, you will need to press the star key followed by the number one on your telephone keypad. If you wish to cancel your request, please press star two. If you're on a speaker phone, please pick up the handset to ask your questions. We'll now pause a moment for any questions to register.

Operator: Thank you. Your first question comes from John Hynd from Wilsons. Please go ahead.

John Hynd: Good afternoon, Gary and Sharyn. Thanks for the presentation, and thanks for taking my question. I was keen on perhaps some insights on the CYA team cohort. That seems to be, I guess, the leading cohort on a number of metrics in terms of centre investment, replied investment, and the ROI. What was the winning formula there? And can we expect you to apply that sort of approach going forward, noting '19 doesn't look like it's been as successful?

Gary Carrol: Yep, thanks John, and thanks for the question. For us when we dissected the performance of the 2018 portfolio, be safe to say more of that cohort had the relative location benefit that we've incorporated into our location assessment. So the overall market supply demand was positive, and they tended to be in slightly better locations if we're comparing against the cohort peers. And for us, that was a bit of a validation of the approach we're looking to take moving forward.

Gary Carrol: In terms of 2019, one of the drivers behind the ROI, because the occupancy is maturing quite nicely, it's 74%. We do have a number of those centres that are more higher cost, in terms of both from a capital and an operating expense point of view. And again, we fed those learnings into our approach moving forward. So we've got a great degree of clarity of what we would accept in terms of rental expense as a percentage of revenue, and we run that through various scenarios, and as you've seen we've clearly moved on quite materially from a capital point of view.

John Hynd: Great, thanks. And I guess looking forward, what do you think is the optimal centre? Like what... How are we going to see the G8 product be rolled out going forward? I mean, can we... Can you talk to some of the products and the brands that you're running at the moment, and synthesise rates, locations, metro versus non-metro, et cetera.

Gary Carrol: Yes. So if I attack a few of those. Certainly in terms of size, we've learned through the experience that larger isn't better. That sweet spot for us is probably that 80 to 100 licenced places, we do find that works quite nicely. We do have hurdles around supply demand from a future perspective, as you can appreciate we won't be sharing the exact details of that, but we've got very clear criteria that we apply.

Gary Carrol: One of the other benefits that we've had through the change in approach, and the change to higher-quality partners, is more active involvement in the design of the centres. We feel that they're actually more functional and more appealing. We certainly look to take lessons learned as we work our way through different designs, because they're not all the same design, and we would incorporate those learnings evolving, moving forward, to ensure that our product is appealing to our children and families. So they're probably the key differences we're looking at making, in terms of making it sustainable.

John Hynd: Thanks. And does that translate to one particular product that we'd be familiar with, one of the brands? Or does... Do you continue, I guess, what's suitable in the specific area?

Gary Carrol: Yeah, no particular product or brand. We actually went through the exercise probably 18 months ago where we've defined our G8 standard. And I won't embarrass Rob by asking him how many of our previous developers got a 100% mark on our standards, because I think it'd be a very low number based off what we've seen. So we would be comfortable saying none of our previous inherited pipeline would get 100% on our current standard, and we have the opportunity to influence that a lot more moving forward.

John Hynd: Okay, thanks. I guess what I was getting at was Greenwood is typically... My understanding it's typically been a bit more of a capital-intensive brand given the product that you offer. Is that still core, or are we going back to previous brands?

Gary Carrol: We're not working with the developer that brought the Greenwood brand to us, and it would be safe to say our design differs a fair bit from what that was. We have a pretty clear view on what we think works, and a number of those centres had features that were very good, but also had some weaknesses in their overall design.

John Hynd: Great, thanks very much.

Operator: Thank you. Your next question comes from Peter Drew, from Carter Bar Securities. Please go ahead.

Peter Drew: Oh hi, Gary and Sharyn. Just a couple of questions. Firstly, just wondering, why are you using CY20 EBIT to measure the return on investment? I just would've thought it's quite a difficult year.

Sharyn Williams: Yeah, it was a more difficult year, although it's the most current earnings. Largely we thought it was a conservative way to measure the return, particularly where the 2019 centres, for example, using the earnings from that year they would have been very young. So we tried to give the centres as much time to mature and show their performance in the earnings, so we took the latest, Peter.

Peter Drew: Okay. And then just in terms of the treatment of the impaired centres, how do they come in on the... like if I look at slide 13, when it says the convert column. Where are they reflected, the actual EBIT contributions?

Sharyn Williams: So the impaired centres form part of the core, Peter. So they are amongst those 457 centres.

Peter Drew: Yeah, okay.

Gary Carrol: And as Sharyn called out, we'll provide some commentary to give people a bit of additional flavour of what we're doing around performance of those impaired centres.

Peter Drew: Yeah, okay. And then just the last one, just in terms of, I guess, that impaired component. Am I right in assuming that although those number of centres made up about 30% of the 44 centres, of the Greenfields over the past few years, it was more like about closer to 50% in terms of the dollars spent?

Gary Carrol: It's certainly true to say that they were larger centres, and the capital would flow

Peter Drew: Yeah,

Gary Carrol: Based on that, Peter. Absolutely.

Peter Drew: Yeah.

Gary Carrol: I think it's around... it's in the high '60s in terms of the capital cost of those 13 centres.

Peter Drew: Yeah. Yeah. Okay. Okay. Thank you.

Operator: Thank you. Once again, if you wish to ask a question, you would need to press the star key followed by the number one on your telephone keypad. We'll now pause a moment for any further questions to register. Thank you. You now have a follow-up question from Peter Drew from Carter Bar Securities. Please go ahead.

Peter Drew: I guess just a question in terms of, how much capital do you think you could spend on this new Greenfield, sort of approach, on an annual basis?

Gary Carrol: Yeah. It's really good question, we're really clear, Peter, that, we want to be measured in our approach for two reasons. One, there are multiple ways that we could invest our capital and we don't want to put all of our eggs in one basket. And two, we're really clear that we've got some other very important strategic priorities that we don't want to distract the group from. So those natural constraints will limit the absolute number of deals that we will do in any particular year. And we flagged somewhere around 10 per year, would probably be a pretty sensible number, moving forward. Taking those constraints into account that would lead you to the capital number of around $5 million per year.

Peter Drew: Yep. Okay. I guess a followup with that is, not withstanding, maybe a larger capital expenditure investment in the core. Will you you be, I guess, rethinking your capital management in terms of a dividend moving forward, given that, you know, $5 million is not a big impost on the business, relative, I guess to the past number of years and the cash generation of the business?

Gary Carrol: We affirmed that dividend policy at the AGM recently, Peter, as you know, and we're very comfortable in that 50 to 70% of that range. That gives us, we think the right balance between returning money to shareholders, which we clearly are focused on, as well as investing in growth opportunities for the group. So we're pretty comfortable at that level.

Peter Drew: Yeah. Okay. Thanks Gary.

Gary Carrol: Thanks Pete. More than happy to take questions from room because then the people that are on the call can also get the benefit of the questions. That we might do one round of that and then see where we get in terms of cutting off the call and continuing the discussion.

Tim Bundy: Gary I might kick it off. Tim Bundy here. Just a quick question, in terms of the fight evaluation. I mean, once you start by experience these fights that originally looked all right, suddenly have competition coming into them. How nimble can you guys be in terms of changing those fights and how much insight do you have into if a new competitor is going to be entering at that market, at the site time that you're thinking about entering, into that specific suburb?

Gary Carrol: Well, we rely on a combination of publicly available information, Tim, and as you know, tracking it through the council approval processes is a murky game. But you do get information on what people provide. Does get tricky when they put in an application for a mixed use development, including childcare, it probably ends up being a resi complex, but we try and capture all of those. We also combine it with an assessment from our ops team and we get continual feedback on what they're seeing in the market. And try and form a view as to what's likely come our way. And in the last thing we do, this is where we're really focused on being the best relative location in the market. So Rob's done, I think, a very good job today. We've identified markets where the overall dynamics look positive and we've secured the way things are the best location in that market.

Gary Carrol: That gives us a bit of additional confidence in going, if in 2, 3, 4 years time, someone does open up in that catchment. Well, we get opportunity to establish our foothold and be there in a disadvantageous-relative location, so we can defend our turf a lot easier. But to answer your question, you can never truly predict someone that's in the next 12 months say that we've got a pretty high degree of confidence on. What we're focused on is, how do we defend changes that happening, that 2, 3, 4-year periods.

Speaker 1: Gary, the 400, 500 grand capital cost percentages, the top end of the sort of allows for the inflation that we're seeing sort of the building industry at the moment.

Gary Carrol: So that's for educating room, educational resources. So it's not tied to any construction cost, per se.

Speaker 1: Okay.

Gary Carrol: So we're pretty happy, we know what that'll look like the next little while.

Speaker 1: So the 5 million you expect to spend per year though, there's no construction cost in that?

Gary Carrol: No, in some centres, we make a pretty small contribution to playground cost but we're not seeing that being the material driver of the number. So we're pretty confident around that capital number.

Robert Dawkins: Any of those costs will be reflected in the rental rates that are negotiated and agreed.

Tim Bundy: Gary, you talk a little bit about what you're seeing from other competitors in the market. I mean, if I look at an average of 10 centres, say you get rid of the 5,200 performing that kind of gives you a supply rate of about 2.4%? There is still an imbalance between demand and supply in the market at the moment. So what needs to happen to neutralise that imbalance and how are you seeing the demand side of things going forward, given changes to migration, given changes to birth rates, et cetera?

Gary Carrol: Yeah. And I'll apologise, this is not a 30-second answer because you asked me about going through the demand signals, as well as what's happening in supplies. So demand, we've had some positive news from the last little while, that's actually strengthened the demand, particularly over in 12 months, plus. We thought we'd had... So what drives demand? Workforce drives demand and I think we'd all agree that the numbers we keep seeing on a quarterly basis are stronger than what everyone had seen, coming out of. COVID. Second thing that drives demand is the birthrate. We thought we did a reduction in the birthrate.

Gary Carrol: The Medicare stats say that there's been a 22% increase in pregnancy-related scans. So we don't think that risk is as material as what it was, in fact it might end up being a slight positive rather than a negative. And the third thing that will impact demand is international migration and clearly that's a negative story. But demand you'd say, is nowhere near as negative as what we thought it's be and arguably it's a kind of neutral gain. You then combine it with the budget announcement, which was stimulatory from a demand perspective, in that it up the subsidy for families, who've got two or more children in care. And also remove the annual cap of $10,560, which family's been bumping up against that for the last few weeks. So we think both they kicking in middle of next year, again, we think that's a broad positive.

Gary Carrol: To answer your question, is that then lead to now every person and their dog is going to go and build a childcare centre? We are hearing anecdotally out of the construction sector, that the pivot that occurred out of residential childcare in 2016 and '17, showing signs of neutralising, it may be even reversing. Because a very strong demand for residential housing, so those developers might, at looking at the margin, they're earning decent returns on those projects, that may help dampen the spike. What's driving supply. What we can tell you, Tim, is it's not the big end of town. We're doing 10, which as you called out, as a couple of cents. Good start, a really pretty neutral, Guardian are growing, they need to grow. They've got a material CBD exposure, that we think, structurally is bit challenging. So they are trying to diversify away from CBD and I would if I was them.

Gary Carrol: There are a couple of smaller players like Edge and Journey that are currently 20 centres, that are looking to grow by about 10, combination of brown and green. But that began to town. At three, if you say that demand is growing at two and a half percent, if you say that the existing network is 8,000 centres. I'm using a bit of rounding. We're just maintaining our share, if we grow [inaudible]. We're not driving an uptick at this point.

Gary Carrol: We will keep a close eye on whether those demand signals start changing smaller operators and developers minds around increasing their network. We're not in the game of being the leader of that pack. We do think there are pockets of opportunities that make sense for us to pursue but we're going to do it in a very sensible way.

Tim Bundy: So what do you need to neutralise that... I mean, everyone says there's an imbalance, right? If everyone continues to grow at the same pace, and then that imbalance never neutralises.

Gary Carrol: So what needs to happen is a longer term game of the scale operators providing a differentiated offer. Those are the smaller operators confidence level in, coming in and taking share gets diminished. And what I see about what operators like PCBs and Guardian and the journey the G8 on, that will happen over time. We have the access to people and capital and resources that we can start presenting a differentiated offer and make it harder for smaller people to enter the market. Over time that then drive supply decisions.

Speaker 2: Gary. Sharyn, just in terms of, back to your competitive positioning, as you just mentioned, you have access to various personnel and resources. But how do we think about when you're selecting new centres, what filter and what rigour is put into understanding labour in a given catchment supply of labour, attracting talent?

Gary Carrol: Yeah. So we actually, part of our assessment is we go in and work with our operations team and get their view of what the local market is. We clearly look at our own metrics as well. Probably a good example would be, by user-specific example. Say a region like Bendigo.

Gary Carrol: If we were looking at a Greenfield centre in Bendigo, first thing we do, we've got a couple of centres that they're performing well in their catchment. We would go, what they're going to do to the labour market in that catchment? We'd reach out to our ops team, we'd look at recruitment data in that market and go, "Where would the outer access the thing that will make that a successful centre?" And of the basis of that, we then form a risk-based view as whether we look at pursuing that opportunity.

Speaker 2: And how far a head in advance do you... You get the data, and just in terms of timing when you're selecting a centre? Because you've got to be nimble and...

Gary Carrol: But I'll probe Rob to talk to about it, it's not a 5-minute exercise when we're going through the assessment. And developers don't expect us to give them an answer in a week.

Gary Carrol: We haven't struck situations where we're taking too much time for them to say or moving on to the next opportunity. And part of that is setting up a repeatable process that we can get through on a timely basis, in terms of picking through all the filters internally.

Robert Dawkins: So generally that assessment process takes 2-3 months for the identification of potential target. With the help of partners to identify suitable locations within our target market. We then go through our internal and external validation processes and that's as Gary's described. We do engage with our operations teams, their opinions regarding market location and we'll send that access to appropriate talent. We make agreements relatively near after, a couple of months through documentation and design. The centre in the formation of agreement for lease at delivery, depending on the development approval and construction process, could take potentially 12 months plus. And so market may move during that time period but the assessments made, having regard to the way in which that markets performed. Not just at that point in time, but generally. So we would generally expect material movement in those market dynamics, with a broad view, unless we grow it as part of our assessment process. We're also mindful of future developments.

Simon Mawhinney: Sharyn. Simon Mawhinney from Allan Grey. Just on the impaired centres in 2020, the $9.6 million loss.

Sharyn Williams: Yep.

Simon Mawhinney: Take a team that come 2021, that will be euro, no locks from impaired centres?

Sharyn Williams: So, in terms of the colouring impaired centres, the pre-AAC16, the metrics we're giving where they lost 12 million and then they're moving downwards. In terms of the 9.6, that's on a pre-statutory basis, basically. The nuance in the reporting, impaired on a statutory basis. Because their asset

Sharyn Williams: ... was impaired. The impact of their rent is a bit smaller in the core. It is quite hard to measure on a statutory basis, the impaired number. What we'll see is the pre-statutory amount, and that moving to nil will very much depend on when we exit those arrangements, basically.

Sharyn Williams: And as we've said before, there is a cohort of centres with quite long lease tails. Mainly those 13 Greenfield Centres. Some terms of the exits for those, we're exploring what the various options are. We've captured the lower hanging fruit in the first parcel, but we have acknowledged that those Greenfield tails will be a bit more challenging.

Simon Mawhinney: So the impairment that you took during the, that incorporates. Often these things happen to make allowance for onerous leases or to neutralise the impact of future losses. You haven't done that in the impairment?

Sharyn Williams: The impairment has reduced the rental expense that we currently have on most centres. But what you'll see is when you look back through our four year reporting, the impact of the leasing standard actually would have made the group $12 million [inaudible] net profit before tax level. We then move into 2020 where we had nine months worth of that reduced rent from the impairment. It brought that impact back to around 3 or $4 million, which is what you're seeing in this converted table. Moving into this year the impact of the standard is neutral. The impaired centres are playing into that. Although, being offset by what would have been a negative in the rent line from the other call centres. And that's why we're getting a neutral impact on the application of the standard now.

Tim Bundy: I think at the AGM you had 13 of these impaired centres, if you've gotten rid of two, the contracts have been fined in another seven that were in negotiation.

Sharyn Williams: Yeah, and that's what we'll keep referring back to. Remember in 2019, that cohort lost 12, we've now exited X representing X amount of premium.

Gary Carrol: I think it was 1.9mill.

Sharyn Williams: Yeah.

Gary Carrol: Yeah, 1.9 mill..

Sharyn Williams: We'll just keep getting that milestone so people can see how the title is being exited.

Speaker 3: That low-hanging fruit was that around the tenure of the lease that made it easier or alternative use case?

Gary Carrol: Predominantly tenure of lease. Yeah, I'd say that was the main driver.

Speaker 3: Is alternative use case a feasible way of getting out of these things, or is the rental that you've got just to high to make that a record?

Gary Carrol: The ones we've sold to date have all been to people that will be operating a childcare centre. What we find is that a local operator with their assessment of the impact they can have on relationships in the local community, et cetera, they have more bullish view of the centre, but we let them take over the obligation for the larger Greenfield touch centres. We will be exploring all avenues around exit, including whether an alternative use is possible and feasible. But your point is very valid that the return that the landlord's currently getting on that asset, that's going to make that pretty challenging, which why we think those are going to take a fair bit longer.

Speaker 2: What is the average length of the lease on those impaired centres that remain?

Gary Carrol: The Greenfield, the 13 Greenfield that we're talking about, that'd be, I live on number 10 plus years because they're pretty new.

Sharyn Williams: [inaudible]62 was around seven years overall with those Greenfields also factored in.

Gary Carrol:	I think what we might do is, we'll let the people on the teleconference go. If there's no more questions, thanks for joining us today. And we look forward to providing you an update down the track. Thanks everyone.
Sharyn Williams:	Thank you.
Speaker 4:	There are two more questions.
Gary Carrol:	Okay. Apologies. I think there are a couple of questions that popped up.
Operator:	Thank you. Your next question comes from Gareth James from Morningstar. Please go ahead.
Gareth James:	Hi guys. Firstly, could I just clarify? On the new Greenfield centres that you're talking about opening, will those centres all have the same brand?
Gary Carrol:	No, not necessarily Gareth.
Gareth James:	Okay. And more generally, what are your thoughts on having a more consistent brand across the group? Is that not a way that you could create a bit of pricing power?
Gary Carrol:	So the, if we'd say, I'll say a couple of things. Certainly in terms of new Greenfield, the number of brands will be limited, very limited, but unlikely to be a single. We are continuing our assessment of how we can rationalise the number of brands in the portfolio. To date that has not been as high priority as our turnaround programme and our network optimization programme. That's certainly something that we'll continue to assess and evaluate over time.
Gareth James:	Okay. Thanks. And just a second one on the invested capital, I think you're talking about a circa $500,000 typical invested capital per centre. Is that right?
Gary Carrol:	Yep.
Gareth James:	Yeah. And how long does it normally take before that invested capital is offset by fees in advance and deposits paid by parents?
Sharyn Williams:	The stays in advance are usually two weeks ahead. We don't really look at the working capital in that way, by taking the $500,000 in your account. We really look at the profile of the earnings and a payback on that capital through the earnings line. Now, as soon as I ramp up, obviously the earlier they happen, you can see in some of the earlier tables where we're talking about the centres that have matured, you can see some metrics there and probably takes averages from those metrics in terms of the central earnings. And that might give you a feel for payback on that kind of capital level.

Gareth James:	Sure. The 500K, I think you've talked earlier about that relating to in-room resources. I was just wondering if there were any other costs relating to the lease or anything like that, that you would have to incur?
Gary Carrol:	I might get Rob to talk to that [inaudible]
Robert Dawkins:	So, not generally from the capex. In-room resources, the IT equipment for centre operations, but that's covered with that provision. There are very limited other expenses associated with the establishment of the centre. Potentially things like legal fees and registration costs, but it's certainly not material. Only by rare exception, have we seen the need to make any form of contribution to the capital cost of the development of centre. Generally our priority is to incorporate that within the rental structure of the lease.
Gareth James:	Sure. Okay. Thanks guys.
Operator:	Thank you. Your next question comes from Deanna Mitchell from Australian Ethical. Please go ahead.
Deanna Mitchel:	Hi. I just wanted to ask if I look at it from an EBIT per centre basis, the EBIT per centre for your mature Greenfields is much higher than on page 13. Your core centres, EBIT per centre. I just wanted to know the reasons that you think that this gap exists. Whether there's a higher earnings capability at the core from an EBIT per centre perspective, whether that's a metric that you look at as well? Thanks.
Sharyn Williams:	Certainly in terms of the core and lifting that EBIT per centre, that's the key focus from our improvement programme. What is good to see is when you do look at those Greenfield centres, where we have a great looking facility, we've been able to support them quite closely, location being good, you do tend to see quite good EBIT returns from those on a per centre basis. So certainly Deanna, the intention from the improvement programme is to lift the EBIT per centre from that core group.
Gary Carrol:	The core has impairments in it as well doesn't it.
Sharyn Williams:	Yes, the core does have impairments in it as well, Deanna.
Tim Bundy:	I have one follow up question from that. If I look at the calendar year, 17, 18 looks like that 630, 640 grand per centre on average, are you saying that that should be higher than normal? If we looked at calendar year 21 and we got 82% occupancy, 83% occupancy, what would that look like in terms of EBIT per centre?.
Sharyn Williams:	Are you referring to the COVID impact that might be in the..?
Tim Bundy:	Yeah, on a business as usual, calendar year 20 had lots of moving parts in it, which I would say isn't necessarily reflective of the business going forward.
Tim Bundy:	So how should we think about the historical portfolio? If they can generate a similar sort of occupancy around that 82, 83? What sort of EBIT does that spit out? And then

also just on the new centres, if you were assuming that 80 to a 100 spaces per centre, what does EBIT look like on your modelling out of maturity?

Sharyn Williams: Since the 2020 EBIT itself, because for these centres, the government subsidy ignoring job keeper, which we had for a few months was linked to their occupancy level. So there is still a link for these 2020 numbers that quite closely resemble the occupancy that that sent ahead. So it's not a completely separate link in terms of these numbers. Because we were missing out on parent revenue, that's why these numbers potentially a fraction lower. Although when you look at them there was a job keeper subsidy as well.

Sharyn Williams: What we saw out of these Greenfield centres during COVID and we sort of crossed the broad network, some centres weren't as impacted by COVID as other in terms of occupancy. You can see that the average occupancy of these centres were still very strong, even in a COVID impacted year. That would be centre by centre. In terms of the broad production of EBIT from a centre, very much reliant on the average fee for the centre, the size of the centre. But if you have a look at our historical wages as a percent of revenue, rent as a percentage of revenue, you can start to get a feel for a 100, 125 centre at an average fee. Our average fee is about $119. But if the centre is run well and produces good occupancy, you are talking about EBITs higher than our current average per core centre.

Gary Carrol: So, Harmony, on the basis there's no more questions from people on the call, we might let the callers go and thank them for their time. And look forward to giving you an update down the track. Thanks everyone.

Operator: Thank you. That does conclude our conference for today. Thank you for participating. You may now disconnect.

[END OF TRANSCRIPT]