TRANSCRIPTION

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[START OF TRANSCRIPT]

Operator: Thank you for standing by, and welcome to the G8 Education Limited 2024 Half Year Results. All participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session. If you wish to ask a question, you will need to press the star key followed by the number one on your telephone keypad.

I would now like to hand the conference over to Mr. Pejman Okhovat, CEO. Please go ahead.

Pejman Okhovat: Good morning, and welcome to the 2024 Half Year Results Call for G8 Education Limited. My name is Pejman Okhovat, and I'm the Managing Director and CEO of G8 Education. I'm joined today on this line by the Group's Chief Financial Officer, Sharyn Williams. Sharyn and I will take you through the investor presentation that was released to the ASX earlier this morning. Following the presentation, we will open the line for Q&A.

To begin with, I'd like to start by acknowledging the Gadigal people of Eora Nation who are the traditional custodians of the land on which we are conducting this presentation today. We respect their spiritual leadership and relationship with their country and pay respects to the Elders past, present and emerging. I extend that respect to any Aboriginal and Torres Strait Islander people joining us today.

I would also like to acknowledge the G8 Education team who passionately support children's outcomes and play a pivotal role in our society and local communities. This morning, we will cover a summary of the six months ended 30th June 2024, providing updates on our progress, outlining operating and financial performance for this period, and conclude with a brief current trading and outlook.

Beginning on Slide Six, we have delivered a number of achievements during the half along with earnings growth in a challenging environment. Earlier this year, we called out our focus on a number of high-impact areas, including maintaining our team engagement position, delivering a strong enrolment and transition outcome, improving operational execution and a fit core, and maintaining our strong cost and capital discipline.

Pleasingly, we've demonstrated traction across all of these areas in a period where the sector has been under pressure from affordability challenges for families, numerous regulatory inquiries and continued workforce constraints.

Firstly, the Group's financial results reflect solid earnings growth compared to the prior comparative period, driven by higher revenues and margins. This reflects an improved enrolment transition period, a focus on achieving value from our cost base and our improved portfolio quality as we exited some underperforming centres.

Occupancy was above PCP for the first half, a reflection of the positive enrolment and transition period and also network optimisation initiatives. Occupancy continues to be supported by the positive trend in increased frequency. However, we have seen some flattening of this trend from May onwards, a reflection of the challenges associated with the cost of living and affordability and the impact this has on discretionary bookings.

While sector challenges around the availability of the staff have somewhat improved, constraints remain. We have continued to alleviate the impact within our network as evidenced by our lowering of vacancy rates and further decreasing agency usage.

Progress continues to be made towards improving the experience for G8 families measured through our always-on customer service survey that provides our operational team with regular centre-specific feedback.

Strong operating cash conversion through the period and stronger earnings sets the balance sheet up well for a second half with the Group today announcing an on-market buyback. The approach to capex continues to be guided by our capital allocation framework as we continue to invest in centre resources, IT and property where it's been flat on prior year.

As a Group, we are focused on delivering on our purpose, creating the foundations for learning for life, while improving our execution capabilities as a business and supporting communities and societies more broadly.

Now turning to Slide Seven, which outlines the positive operating financial performance versus the 2023 half year of circa 20% growth in both EBIT and NPAT. This is a result of the combination of revenue growth, portfolio optimisation and solid cost management, particularly in labour-related areas such as agency usage and network support office costs.

From a strategy perspective, net profit after tax and earnings per share both increased by over 33% after including non-operating items, as outlined on Slide 16. This resulted in a fully franked interim dividend of $0.02 per share being declared, representing 81% of the reported CY'24 H1 NPAT.

A combination of a positive enrolment at the start of the year and portfolio optimisation has resulted in occupancy for the period of 68.2%, which is 0.8 percentage points above the prior year. From a sport perspective, the slowing in this sector has also impacted G8 with year-to-date occupancy contracting to 0.7 points above prior year and our current sport rate largely been slightly below the same week in the prior year.

Slide Eight reflects our commitment to drive a sustainable future through our ESG journey. A key focus for the past period has been our sect advocacy through our participation in the multi-employee bargaining process. We are proud that this has resulted in the government supporting, funded 15% pay increase over a two-year or ECEC employees. EBITDA continue to be worked through for the December 2024 proposed implementation.

From an emission perspective, we achieved a 10% reduction in the Scope one and two emissions and transition 61% of our vehicle fleet to hybrid vehicles. The first phase of our solar installation in CY '24 Half 1 has generated the equivalent of approximately 24 average G8 centres was worth of solar power by an entire year.

G8's efforts to be an attractive employer through team recognition, flexibility benefits, professional development, and incentive programs have been recognised with the Groups being ranked fifth in the Randstad's Australia's top 10 desirable workplaces. We have also reduced our overall gender takeout.

Improved quality ratings results were achieved during the half with G8 results remaining above the sector for meeting and exceeding. We continue to build and reflect reconciliation action plan with 86% of our centres having now commenced or published a reconciliation action plan.

Moving to Slide Nine, our balance scorecard. We continued our focus on refining our operational execution and enriching our families' everyday experience. Maintaining momentum in our team-related outcomes, improve the quality of network through improving our national quality standard results and portfolio optimisation.

In all our strategic focus areas, we have made positive progress since the end of '23. For us, occupancy is ahead year-to-date. We are conscious that there has been a slowing recently and the broader sector headwinds, in particular from affordability that are being experienced. We are pleased with our solid team retention outcomes up 6% on PCP to 76%, and the 43% reduction on PCP in vacant roles across the G8 network.

On the back of these significant improvements, we are able to reduce further the use of high-cost agency fees down to 0.3% from 2.2% in PCP. Quality assessment ratings of meeting or exceeding have increased to 91%, which is 2% ahead of the long day care sector average. From a family perspective, NPS has increased to 48%, up 16 points on PCP, a reflection of our continued focus on responding to a regular feedback centre-by-centre.

Now, turning to Slide 10. Our team results continue to be highlighted with our reduction in team vacancies, strong retention, and improvements in enrolment participation, participating numbers for our development programs. There are tangible results from these investments across our cost base, quality and NPS, particularly from having more stability and capability in our team.

Turning to Slide 11. The experience our families have is a top priority for us and is critical for improving our occupancy performance. The trend in NPS has been positive as we cycle the implementation of our always-on NPS program. The themes we have seen over the past 12 months from the family feedback have resulted in development of initiatives that support our centre managers to respond to our family's needs and wants, thus improving their experience.

Supporting occupancy this half has been an increase in frequency. However, as mentioned before, there has been some flattening in this growth, largely a result of increasing affordability challenges impacting discretionary bookings. We continue to leverage our data and analytics to help families to efficiently utilise their childcare subsidy and maximise our opportunity for the children to increase their ECEC participation.

The final experience measure is family retention, which has seen an improvement on PCP. We continue to leverage our improved team retention and stability, high quality, inclusivity, and age-appropriate educational programs and deepening relationships to retain our families.

Turning to Slide 12, delivering better outcomes for children, families, and team is at the heart of all we do and key to our success. Our continued investment and focus on quality have resulted in another period of improvement in our national quality ratings. With 91% of our long day-care centres meeting or exceeding the national quality standard, which is now 2% better than the LDC sector average.

As always, there's an ongoing focus on child protection and safety across our network. The implementation of internal quality measures is a reflection of the proactive approach required to ensure we continually improve our quality. The opportunity to leverage digitalisation through a dedicated compliance management system, which further enhances improvements, increasing visibility, and capture efficiencies.

In line with numerous state governments, a clear strategic focus is on the 3- to 5-year-old offerings with the recognition of the benefits of early education continuing to increase. Critical elements of this offer include improving our ECT retention rates, continuing our Study Pathway Programs, increasing our ECT teacher registration support, and growing our teacher workforce.

Turning to Slide 13. Group occupancy has started the period positively with an improved enrolment and transition outcome, coupled with portfolio optimisation as the half progress. Coming out of May, there's been a slowing in the momentum with inquiries lower across the sector and frequency flattening. Both signals of affordability are likely a potential driver of family bookings to reduce some bookings.

In terms of our progress to develop a fit core, we continue to simplify our work with teams, introduce DSO tools for our centre managers and area managers to assess performance in real time and improved workforce planning, delivering better team utilisation and reducing agency reliance.

Now, moving to Slide 14, our financial stability. The half produced a stronger end profile, resulting in a strong operating cash flow and a conservative balance sheet position. Our capital allocation framework continues to guide investment with capex level being in line with the prior comparative period.

Our disciplines in cost management, particularly in variable costs, combined with our strategic procurement programs and initiatives to lower cost of doing business resulted in delivering better earnings for the year.

Optimising the Centre network remains an important element of Group's strategy and is a fundamental basis for creating a profitable portfolio for G8. During the half, we exited 18 underperforming centres and opened 2 new locations. In quarter 4 last year, we indicated our intention to divest 31 of our centres through a sales process.

As of today, we have divested 18 of these centres, 16 in the first half. They exited multiple of circa 2x pre-AASB 16 losses in line with the commercial approach we committed to undertake with these divestments. We will provide a further update at full-year results.

I will now hand over to Sharyn Williams to take us through the financial performance information and more details on our portfolio optimisation.

Sharyn Williams: Thanks, Pejman. Focusing on our Group financial performance on Slide 16. Increased revenue and disciplined cost management resulted in operating and statutory NPAT growth along with margin expansion. The first half centre operating EBIT grew by almost 12%.

A combination of improved performance from operating centres and divesting underperforming centres contributed to improved earnings and margin outcomes. Support costs were well managed with headcount remaining flat. We did accrue an extra amount in support office as a bucket for incentives. We'll know a bit more in the second half about how much relates to centres versus support office.

The Group net finance costs were flat versus PCP, reflecting a slightly higher RBA rate on lower average debt levels. The combination of stronger centre performance and prudently managed network support cost increases resulted in a 20% increase in operating EBIT and further recovery of Group margin.

In terms of our non-trading items, software development costs reduced significantly as we flagged in February, with the predominant driver of non-operating costs being the divestment of underperforming centres, impairment of predominantly AASB 16 right-of-use assets, and a slight increase in the provisions we have for historical regulatory and legal matters. The result is non-trading expenses are below the prior year.

Turning to Slide 17, we'll be focused on centre performance. The centre network delivered higher revenue and earnings than the prior comparative period and experienced margin expansion. Occupancy was ahead of the PCP by 0.8 percentage points and revenue increased circa 5.5%, reflecting the January and July fee reviews, our higher occupancy, but also offset by revenues of centres we have exited.

Employment costs demonstrated strong discipline and positive outcomes from our team retention results. Weight inflation increased by circa 8%, including on costs when we compare the six-month period of June '24 to June '23. This uplift reflects the annual award increase effective in July 2023 of 5.75%, increases in pay rates as our team increased their qualifications and additional on costs in some states, along with an increase in the superannuation rate.

Buffering this inflationary impact are wage efficiency improvements, lower agency usage costs, and the removal of wages relating to divested centres. The continued benefit of our improved team retention and lower vacancies is the further reduction of agency usage to 0.3% of wage hours, down from 2.2% in the prior corresponding period.

Given team costs are our largest cost line, this strong result contributed strongly to our margin recovery. Rent is another material cost for our business. Rent expenses increased 3.7% on PCP, noting divesture centres mitigate this increase somewhat and excluding those, increases of circa 4.6%. This reflects the composition of our network where we have a combination of CPI and fixed annual increases.

The higher CPI flowing out of the second half of last year, where leases would have been linked to June, September, December CPI results and an increase slightly above CPI for the June '24 half year. Depreciation increased slightly versus PCP, with an increase of circa $1 million, offset by the reduction in depreciation due to a reduced centre network size.

Other costs saw some increase as a percentage of revenue in the first half. These costs relate to direct cost of servicing our bookings, administrative overheads, and property utilities and maintenance. Out of these costs, where we did see an increase in expenditure in the first half was in the property, utilities, and maintenance area, particularly in Q1 as we sought to ensure our centres presented well for enrolment and transition. These are largely timing differences.

And in the second half, we expect these costs to be more in line with second half '23 as a percentage of revenue. With overall expenses increasing 4.5% versus revenue of 5.5%, centre margins improved by 0.8 percentage points to 15.1%. Similar to the previous year-end results, improvements continued due to the benefits of reduced external labour usage, effective cost discipline, and an active response to inflation.

I'll now touch on capital allocation. The Group declared a $0.02 fully franked interim dividend and 81% payout ratio of the first half earnings, slightly higher than our full-year dividend policy range of 50% to 70%, given the first half earnings are seasonally lower than the second half.

The Group has a strong balance sheet with conservative leverage levels of less than 1x and ample liquidity, and we're pleased today to announce we will be commencing a buyback of up to 5% of the issued capital of the company.

Cash flow generation was strong with cash conversion of above 100% and operating cash flows of $31 million after interest and tax. Of this, we invested 15 million in capex similar to the prior comparable period and paid our larger final dividend of 24 million during the first half. This results in a free cash flow deficit for the half of 8 million, as expected, due to the lower first-half seasonal profile of our earnings.

We also expended $6 million in exiting loss-making centres that we announced in late CY '23. The result of these movements was net increased by about $10 million since December '23, resulting in a leverage of 0.5x. The Group maintains a strong balance sheet with net debt at the half of 68 million.

We have access to a further 156 million of committed bank debt facilities, and we will be reviewing our debt funding facilities in the second half of '24, given we have an upcoming expiry in December '25. Capital and cost management discipline will continue to be a focus as the Group builds capability towards a more consistent and efficient operating model.

Pejman will now talk through the current trading and outlook.

Pejman Okhovat: Thanks, Sharyn. I will now speak to the current trading. Our efforts continue to be maintaining our rigor on execution and family experience. The Group spot occupancy is 72.7%, 0.1 percentage points lower than PCP and our year-to-date occupancy is 69%, 0.7% higher than PCP.

Our fund experience measured by NPS continues to improve, coupled with optimising our conversion and family turnover in a lower inquiry environment. A fee increases of 2.4% was implemented at midyear mitigating inflationary impacts whilst ensuring we balance family affordability.

Putting our capital allocation framework into practice with diligence, we estimate 2024 capex expenditure to remain circa 40 million to 45 million, contingent on construction capacity, timing, and cost. Network optimisation is ongoing with 3 centres divested and one centre exited host 30 June, totalling 22 year-to-date.

Currently, net debt is 90 million. We are maintaining a conservative leverage position to support the commencement of an on-market buyback of up to 5%. The volume of the buyback will be determined by appropriately balancing shareholder returns and leveraging levels, funding our strategic priorities, and other funding needs, including network optimisation and dividend payments.

Now, to our outlook. CY'24 half two sector conditions are anticipated to be more challenging with themes such as sector inquiries remaining lower than PCP. Net supply growth remaining steady at 3.3% year-on-year, and cost-of-living pressures continue to be a key factor in our families resulting in the discretionary stand.

The government and regulatory environment is evolving slowly. Recently, the federal government made an announcement to fund a 15% wage increase for the ECEC sector over two years where the condition of capping fee increase at 4.4% for 12 months from the 8th of August 2024. The Productivity Commission final report is due to be published by November and we continue to be involved into multi-employer bargaining process.

Our near-term focuses remain on maintaining our team engagement momentum, improving our family experience and delivering an improved enrolment and transition program according to next year.

From an operational execution point of view, targeted focus on underperformance centres, maintaining capital and cost discipline, implementing Fit Core strategic plan initiatives leading into 2025. We remain focused on delivering full-year outcomes.

I'm now going to hand back to the moderator to enter into the Q&A session.

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 speakerphone, please pick up the handset to ask your question. We ask today that you please keep to one question per person, after which you may then rejoin the queue. Your first question comes from Tom Tweedie with MA Moelis Australia. Please go ahead.

Tom Tweedie: Good morning, team. Thanks for your time this morning. My one question I have at the moment is just of the occupancy growth of 0.8% for the half. Are you able to give a sense of ex the divested centres, how the occupancy performance went of the remaining sort of 414 centres?

Pejman Okhovat: Good morning, Tom, and thank you for joining and thanks for your question. Tom, as we spoke even at the tender year and at AGM, I think we're going to maintain the kind of -- our occupancy is our occupancy. And I'm not going to really break that detail out. Our job is to put whatever levers that is available to us to improve our overall Group occupancy and that's what we're doing.

Tom Tweedie: All right. Not a problem. I'll jump back in the queue. Thank you.

Pejman Okhovat: Many thanks.

Operator Your next question comes from Brendan Carrig with Macquarie. Please go ahead.

Brendan Carrig: Good morning. Just on the ECEC wage increase, in terms of that fee cap at 4.4% and then with the next 12 months and then the funding being 2 years, do you have any, I guess initial thoughts as to what the potential fee capping could be on a go-forward basis if that funding was to be implemented into perpetuity, which, I mean, I assume sensibly that it would be otherwise the fees would obviously just need to be increased subsequently? So, yes, just any thoughts around how that might transpire would be useful.

Pejman Okhovat: Thanks, Brendan and good morning to you. The real answer is no. Actually, we don't know and that's genuinely factual. We are very much working with the Federal Department to get more clarity on this. And the only thing that we do know is what was published by the government, which was they are working on a new ECEC index, which is actually quite good news.

This was one of the things that the Productivity Commission highlighted, and we are pleased that the government from that respect has listened. If you go back historically, indexing of anything most funding has typically been potentially based around the CPI and the Productivity Commission when consulted with the sector that did take now that CPI is probably not on its own the best index to use.

So, good news, they are going to create an ECEC index, which hopefully will reflect better on our cost overall. So, once we know, I think that will be published as well.

Operator Your next question comes from Wei-Weng Chen with RBC Capital Markets. Please go ahead.

Wei-Weng Chen: Hi, guys. Just a question on agency costs, I guess. What's the multiplier we should think about when thinking about agency staff versus non-agency staff? I guess it's more than just a headline number. I'm assuming because of factors like superannuation and other entitlements. I guess, factoring all of that in. How much more expensive is agency versus staff?

Sharyn Williams: Yes. In terms of working at the bottom-line impact, it is a bit more numerous as you suggest, Wei-Weng because agency team also provide a little bit more flexibility where for example, you might have an agency team member for 4 hours versus replacing with a permanent team member.

You have a bit more rigidity in your roster or lose a smidge of efficiency. In terms of the rates themselves as is public knowledge they're usually at a headline rate potentially, say, double of an internal rate. But as you suggested, it's a bit more nuanced than that in terms of the impact on the bottom line.

What we are pleased with, you can see that coming down into our employment cost as a percentage of revenue to that 1.1% points change in margin and the contribution it made but having our agency down now in that 0.3% has made a contribution but we also don't want to lose sight of the team has done a really good job of managing rosters, etc. as well. So, it's not a 100% agency flow through that increment.

Operator: Once again, if you wish to ask a question, please press star 1 on your telephone and wait for your name to be announced. Your next question comes from Tom Tweedie with MA Moelis Australia. Please go ahead.

Tom Tweedie: Hi again. Look, I just wanted to ask a question about inquiry trends that you're seeing sort of so far in the first sort of 6, 7 weeks. Some of your competitors have been suggesting that the May-June lull has showed some signs of improvement in the second half to date.

So, just curious to see what you're saying. Obviously, you've flagged that you want to -- that's going to be down on PCP is your anticipation, but is the trend improving? Or what are we expecting there?

Pejman Okhovat: A little bit mixed, Tom. I think what we're saying here is certainly in that half, when we talk to the big aggregators in the market who serve actually the majority of the large players, they have seen a year-on-year decrease. So, that's, let's call it, factual.

Going forward, do we anticipate the inquiries to be a bit lower than last year potentially? But in some locations, a little bit different. So, yes, you are right. There's been a bit of mix, certainly in this probably coming out of June, July term, but we remain cautious.

Tom Tweedie: Thank you.

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

Peter Drew: Just a question on support cost. That $3.5 million incentive seems to be a fairly big swing factor in the increase. I'm just wondering, will that flow into the second half just if you can just give commentary on what we should expect for support costs in the second half, please?

Sharyn Williams: Sure. Stepping back, we've got an incentive program that we have had in prior year, Peter. The reason we called this out was in the prior year, we took up more of an accrual in the centres. And then as we went through the year, we rebalanced in the second half, the incentive between support office and centres.

So, it's not a bottom-line impact that reverses. It's really something that as we come into the second half and do our centre-by-centre calculations across our metrics, we then get better insights into how much relates to centres versus support office. So, it's not something that just reverses in the bottom-line earnings, but you will see some movement in centres and support office in the second half once we get some more visibility.

Peter Drew: And what should we expect sort of generally in the second half versus the PCP? Should we expect growth in second half '24 versus second half '23 in support cost?

Sharyn Williams: You mean support costs?

Peter Drew: Yes.

Sharyn Williams: So, we will have inflation coming through, Peter, that as we've seen in the support office headcount, it's flat or a tiny bit under. So, we keep our disciplines on headcount. There will be some increases in salary rates that came through in July, etc. so inflation.

Peter Drew: Okay, great. Thanks.

Operator: There are no further questions at this time. I'll now hand back to Mr. Okhovat for closing remarks.

Pejman Okhovat: Thank you. In closing, I would like to once again thank the G8 Education team for their outstanding work that has delivered these results and outcomes. Our teams everyday work with us in supporting thousands of families and their children with high-quality education and care. Their passion, dedication, and hard work allows us to live our purpose, creating the foundation for learning for life. I'd like to thank you for joining us today on the call and look forward to talking to you very soon.

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

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