

13 February 2019

VILLA WORLD LIMITED ABN 38 117 546 326 ASX CODE: VLW

Villa World Reports for Half Year Ended 31 December 2018

Key highlights:

- Statutory net profit after tax: \$17.6 million (1H18: \$17.3 million)
- EPS: 13.9 cps (1H18: 13.6 cps)
- Dividend: 8 cps fully franked interim dividend declared post balance date (1H18: 8 cps)
- 517 sales¹ recorded (1H18: 742)
- 1,126 sale contracts carried forward with a gross value of \$340.4 million² with settlements commencing in 2H19 through to FY21
- Net tangible assets \$2.31 per share (FY18: \$2.44 per share)

Financial result

The Company reported a 1H19 statutory net profit after tax of \$17.6 million (13.9 cps), compared with the prior period's result of \$17.3 million (13.6 cps).

The Board declared an interim dividend of 8 cents per share fully franked consistent with its dividend policy of a payout ratio of 50%-75% of annual NPAT, paid semi-annually.

Operational performance

The Company recorded 611³ wholly owned settlements in 1H19 (1H18: 626), resulting in \$232.7 million revenue (1H18: \$202.2 million).

The reported gross margin was \$57.2 million or 24.6% (1H18: \$48.0 million or 23.7%), within the guidance range of 23%-25%⁴.

During 1H19 the Company continued to deploy development management skills into joint venture arrangements, delivering \$1.2 million in fee income (1H18: \$8.0 million which included a one-off \$7.3 million fee). Further, the share of profit from equity accounted investments was \$1.0 million in 1H19 (1H18: \$0.7 million) which related to 59 land settlements at the Covella and Rochedale joint ventures.

¹ Statistics associated with sales, production, settlements and portfolio lots have changed for split contracts and joint ventures.

Previously they were recorded in line with Villa World's ownership interest or as part of a whole transaction; they are now recorded as one single transaction. Refer to ASX investor presentation for reconciliation. 1H19: 365 wholly owned sales and 152 joint venture sales (recorded at 100%). 1H18: 700 wholly owned sales and 42 joint venture sales (recorded at 100%).

² Contracts are included on the basis of 100% for wholly owned projects (933 lots worth \$289.7 million) and 100% for Joint Venture projects (193 lots worth \$50.7 million). Represents gross sales price including GST.

³ Total settlements 1H19: 670 lots (1H18: 648) of which 611 lots are from wholly owned projects (1H18: 626) and 59 lots from joint venture projects (1H18: 22) recorded at 100% and reflected in Share of Joint Venture Profits.

⁴ From FY19 the Company has changed the presentation of borrowing costs previously capitalised and net impairments, into the cost of inventory sold. The changes do not impact net profit after tax. However, gross margin, EBITDA and finance costs have changed. The changes in accounting classifications lower the reported gross margin, with the Company now targeting a gross margin range of 23% to 25%, reduced from 24% to 26%.

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Sales performance

The Company recorded 517 sales during 1H19, down 30% on 1H18 (742 lots).

Demand for the Company's core product – affordable land and housing in the growth corridors – performed as expected in the first quarter. As widely reported, Australia's residential housing market conditions and customer sentiment have declined. Customers are experiencing a reduction in the availability of finance, delayed finance approvals, more stringent assessment criteria and reduced borrowing capacity. This led to lower sales results and enquiries in late 2018.

Demand in Victoria moderated from the cyclical highs seen in FY18, influenced by tightening credit conditions, waning consumer confidence and strong price growth over recent years which is now affecting affordability. Nonetheless, the Company's Victorian projects delivered consistent sales, particularly at the Wollert joint venture.

Queensland flagship projects including *The Meadows* (Strathpine), *Killara* (Logan) and *Arundel Springs* (Gold Coast) sold well. However, an anticipated uplift in the Queensland market is yet to eventuate.

In response to current market conditions, the Company has invigorated its sales strategy in 2H19 to highlight its value offering in the affordable housing sector.

The Company maintains a strong presence across its key customer segments, being retail buyers comprising of first home buyers and other owner occupiers, as well as builders and local investors.

The Company will carry forward into 2H19 1,126 sales contracts worth \$340.4 million⁵. 30% of contracts (342 lots valued at \$116.6 million) are anticipated to settle in 2H19, a further 59% settling in FY20 (666 lots valued at \$193.5 million) and the balance of 118 lots valued at \$30.3 million settling in FY21. The Company is carrying significant unconditional sales at *Lilium* (Clyde), *Sienna Rise* and *Sienna North* (Melbourne North West). While planning delays have been resolved and delivery is progressing, the Company now anticipates settlements at *Lilium* to commence in 2H19 and *Sienna Rise* and *Sienna North* in 1H20.

Adoption of AASB 15

The new accounting standard AASB 15 came into effect on 1 July 2018. AASB 15 – revenue from contracts with customers has changed the point in time at which the Company recognises revenue for certain contractual arrangements. Land only and house and land contracts in Queensland and Victoria are now recognised at cash settlement. The Company adopted the standard under the modified retrospective approach where comparatives are not restated, rather, a one-off retained earnings adjustment of \$21 million was made for contracts not completed. Further information can be found in the Interim Financial Report in note A1(c) *Accounting for Revenue* and E2(c)(ii) *New accounting standards and interpretations – AASB 15 Revenue from contracts with customers*.

Cash flow performance

The Company generated strong net cash flows from trading activities of \$85.4 million which supported expenditure of \$19.1 million on the acquisition of new land while retaining a strong cash and debt position. The land acquisition payable at 31 December 2018 is \$51.4 million (FY18: \$33.7 million). This will be settled from operating cash flows, existing debt facilities and settlement proceeds from third parties.

Balance sheet

Net tangible assets at half year-end were \$290.0 million (FY18: \$309.7 million), representing \$2.31 per share (FY18: \$2.44 per share) before the declaration of the interim 8 cps dividend.

⁵ Contracts are included on the basis of 100% for wholly owned projects (933 lots worth \$289.7 million) and 100% for Joint Venture projects (193 lots worth \$50.7 million). Represents gross sales price including GST.

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As forecast, during this current delivery phase the gearing at 31 December 2018 was 27.9% (30 June 2018: 29.7%), within the Company's target range of 15% to 30%. Net debt as at 31 December 2018 was \$149.2 million (FY18: \$171.1 million).

The Company commenced an on-market share buy-back in October 2018 for up to 5% of shares on issue, as part of its capital management strategy. The buy-back is being funded from working capital. At 31 December 2018, the Company had purchased 1,376,642 shares at an average price of \$1.89. The buy-back represents a prudent deployment of capital, being NTA and earnings per share accretive.

Portfolio

The Donnybrook joint venture has previously entered into contracts to sell 960 Donnybrook Road to 960 Blueways Pty Ltd and 1030 Donnybrook Road to Satterley Property Group Pty Ltd, both of which are conditional on Precinct Structure Plan (PSP) approval. On 21 December 2018 the Company confirmed receipt of \$5.5 million under the contract for 960 Donnybrook Road, taking the total payments held under that contract to \$10 million.

The Company's share of revenue from the sales will be recognised progressively in line with the staged settlements, and will therefore be dependent on timing of PSP approval. The PSP approval process has progressed positively. Consultation with relevant authorities has enabled the Company to revise its estimate of the likely timing for PSP approval. Based on that, it is now expected that revenue from the sale contracts will begin to be recognised from 1H21, underpinning earnings through to FY24.

Villa World expects current market conditions to present opportunities commencing in FY20, for astute acquisitions and strategic partnering relationships. With a strong balance sheet and disciplined capital management, the Company expects to be well placed to capitalise on these as they arise.

At 31 December 2018, the Company had a portfolio of 6,910 lots⁶ (FY18: 7,064) representing approximately five to six years of sales.

1H19 Dividend

The Board has declared an interim dividend of 8 cents per share fully franked post balance date. The ex-dividend date for the interim dividend is 12 March 2019, the record date is 13 March 2019, and payment is scheduled for 2 April 2019.

Outlook

In 2H19 the Company will continue to focus on operational delivery and cash settlement of carried forward sales. Sales conditions are expected to remain difficult. This will be balanced against an invigorated sales strategy with pricing and products positioned to meet the needs of key customer segments.

The Company is progressing its joint venture strategy. In FY19, these arrangements are expected to contribute ~\$4 million to profit before tax comprising of development management fees and share of profit, primarily from the Rochedale and Covella joint ventures. The presales from the Wollert joint venture are expected to contribute to profit from FY20, with the Donnybrook joint venture likely to contribute from 1H21 as noted above. Development management fees continue to provide an ongoing revenue stream, as the Company pursues capital-efficient growth opportunities that provide a strong return on assets.

The FY19 gross margin is expected to be within the range of 23% to 25%.

The Company expects cash outflow for acquisitions in FY19 of ~\$32 million, inclusive of \$16.6 million in capital lite transactions, with the balance funded from existing debt facilities.

⁶ Inclusive of joint venture projects recorded at 100%.

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Despite current market conditions, the Company remains confident that its medium to long term strategy and affordable price point will provide sustainable success and shareholder value beyond the current sector dynamics.

A key strength is the Company's fully built turnkey housing model which has strong operational efficiencies. This will enable the Company to deliver more housing product which has a higher profit component compared to land only. As is prudent in current market conditions, the Company will continue to responsibly manage its cost structure.

FY19 Guidance

Market conditions and the availability of customer credit are likely to remain challenging for the remainder of FY19. Upcoming federal and NSW elections may also lead to increased customer uncertainty.

Several stages in the Company's Victorian projects are scheduled for completion in late FY19, with some likely to extend into 1H20.

Given those factors, the Company considers it prudent not to provide guidance for FY19 at this time. The Company will continue to monitor progress and update the market when appropriate.

The Board recognises the importance of returns to shareholders through fully franked dividends, whilst also being mindful of long-term, sustainable value creation through reinvestment of capital. The Board intends to continue with a full year payout ratio consistent with its stated dividend policy (payout ratio of 50%-75% of annual NPAT, paid semi-annually).

This phase of the property cycle will bring opportunities. The Company has a long history of successfully navigating through market cycles, and has a forward strategy focused on its customers and long-term value creation.

The Company has conviction that its projects are located where people want to live, its homes are priced within reach of its customers and its turnkey homes offer a unique customer experience. With sound financial fundamentals, prudent capital management and a committed team, the Company has the foundations and resources in place to deliver shareholder value.

1H19 Financial Results live audio stream

The Company's 1H19 results presentation will be webcast on Wednesday 13 February 2019 at 2pm AEDT at the following link <https://webcast.openbriefing.com/4990/>

Subsequently, the webcast will be archived on the Company's website <http://www.villaworld.com.au/investor-centre/media-release/videos> and at <http://www.openbriefing.com/OB/3197.aspx>

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