Mears Group PLC

Final results for the year ended 31 December 2017

Agenda

- → Highlights and lowlights
- → Finance review
- → Operational and strategic review
- → Outlook

Highlights

- → Operational progress and a broader service offering continues to develop
- → Excellent customer service maintained which underpins our success in Housing
- → Better financial performance in Care, returning to profit as planned
- → Dividend increasing by 3% to 12.00p reflecting Board confidence in the underlying performance and long term prospects of the Group
- → New £30m debt facility to fund short-term purchases of properties as part of the Group's development of longer-term homelessness solutions
- → Well positioned with two significant bidding opportunities, previously beyond the reach of the Group

Lowlights

- → A challenging year
- → Postponed work streams due to clients understandably prioritising fire safety works
- → Mixed perception of public sector outsourcing
- → Opportunities missed on traditional housing bids
- → Some disappointing financial outputs

Group revenue

£900.2m -4%

2017	£900.2m
2016	£940.1m
2015	£881.1m

Group operating profit*

£39.2m -6%

2017	£39.2m
2016	£41.9m
2015	£38.7m

Dividend per share

12.00p +3%

2017	12.00p
2016	11.70p
2015	11.00p

Normalised diluted earnings per share*

28.05p -8%

2017	28.05p
2016	30.36p
2015	27.94p

* On continuing activities, stated before amortisation of acquisition intangibles. The normalised EPS measure is further adjusted to reflect a full tax change.

Finance review

Andrew Smith

Income Statement*

	2017 £m	2016 £m	Change %
Sales revenue	**900.2**	940.1	-4%
Operating profit**	**40.0**	42.9	-7%
Long term incentive plans	**(0.8)**	(1.0)	
Net finance costs	**(2.0)**	(1.8)	
Amortisation of acquisition intangibles	**(10.6)**	(10.7)	
Profit for the year before tax	**26.5**	29.4	-10%
Tax expense	**(4.3)**	(3.7)	
Profit for the year	**22.2**	25.7	-14%

Normalised diluted earnings per share (p)**	**28.05**	30.36	**-8%**
Weighted average number of shares (m)	**104.03**	102.92	
Dividend per share (p)	**12.00**	11.70	**+3%**

* Continuing activities.

** On continuing activities, stated before amortisation of acquisition intangibles. The normalised diluted EPS amount is further adjusted to reflect a full tax charge.

Group

2017	H1	H2	Total
Revenue £m	470.8	429.4	900.2
Operating profit £m*	19.8	20.1	40.0
Margin%	4.2%	4.7%	4.4%
2016			
Revenue £m	466.2	473.9	940.1
Operating profit £m*	19.9	23.0	42.9
Margin %	4.3%	4.9%	4.6%

Group revenue
£900.2m -4%

Operating profit*
£40.0m

Operating margin*
4.4%

* On continuing activities, before amortistion of aquired intangibles and long-term incentive plans

Housing

2017	H1	H2	Total
Revenue £m	402.0	364.1	766.1
Operating profit £m*	20.8	18.7	39.5
Margin%	5.2%	5.1%	5.2%
2016			
Revenue £m	389.6	397.9	787.5
Operating profit £m*	18.9	25.2	44.1
Margin %	4.9%	6.3%	5.6%

→ Reduction in client discretionary spending

→ Slower period for new contract mobilisations

→ Reduced overhead recovery impacted on margin

Revenue

£766.1m -3%

Operating profit*

£39.5m -10%

Operating margin*

5.2%

* Before amortisation of acquired intangibles and long-term incentive plans.

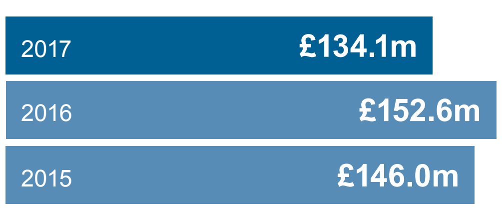
Care

	Hours per week	Annualised revenue	Charge rate per hour
As at 1 January 2016	216,000	£148.1m	£13.19
Net volume decrease	(54,600)		
As at 31 December 2016	**161,400**	**£126.2m**	**£15.04**
Net volume decrease	(22,200)		
As at 31 December 2017	**139,200**	**£117.9m**	**£16.29**

- → Restructuring now complete
- → Charge rates increased in line with cost base
- → Continuing improvement in charge rates
- → Scope for improving margins going forward

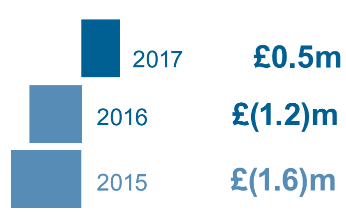
Revenue

£134.1m -12%



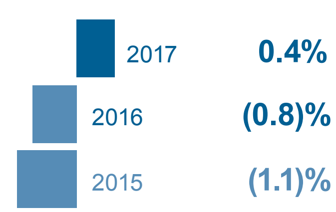
Operating profit*

£0.5m



Operating margin*

0.4%



* Before amortisation of acquired intangibles.

Balance sheet

	2017 £m	2016 £m
Goodwill and intangible assets	**210.9**	219.6
Property, plant and equipment	**22.0**	20.3
Inventories	**18.7**	11.2
Trade receivables	**153.9**	157.2
Trade payables	**(178.3)**	(186.6)
Net debt	**(25.8)**	(12.4)
Deferred consideration	**(11.1)**	(16.5)
Cash flow hedge	**(0.3)**	0.4
Pension, net surplus	**22.3**	8.5
Taxation	**(2.7)**	(3.0)
Net assets	**209.6**	198.7

→ New property acquisition facility disclosed separately from core working capital

→ Deferred consideration settled in full in January 2018

→ Significant increase in net surplus on pension arrangements

Balance sheet - assets held for resale

	2017 £m	2016 £m
Assets held for resale	**13.9**	-
Short term borrowing	**(13.9)**	-

- → Broader Housing services increasingly involve “funding solutions”
- → New debt facility of £30m disclosed separately from core working capital
- → Additional funding to facilitate significant client opportunties
- → Land and property acquisitions held for short periods only

Pensions

	Group Schemes (Long term risk) £m	Other Schemes (Medium term risk) £m	Other Schemes (Limited risk) £m	**Total £m**
Scheme assets	**157.3**	46.1	**276.4**	**479.8**
Scheme obligations	**(132.6)**	(47.5)	**(277.4)**	**(457.5)**
Net surplus / (deficit)	**24.7**	(1.4)	**(1.0)**	**22.3**

→ The Group seeks to minimise its exposure to pensions at the point of bidding new opportunities

→ Client indemnities reduce risk exposure

Cash performance

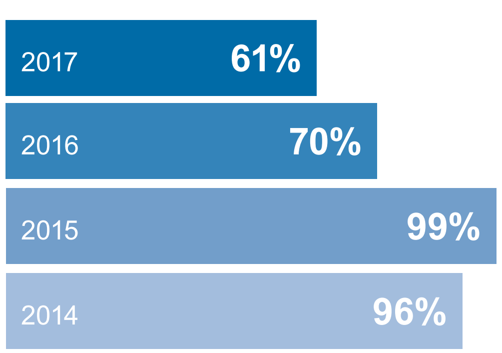
	2017 £m	2016 £m
Operating profit*	**39.2**	41.9
Depreciation and amortisation	**8.2**	7.4
EBITDA	**47.4**	49.3
Cash inflow from operating activities	**28.7**	34.5
EBITDA to cash conversion	**61%**	70%
Net debt at balance sheet date	**25.8**	12.4
Average debt in year**	**96.4**	85.0

* Before amortisation of acquired intangibles

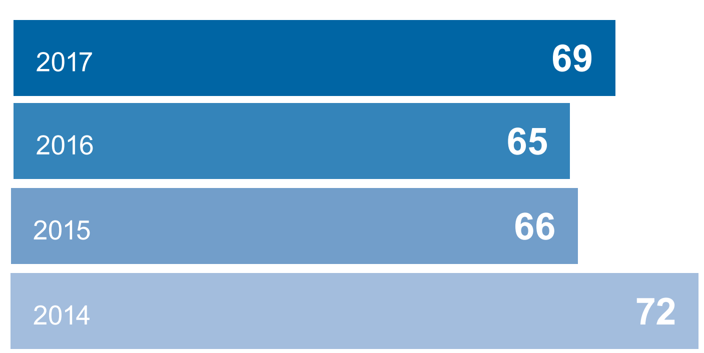
**Average debt represents a 365-day mean

- → Average debt £96.4m; range £66m to £117m
- → Bank facility extended to November 2022
- → Property acquisition facility excluded from working capital measures

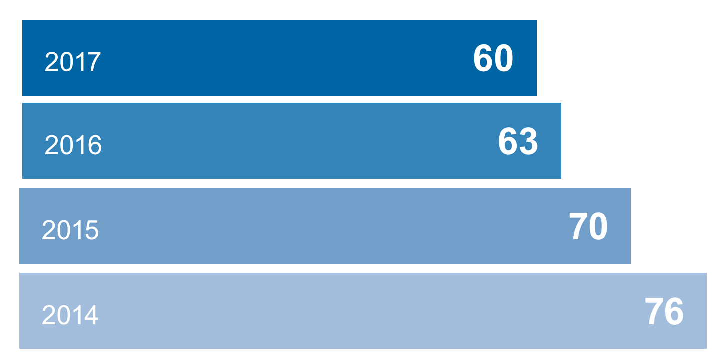
EBITDA to cash conversion



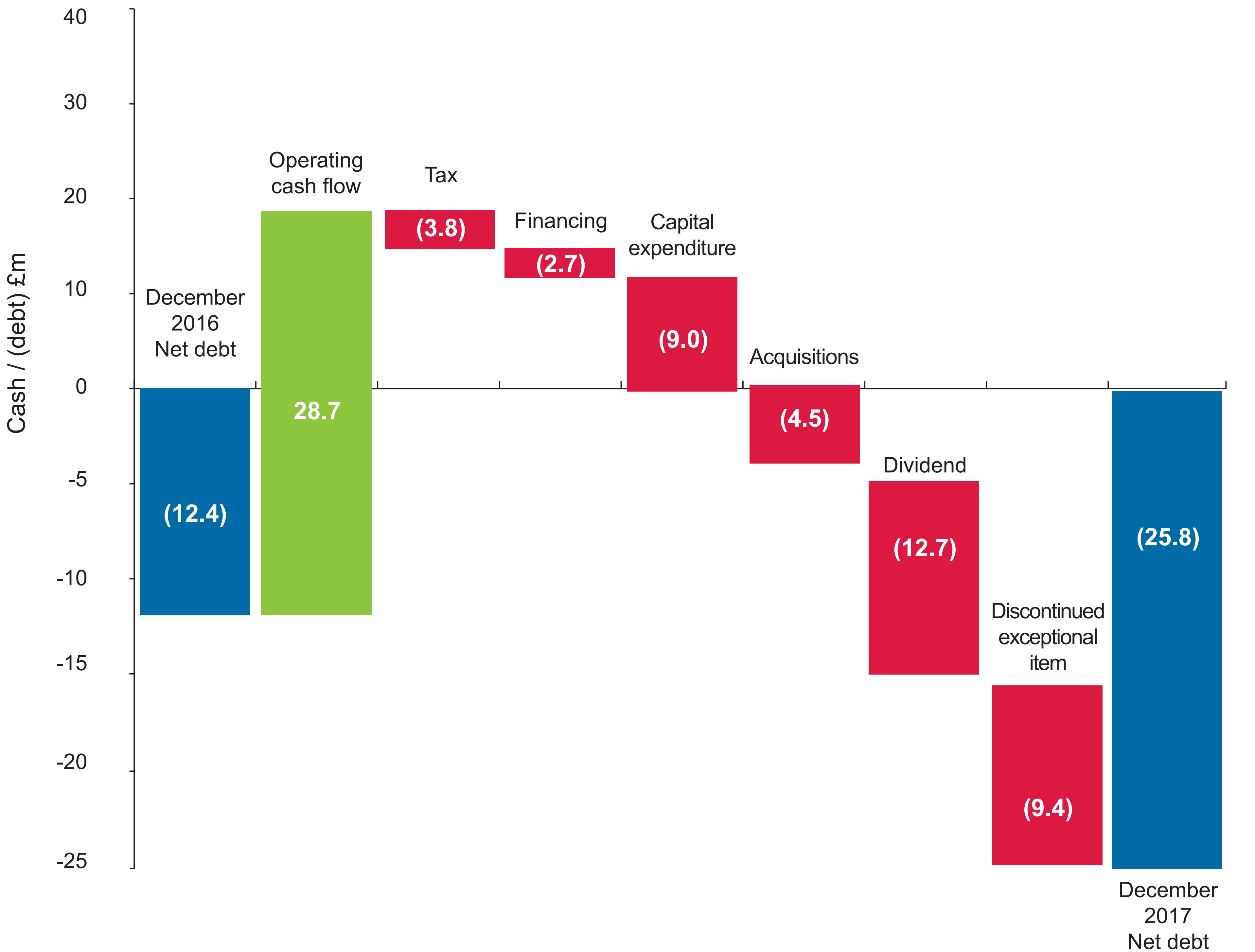
Average trade receivable days



Average trade payable days



Net debt (excluding property aquisition facility)



Changes to Accounting Standards

- Two new standards coming into force
- IFRS 15 Revenue from Contracts with Customers (effective from 1 January 2018)
    - No significant impact expected
    - New accounting methodology for the timing of revenue recognition for a small number of long-term, multiple workstream contracts
    - For the large majority of contracts; no change
    - A reduction in opening reserves of between £13m - £20m, increase in profit recognition over 2018 to 2026 as contracts run-off
- IFRS 16 Leases (effective from 1 January 2019)
    - No current intention to adopt early
    - Aligns the treatment of operating leases and finance leases to recognise all leases on the balance sheet
    - Balance sheet will recognise right of use lease assets, together with the associated lease liabilities
    - The expected balance sheet impact would be an increase in assets and liabilities in the range £80m - £140m
    - Impact on PBT expected to be neutral

Guidance for 2018

→ Firm and probable revenues	£900m	→ More conservative basis for our expectations
→ Housing margin	5.6%	→ Cost saving initiative to drive margin improvement, reflecting evolution of the business
→ Care margin	>3%	→ Continued margin improvement reflecting the quality of order book, improvement in operations and more efficient processes
→ EBITDA to cash conversion	>85%	→ Payment mechanisms in core Housing and Care contracts remain favourable. New development contract opportunities absorbing some working capital.
→ Average net debt*	£110m	→ Reflects cash outflow on discontinued activities in late 2017 and settlement of deferred consideration in January 2018
→ Dividend	In line with earnings	→ Maintain dividend cover at current level

* excludes property acquisition facility

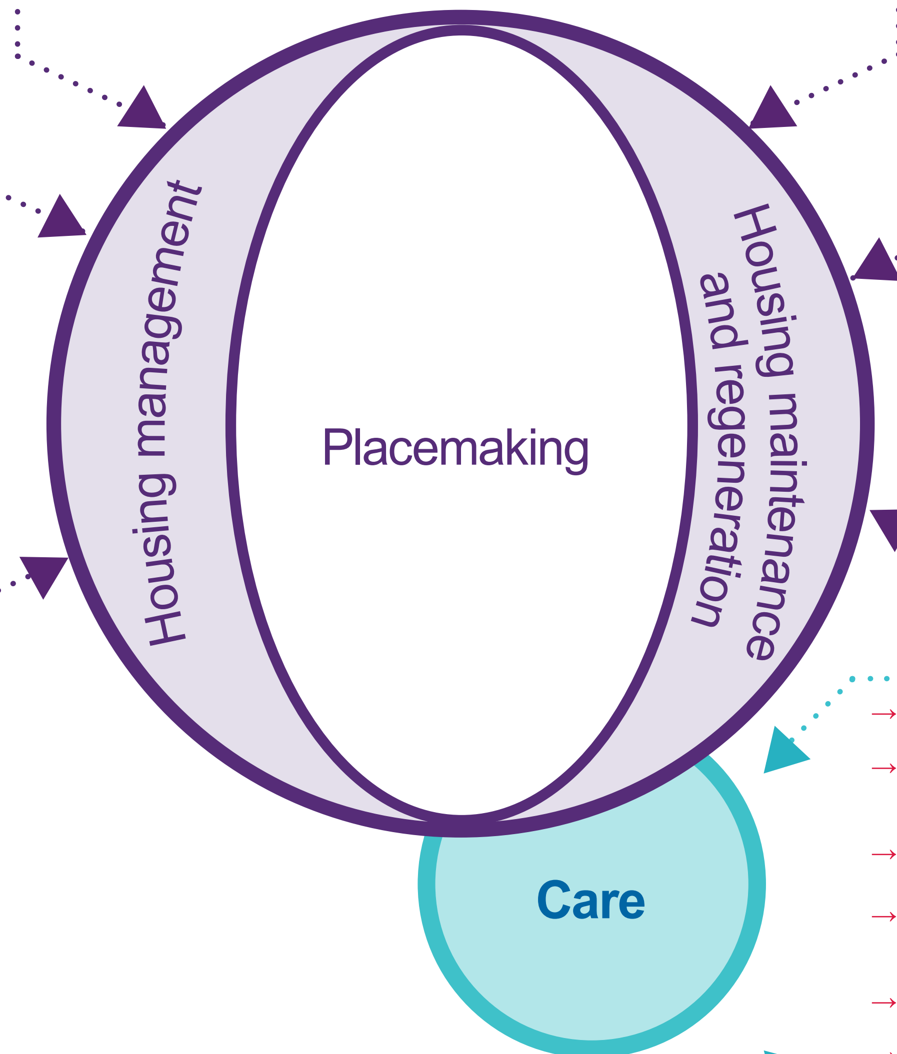
Operational and strategic review

David Miles

Market drivers

- Green Paper due in summer of 2018
- Rent increases from 2020 will generate additional funding
- HRA surpluses

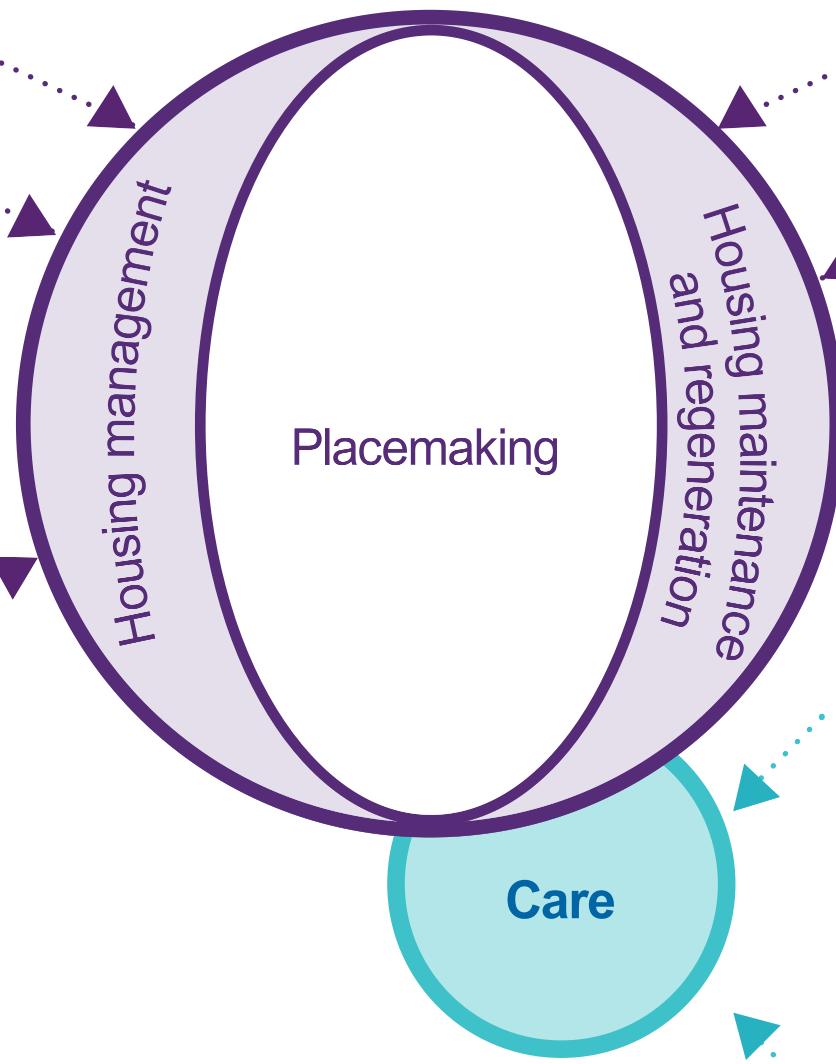
- Waiting lists increasing
- Growing dependency on temporary housing
- Homelessness Reduction Act
- Cross party drive to tackle housing shortage
- Universal Credit risk
- Solutions to address poorly delivered, Central Government funded, key worker housing



- Increased focus on Social Housing, neglected since 2010
- Greater emphasis on fire safety and compliance
- Increased consolidation of Registered Providers, a number of recent mergers
- Central funding to build more homes
- Some redirection of funds from capital repairs to new build projects

- Significant shortage of specialist housing for elderly
- Five times as many elderly people rent in Social Housing rather than private sector
- Ageing demographics
- Green Paper expected in summer of 2018 addressing funding and future of Social Care
- Local merged budgets
- Health Minister responsibility extended to Social Care
- Increase in delayed hospital discharges

Mears differentiators



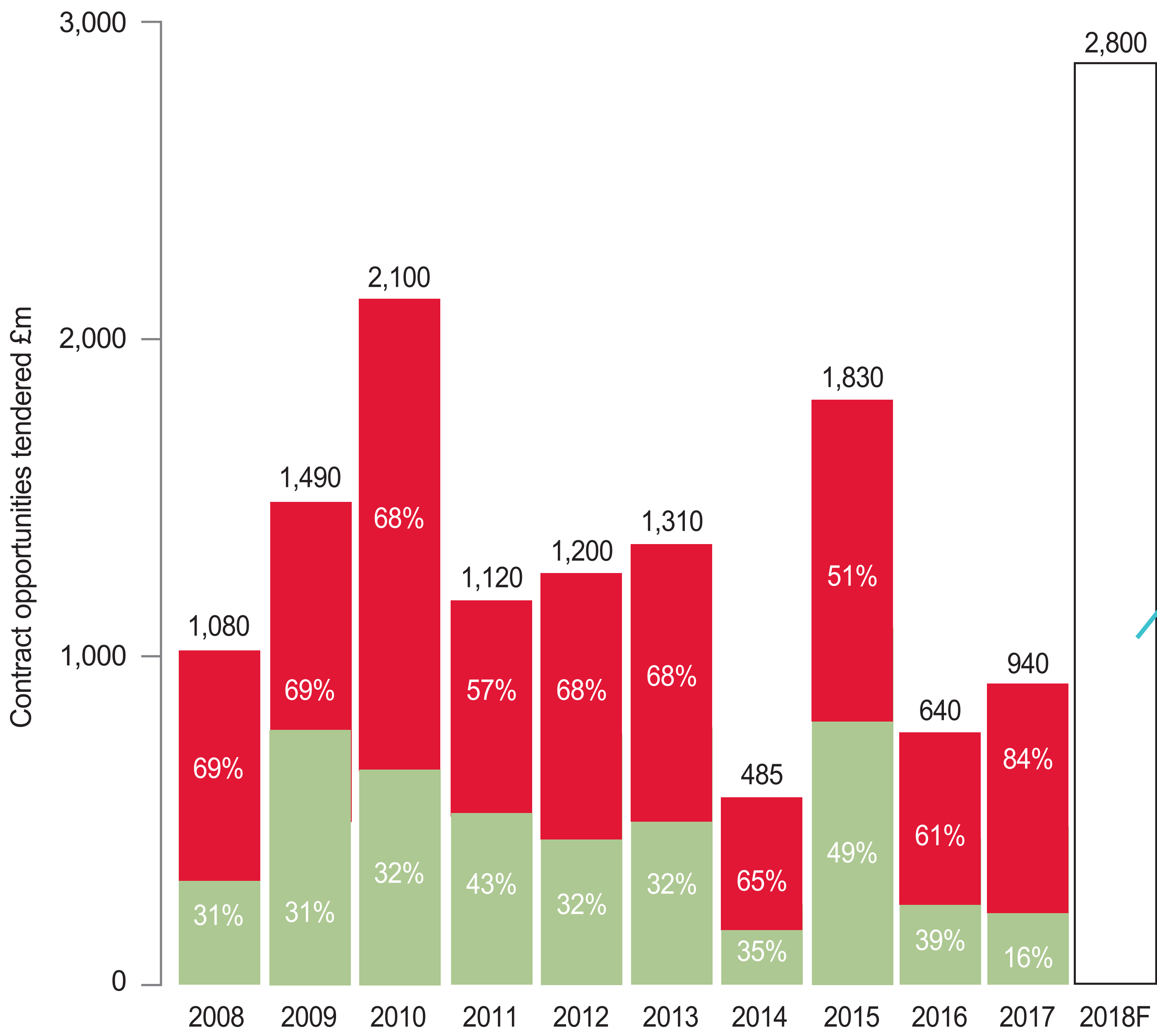
- Market-leading team
- Access to decision makers
- Track record

- Access to financial partners
- National coverage
- High number of housing sector relationships
- Call centre capability
- Registered Provider, landlord of choice
- Mixed tenure portfolio

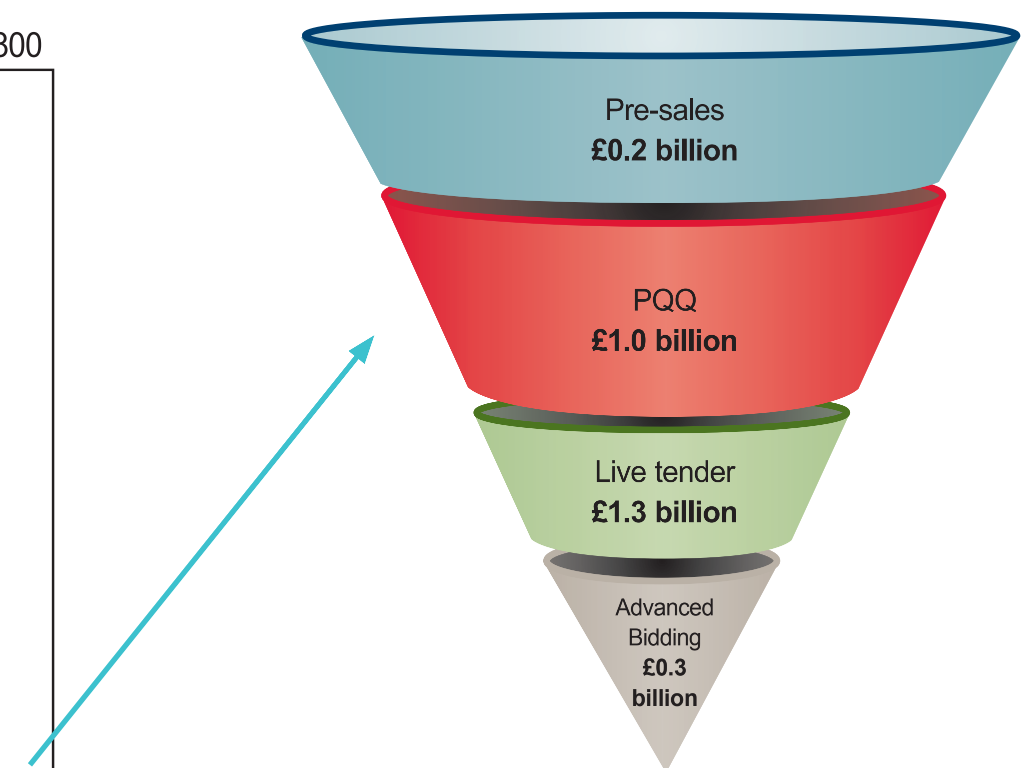
- The best blue collar delivery team
- Trusted partner
- Market-leading IT systems
- Integrated supply chain
- Remote working
- Historical housing data

- CQC registration
- Good core capability
- Track record of self-delivery

Competitive bidding - Housing



Bidding expectation for 2018: £2.8 billion



- Mears will remain highly selective and is confident in its bid model
- Addressable market becoming larger and more complex
- Increasingly, new opportunities can be secured outside a competitive process
- Target bid conversion rate 33%, in line with historic norm

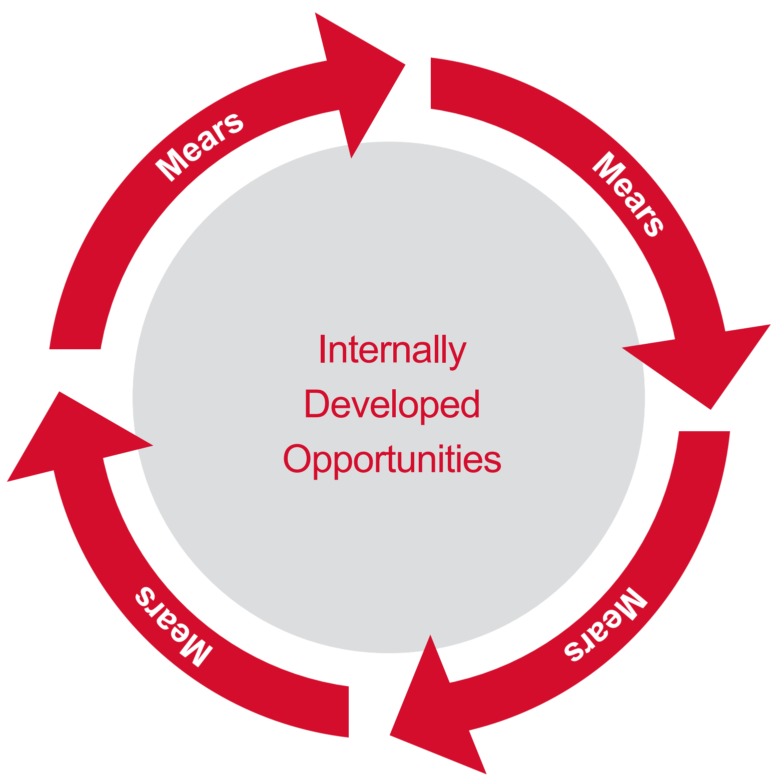
KEY

- Tendered - unsuccessful
- Tendered - contracts awarded

Key competitive bidding opportunities in 2018

Partnership type	Annual value (£m)	Term (years)	Contract value (£m)	Start
Contracting	22.0	4	88	Apr-18
Contracting	9.0	5	45	Jun-18
Contracting	12.0	10	120	Oct-18
Contracting	8.5	10	85	Oct-18
Placemaking	110.0	10	1,100	Dec-18
Placemaking	23.0	10	230	Apr-19
Placemaking	70.0	10	700	May-20
	254.5		**2,368**	

Other key development opportunities for 2018



Purchase and Repair

Client: Local Authorities
Imminent pipeline: circa 1,200 properties
Work type: funding arranger, regulation, purchase, refurbishment, management, maintenance
Contract term: 40 years
Contract value: £300m

Affordable, s106

Client: REIT / Local Authority
Imminent pipeline: circa 2,000 properties
Work type: regulation, management, maintenance
Contract term: 22 years
Contract value: £264m

Extra Care

Client: REIT / Local Authority
Imminent pipeline: circa 5 schemes
Work type: funding arranger, regulation, purchase, refurbishment, management, maintenance
Contract term: 40 years
Contract value: £150m

Outlook

- More conservative approach to market guidance
- Our unique strategy leaves Mears better placed than ever to achieve long-term success

Housing

- Broadened service offering continues to develop, with Mears well positioned to address the changing needs of our clients
- Addressable market in Housing becoming larger and more complex
- Increased focus on compliance and safety fits well with Mears' differentiated offering
- Targeted acquisitions, joint ventures and partnerships to accelerate the breadth and depth of service

Care

- Continued focus on better quality contracts providing clear and sustainable margins
- Increasing emphasis towards clients with likely opportunities to provide a complete Housing service

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