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Q1 FY24 D&G Bondholder Call

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29 August 2023

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Domestic & General's Q1 FY24 Bondholder Call. Today's discussion may contain some forward-looking statements relating to future events and expectations. As usual, the factors that could cause actual results to differ materially from these projections are set out in the latest results statement. In addition, we have included some non-GAAP financial measures in our discussion, reconciliations for which can be found in the results statement. With that, let me hand over to the CEO, Matthew Crummack.

Matthew Crummack

Thanks very much, and good morning. Thank you, all of you, for joining us this 29th of August. Matthew Crummack, CEO, here; Joe Fitzgerald, CFO, and the team speaking to you live from our Wimbledon head office. Once again, welcome to our results announcement for the quarter ending 30th of June 2023, which is the first quarter of our new financial year, FY24.

It's going to be a shorter session today given that it's only been a few weeks since we took you through our year-end results and a detailed business update, including track record, strategy, and so on. So, we'll focus more on the Q1 financial results and less on the non-financial areas. I'll go through those headlines and then Joe will take us a bit more through the detail as we go. And then obviously we'll pick up again when we do the half year, later in the year.

So, if we can turn to slide two, please. We have had an encouraging start to the year and generated 10% total revenue growth compared to the same quarter last year, which is in line with what we expected. As part of our total revenue growth, we've grown subscription revenue further by 9%, including continuing strong subscription revenue growth of 20% in our combined international businesses. Group subscription retention rates once again remain stable for the quarter, tracking the long-term average of 85%, which is great news as the business continues to successfully weather the wider cost-of-living pressures in our markets.

EBITDA has similarly continued to grow in line with our plan such that adjusted EBITDA, including the results of our US business, grew by 9% compared to the equivalent quarter last year to £38 million. On a basis that excludes the US, we recorded 8% EBITDA growth to £40 million.

We continue to have strong levels of liquidity in the group following our acquisition-related borrowing facility increase and the accompanying injection of shareholder equity. And we have a substantial solvency coverage ratio in our regulated business. Net debt leverage has remained stable in the quarter, whilst net debt itself has increased slightly, to £727 million, which is inclusive of the RCF drawings that were used to part fund our acquisition of After Inc. during the quarter.

In Europe, we're really pleased to have signed a distribution agreement with a brand-new client, Carrefour, whom I'm sure you know very well, which initially enables us to start providing protection to Carrefour customers via over 200 retail stores

in Spain, with potential for further collaboration in other countries in Europe in the future. This is an important new relationship for us at D&G, with Carrefour being such a significant appliance retailer across Europe.

We have also recently signed another important Pan-European agreement, this one with Panasonic, including country-specific agreements for Germany and Austria and we've also updated our European contract with our largest client, Whirlpool. Collectively, we expect that all these developments will support the growth of our European business for the years to come.

Finally, on the US, we spoke at length about our acquisition during our annual results announcement just a few weeks ago, and our enlarged, combined US team is now working at pace on integrating our acquired business together with our own organic US operations. And if you look at our Q1 results statement, you'll see that it includes the relevant IFRS acquisition accounting disclosure.

So, with that overview of highlights complete, I'd like to hand over to Joe to run through financial results in more detail and of course, we'll take questions at the end, as usual. Thanks. Over to you, Joe.

Joe Fitzgerald

Thanks, Matthew. Good morning to those of you listening and welcome to our quarter one results call. As Matthew has given an overview of our headline financial results, I will move on to our usual KPIs on slide four.

On this first KPI slide, you can see the customer-focussed indicators. At the top, we have recorded a rise in subscription customer numbers, from 6.1 million in Q1 of FY23 to 6.3 million at the end of the most recent quarter. Besides new business sales, the main factor influencing subscription customer numbers is, of course, our customer retention rate, which remains stable at 85%, in line with our long-term average retention performance.

In the middle, left-hand shot, you can see the average revenue per customer continues to rise. And whilst the rise from Q1 last year partly reflects pricing impacts which we put through in view of the inflationary environment, it also reflects ongoing improvements in household penetration. These twin factors of customer numbers and revenue per customer have delivered growth in subscription revenue to £229 million for the quarter, as shown in the main chart.

Moving on to slide five, this slide shows our principal financial KPIs. As just mentioned, subscription revenue grew to £229 million from £210 million in the same quarter last year, whilst non-subscription revenue also rose slightly, going from £28 million in Q1 FY23 to £33 million Q1 FY24. This was partly due to a contribution from After Inc. for our month of ownership

and also partly due to earnings patterns from European extended warranty sales made in prior periods. Subscription revenue now represents 88% of total revenue for the group.

The lower set of graphs shows the EBITDA margin at the end of the relevant quarter on a last 12 months basis. This shows an EBITDA margin of 13.3%, which is slightly up on the prior year, as we have aimed to maintain margins despite the inflationary pressures we've seen in the market, delivering a quarterly US-inclusive EBITDA of £38 million.

On our next slide, slide six, we look at our revenue in more detail, where as usual, we break down the results into UK, Europe and Other, and the US. As I mentioned during our annual results call, the Europe and Other category includes the results of our run-off Australian business, but I will refer to it as Europe for simplicity.

As the chart shows, on a comparative quarter basis, growth in total revenue for the quarter was 10%, including 7% growth for the UK and 15% for the European business. As a component of total revenue, subscription revenue in our mature UK market grew at 7%, which mirrors the 7% growth in total UK, given that in the UK subscription revenue represents 95%. In our European business, subscription revenue grew at 16% and represents 61% of the division's revenue. With the addition of US to Europe, overall international subscription revenue grew at 20% compared to the comparative quarter.

Non-subscription revenue also grew, as noted earlier, disrupting its longer-term downward trend, as we have included After Inc. revenue for one month of ownership and that is currently cash business rather than subscription. US non-subscription revenue will therefore rise for the time being at least.

Looking ahead to the rest of the year and continuing with recent trends, we expect our full-year total revenue growth percentage to be in the mid-to high-single digits once again.

Moving on to slide seven and to EBITDA. The slide shows that our adjusted EBITDA for the quarter rose by 9% compared to the comparative prior year quarter, coming in at £38.3 million, including a £2.9 million increase in our mature UK and European business and a reduction in losses for the US business. EBITDA is stated on a basis which includes the adoption of the new insurance accounting standard, IFRS 17, which means the prior year comparators have necessarily been restated. At this stage, of course, these adjustments are unaudited and potentially subject to change, but they do represent our best assessment of the adoption impact.

The impact of IFRS 17 adjustments on EBITDA is expected to be in the mid-to high-single digits in terms of absolute millions for the full year for both this year, FY24 and the prior year, FY23, which means post-IFRS growth rates will be

broadly consistent when compared to a pre-IFRS 17 basis. Please note here that we do not plan to report separately these impacts going forward and will report and guide on an IFRS 17 basis-only accordingly.

The US results primarily reflect early-stage costs and revenue earnings patterns in relation to our organic start-up business, as the month's ownership of After Inc. up to 30 June means its contribution is not material.

Excluding the US loss in the quarter of 1.6 million, adjusted EBITDA for the quarter was £39.9 million, which is an 8% increase.

Now we'll turn to cash flow for the quarter, on slide nine. So here we have presented our unrestricted cash flow in the revised format we first showed you at year end, which we hope is a more intuitive way of presenting cash. This cash flow shows the movement from opening to closing and unrestricted cash over the quarter compared to the equivalent first quarter last year. And as discussed previously, unrestricted cash represents the cash and liquid investments of our unregulated business, plus the capital of our regulated business that is in excess of its solvency capital needs.

On the first line of the cash flow, you can see the US-inclusive EBITDA result for the group, and we have started the cash flow for the quarter with this US-exclusive number to best illustrate the cash performance of our mature and established businesses. Next down from EBITDA, we show the working capital outflow from our unregulated business, which was a £5 million outflow for the quarter, largely reflecting the settlement of the group's annual variable remuneration element, which was payable in June. As with our annual results, the unregulated working capital amount excludes the distortive working capital impact of our Australian run-off, which is showing further down the page for clarity.

The next line-item shows the amount of regulated EBITDA, which exceeds the change in distributable reserves of the regulated business with a simple reconciliation included at the foot of the page. As explained previously, the increase in distributable reserves of the regulated business is derived on Solvency II actuarial principles rather than IFRS principles and should generally be expected to be lower than the amount of regulated EBITDA, due to differing balance sheet measurements under IFRS and Solvency II, as well as general growth in our insurance business.

After these working capital and quasi-working capital items have been deducted, we have a view of operating cash flow of the established business prior to CapEx. We then deduct capital expenditure of £7.2 million for the quarter. And as mentioned on the previous call, we expect CapEx for the full year to be lower than it was in FY23, as we come down from the increased level of investment spend we incurred in recent years.

Next down, we deduct both the working capital associated with the funding of the Australian run-off over the quarter and the cash outflow of our US business, which includes both net US EBITDA losses and working capital. The result is

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operating free cash flow of £11.4 million for the quarter and this is then reduced for debt interest and tax payments to give a measure of free cash flow before M&A and significant items, which was an inflow of £6.4 million for the quarter.

During the quarter, as you know, we completed the acquisition of After Inc., and so we have shown the incoming cash flows related to the new cash equity funding and RCF drawings and outgoing cash flows for the acquisition payments net of cash acquired.

With these M&A-related flows included, and including significant items of £1.4 million, we delivered a closing unrestricted cash flow of £12.2 million for the quarter and closing unrestricted cash of £67.8 million. As guided previously, over the full course of FY24, we expect our level of unrestricted cash to be broadly maintained versus its closing position in FY23.

Moving on to slide ten, our capitalisation slide. Net debt and the total leverage ratio at the end of the quarter were £727 million, and 5.4x respectively., with leverage here shown on a basis which includes the impact on EBITDA of conversion to the new insurance accounting standard, IFRS 17. This leverage ratio is stable despite the impact of the RCF drawings we made to fund our US acquisition. As mentioned in our annual results presentation, we expect there to be no deterioration in leverage, taking into account the acquisition on a pro-forma, full-year annualised basis. Excluding the impact of additional borrowings in the quarter to fund the acquisition, we would have reported a continued fall in the leverage ratio.

In any case, the group remains in a strong financial position with significant headroom, including that provided by our £107.5 million of undrawn RCF capacity.

And finally, on slide seven, to sum up, we return to our opening slide to recap the strong start we've made to this new financial year and the overall good health of the business and its plans. Matthew and I would now like to open the call to any questions.

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Q&A

Operator

Thank you very much. If you would like to ask a question, please press *11 on your telephone keypad and wait for your name to be announced. A reminder that if you would like to ask a question to please press *11 on your telephone keypad and wait for your name to be announced.

Matthew Crummack

Thanks, Operator. We also have the option, I think, for people to send through questions digitally as well, to submit questions online. And there are no questions at this time online.

Operator

There are also currently no questions standing by on the phones at this time.

Matthew Crummack

Okay. Thanks. We'll give it a minute, and then if there are no questions in a minute, we'll take it as a wrap from there. Thank you.

Operator

Perhaps another reminder that if you would like to ask a question, please press *11 on your telephone keypad and wait for your name to be announced. We still have no questions coming through at this time.

Matthew Crummack

Okay, great. Well, if there are no questions from anybody. Thank you, Operator, and thanks, everybody, for joining this morning. Have a good day.

Operator

Thank you very much. That does conclude our conference for today. Thank you all for your participation. You may now disconnect.

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