Annington Funding plc
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ANNUAL INVESTOR CONFERENCE CALL FOR THE YEAR ENDED 31 MARCH 2023

Good afternoon everyone and welcome to the annual investor update conference call for Annington Limited. The call today will be presented by myself, Ian Rylatt, Annington's CEO and Stephen Leung, Annington's CFO.

The commentary we are going to give is primarily based on Annington's Consolidated Financial Statements for the year ended 31 March 2023, which were posted on our website in July.

We are unfortunately not able to take any questions on this call and have not received any in advance. If there are any clarification questions we are happy to consider these by email.

A transcript of the call will be available on our website together with a link to a digital recording of the call which will be available for 7 days.

I trust you will all have been able to access the Annual Report from our website and will have familiarised yourselves with its contents. The report and this telephone call contain forward looking statements which reflect our current views with respect to future events and anticipated financial and operating performance. Whilst they are made in good faith, any forward-looking statements made in this telephone call are subject to the same caveats as those in the note on page 2 of our Annual Report.

Annual Update

Annington continued to demonstrate its operational stability and resilience over the past financial year benefitting from stable and growing rental income both from its primary asset, the Married Quarters Estate and from its Non-MQE rental portfolio. In addition, as the MoD has continued to release surplus units back to the Group, these continue to be successfully repurposed either for sale or for rent.

The December 2022 MQE Beacon Unit Rent Review delivered an uplift of 28.4%, compared to circa 11% for the December 2021 review, supported by strong underlying market rental growth driven by high tenant demand combined with a lack of available properties. This uplift increases passing rent by circa £14 million with a further £8 million increase due to the site review. We expect future Beacon Unit reviews to also benefit from the higher rental growth currently being experienced in the residential market. In addition we continue to see strong rental growth in our non-MQE rental portfolio.

Adjusted EBITDA for the financial year 2023 was £193.8 million, an increase of £10.0 million or 5.4% over financial year 2022, predominately driven by the increase in gross rental income from the Site review and Beacon Unit reviews.

The Fair Value of the investment properties at 31 March was £7.8bn, slightly down from £8.0bn in September 2022, with SAVPV at a 44% premium to fair value. Stephen will cover fair value movements in more detail later.

The Group returned to the debt markets in August 2022 and successfully refinanced €427 million 2024 Euro bonds and £144 million 2025 Sterling bonds, funded by a new £400 million 11-year bond and a £135 million tap issue of the 2047 bonds. Additionally, we have agreed an extension of our £400 million Term Loan and £100 million Revolving Credit Facility from 2025 to 2028.

And finally on ESG, Annington is committed to being a responsible corporate citizen and we have made significant strides in our sustainability journey by completing our first materiality assessment and setting of ambitious ESG targets.

Summarising the markets in which we operate:
The UK housing market continues to be characterised by long-term and persistent undersupply which has historically supported house prices. However, both the housing market and the wider UK economy are feeling the effects of higher inflation and rising interest rates. This has affected buyer sentiment, their ability to transact and therefore house prices have generally softened over the past year.

Conversely strong demand for homes in the private rental market is evident across the UK and is expected to persist as affordability factors make it harder for people to purchase a property. In March 2023, the RICS reported that all parts of the UK were expected to experience an increase in rents over the coming 12 months. These trends have been clearly seen in the Group's market rent reviews conducted during the year – both for the proportion of the MQE subject to Rent Review in the year and for properties in the Non-MQE Rentals Portfolio – and provides a positive backdrop for potential rent inflation in the coming year.

In relation to our portfolio:
The MoD is our major customer, and we continue to have a good day-to-day working relationship with them.

In the year to March 2023 the MOD released 298 units across 13 Sites. Subsequently we have received termination notices for 285 units of which 107 have now been released.

As at 31 March 2023, Annington owned 39,542 residential property units. Of these, the Married Quarters Estate, which are units leased to the MoD, comprised 37,100 units, while the non-MQE comprised 2,442 units, which mainly includes the Rental Portfolio and the Surplus Estate. The Surplus Estate being units that were previously part of the MQE that have been released to us but not yet sold or transferred to the Rentals Portfolio.

The Group generated gross property rental income from its investment property portfolio of £219.3 million for the year to 31 March 2023, £197.4 million of which comes from the MQE.

Annington operates at the more affordable end of the UK market and sold 398 Units during the year to 31 March 2023 generating £98.1 million. We are continuing to see demand in the sales market with steady reservations and completions whilst pricing has been resilient.

ESG
In the year to March 2023, the Group implemented all 26 recommendations resulting from the ESG audit undertaken by a specialist ESG and sustainability consultancy in the previous year. This included three significant projects – the Group's first carbon footprinting exercise, its first materiality assessment and publication of its inaugural ESG Performance Report.

The Group completed the carbon project six months ahead of schedule and having determined its operational and organisational boundaries, the Group included expanded Scope 3 categories and measured emissions from Products and Services for the first time. The Group's first materiality assessment captured the views and opinions of a total of 61 key internal and external stakeholders and the results will be used to help the Group further develop its ESG strategy. Publication of the Group's inaugural ESG Performance Report revealed the Group's alignment with UN Sustainable Development Goals and included the Group's ESG targets against which progress will be measured.

Enfranchisement
We previously provided an update on Enfranchisement in May 2023 following the judgment from the High Court. We are in the process of appealing the decision. In our view, the Court's decision risks setting a dangerous precedent for businesses and international investors in the UK and if upheld would mean that the Government can disregard long-term contracts if it believes it is in its interests to do so. We do not consider that the purpose of the legislation was to allow the MoD to renege on deals where it has seller's remorse and we consider this to be a matter of public importance.

The hearing of an appeal would be likely to take place around 12 months after the date on which permission is granted. The judgment would be expected around three months after the hearing. There is also the potential of a further appeal following this to the Supreme Court. In totality these appeals are likely to take several years. Additionally, if the notices are upheld, any decisions on the price payable for units subject to enfranchisement would also be capable of appeal.

Subsequent to the Court's decision, in May 2023, the Minister for Defence Procurement, James Cartlidge MP, confirmed that no formal decision has been taken by the Ministry of Defence on further enfranchisement of the estate, but said that the Department will consider further the potential implications for taxpayer value of the High Court's ruling. Notwithstanding the current legal process, the Group reiterates its commitment to maintaining a positive, constructive and mutually beneficial working relationship with the MoD.

I will now hand over to Stephen to discuss the results for the year.

Thank you Ian

Financial Performance
Rental income for the financial year was £219.3 million, a £13.8 million or 6.7% increase on the prior year. The majority of our rental income continues to be from the Married Quarters Estate, which generated £197.4 million in the year, a £12.6 million or 6.8% increase on the prior year. This increase reflects the contribution from the Site Review rent adjustment agreed in December 2021, now effective for two of the four tranches into which the portfolio is divided, combined with Beacon Unit Rent Reviews which include the impact of the recently agreed BURR 22 uplift in the final three months of the year. The combined effect of these gives a £16.7 million increase in rent partially offset by a £4.1 million decrease resulting from releases of Units during the year.

Rent from the Group's Non-MQE Portfolio increased from £20.7 million in 2022 to £21.9 million in 2023. This reflects the addition of surplus Units to the portfolio over the last two years and a 4.6% increase in like-for-like rental income, partially offset by disposals.

Profitability for the Financial Year
The Group uses Adjusted EBITDA to measure the normalised performance for the business. Adjusted EBITDA for the financial year was £193.8 million, compared to £183.8 million for the prior year. This increase is the result of a combination of factors but predominantly driven by the increase in gross rental income.

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Property operating expenses totalled this year at £8.6 million vs £6.8 million in 2022, with the high number of MoD properties released towards the end of the 2022 financial year giving rise to increased survey and investigation costs which have not been capitalised.

The increase in administration costs from £15.3 million in 2022 to £17.8 million this year was due in large part to employee costs and an additional interim valuation.

The Adjusted EBITDA margin was 88.3% just below that of last year's 89.5%. The high level of conversion of rental income into Adjusted EBITDA reflects the fact that we are not responsible for the operation of the MQE.

During the financial year, the Group incurred £10.6 million of exceptional costs in relation to the legal proceedings which arose as a result of the MoD's attempts to enfranchise eight properties within the MQE. This includes a £2.25 million accrual for an element of the MoD's costs.

Reviewing our Annual Sales
Annington sold 398 properties during the year compared to 487 in the prior year.
Most of these sales took place from our investment property portfolio, where 394 Units were sold for £95.5 million with an average value of £242,000. Of this, 208 disposals related to units released from the MQE portfolio and 186 from the Non-MQE Rentals portfolio, of which 149 units on three sites were sold in bulk transactions.

Profit on disposal of investment properties amounted to £6.1 million in the current year. The profit/loss on investment property disposals is the amount by which the net sales proceeds exceed the March 2022 valuation.

Balance Sheet
The Group's total assets amounted to £8.1 billion at 31st March 2023 down from £8.2 billion at 30th September 2022 and £8.8 billion at 31st March 2022.
CBRE continued as valuer of both the MQE and the Non-MQE Portfolios, following their appointment in 2021.

The carrying value of the Group's investment property portfolio has decreased from £8.0 billion at 30 September 2022 to £7.8 billion at 31 March 2023. This decrease principally reflects movement in wider market trends impacting yields and discount rates applied to property and other long-term investments. Offsetting this have been increases in the underlying rental income streams.

In relation to the 31st March 2023 MQE valuation, CBRE were required to take into account the High Court's judgement that the MoD may enfranchise units within the estate and Annington's plans to appeal. To reflect the risk associated with the liquidity and marketability of the MQE the £360m reduction included in the 30th September 2022 valuation was increased to circa £500 million in the 31st March 2023 valuation, representing 7% of the reported fair value.

The Group uses Special Assumption Vacant Possession Value or "SAVPV" as a measure of what the properties would be worth were they to be released. MQE SAVPV was calculated by CBRE using market values for a representative sample of units, which were extrapolated over the total portfolio at the valuation date. This resulted in an SAVPV for the MQE of £10.5 billion,

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compared to £10.6 billion in September 2022. This equates to an average SAVPV of £281,000 per Unit and represents a 44.1% premium on Fair Value.

Financing
We continue to operate an unsecured debt strategy and a policy of retaining a BBB rating. Net debt at the March 23 year end was £4.0 billion with an LTV of 51%. The £100m RCF remains undrawn.

As Ian mentioned the Group returned to the debt markets in August 2022 and successfully refinanced €427 million 2024 Euro bonds and £144 million 2025 Sterling bonds, funded by a new £400 million 11-year bond and a £135 million tap issue of the 2047 bonds. The new notes carry a coupon rate of 4.75%. We have additionally agreed an extension of our £400 million Term Loan and £100 million Revolving Credit Facility from 2025 to 2028. The terms are largely unchanged and carry a headline margin of 185bp.

At 31 March 2023, the weighted average cost of debt was 3.39%, compared to 3.00% at 31 March 2022, with a weighted average life of 12.3 years vs 11.5 years for 2022.

Cash and Dividends
The cash balance at 31 March 2023 was £186.7 million. The Group does not plan to make a distribution from this balance, with cash instead being held to repay the remaining circa £152m of 2024 bonds and to fund the working capital requirements of the Group.

I will now hand back to Ian to wrap up.

Thanks Stephen.

So in summary, Annington continues to operate in a market with attractive fundamentals with strong underlying market rental growth benefiting both our MQE and NON-MQE portfolios. As I referred to earlier, whilst UK house prices are expected to fall in the short term given the current cost of living crisis and rising mortgage rates, the continued shortage of housing supply and the Group's ability to flex rental and disposal strategies means that Annington is well positioned to adapt to changes in market conditions. The Group also operates at the more affordable end of the UK housing market which offers further protection in the current downturn.

As Stephen summarised, we are proactively managing our debt maturity profile. We were particularly pleased to have completed the August 22 refinancing and term loan extension and have committed to repaying the remaining 2024 bonds with cash held on balance sheet. We will continue to monitor the markets going forward.

As we have received no questions in advance this now ends the call.

Many thanks.