

Chairman and CEO's Review

Japara delivered EBITDA of \$49.6 million in FY2019 despite the challenging operating environment.



Dear Shareholders,

On behalf of the Directors, we are pleased to present the 2019 Annual Report for Japara Healthcare Limited.

Caring for our residents

Our vision at Japara is to enrich every life that we touch. We welcome the special opportunity we have to share in and nurture the lives of our almost four thousand valued residents under a model centered on providing excellent care and services with dignity and respect.

We now operate a portfolio of 50 homes throughout Australia, having opened our newest home in Robina on the Gold Coast in July 2019. Our high calibre and dedicated employees across all of our homes support our residents, the majority of whom have high acuity and include many living with dementia, and we are appreciative of their dedication and effort. Their ongoing commitment to excellence in care saw 10 of Japara's homes re-accredited by the Federal Government regulator during the year in addition to 57 unannounced assessment contact audits undertaken. We have maintained full accreditation across our entire portfolio and continue to have registered nurses on every shift at all of our homes.

Our industry

Australia has a growing elderly population, a result of people living longer and the significant increase in births in the post-war era. Such growth requires delivery of a large volume of new places to the residential aged care sector over the next 10 years. This is positive for the sector which continues to face a number of challenges. Changes to aged care funding implemented in 2017 have unfavourably impacted revenue growth. It is now harder to qualify for acute aged care funding under a revised scoring system. Additionally, our largest expense categories, including staff and utility costs, continue to increase faster than revenue. The majority of staff costs are set under state-based enterprise bargaining agreements (EBAs) that typically contain fixed annual increases which are higher than the aged care funding instrument (ACFI) increases set by the Federal Government.

The industry also continues to experience near-term softening occupancy rates as places from the large number of aged care licenses issued by the Federal Government in anticipation of the 'baby boomer generation's' needs are activated at levels in excess of current demand.

Royal Commission into Aged Care Quality and Safety

The Royal Commission into Aged Care Quality and Safety commenced in February 2019. The Royal Commission has held numerous hearings and community forums across Australia to hear evidence and receive feedback as part of a thorough and wide-ranging review of the aged care sector. Japara was called to give evidence at the Perth hearing in June 2019. This evidence was largely centred around a case study from 2015 focusing on the delivery of person-centred care at our Mitcham home in South Australia. The Royal Commission also inquired into Japara's compulsory reporting processes. We envisage that any findings relating to Japara will be considered in the Royal Commission's interim report which is due at the end of October 2019, noting that its final report is expected in April 2020.

Delivering on growth

We made excellent progress with our greenfield and brownfield developments and significant refurbishment program during FY2019. Three new greenfield developments were completed and opened in Glen Waverley (Vic), Rye (Vic) and Brighton-Le-Sands (NSW) adding 219 new places to the Company's portfolio. Additionally, two brownfield extensions at our Kingston Gardens (Vic) and Mirridong (Vic) homes were opened providing a further 84 new places and six homes underwent significant refurbishment during the year. In all, 33 of our homes, including our new Robina Rise home in Queensland, now qualify for the maximum accommodation supplement associated with their refurbishment or high amenity levels.

Japara recently received planning approval for greenfield developments in Belrose (NSW) and Lysterfield (Vic) which together will add a further 192 places to our portfolio once completed. During the year we also secured vacant land adjacent to homes in Victoria and South Australia for future development purposes.



Chairman and CEO's Review continued

During July 2019 we completed and opened our newest home in Robina (Qld). This six-level home comprises 106 places including an area dedicated to specialised dementia care and is Japara's 50th home. Thoughtfully designed to include smaller hubs which create a home-like environment, residents are able to enjoy the luxuries of an on-site café, beauty salon, bar and theatre as well as a rooftop garden and entertainment space.

We currently have seven brownfield and eight greenfield projects in progress which are scheduled to deliver over 1,100 net new places by the end of FY2022. The significant refurbishment program underway for our existing homes continues with a further six scheduled for renovation works during FY2020 for the benefit of our residents.

Progress on initiatives

We are pleased to report on the progress of new and on-going business initiatives during FY2019.

We continued the roll-out of our specialist dementia care model across a number of our new and re-developed homes. The small home concept has been adapted to reflect optimal design and living principles for residents living with dementia. This model of support promotes independence, personal choices and quality of life. Residents are encouraged to live actively and purposefully in a home environment, where resident choice is paramount reflecting our philosophy of residents being able to "live life as usual". "Living life as usual" is enabled by our dedicated and passionate support team who are committed to understanding each resident's life story, their personal choices, values and beliefs. Resident outcomes are overwhelmingly positive including reduced and better managed interventions and improved lifestyle and behaviours.

We further invested in new technology to support our care and business operations over the year. This included a new financial reporting system and a third-party whistle-blower service, "Your Call". We are also commencing pilots of a new IT-based clinical and medical management system for deployment across all homes once tested.

Dining with dignity continues to be a focus across all Japara homes. Our Head Chefs create appetising meals served fresh to the table in intimate dining spaces. Attention to table settings, customer service and overall ambience adds to the dining experience ensuring meal times are a highlight for our residents. We were delighted our Yarra West home was awarded Chef of the Year at the 2018 Oscar Hospitality Awards.

We continue to invest to support and improve our leadership and governance and were pleased to announce Professor Leanne Rowe AM was appointed to the Board on 1 July 2019. As a Clinical Professor and Medical Practitioner, Leanne has over 30 years of clinical experience across acute care, aged care, mental health and community health, and brings valuable insight to Japara during challenging times for the sector. We also made several senior executive appointments during the year to improve consumer engagement and the development of, and returns on, our property portfolio.

There has been a significant focus over the last year on preparing for the introduction of the new Aged Care Quality Standards which came into effect on 1 July 2019. Japara implemented an innovative, digital program in the form of a gamified application to help train our home staff in delivering care in line with the new Standards. The Board, Executive Leadership Team and support office staff also participated in this unique form of training which we intend to use more extensively in the future for other training and education purposes.

Financial performance

Japara delivered earnings before interest, tax, depreciation and amortisation (EBITDA) of \$49.6 million in FY2019 despite the challenging operating environment.

Total revenue of \$399.8 million was up 7.1% on last year while net profit after tax (NPAT)¹ was \$16.4 million, a decrease of \$6.9 million.

Revenue improvement was achieved through contributions from greenfield and brownfield developments completed during the year and throughout last year, by a full year contribution from the Riviera Health portfolio which was acquired in April 2018, and the Federal Government's temporary subsidy increase. Revenue growth was more than offset by the impact of wage rate increases from state-based EBA's, which exceeded increases received in Federal Government care funding, and increases in other items such as utility expenses and additional costs incurred relating to the Royal Commission. Average occupancy for FY2019 was 93.0% compared with 93.2% in the prior financial year.

NPAT¹ was lower for the year due to the overall decline in EBITDA, increased interest expense as we invest in our development pipeline to underpin future growth and increased depreciation attributable to new and re-developed homes.

Net operating cash flows of \$34.0 million plus net cash inflows from Refundable Accommodation Deposits (RADs) of \$44.7 million were delivered during FY2019.

Total dividends of 6.15 cents per share were determined for the year (7.75 cents per share last year), which includes a 3.35 cents per share final dividend which is franked to 50% and payable on 30 October 2019.

Our stated dividend policy is to pay full-year dividends of up to 100% of NPAT¹, franked to the maximum extent possible having regard to available franking credits. The dividend payout for the year is 100% compared with 88% last year, that reflected a non-cash gain on the acquisition of the Riviera Health portfolio of \$9.6 million.

The Board has suspended the Company's dividend reinvestment plan due to the recent low take-up rate and weaker share price.

1. Profit attributable to members of the Group.

Committed to future growth

Japara remains committed to delivering additional capacity to meet the expected future demand for residential aged care services. We are well positioned to do so with a sound, diversified growth strategy bolstered by a focus on high quality resident care and services. Our extensive developments program is supported by a strong balance sheet and cash flows. A new \$345 million syndicated loan facility with our relationship banks, the Commonwealth Bank of Australia, National Australia Bank and ANZ Banking Group, was secured during FY2019, extending the facility availability date to September 2023. The new facility has similar terms to the previous facility and provides financial certainty that aligns to Japara's business strategy including funding for the developments program as well as for general purpose requirements.

Net bank debt was \$179.0 million at 30 June 2019, of which \$44.5 million is considered core net debt and \$134.5 million is development debt. We have available liquidity of circa \$166.0 million with development debt expected to be repaid over time from RAD inflows received from new residents entering our new or re-developed homes once completed.

Outlook

Looking ahead, Japara expects FY2020 EBITDA to be 5% to 10% lower than FY2019, mainly as a result of the removal of the Government's temporary subsidy increase that applied from 20 March 2019 to 30 June 2019 and as the funding environment continues to present challenges and occupancy remains below historic levels. This outlook is subject to no further material changes in market or regulatory conditions. Recently completed developments are expected to help mitigate industry headwinds as they contribute a full year of earnings and annual ACFI indexation, whilst modest, is expected to partially offset wage rate increases.

Japara continues to focus on the delivery of its development program with over 300 net new places expected to be opened in FY2020 following completion of existing greenfield and brownfield projects.

Thank you

We would like to acknowledge and thank our extraordinary team of over 5,600 nurses, carers and other home and support office staff who provide a vital service in supporting elderly Australians to continue to live meaningful lives with purpose, dignity and respect. Their dedication and commitment to our valued residents and contributions to their local communities is appreciated.

We would also like to thank the senior management team and the Board for their unwavering efforts and contributions during the year.

Finally, we would like to thank you, our shareholders, for your on-going support of our Company and its vision during these challenging times.



Linda Bardo Nicholls AO
Chairman
26 August 2019



Andrew Sudholz
CEO & Managing Director
26 August 2019

