Market Update

Hills restructure to deliver sustained profitability

Further to the market update in May 2019, Hills Limited (ASX: HIL) has defined a path to long-term growth in profitability and shareholder returns.

Key points

- Strategic Review recommends increased focus on growing Health business, which showed 50 per cent growth in EBITDA in FY2019 [1]
- Focus on returning the streamlined Distribution business to profitability
- Hills to exit underperforming Communications assets
- FY2019 results to include one-off provisions and costs of $7.7 million related to Distribution business restructuring and non-cash impairment of approximately $6.5 million of intangibles and non-current assets following review of asset carrying values
- FY2019 statutory loss of approximately $8.8 million after one-off provisions
- In line with market guidance, a small underlying profit after tax of approximately $0.5 million for FY2019 compared with an underlying profit after tax of $0.1 million in FY2018 [2]
- Board directors' fees reduced

Strategic and Operational Reviews

In February 2019, Hills announced an Operational Review of its Distribution business with a view to returning it to profitability. In May 2019, Hills also confirmed a Strategic Review to explore options to improve the performance and growth prospects of Hills' underlying businesses and ensure their value was properly reflected in the Hills share price.

As a result of the Strategic Review, the Hills Board has taken the decision to increase focus on its growing and profitable Health business, which provides patient care systems for hospitals and health care facilities. In addition, the Distribution business, which provides audio visual, security and IT systems and services for customers in Australia and New Zealand, will be streamlined.

Hills will exit its Antenna and STEP satellite services businesses and will not be renewing its contract to supply satellite dishes to Foxtel. These decisions reflect the declining profitability of the Communications business and the continued fall in Foxtel volumes.

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[1] Earnings before interest, tax, depreciation, amortisation and impairment of intangible assets, goodwill and other receivables (EBITDA) is a non-IFRS measure not subject to audit or review.
[2] Underlying profit after tax excludes one-off costs, provisions or impairments and is a non-IFRS measure not subject to audit or review.

As a result, manufacturing will cease at Hills O'Sullivan Beach facility in Adelaide by the end of the calendar year. All costs associated with this closure have been provided for in the FY2019 financial result.

Hills is pleased to confirm that it has received a conditional offer for the Antenna business that will ensure the continued manufacture of the Black Arrow range of antennas in Australia.

Hills will continue to review the operations of the Distribution business and strategic opportunities and will provide further updates at or before the Annual General Meeting in Adelaide on 8 November 2019.

Hills Chief Executive Officer and Managing Director David Lenz said: "The Strategic Review has delivered the roadmap to focus on the exciting potential of Hills Health business, with a streamlined Distribution business expected to return to profitability as early as the first half of FY2020."

Financial update

Hills advised in the Market Update of 21 May 2019 that it would incur one-off provisions as a result of the Operational Review of its Distribution business.

To deliver a profitable and sustainable Distribution business and to exit the Communications business, Hills has incurred pre-tax one-off provisions of $6.3 million in FY2019 related to inventory and property. The Company has also recorded one-off redundancy costs of $1.4 million in FY2019.

Following a review of the carrying value of assets and to ensure the Hills balance sheet appropriately reflects the new structure of the business going forward, Hills has also incurred an impairment of approximately $6.5 million (pre-tax) in FY2019 for intangibles and other non-current assets.

Hills will deliver an underlying profit after tax of approximately $0.5 million (preliminary, unaudited) for FY2019, however the statutory loss after tax for FY2019 is expected to be approximately $8.8 million (preliminary, unaudited).

Segment reporting

Following the Strategic Review and reflecting the growing scale of the Health business, Hills is pleased to announce it will now break down its results into operating segments.

The Hills Board believes segment reporting will provide investors and financial markets with greater clarity about the underlying performance and value of its business units.

Further details will be provided at the full year results but the preliminary unaudited EBITDA results for the Health and Distribution businesses for FY2019 versus FY2018 are provided below.

Division	FY2018	FY2019 (preliminary, unaudited)
Health	$7.4m	$11.1m
Distribution	$4.5m	$1.6m
Corporate	($2.6m)	($2.7m)

The preliminary unaudited segmented results demonstrate the strength of the Health business – including year-on-year EBITDA growth of 50 per cent – and provide the Hills Board with confidence the Company will deliver a strong net profit after tax that will position Hills to resume dividends in FY2020, subject to the capital requirements of the Company.

Director remuneration

To bring fees in line with similar sized companies, effective 1 July, non-executive directors' fees were reduced from $80,000 to $60,000 and the chair fee from $160,000 to $100,000. The Audit Committee chair fee was reduced from $16,000 to $10,000. The Board will continue to review its membership, skill requirements and size in light of the Strategic Review. At this time, Hills has no plans to increase the number of non-executive directors above four.

Outlook

Ms Hill-Ling said: "The results of our Strategic and Operational reviews will restore sustainable profitability and ensure the market correctly values the Company for the benefit of all shareholders. While we are disappointed by the write-downs to effect the required turnaround in performance and refocussing of the business, the results are starting to show, particularly in Health where profitable growth is very pleasing. We will provide a further update to shareholders on the Strategic Review as appropriate or at the Annual General Meeting."

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