**Company:** **Foxtons Limited**

**Conference Title:** **Foxtons Interim Results Half Year Ended 30 June 2018**

**Moderator:** **Jenny Matthews**

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**Conference Time:** **10:00 AM UK**

Operator: Good day ladies and gentlemen and welcome to the Foxtons Interim Results Half Year Ended 30th June 2018 conference call. There is a presentation pack to accompany the call, which you can find on www.foxtonsgroup.co.uk. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr Nic Budden, CEO of Foxtons. Please go ahead.

Nic Budden: Thank you very much and good morning everybody and thank you for joining us for our 2018 half year results presentation. Today, I am joined by Mark Berry, our CFO and Patrick Franco, our COO. And as usual, I will begin this session by providing an overview and market update before Mark outlines our financial results in detail. I'll then come back toward the end, but to give an update on the investments to be announced in February and to take you through the outlook for the remainder of the year. As usual, we will be available after the presentation for Q&A.

So, starting with an overview of our performance on slide four in the pack, as expected, it has been a challenging half with our group performance impacted by ongoing weakness in the London property sales market and this drove a 9% reduction in group revenue to £53 million. These lower revenues together with the cost of investment in people brand and technology that we announced at the beginning of the year were the main reasons for the fall in profitability. The lettings business continues to prove resilient with revenue falling by 1% to £31.7 million due to slightly lower rents on broadly flat volumes. The lettings programmes we launched earlier in the year are now starting to have an impact with Q2 revenue up several percentage points on prior year and a strong start to Q3.

Sales commissions fell by 23% to 17.2 million in a very difficult market with transaction levels at record lows, but we delivered a solid performance at Alexander Hall, our mortgage broker where revenue fell just 3% due to a strong sales focus on our remortgage business. As I mentioned, we did make targeted investments in the first half, which are designed to enhance our differentiated business model, and I'll come back to tell you more about those later on. Our balance sheet remains strong and we ended the period with net cash of £11.8 million, and in line with our dividend policy, we're taking the decision not to pay an interim dividend.

From our operational point of view, our proposition continues to resonate with customers and drive listings with Foxtons retaining its number one position for both sales and lettings listings across London this year. Strategically, given the conditions of the sales market, we're focused on lettings with the improvements made to our My Foxtons portal and the additional investments made in our people meaning that we're well placed going into the busy summer season. In sales, we're confident in our offer and remain well-placed for any improvement in market conditions in the future. The investments we've made are designed to reinforce our proposition by adding capability to our workforce and technology and to more forcefully communicate our offer to potential customers with the most recognised estate agency brand in London. We have a strong platform from which we can communicate our key sales proposition of excellent service, which delivers results. And again, I'll come back to our marketing programmes later on.

Turning to slide five, let me give you a few perspectives on the market starting with lettings. As you know, the London letting market continues to be driven by a structural shift away from home ownership towards renting. 30% of households now live in private rented accommodation in London, nearly double the proportion of the UK overall, and the signs are that this is only going to increase in the medium term providing further potential opportunity for us to grow our lettings business. With this shift in tenure preferences comes more regulation for landlords to comply with and we believe our high-touch high quality service model underpinned by sector leading compliance and operational systems offers clients a strong overall value proposition in what has become a very competitive market. Pricing in the lettings market this year has been broadly flat with a small decline in Q1 rents coupled with flat rents in the second quarter. Overall, we see rents being about 5% down since the Brexit vote and we attribute that primarily to softer demand from overseas corporate tenants. Last year, we made an excellent start to our institutional PRS proposition. We believe we're very much the leading agent in this area providing institutional investors with expert advice, high quality data, and an effective channel to market. We're currently working with many of the key players in this space and they're jointly planning to deploy very large amounts of capital in new build rental schemes over the next five years and we see this as an attractive and incremental growth opportunity for us.

Moving on to sales. So far, this year, we've seen a continuation of the downward trend in sales transactions levels which began back in 2015 and as a result H1 property sales transactions in London were very subdued with Q1 completions around 20% below prior year. We won't see the latest Land Registry date for the first half of the year until later in the year, but given the Q1 trajectory, we wouldn't be surprised if 2018 ended up being a record low for transaction levels in London. As you know, the dynamics around these lower transaction levels are driven primarily by a mixture of affordability, stamp duty changes, and political uncertainty, and whilst there's been some downward pressure on prices during the first half, it has not been enough to significantly alter affordability levels in London, which are by far and away the tightest anywhere in the country.

Since the start of the year, we have seen a marked improvement in our under-offer pipeline which is good. And whilst our weekly sales revenues have responded, deals remain relatively fragile requiring significant sales effort to progress them through to completion. And what this means really is that it's currently quite difficult to accurately predict sales commissions for the second half of the year. Notwithstanding these challenges in sales, our listings remain at consistent levels giving us confidence that our offer remains attractive for clients. That's all I wanted to say by way of an update. I'll now hand over to Mark who'll give you an update on key areas of our financial report.

Mark Berry: Thank you, Nic, and good morning everyone and thanks for joining us today. I'm Mark Berry, Foxtons CFO, and I'll now briefly take you through the financial review. So, to begin with, I'd like to take you through the composition of the business.

And slide eight shows the balance we have from a revenue perspective. If we take a look at the sales business first, sales revenues were 17.2 million in the half, which was down 23% from 22.2 million in 2017 and comprised 32% of overall group revenue. Sales contribution margin, which represents sales revenue less direct costs prior to the allocation of shared central costs declined from 61% to 51% in the period due mainly to the lower sales revenue. We also made some modest headcount investments as we refocused on... as we focused rather on rebuilding our sales pipeline.

Overall, our transaction volumes in the period were down 23% year on year at 1,188 comprising 560 in the first quarter and 628 in the second. Average revenue per unit was broadly flat at £14,500 with a slightly higher proportion of higher value transactions being offset by lower overall prices, and the average price of the Foxtons sale was £582,000 pounds in the period.

Moving across to lettings, the lettings side of the business now comprises 60% of group revenue and continues to provide a valuable and recurring revenue stream. Lettings revenue in the half was 31.7 million, which was marginally below the 32.1 million achieved in 2017 and reflected a small decline of 1% in average revenue per lettings unit on broadly flat deal volumes. Lettings revenue for Q2 was 5% higher than prior year against a Q1 that was 8% lower than prior year with the difference being partly due to the timing of Easter.

In terms of our mix in lettings, we again grew the proportion of actively managed properties increasing that proportion from 32% to 34%. And, finally, within lettings, our contribution margin was resilient at 72% versus 73% in half one last year with the small decrease mainly due to revenue alongside a modest increase in headcount investments. Our mortgage broking business Alexander Hall performed well in the context of sales markets with revenue 0.1 million below the same period last year at 4.1 million. This reflected a focus on our remortgage business, which provides a level of protection versus the secondary sales market. Alexander Hall comprises around 8% of group revenue.

On slide nine, we move on to the income statement. Group revenue was 53 million in the period, 9% lower than in 2017, and after deducting operating costs of 52.9 million, we delivered 0.1 million EBITDA compared to 7.1 million in 2017. 5 million of the 5.5 million declining revenue was from the sales business and driven by reduced volumes across the London market. Operating costs, which exclude depreciation, amortisation and share based payment charges increased by 1.5 million in the period to 52.9 million, and the net increase was a result of new targeted investments that we first talked about in February. These comprised an overall additional spend of circa £2 million on marketing and branding initiatives, customer service, staff retention, and recruitment. In addition, a further one million of general cost inflation was partially offset by 0.5 million lower commission arising on lower sales revenue as well as a further circa one million of underlying cost savings in the period, which were in addition to the 6 million of cost savings we achieved in FY17.

Overall, therefore the loss before tax in the period was 2.5 million after charging depreciation, amortisation, and share based payment costs. Small tax charge arose in the year due to timing differences and the add back of share based payments, and lastly the basic loss per share was 1.1 pence compared to earnings per share of 1.2 pence in the prior year.

On slide 10, we take a look at the cash flow statement, and on the left-hand side of this slide, we show our EBITDA to free cash flow conversion. EBITDA of 0.1 million in the period of course led to a cash outflow in the first half. From EBITDA, we deduct 2.5 million for the working capital outflow in the half, which reflects a normal reflection of trading levels at the end of June compared to the end of December. We'd ended up 0.7 million for the cash costs of the adjusted item we recorded in FY17. Added to that, capex for the half was 1.5 million, one million of which comprised our investment in Properly, which Nic will come on to as well as ongoing spend in respective IT development.

Finally, tax paid in the period was 1.4 million leaving us with a free cash outflow of £6 million. On the right-hand side, we show the bridge between cash at the beginning and the end of the period. And with the 2017 dividend of 0.7 million being paid in May, this gave rise to a total net outflow in the half of 6.8 million, and cash therefore decreased to 11.8 million at the end of June. In terms of guidance for the full year, capex and investments guidance is circa 2 million and guidance for depreciation, amortisation, and share based payments is circa 6 million.

On slide 11, we set out our cash flow priorities and dividend policy. Our priorities for free cash flow are threefold. These are to fund investments in the future development of the business, to maintain a strong balance sheet, and to return any excess cash to shareholders. The board remains committed to returning excess capital to shareholders when appropriate and maintains a policy of returning 35-40% of profit after tax to shareholders in the form of an ordinary dividend. And as Nic mentioned, there will be no interim dividend in the period.

So, to finish off, I'd like to recap the main themes of the financial review. We have a balanced business, which has been built to withstand the sale cycle with both lettings and mortgage broking producing a resilient performance in the period. And in a difficult sales market, we're focused on cost control and efficiency as market conditions remain subdued. However, we have continued to selectively invest in tools which we believe will maximise the productivity of our people as we said we would back in February. Lastly, we carry no debts; and despite the trading backdrop, the cash characteristics of the business are clear with period end cash standing at 11.8 million. And although there is no interim dividend, the board remains committed to returning excess cash to shareholders when appropriate. And with that, I'll now hand you back to Nic for the operational update and outlook.

Nic Budden: Thanks very much, Mark. We are now on slide 14 and what we do here is set out our key priorities in terms of our investment for future growth. You will remember at the prelims we set out our plans to redirect investment away from branch expansion capital expenditure, now that our network covers the vast majority of London geographies, and into expenditure to enhance our service led results-based proposition. Our aim here is to ensure that we maintain the best people in tech; and we've made some good progress with that transition. Today there's a growing range of options for landlords, tenants, buyers, and sellers, but what's not changed is the fact that clients still value service quality, a local professional, and perhaps more than ever they want results. And this is why it's important to us to keep delivering high levels of customer satisfaction and clear price premiums for our sellers and landlords. Our track record in these areas provides a strong foundation for positive messaging and we're just about to launch a number of new marketing communications campaigns that will more forcefully articulate our proposition into the marketplace.

In Q1, we introduced enhanced account management for our largest landlords with the objective of winning a greater share of their portfolios and upselling premium managed services to them. And whilst these are early days, we are encouraged by the feedback and initial results, which show an 11% increase in the properties under management from this segment between Q1 and Q2. Foxtons Prime was launched at the same time providing a bespoke service for customers selling high-value properties. And we've already had some early successes here too taking on approximately £500 million worth of new £3 million plus property lessons. The sales cycle for these properties does tend to be quite lengthy, but we've already completed the most expensive property sale in London this year of 25 million and we have several other high-value properties currently under offer.

As I mentioned earlier, having completed our branch expansion programme, we're investing more heavily in our people to ensure we recruit and retain the most experienced agents. We know our people drive our business forward at the sharp end and they're a key part of our difference. We're pleased with the changes we've made in this area. And as we go into the busy summer season, we're well resourced with well incentivised people. Our ongoing investment in tech continues to enhance the customer experience with Foxtons, and our My Foxtons portal, which was launched just over a year ago is now in its third generation. The latest development that we implemented in May this year was to integrate our property management processes so that landlords and tenants can track and report tenancy issues online in real time using pictures, videos, and messaging. This latest improvement has had the impact of increase in portal usage by 22% meaning that today the majority of landlords and tenants complete many administrative and property management tasks online. And this has allowed us to free up our people to focus on more important sales and complex service interactions. Maintaining leadership in technology is vital for us as it will play an increasingly important role enabling us to deliver exceptional service to our customers and grow new revenue streams. As part of this aspiration, we regularly consider investments and partnerships with companies that could potentially enhance our offering, and in the first quarter we made an investment in a new company called Properly, which has developed pioneering capability for the lettings market. This investment gives us access to nascent technology with exciting potential to establish B2B proposition for online agency.

Turning to slide deck 15, let me finish by summarising where we are now and how we see the future panning out. Today, we remain London's leading agent with a strong position across London, the combination of our premium brand. People, tech, and coverage gives us a compelling offer, and we have a successful track record of delivery for our customers, and we believe this sets us out against the competition. Service that delivers results is what we want our brand to be associated with and we will continue to ensure that we deliver on this. There is no getting away from the fact though that our current business performance overall is largely a function of the sales market we find ourselves in, and our solid lettings performance was offset somewhat by ongoing weakness in the London sales market, but our balance sheet remains strong as Mark outlined and our net cash position is a good place to be at this stage in the cycle.

From an outlook perspective, it's a mixed picture. We've seen improvements in our sales pipeline and weekly sales revenues, but the market is skittish. So, it's hard to predict accurately where we'll be at the end of the year and how much of our enlarged pipeline will flow through to completions. Lettings improved throughout the period, and the people investments we've made give us confidence that we go into the peak season better resourced than we were last year. We're keeping a very careful watch on our costs and we do have the flexibility to take further action if necessary.

Looking further out, London's long-term fundamentals remain attractive and our market position and offering give us confidence that we're well placed to take advantage of any positive changing conditions over time. And with that I'll take questions that anyone has on the phone and we'll conclude the formal part of the presentation.

Operator: Thank you, sir. Ladies and gentlemen, if you'd like to ask a question at this time, please press the star or asterisk key followed by the digit one on your telephone keypad. Please do ensure that your mute function on your telephone is switched off to allow your signal to reach our equipment. If you find your question has already been answered, you may remove yourself from the queue by pressing star two. So, once again, please press star one to ask a question. We'll pause now for just a moment to allow everyone an opportunity to place a question. Our first question comes from Jon Bell from Barclays. Please go ahead. Your line is open.

Jon Bell: Yeah, morning all. I think I've got three, if you don't mind. The first one is what would you estimate has happened to your market share in the sales market over the period, just in rough and ready terms would be fine.

Secondly, any thoughts around commission rates just in light of I guess ongoing downward pressure elsewhere in the market.

And thirdly is it possible to split the mortgage broking volumes, and you did just over 2,000, but could you split those between new and remortgages please? Thank you.

Nic Budden: Jon okay, this is Nic Budden here. In terms of share, the market in London generally was about 20-odd% down, we're 23% down in volumes. There's always a bit of a mix issue there. We're focused largely in terms of volumes on the more central parts of London. So, from a listings perspective, we're relatively comfortable in terms of our share, always looking for more obviously. And in lettings, much more difficult to tell, but we think we've had a pretty strong sort of Q2 and looking to get a strong Q3 on lettings share. Fees, we don't have any proposals at the moment to change sales commissions generally. Part of the Foxtons Prime initiative that I mentioned to you was to take a more flexible approach on fees for the very high value properties that we're selling and to take a more flexible approach in terms of sharing those fees both with the London sort of portal [inaudible] and with buyer's agents; but no plans currently to change our sales fees going forward on our base business. And then mortgage, Mark, I'm not sure you have those.

Mark Berry: We don't, we don't disclose that level of detail, Jon, on splitting between remortgage and secondary sales.

Jon Bell: Okay, understood. Thank you.

Mark Berry: Thank you, Jon. Thank you.

Operator: Ladies and gentlemen, just as a further reminder, please press star one to place an audio question. We'll now take the next question from Chris Millington from Numis Investment Bank. Please go ahead. The line is now open.

Chris Millington: Morning all.

Nic Budden: Morning.

Chris Millington: Morning, yeah, just a few if I could. Quite encouraging to see the sales pipeline up, but noted what you're saying about kind of conversion of these. And I'm just wondering if you'd give us any more detail on kind of conversion rates of the pipeline and perhaps put it in a bit of historic context just so we can kind of understand exactly what you mean. So, that's the first one.

Second one is really just about the lettings market and that comment about a bit momentum there. I'm just wondering if you feel that's kind of more underlying market or more your own initiatives driving that.

And then sorry I've just got two more, but these are quite straightforward is should we think about a continuation of the same operating costs in H2 and also just the working cap[?] profile in H2, should we see a reverse with that trend? I think you alluded to something like that, Mark, in the commentary before.

Nic Budden: Yes, why don't I take, Chris, the lettings one first and then I'll pass the other two to Mark. I'm actually pretty pleased with lettings. It's very early days, but I feel that we're better resourced. I think we cut headcount as you know over the last couple of years and we've sort of added back a little to lettings because we see the opportunity to do so there tactically in some areas of the business. And so, I'm actually quite encouraged by that. I don't think it's really anything to do with a massive increase in momentum in the marketplace. We're seeing if you look at the listings across London that they're actually quite tight. So, I think we're doing relatively speaking pretty well in lettings, and we're not being helped really or we haven't so far anyway by any sort of value increase in rents. So, no, I'm genuinely quite pleased about that. Obviously don't want to sort of be too optimistic; it remains to be seen what happens on a month to month basis. We're... Q3 and Q4 were pretty strong for lettings last year, so from a comparables perspective we go into reasonably tight comparables for the rest of the year. But we're more pleased than I've been for a little while on lettings, I think it's probably true to say.

Mark Berry: Chris, thanks for the other questions. I think the comments I'd make on the pipeline conversion are the pipeline is not an exact science which is what we said when we were together in February. But I think it is – and therefore we don't quote specific numbers, but I think it is fair to say that two to three years ago, you would have had a much clearer idea as to the percentage of the pipeline that would be likely to convert, and a very clear idea over which timescale that would happen. What we've got at the moment in the market is two things going on. One is that the length of a transaction being under offer or going under offer to then when it subsequently exchanges has definitely lengthened over the last two years. And then within that as well there are a number of factors that contribute to why firstly that chain has increased in length, but then also why there are more factors at play which may contribute to that chain falling over. And some of those are directly related to buyers and sellers, others are from third parties such as surveyors or lawyers or mortgage provisions. So, I think there are a lot of factors at play, but the general message that we would say is clear is that the visibility of transactions proceeding from under offer to exchange is not what it used to be. So, I hope that's helpful.

On the other two points, yeah, in the second half, I would say we have 53 million of operating costs in the first half. I'd expect that to be broadly in line with that in the second half, all other things being equal if we have an extension of existing run rates. So, if our sales business continues on its current trajectory and we experience a normal Q3 in lettings, I'd expect the profile of operating costs to be equal. And that would mean circa 106 million versus the 103 that we had last year, therefore circa three up, which I think is a number I spoke two or three in February.

And then a working capital, yes, from a cash perspective that's a really important point in the business because however we perform in the second half, December is a seasonal low for both sales and lettings, and therefore the December revenue number is our annual low point. And there is a natural working capital outflow from December to June and then an inflow as it all unwinds from June to December. And if you look at last year's working capital profile of the business, by the time we got back to December, I think revenue was roughly in line with the previous year, and the working capital outflow we experienced in the first half was mirrored as an inflow in the second half. So, yes, you should certainly view the 2.5 million would come back in.

Chris Millington: Got you. All right. Thanks so much.

Nic Budden: Thanks Chris.

Operator: Ladies and gentlemen, just as a further reminder should you wish to ask a question at this time please signal by pressing star one on your telephone keypad. We'll just give a further pause now just to allow everyone an opportunity to place questions. That's star one to place a question. [Inaudible] we currently have no further questions. So, I'll turn the conference back to you for any additional remarks. Thank you.

Nic Budden: Thanks, everybody for calling in. And if there are any further questions, feel free to get in touch with us. Thank you and goodbye.

Operator: Thank you. Ladies and gentlemen, that now concludes today's conference call. Thank you for your participation. You may now disconnect.