



21 February 2024

## Chair and CEO Commentary

*Steady progress despite some headwinds*

### HIGHLIGHTS

- > Progressing turnaround strategy
- > Net Profit After Tax of \$0.05m versus loss of \$0.19m for same prior year period
- > Operating costs down \$0.85m (7.7%) on same prior year period
- > Wireless channel strategy delivering results
- > Wired customer engagement and order automation improvements
- > Key contracts renewed: St John, Powerco and FENZ
- > \$3.7m of new contracts signed in 1H
- > FY24 guidance adjusted: revenue and earnings slightly lowered, free cash flow towards upper end of plan

### FINANCIAL PERFORMANCE

Vital Limited (“VTL” or “Company”) reported a modest net profit after tax of \$0.05 million for the first half of FY23 versus a loss of \$0.19 million in the prior financial year period. The result includes an after-tax lease adjustment accounting loss of \$0.10 million (prior period included a loss of \$0.38 million), so the adjusted result for the interim period was a net profit of \$0.15 million.

While the underlying result (net of the lease accounting loss) is a small profit of \$0.15 million, this is not where VTL wants to be given the size and value of the network infrastructure the Company owns and operates. VTL’s turnaround strategies are geared toward generating a fair and adequate rate of return on the Company’s network asset base, and a key to this will be further stabilising and growing revenue.

## REVENUE

Vital Revenue Breakdown (all figures \$'000)	1H FY2024	1H FY2023 Restated <sup>(1)</sup>	Percentage Change
Wired (Fibre)	4,617	4,782	-3.5%
Wireless (Mobile Radio)	8,524	8,803	-3.2%
Installation	194	236	-17.7%
Hardware & Other	120	327	-63.3%
<b>Total Services Revenue</b>	<b>13,455</b>	<b>14,148</b>	<b>-4.9%</b>

(1) 1H FY2023 restated to allocate certain amounts previously in "Hardware & Other" and "Installation" into the Wired and Wireless categories. There is no change to the total revenue amount.

VTL's revenue declined 4.9% to \$13.46 million with recurring revenue down slightly. The decline in the Wireless segment was mainly from the active decision to de-commission a non-commercially viable network. Recurring revenue continued to fall in the Wired (i.e., fibre) network where ongoing rationalisation of customer circuits is still occurring at a slightly faster rate than new circuit additions, however we are seeing momentum with increasing feasibility requests. The macroeconomic environment is seeing customers focussed on costs. VTL's channel strategy in Wireless is generating customer gains through dealer partners. The Company's channel and customer engagement efforts in Wired, including a customer portal to automate circuit ordering, are beginning to gain traction although there is further work required to fully complete order automation so any revenue effect is unlikely until FY2025.

VTL's first half profit was net of lease accounting adjustment losses (after tax) of \$0.05 million. Lease adjustments through the Income Statement are required when lease terms are changed; this is a non-cash accounting entry resulting from differences in balance sheet asset and liabilities created on the lease renewal or alteration. VTL has around 350 lease sites around New Zealand.

Summary Financial Performance (all figures \$'000)	1H FY2024	1H FY2023	Percentage Change
Total Revenue	13,455	14,148	-4.9%
Staff costs	4,046	4,058	-0.3%
Lease/rent costs <sup>1</sup>	3,133	3,346	-6.4%
Other Selling, General & Admin costs	3,075	3,700	-16.9%
<b>EBITDA (Adjusted) <sup>2</sup></b>	<b>3,201</b>	<b>3,044</b>	<b>5.2%</b>
EBITDA (Adjusted) margin (%)	23.8%	21.5%	
Depreciation <sup>3</sup>	2,267	2,183	3.8%
<b>EBIT (reported)</b>	<b>934</b>	<b>861</b>	<b>8.5%</b>
Net Interest <sup>4</sup>	728	599	21.5%
Income Tax	58	73	-20.9%
<b>Net Profit after Tax (Adjusted)</b>	<b>149</b>	<b>189</b>	<b>%</b>
Lease accounting gain/(loss) (after tax) <sup>5</sup>	-97	-379	-74.5%
<b>Net Profit after Tax (Reported)</b>	<b>52</b>	<b>-190</b>	<b>n.a.</b>

1. Lease/Rent costs including those otherwise included in Depreciation and Net Interest charges
2. Post lease costs that are otherwise treated as depreciation and Interest
3. Excludes IFRS 16 adjustments resulting from changes to lease profiles
4. Excludes interest component of capitalised lease costs (this is in Lease/Rent costs)
5. Adjustments (non-cash) under IFRS 16 for changes to lease terms (net of tax at 28%)

The following table highlights the adjustments between pre- and post-NZ IFRS 16 results.

<b>NZ IFRS 16 Pre/Post Reconciliation (all figures \$000)</b>	<b>Pre IFRS 16 Adjustment</b>	<b>NZ IFRS 16 Adjustment</b>	<b>NZ IFRS 16 Reported</b>
Total Revenue	13,455	–	13,455
<b>EBITDA (Adjusted)</b>	<b>3,201</b>	<b>2,527</b>	<b>5,727</b>
Depreciation and Amortisation	-2,267	-1,934	-4,201
Finance Income	9	–	9
Finance Expense	-737	-737	-1,474
<b>Net Profit before Tax (Adjusted)</b>	<b>207</b>	<b>-145</b>	<b>61</b>
Income Tax expense	-58	448	-10
<b>Net Profit after Tax (Adjusted)</b>	<b>149</b>	<b>-97</b>	<b>52</b>

### **Balance sheet, liquidity and debt**


VTL's bank debt facility, which consists of secured funding facilities with Bank of New Zealand with a combined limit of \$16.3 million, has a maturity date of January 2025. The impact of higher interest expense is being felt with net interest cost rising 21.5%. Debt reduction is a key priority for VTL.

<b>Selected Balance Sheet and Cashflow Figures (all figures \$000)</b>	<b>H1 FY2024</b>	<b>H1 FY2023</b>	<b>Change</b>
Bank debt	13,300	14,000	-700
Cash	79	752	-673
Right of Use Assets <sup>1</sup>	18,236	22,093	-3,857
Right of Use Liabilities	19,848	23,413	-3,565
Wired assets <sup>1,2</sup>	31,081	33,972	-2,891
Wireless assets <sup>1,2</sup>	32,834	36,793	-3,959
Operating Activities cashflow (Adjusted) <sup>3</sup>	3,201	3,044	157
Capital expenditure	1,203	1,699	-496
<b>Op cashflow (Adjusted) less Capex</b>	<b>1,998</b>	<b>1,345</b>	<b>653</b>

1. Note that Network assets (Wired and Wireless) include Right of use assets (mostly in Wireless)

2. Note that the prior period interim report reflected Wired and Wireless assets that excluded Right of Use assets. H1 FY2023 has been restated to show a like for like comparison.

3. Cashflow from Operating Activities in Financial Statements less Principal payment of Lease Liabilities



Capital expenditure for the 1H FY24 was \$1.20 million (58% being customer funded) versus \$1.70 million in the prior period. As flagged last year, non-customer requested capex continues to decline.

## OPERATIONAL PROGRESS

The operational improvement plan that commenced in 2022 continued to deliver cost savings and efficiencies in the first half of the FY2024 financial year. These results are largely in line with those metrics, although revenue was slightly weaker than expected, offset by slightly better cost savings. VTL's strategy is gaining traction, however there are revenue headwinds in challenging macroeconomic conditions, along with some industry restructuring and costs saving initiatives by some cellular market participants which is affecting fibre circuit cancellations for the Company.

### *Revenue stabilising, costs down*

Revenues declined against the prior corresponding six-month period although the rate of decline has slowed, even after accounting for one-off project revenues in prior periods.

Operating costs reduced, down around \$0.85 million or 7.7% on the corresponding prior period. Staff costs were largely flat which was a solid result given ongoing general and sector wage pressures. With little network build out now required – aside from one-off, customer-initiated projects – current capital expenditure is forecast to hold steady around current low levels and will mainly be for network assurance activities.


Leases represent VTL's second largest cost item. Work continues to optimise site locations, site costs and network efficiency. This has delivered significant savings (lease and maintenance costs) and productivity gains. Prior capital expenditure has resulted in the Company having extensive and modern networks with ample capacity and resilient solutions – a key factor when engaging with existing and prospective customers, and important as digital infrastructure becomes more critical.

### *Ongoing emphasis focus on customer and culture*

The refocused and restructured sales activity is improving relationships and the sales pipeline has now significantly improved as has the level of customer and channel partner contact and engagement. While this is reflected in improved NPS, this has yet to translate into meaningful revenue growth although there were several new business wins that will commence contributing revenue late in FY24. Offsetting that, the macroeconomic environment is clearly challenging, with customers looking for cost savings which is a contributing factor to fibre circuit relinquishments.

The 2023 focus on improving organisational culture has continued with engagement metrics gaining and eNPS (Employee Net Promoter Score) closing the half at 35.

VTL moved back into its “old” Cambridge Terrace premises late in 2023. These had been vacated while undergoing strengthening remediation work. The move was undertaken



seamlessly, has been welcomed by staff and is likely to assist culture and engagement metrics.

### *Cyber incident*

In November 2023, VTL confirmed a cyber incident involving unauthorised entry to its internal corporate servers. After verifying the nature and credibility of the activity, the breach was immediately contained, and the appropriate Government and privacy authorities contacted. External security consultants assisted with establishing what had occurred, the scale of the breach then commencing the process to restore internal services once these were cleared of risk.

As far as VTL is aware, only its corporate servers were accessed, with no evidence that systems operating the customer fibre and radio network services were affected. These systems continue to operate as normal. The corporate server networks have largely been returned to normal operating condition.

Remediation costs have been incurred for consultants and changes to software licenses, although these are unlikely to exceed \$0.2 million. Additional measures have been put in place to help defend against future incident of this nature.

## OPERATIONAL PERFORMANCE

### *Wired*

VTL provides customers with access to wire (fibre optic) networks in Auckland and Wellington where there is fibre presence in both CBDs, although there is greater fibre concentration in Wellington.

<b>Wired segment (all figures \$000)</b>	<b>1H FY2024</b>	<b>1H FY2023</b>	<b>Percentage Change</b>
Revenue	4,723	4,942	-4.4%
Lease/rent costs <sup>1</sup>	941	1,097	-14.2%
Other operating costs	1,669	1,721	-3.0%
<b>EBITDA (Adjusted) <sup>2</sup></b>	<b>2,113</b>	<b>2,124</b>	<b>-0.5%</b>
EBITDA Margin (Adjusted) <sup>2</sup>	44.7%	43.0%	
Capital expenditure	338	350	-3.6%
Total assets	31,081	33,972	-8.5%

1. Lease/Rent costs including those otherwise included in Depreciation and Net Interest charges

2. Post lease (rent) costs that are otherwise treated as depreciation and interest.

The benefits of VTL's network optimisation efforts are producing a reduction in operating costs and are driving EBITDA (Adjusted) growth.

Significant efforts have seen the implementation of a refreshed sales channel strategy utilising VTL's market positioning as an unregulated provider of fibre capacity. The refreshed approach has seen much higher levels of engagement with key customers and prospects. VTL's new fibre portal provides self-serve capability that allows customers to search for VTL's fibre circuit availability. The remaining functional step to be added to the portal is APIs that will automate fibre circuit lookup, ordering and provisioning requests and this should complete development and roll out during H2 FY24. VTL has already had one customer commit to switch around 30 new circuits over to the Company's network by around mid-2024. This is complimented with an increase in feasibility requests.

### Wireless

VTL provides the only New Zealand-wide commercial nationwide mobile radio infrastructure. The network is supported by a 24/7 Network Operations Centre (NOC) located in New Zealand.

Mobile radio provides wider geographic coverage than cellular and is more resilient and reliable than cellular in times of emergency or disaster (lower congestion risk than cellular as it is not used by the general public, plus it usually has better battery backup than cellular sites). Mobile radio is utilised by organisations that supply critical services (e.g. electricity network providers) that require "always available" reliability, or have remote work in areas outside cellular coverage as well as commercial operations.


The market/replacement value of VTL's mobile radio assets is likely higher than current book value, subject to the Company being able to generate an adequate rate of return on the assets.

Wireless segment (all figures \$000)	H1 FY2024	H1 FY2023	Percentage Change
Revenue	8,732	9,206	-5.1%
Lease/rent costs <sup>1</sup>	2,192	2,248	-2.5%
Other operating costs	4,472	5,110	-12.5%
<b>EBITDA (Adjusted) <sup>2</sup></b>	<b>2,068</b>	<b>1,847</b>	<b>11.9%</b>
EBITDA Margin (Adjusted) <sup>2</sup>	23.7%	20.1%	
Capital expenditure	866	1,349	-35.8%
Total assets	32,834	36,793	-10.8%

1. Lease/Rent costs including those otherwise included in Depreciation and Net Interest charges

2. Post lease (rent) costs that are otherwise treated as depreciation and interest.

VTL's important contract with Powerco was renewed during the half year, along with the St John contract being extended through 2027 (with additional rights of renewal out to 2029). VTL provides Powerco with a managed telecommunications network service that includes a Digital Mobile Radio (DMR) Tier 3 voice radio network and a WAN (Packet Transport network or PTN). The Powerco contract has been extended until 2026.



VTL signed new contracts in 1H24 with a combined Contract Value of \$3.2m with the revenue to be recognised between 1-5 years.

VTL's strategy is to move smaller customers to channel partners and maintain direct enterprise sales activity although this is also now occurring in conjunction with partners. Wholesale agreements in place with a number of regional mobile radio operators have seen progressive transfer of smaller customers for service and support. This has lowered VTL's "cost to serve" at minimal gross margin drop.

Additionally, channel partnering has generated revenue growth including new customer wins and as partners move some of their customers onto VTL's network.

## **GOVERNANCE**

Mr Mike Shirley retired as an independent director on 30 September 2023 to avoid any conflict of interest arising from his appointment to the Executive Team of Chorus Limited. Mike was a valued contributor to the Board over his short tenure, providing exceptional industry knowledge and skills.

The Company is presently undertaking a search process for a replacement Director.

## **TURNAROUND METRICS GUIDANCE AND LOOKING AHEAD**


The first half result confirms VTL's recovery is progressing. VTL is confident in its strategy. Operating costs and capital expenditure continue to be well controlled. Tangible revenue progress is underway in the Mobile Radio network. Significantly improved engagement with Fibre customers, including recent steps to automate customer Fibre circuit ordering are expected to progressively deliver benefits during 2024.

The Company has renewed or extended its contracts with major customers including St John and PowerCo, and won new customers in both the Wired and Wireless divisions.

VTL's key objective is to achieve an appropriate rate of return on its infrastructure asset base. This may involve taking advantage of any network optionality or partnering or channel opportunities to improve network utilisation.

VTL provided turnaround outlook guidance on several metrics as part of its turnaround plan announced at the FY2022 results.

The six months to 31 December 2023 have seen a steady progression of the VTL turnaround strategy. The broader macroeconomic environment and high interest rates however has seen a widespread customer focus on rationalising network costs. VTL is working hard to mitigate the impact of a slowdown in economic activity, additionally the significant increase in interest rates means that interest cost on VTL's debt is higher than expected when the Turnaround Metrics were first outlined.



As a result, VTL has amended and tightened its FY24 metrics as seen in the table below. A range of scenarios was modelled in arriving at these metrics and typical risk caveats apply, including no material adverse or unforeseen events or circumstances.

<b>Turnaround Metrics (all figures \$m)</b>	<b>H1 FY2024 (Actual)</b>	<b>FY2024 (updated)</b>	<b>FY2024 (Previous)</b>
Revenue	13.46	26.7 – 27.2	28.0 – 29.0
Adjusted EBITDA <sup>1</sup>	3.20	6.4 – 6.7	6.6 – 7.1
Net Profit after Tax (adjusted) <sup>2</sup>	0.15	0.4 – 0.7	0.7 – 1.1
Adjusted free cash flow <sup>3</sup>	2.06	3.8 – 4.4	3.0 – 4.0

1. Post lease costs that are otherwise treated as depreciation and interest

2. Excludes IFRS 16 accounting adjustments resulting from changes to lease profiles

3. Adjusted EBITDA (as above) less capital expenditure)

To date VTL is broadly tracking to its turnaround plan. While the FY24 revenue outlook has softened, operating costs are tracking ahead of original guidance and Capex is in line with forecast expectations, so free cash flow is currently tracking towards the upper end of plan.

VTL is confident of recurring revenue growth moving into FY25.

The turnaround strategy represents a planned path to return to positive free cash flow, enabling debt reduction. The Board is aware of the significant discount VTL shares are trading at relative to the book value of its net tangible assets and remains committed to ensuring value is delivered to shareholders.

## RESULTS BRIEFING

All shareholders are invited to attend a virtual briefing on Tuesday 27th February at 11.30am with Jason. To register to attend, please follow the link [www.virtualmeeting.co.nz/vtlhy24](http://www.virtualmeeting.co.nz/vtlhy24)

This NZX release, the half-year results and related materials were authorised for lodgement with NZX by the Board of Vital Limited.

## ENDS

### For investor enquiries contact:

Jason Bull

[jbull@vital.co.nz](mailto:jbull@vital.co.nz)

027 497 4548

### For media enquiries contact:

Rich Llewellyn

[richard@shanahan.nz](mailto:richard@shanahan.nz)

027 523 2362