

The Colonial Motor Company Limited

CHAIRMAN'S ADDRESS TO THE 102nd ANNUAL MEETING

Ladies and Gentlemen,

Results

It has been a challenging year. Revenue for the first eight months was down on the previous year, but it was part of a longer term trend, there were no surprises. There were numerous dark clouds on the horizon, all with the potential to impact on the trading conditions, but they had not materialised and had been there for some time. Meantime, it was business as usual.

In March, business as usual ended. Covid quickly moved from someone else's problem to a real threat. The impact was sudden, starting before lockdown, in mid-March, as consumer confidence fell. March Group revenue was down 37% on the previous year, an indication of what to expect when lockdown was announced at the end of the month.

Lockdown had a dramatic impact, especially on the car dealerships. Suddenly all of the dealerships were to go into hibernation at the same time. There would be very little income for the duration of the lockdown, and probably very weak consumer demand after that. The Company had money in the bank and unused credit lines, but how long would it last. The immediate focus was cash control. That was the context of the decision to cancel the previously announced dividend.

At dealership level, cash control is a combination of operating expenses and managing inventory. Both were managed exceptionally well.

The dealerships management, all of them, faced unprecedented problems, pressures, and huge uncertainty. In addition, as individuals, they had to cope with the numerous personal pressures that arose. They managed exceptionally well. I want to acknowledge and thank them for that effort. Past experiences, such as the Christchurch earthquakes in 2010 and 2011, the GFC in 2009 and 2010, and the market upheavals in the 1990's all helped shape awareness of what needed to be done.

Cash was retained, employees were retained, customers were retained.

Some numbers. Revenue for the second half of the year was down 24%, 17% for the full year, with the worst month, April, down 82% on the previous year. Despite the revenue drop, employment was retained, total employees at the end of June was 965, only 3% down on the same time 12 months earlier. Total remuneration paid for the full year, including the wage subsidy, was actually up, from \$75.9 m to \$76.1m. The wage subsidy received during lockdown contributed around 40% of the actual remuneration costs for the period.

The revenue bounce after lockdown ended started unevenly, but soon was stronger than expected. Revenue in March, April, and May were all materially down, but June revenue was only down 2% on the previous year. Revenue in the first quarter this year, covering July, August and September, is down by the same 2%. We have bounced back to a level of revenue that is similar to last year. But we have not recovered the revenue lost during lockdown or the periods immediately before and after. The significant revenue lost in March, April and May has not been recovered.

The market post-Covid is different to the immediate past. There are very few new rental cars, so total industry numbers, comparing this year with last year, give a confusing picture. Near new used vehicle sales are strong, the complete reversal to predictions back in April. It all adds up to good numbers, but it could all suddenly slow down if consumer confidence is hit again. But for now, to use a concept that is familiar to salesmen, buyers are buying, not just looking. Its day-by-day trading, but it adds up.

There are two key strengths that helped the Company through the last six months. One is the strong balance sheet and the other is the depth and experience of its management.

The Company has two major asset groups on its balance sheet, inventory and property. There is very little goodwill or long term right of use leases. Borrowing is short term, used to fund current inventory. Our balance sheet does not lock us into yesterday's trading patterns. Our assets are all marketable. We can expand or reduce as conditions dictate. A national lockdown was never on anyone's list of foreseeable risks, but hibernation for a period of time caused by a lockdown is possible when there is strong balance sheet.

The second strength is the experienced management. The Company has a very small Wellington office, only 6 employees. Most operational decisions are made at the individual dealership level, by experienced managers who understand their responsibilities and thrive on the autonomy. It's not easy balancing the often conflicting demands of customers, employees, and franchisors, all while staying profitable. But the challenges build experience, and employment stability leads to depth.

This management structure has evolved over time reflecting the specific circumstances that have shaped the Company for the last 100 years. The shareholding has been stable, and with that there has been stability at Director and at CEO level. Over the past 100 years there have only been 4 CEO's and 9 Chairmen. Another contributing factor is the long term nature of the franchise relationships, especially, but not restricted to Ford. The senior level stability filters down to the individual dealership managements. The result is a stable core of people with huge experience.

However change does come, and as announced earlier, the CEO, Graeme Gibbons, will be turning 65 in a year's time, and will be retiring from his role as CEO next year. He will however continue in his role as a director. Graeme has been CEO since 1990, 30 years.

Succession is a gradual transition to a new leadership team in the CMC Office consisting of Alex Gibbons, June Gibbons, and Paul Stephenson. Not surprisingly with a small office and long tenure, job descriptions reflect the personalities and personal skill sets of the people involved. Succession will not be a replacement of like with like.

Both Alex and June are Gibbons family shareholders, but Paul is not. Alex and June are in the 35 to 40 year age group.

Paul has a financial background and is currently the Finance Manager at the CMC office. Before coming to the CMC two years ago, he was the CFO at an aged care provider, Heritage Life Care. Alex started with Southpac trucks in 2015, later moving to the CMC office initially specialising in information technology and more recently as General Manager. Alex did a double major in Marketing and Economics at Otago University followed by a Masters Degree in Marketing Management. June started at Stevens Motors in 2016 and is currently the CFO for Capital City Motors where she has been heavily involved with the integration of Stevens and Capital City Motors. She will be transferring to the CMC office in mid-November. June has both a Bachelor of Arts and a Bachelor of Science degree from Victoria Wellington, and a Master of Science in Resource Management from TUM University in Munich, Germany.

There is depth of experience surrounding the new team, above at Board level, and below at dealership CEO level. There will be a gradual phased change with Graeme remaining available.

Property

The Company had an unusually large number of property developments and upgrades under construction or just completed during the year. Most have been in the planning stage for some time, the longest, Tuam Street in Christchurch goes back to the 2011 earthquakes. Covid has delayed the completion of many, some significantly. All projects that were under construction before lockdown will be completed, some others that had not physically started have been deferred (to next year).

In central Otago, Agricentre South's new Case Tractor service centre in Cromwell was opened in September. This is a new purpose built, company owned facility, replacing an older leased facility.

Nearby at Wanaka a new Company- owned service centre has just been opened. This is a new concept, one half of the building branded Macaulay for Ford and Mazda, the other half branded Southern Lakes for Mitsubishi and Nissan. Individually, none of them could justify being in Wanaka, but a cluster of four can.

At Christchurch work is underway to put the city's planned greenway through Team Hutchinson Ford's workshop. This is a major project, involving demolishing part of the 1930's era workshop and rebuilding the administration and sales buildings, with the greenway running through the middle of the property. The project is expected to be completed early in 2021.

Lower Hutt. This is another large project. Following the purchase of properties alongside the existing Stevens Motors site on High Street in Lower Hutt, work is underway to build separate Ford and Mazda showrooms and workshops. This project has had significant Covid delays and is not ready in time for the previously committed exit from Taranaki Street in Wellington City. Merging two dealerships into one is difficult enough, more so with the complications of working around the shifting requirements of a building site.

Auckland. South Auckland Motors has occupied its current site on Great South Road since 1986. Over that time the building has been modified many times to adjust to changing requirements. This time, when adjusting the facility to the latest Ford and Mazda branding requirements, it was decided to address the long term roof and gutter leaking problems with the building. The fully upgraded showroom was officially opened two weeks ago.

At Botany, the Company purchased a site at 271 Botany Road and is developing this into a Suzuki and Isuzu facility for Southern Autos Manukau. This is quite separate from the South Auckland Motors Ford and Mazda Botany facility on Harris Road.

Finally at Nelson, the new separately leased facility for Nelson Kia in Rutherford Street was occupied early this year.

Trucks

Southpac's year started with planning for a major model change for the DAF truck line featuring a Euro6 compliant range, new cabs and specifications, to be launched in the first quarter of 2020. As part of this plan, additional inventory was ordered. Southpac entered lockdown with a full inventory of the new model, and an interrupted launch program. However, lockdown for Southpac was not as severe as it was for the car dealerships, as many of the heavy truck customers were classified as essential. Parts, servicing and some replacement trucks for those customers who were essential service providers, was able to continue though under strict controls. Primary producers in particular continued working through lockdown. Consequently Southpac did not get the dramatic revenue falls experienced by the car dealerships, but nor did it get the dramatic rebound after lockdown. Southpac's two brands, Kenworth and DAF have different ordering cycles, with Kenworth mainly built to specific customer requirements, while DAF are ordered as standard builds. Australian assembly of Kenworth's continued through the Victoria, Australia lockdowns, and the pre-build of the new model DAF insulated Southpac from build shortages in Europe.

Southpac's forward order position is improving month by month. Logs are being milled, livestock is being moved, and goods transported around the country, and Southpac keeps that side of the economy working.

Holden

General Motors decision to close down the Holden Brand in New Zealand and Australia is a reality check on the small scale and international significance of the New Zealand new vehicle market. At a world level, right hand drive is the minority. The big markets, North America, Europe and China, are all left hand drive. Right hand drive is restricted to Japan, Britain and the old British Commonwealth countries. Not only is right hand drive a minority, but on a world level, it's scattered and fragmented. General Motors do not have a presence in Japan, and when they sold their British and European subsidiary, Opel, it was obvious that Australia and New Zealand were not big enough to justify a full range of specially adapted products. In a way it's surprising that they did not exit immediately after selling Opel.

New Zealand is in the minority right hand drive market, and within that it has quite distinct preferences. Unlike right hand drive Britain, we like automatics; unlike right hand drive Japan, we like vehicles that can tow.

As the international car markets evolve and increasingly fragment into different technologies, we cannot assume that our preferences will always be available.

Holden's exit from New Zealand, is one less competitor, but it is not a cause of celebration. Instead it creates problems for everyone. It upsets the balance between dealers and their franchisors, as the old Holden dealers look to swap their empty sites into other brands and some franchisors use the opportunity to change their dealers. The partnership, the tension, between franchisor and franchisee is delicate; the exit of Holden exposes how delicate the relationships are.

Outlook

This financial year has started on a positive note. Despite a 2% drop in overall revenue, trading profit for the first quarter, July to September, is up on last year. This reflects ongoing skilled management of details to ensure the best result from the available activity. It is not a growing market, but it's much stronger than earlier economic projections. There are some forward orders, some supply shortages. If it carries on at the current level, then the half year will be ahead of last year. But, it can all suddenly slow down again. Confidence is fragile, we all live for today, and start again tomorrow.

J P Gibbons
CHAIRMAN

6 November 2020