

Chairman's Address

Good afternoon, Ladies and Gentlemen.

Welcome to Hills 59th Annual General Meeting.

My name is Jennifer Hill-Ling and I am the Chairman of your Company.

I would like to acknowledge the traditional custodians of this land, the Kaurna people, and pay my respects to their Elders, past and present.

We have a quorum and I declare the meeting open. The Notice of Meeting has been sent to all shareholders, with your consent, I will take it as read and move forward.

The Minutes of last year's AGM held on 26 November 2015 are in order. They have been signed by me and are available for any interested shareholders to review. In addition, to shareholders present here today, I can confirm that 34% of the Company's shares are represented by proxies.

I am pleased to introduce my fellow directors:

- Ian Elliot;
- Fiona Bennett;
- Philip Bullock; and
- I particularly welcome our newest director Ken Dwyer.

Ken joined us in September this year as part of the ongoing renewal of the Hills Board and the need to focus on strengthening the performance of our distribution businesses.

Ken brings a wealth of experience in the distribution industry at a time when we are poised for growth. He commenced his career in marketing and investment banking, and subsequently entered the audio industry, founding a chain of specialist home entertainment stores and more recently, a major audio products distribution business operating across Australia and New Zealand.

I would also like to sincerely thank Ian Elliot who retires at the end of today's meeting after 13 years' service, and David Spence who retired from the Board in September, having served for a period of 6 years. We have appreciated their extraordinary efforts and diligence in helping guide Hills from a diversified holding company into a focussed technology based company.



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I would like to welcome:

- Our new Chief Executive Officer (CEO), David Lenz;
- Gareth Turner, our Chief Financial Officer (CFO); and
- Gai Stephens, our Company Secretary.

Scott Fleming, from KPMG, is our auditor, and he is available to answer any audit related questions you may have in due course.

OVERVIEW

Let me briefly outline what we will cover this afternoon.

First, I will discuss the recent leadership changes at Hills.

Secondly, I will provide an overview of our performance over the past financial year, including the implementation of the “Back to Basics” program that we launched last year.

Then, David Lenz, will:

- update you on the performance of each of our businesses;
- outline the Company’s direction and strategic focus for the current financial year and beyond; and
- finally, provide an overview of the outlook for the current financial year.

LEADERSHIP CHANGES

Turning first to leadership changes in your Company - as shareholders you would be aware that the Board appointed David Lenz, to the position of CEO on 1 September this year. This appointment followed the retirement of Grant Logan at the end of his employment contract. Grant ably led Hills through its “Back to Basics” program and introduced new longer term financing arrangements. I would like to take this opportunity to thank him for his dedication and loyalty over his 5 years with the Company in the roles of CFO, COO and CEO.

Grant continues as a consultant to Hills to assist in the CEO transition, and with specific projects including the merger of Hills Health Solutions with Lincor Limited.

David Lenz has moved seamlessly into the role of CEO having worked at Hills since May 2015, as head of Hills key Building Technologies division and Hills Chief Operating Officer, during which time he played a key role in the implementation of our strategy and crafting our future plans.

He has over 25 years proven experience in sales, business development, management and operational leadership across Australia, New Zealand and

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Asia Pacific. He is well positioned to focus on our "Back to Growth" strategy which he will outline for you.

I am also pleased to announce that Chris Jacka, Hills deputy CFO will shortly be appointed to the role of CFO upon Gareth Turner taking up the position of CFO of Lincor Limited. I would like to take this opportunity to thank Gareth for his hard work and dedication over nearly 4 years with Hills.

STRATEGIC FOCUS IN THE 2016 FINANCIAL YEAR

Moving now to review our strategic focus in the 2016 financial year (FY16). The past 12 months has seen the implementation of the "Back to Basics" program and our new "fit for purpose" banking arrangements.

The "Back to Basics Program" had at its heart:

- Improving our underlying Profitability;
- Efficient Capital Management;
- Improving Vendor relationships;
- Improving Customer engagement; and
- Our people.

I am pleased to report that we have made progress in each of these areas.

IMPROVING OUR UNDERLYING PROFITABILITY

Our underlying financial results are a long way from where we want them to be but as anticipated this time last year, we don't expect to see the full benefits of the "Back to Basics" program until FY18.

Our 2015 financial year (FY15) results included businesses that were divested or discontinued during that financial year. The Home Division was a trading business before it was converted to a brand licensing arrangement and Crestron sales were also included in the FY15 results.

At last year's AGM I advised that we were anticipating improved earnings on the first half as the "Back to Basics" program gained traction. I am pleased to confirm that our Earnings before interest tax, depreciation and amortisation (EBITDA) increased by 25% from \$5.2 million in the first half of to \$6.5 million in the second half of the year in review and pleasingly, the full year EBITDA result of \$11.7 million was 8.3% higher than the guidance number we had provided at the first half results announcement.

Our key Building Technologies Segment showed an improvement in both Revenue and EBITDA for the second half, while the Hills Health Solutions went from an EBITDA loss of \$0.1 million at the end of the first half of FY16 to an EBITDA profit of \$1.4 million in the second half.



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Our underlying Net Profit after Tax (NPAT) also increased by \$5 million in the second half.

STATUTORY REPORTED RESULTS

While the trading EBITDA results of the Hills business show positive signs of improvement, it was disappointing to have to recognise some significant non-operating accounting charges in the first half of FY16 following the decline in the Hills share price early in the year.

This decline in share price triggered a review and reduction in the carrying values of goodwill, intangible assets, deferred tax assets and freehold property and a non-cash impairment of book values by \$66 million. The remainder of the balance sheet after these write-downs is comprised almost entirely of net working capital and tangible assets.

The non-cash accounting charge does not impact on future operating cash flows and has no impact on the economics of the Hills businesses.

EFFICIENT CAPITAL MANAGEMENT - REDUCED NET DEBT

Hills net debt continues to reduce and was \$24.2 million at 30 June 2016 – a significant \$14.3 million reduction from 31 December 2015. The pleasing reduction was driven by a substantial decrease in our working capital including a reduction of \$16.8 million in our inventory during the year in review.

The sale proceeds from the disposal of the remaining O'Sullivan's Beach property in South Australia also contributed to the reduction.

Hills net debt at the end of the first quarter of the current financial year was \$26.4 million.

FIT FOR PURPOSE BANKING FACILITIES

The Company's long term financing facilities were updated in May this year, and are more suited to the activities of the Company both in terms of their size and nature. They comprise:

- a \$36 million, 5-year debtor finance facility provided by Assetsecure; and
- a \$15 million facility from the Commonwealth Bank of Australia of which \$10 million has a term of 18 months and \$5 million for a term of 12 months. The \$5 million tranche has since been repaid and cancelled.

IMPROVED OPERATING CASH FLOWS

Cash generated from operating activities in FY16 was an inflow of \$9.4 million. We recorded an \$8.6 million improvement in the second half of the year and a \$22.4 million improvement from the prior year's outflow of \$13 million.

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The excellent turnaround in operating cash flow is calculated after the payout of \$10.3 million in legacy restructure provisions in the year in review. These payments cover warranty costs, make-good provisions, onerous lease costs, redundancy and restructuring costs resulting from the sale of steel and manufacturing assets in prior years.

IMPROVED CUSTOMER ENGAGEMENT AND VENDOR RELATIONSHIPS

Moving now to review our progress in improving our customer engagement and vendor relationships.

Many of our customers, suppliers and employees have reported that we continue to improve our vendor and customer service levels. The introduction of a new e-commerce platform in the current year should see further improvement - but we have more work to do and David and his team are very focused on this aspect of the business.

The power of our:

- national sales presence,
- extensive branch network,
- qualified personnel;
- training services; and
- success in attracting the best range of products and services,

was reflected in the large number of projects we won during the period. These included:

- The supply of Genetec unified IP security solutions to Sydney Trains, partnering with Indra;
- The supply of Ruckus Wi-Fi networks at Western Sydney University in conjunction with Big Air Group Limited;
- The supply of Genetec unified IP security solutions to the Auckland International Airport, partnering with Datacom; and
- The supply of L-Acoustics speakers to Novatech in South Australia and Power Audio in Victoria.

Attracting and retaining the best people in Hills

We continue to focus on improving our communication with staff. David and I have visited each state of Australia and Auckland during September and October this year to provide an update on the Company's FY16 results and plans for the current financial year.

We also conducted an employee engagement survey during the period to better understand where to focus our resources in the current year. Areas in focus



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include communication with customers and employees, product and systems training and stock ranging.

We continued our Hills Heroes recognition program and the Hills Xtra benefits program in addition to refining our bonus plans, which we consider better aligns salaries to the Company's business plans, market expectations and the interest of our shareholders.

POST 30 JUNE 2016 ACTIVITIES

Since June this year we have made two important announcements – The first relates to the merging of our Hills Health Business with the business of Lincor Inc and the second relates to the termination of the licensing arrangements with Woolworths Limited.

LINCOR MERGER

In September this year we announced that subject to shareholder approval we will merge our Hills Health Solutions (“HHS”) business with Lincor, Inc to form a newly incorporated company Lincor Limited.

On completion of the transaction, Hills shares in Lincor Limited will be distributed pro-rata to our existing Hills shareholders, and listed on the ASX.

While Hills healthcare solutions has the potential to become a key profit driver within your company in the future, we believe that the opportunities for the healthcare business and its growth potential are much greater by combining the Lincor Inc Platform with Hills extensive hospital and aged care footprint.

As a result of the merger, Hills will also receive monies from Lincor which we will use to further reduce debt and invest in our “Back to Growth” strategic initiatives which David will outline shortly.

An Extraordinary General Meeting of shareholders of Hills will be held later this year to seek the approval of Hills shareholders for the transaction and if approved, Hills shareholders receive shares in the newly listed Lincor Limited in addition to the shares they hold in Hills.

TERMINATION OF THE WOOLWORTHS LICENSING ARRANGEMENTS

The second significant event that occurred since 30 June this year was the announcement that our licencing arrangements with Woolworths to use the Hills Home brands had been terminated following their decision to exit the Masters Hardware Business. Hills received a payment equivalent to 3 years' licence fees from Woolworths' in October, as part of the termination arrangements.

We are currently reviewing a number of options around re-licensing the brand. We will update the market when a decision has been made, but be assured any



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decision will be one which the Board considers is in the best interests of our shareholders.

SHARE PRICE MOVEMENT

Since we last met our share price has been quite volatile. I am pleased to advise that we have seen a 35% increase since this time last year and that our share price closed at 58.5cents yesterday. The recent increases followed the release of our full year results, the announcement of the Lincor transaction and the payment from Woolworths.

I will now hand over to our CEO, David Lenz to update you on the performance of each of our businesses in FY16 and provide an outline of our "Back to Growth" strategy for the current financial year and beyond.

[CEO PRESENTATION]

OUTLOOK

As I mentioned at last year's AGM, rebuilding takes time to do well.

Given the level of profitability forecast for the current financial year and the planned investment in our growth strategies, combined with the additional costs associated with the Lincor transaction, we will not be in a position to pay a dividend this financial year. However, subject to your approval, we will be in a position to deliver substantial value to our shareholders in the form of shares in the new Lincor Limited later this year.

CLOSING REMARKS

The Board and Management team clearly understand that further improvement in profit is required and the importance of returning to paying a dividend as soon as it is prudent to do so. We continue to stand behind our strategic decisions which will deliver long term benefits to shareholders.

Our continuing businesses, together with the acquisitions we made in previous years, provide a solid base from which to expand in the future.

We remain undivided in our optimism for Hills to increase its share in existing markets and build new opportunities.

In closing, I want to thank my Board colleagues for their valuable contribution and all of our employees for their commitment throughout the year.

Finally, I want to personally thank my fellow shareholders who have expressed their support. I appreciate your patience and support and I can assure you of our dedication to continue to improve the performance of your Company.

Thank you.

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