

# **2007 Interim Results**

**22 February 2007** 



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#### **Presentation Sequence**

- Introduction and Overview
- PaperlinX 2007 Interim Result
- Paper Manufacturing
- Paper Merchanting
- Summary and Outlook
- Questions and Answers



#### **Market Overview**

- Forecast growth in global demand for CWF and UCWF exceeds announced growth in global supply, though regional variations are evident
- Currency movements additionally impact trade flows, particularly between Europe and the U.S. The strengthening Euro/U.S. \$ rate reduces desirability of exports to the U.S. over time (increasing product held in Europe)
- Higher input costs force mill closures and have stirred mills to raise the price floor
- Though European demand is improving on CWF and UCWF, current pricing is heavily driven by the need to recover higher input costs and is therefore inherently less stable
- Supply/demand driven pricing is present in North America, and is expected to occur globally based on industry forecasts
- In this environment, PaperlinX has seen revenue growth but only been able to hold gross margins as paper prices from suppliers have lifted
- Underlying EBIT has improved as a result of internally generated initiatives and productivity, with little assistance from improved market conditions



#### Results For Six Months Ended 31 December 2006

- Revenue of \$3.9 billion (up 10% on the prior corresponding period (pcp)) and volume of 2.2 million tonnes (up 3%).
- Profit after tax of \$32.7 million (\$35.3 million pcp) included net \$(10) million impact of after tax one-off costs largely attributable to the pulp mill upgrade
- Underlying EBIT of \$96.0 million, up 24% (\$77.7 million pcp), reflects benefits from strategic initiatives and tight cost management, though minimal net benefit has been realised from market conditions
  - Net positive EBIT benefit of \$16 million from strategic initiatives, including M1 upgrade, Spicers Canada acquisition, Shoalhaven PM1 and PM2 closures and PaperlinX Office
  - Productivity and positive mix/pricing were largely mitigated by higher input costs (pulp, fuel, chemicals and sourced paper).
- The announced strategic initiatives are on-track to exceed \$23 million/\$100 million net benefits in 2007/2009
- Merchant margins have benefited from growth in sign and display, industrial packaging, branded volumes, and the European stock to indent ratio
- Australian Paper underlying EBIT of \$12.6 million is improved from both the first and second halves of fiscal 2006 due to production line efficiencies, cost control, implementation of previously announced initiatives, some export price increases and the market success of the PaperlinX Office consolidation



#### Results For Six Months Ended 31 December 2006

- The working capital to sales ratio improved (19.0% to 18.7%) and average working capital (excluding currency and acquisition impacts) reduced, but total period end working capital was up \$238 million due to seasonal factors, revenue growth and an adverse movement in period end creditors
- Cash generated from operations excluding working capital movement was \$102 million. Net operating cash outflow was \$(142) million largely as a result of higher working capital.
- Return on average funds employed (both pre and post one-offs) has begun to improve as benefits of strategic initiatives are beginning to be reflected and average funds employed reduces on a comparable basis
- The proposed sale of the PaperlinX business in France and acquisition of a business in Italy recognises the benefits of in-market scale and is consistent with the Core Operating Principles
- Employee safety performance was only level after last year's substantial gains
- Environmental footprint (particularly in water utilisation) is improving at healthy rates through discrete initiatives and as a result of the pulp mill upgrade



# **Financial Summary**

		6 months to Dec 2005	6 months to Dec 2006	% change
Sales Volume	'000 tonnes	2,105	2,176	+3%
Sales Revenue	\$m	3,574	3,949	+10%
Underlying EBIT	\$m	77.7	96.0	+24%
EBIT	\$m	79.2	87.1	+10%
Reported Earnings after Tax	\$m	35.3	32.7	-7%
EBIT/Average funds employed	%	6.2	6.6	+0.4pts
Earnings per share	cps	7.9	7.3	-0.6cps
Interim dividend (unfranked)	cps	5.5	5.0	-0.5cps



#### **Core Operating Principles**

Our Core Operating Principles have provided guidance to improve our competitiveness and position ourselves for improved returns going forward:

- Strengthen then build off existing business platforms
- Productivity to provide funds to improve sustainability and growth
- Simplification
- Actively prioritise activities based on value creation for our customers, suppliers and for PaperlinX
- Fully leverage our global opportunities
- Invest in our people and their skills
- Compliance is mandatory
- Results oriented teamwork/success as a team.



#### **Major Business Initiatives - Update**

•	Upgrade	of Mar	yvale PM1	
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Closure of Shoalhaven PM1

Spicers Canada Acquisition

PaperlinX Office

The Delivery Company

Netherlands Restructure

European IT platform

Maryvale Pulp Mill upgrade

Maryvale Wood yard outsourcing

Growth of own brands

Strategic Sourcing Alignments

European Portfolio Change

Global Customer Solutions

Complete, in market

Complete and on plan. PM2 also shut

Complete, exceeded expectations

Complete, market successes

On track, 5<sup>th</sup> site operational

On track, DRiem integrated

On track, Ireland successful

On track for targeted returns

On track

Strong first half

On going

Additional conditional agreements

Structure developed

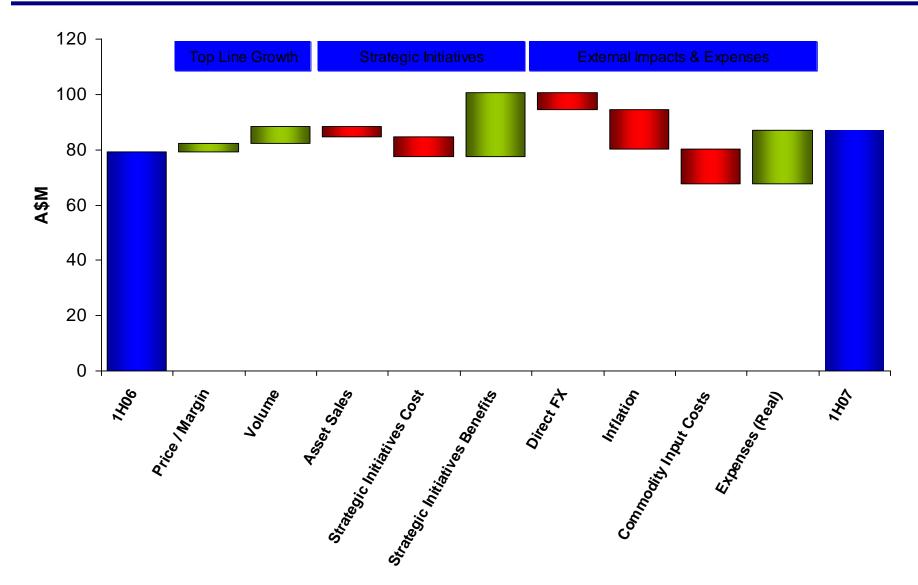


# **Key Financial Measures**

		6 months to Dec 05	6 months to Dec 06
Working Capital	\$m	1,359	1,475
EBITDA	\$m	129	138
Operating cash flow	\$m	(32)	(142)
Net Interest cover	X	2.4	2.4
Net interest expense	<b>\$</b> m	32.9	36.4
Effective Tax Rate	%	23.9	35.5
EBIT / Average funds employed	%	6.2	6.6
Capital Expenditure (including acquisitions)	\$m	47	75
Net tangible assets per share	\$	2.38	2.55
Net Debt / Net Debt & Equity	%	39.6	39 7

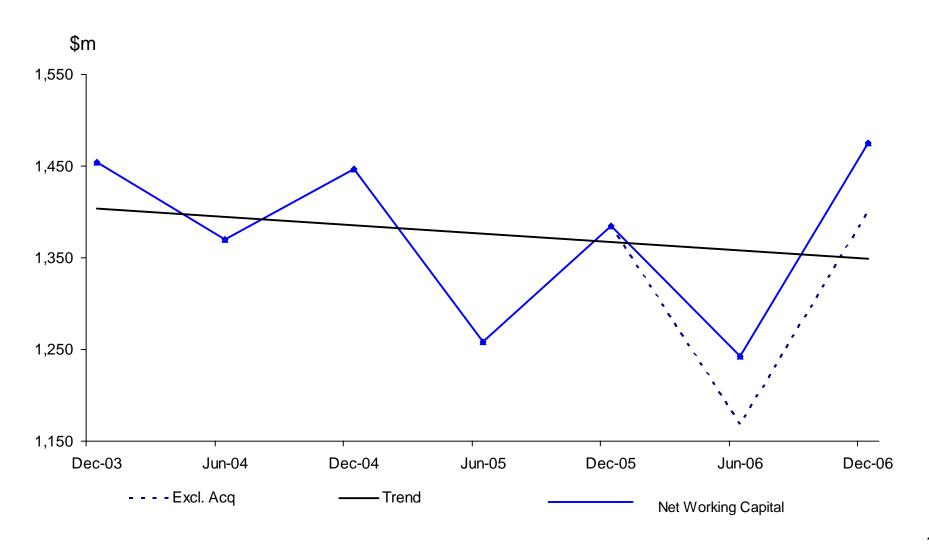


#### **Key Variances to EBIT**





# Net Working Capital – Currency Adjusted



#### **Issue of Hybrid Equity**

- PaperlinX is proposing to issue between \$250 \$300 million of hybrid equity capital
  - This will be in the form of perpetual Step-up Preference Securities (SPS) which are preferred units in the PaperlinX SPS Trust
  - Application will be sought to list the PaperlinX SPS on the ASX
- The PaperlinX SPS are expected to pay discretionary, unfranked, semi-annual, floating rate, non-cumulative distributions
- Funding raised from the issue will be used to repay senior debt
- The issue will:
  - reduce debt
  - further strengthen the Group's balance sheet;
  - increase the Group's financial flexibility; and
  - provide a solid financial platform to take advantage of future opportunities.
- For full details we recommend that you obtain a copy of the product disclosure statement lodged with ASIC today



### **Australian Paper - Consolidated Result**

		6 months Dec 05	6 months Dec 06	Change <u>%</u>
Sales Volume	'000 tonnes	429	413	(4)
Australia/NZ Share of Volume	%	80	80	nc
Sales Revenue	A\$m	525	510	(3)
Underlying Earnings before Interest & Tax	A\$m	6.0	12.6	110
Net One-off Costs	A\$m	(1.9)	(9.6)	
Reported Earnings before Interest & Tax	A\$m	4.1	3.0	(27)
Return on Average Funds Employed	%	0.9	0.6	







# **Australian Paper – Interim Result**

- Overall earnings remain under significant pressure due to low pricing and the inability to recover input cost increases over three years. This has been the key issue for this business for some time and remains the case
- Underlying earnings, however, were up 110% on pcp (or \$6.6 million), albeit off a low base. Underlying operating earnings benefited from internal efficiency programmes and the benefits of completed strategic initiatives including the closure of Shoalhaven Mill PM1 and PM2 and the Maryvale M1 upgrade
- Operating earnings include a net one-off charge of \$9.6 million mainly relating to the outsourcing of the Maryvale wood yard, the consolidation of PaperlinX Office
- Australian Paper earnings now include PaperlinX Office results with adjustments to historic segmental results
- Overall volumes were 4% lower due to Shoalhaven closures
- Commodity input costs have negatively impacted earnings by \$13 million on pcp,
  \$11 million of which is pulp
- Improved mill operating efficiencies contributed positively to earnings



### **Australian Paper – Interim Result**

- Overall average price realisation was flat on pcp with a better mix
- Selling prices in domestic markets generally remained under pressure, with imported paper prices held down by the strong Australian dollar
- Sack Kraft markets have been strong, with good gains in export prices in US\$, negated to some extent by currency translation
- The drought in Australia has had an impact on some linerboard segments which have been balanced to some extent by robust demand in industrial markets, although overall sales volumes were lower
- Communication papers overall volumes were lower due to reduced exports and the closure of the Shoalhaven machines. Both of these activities were however positive to earnings
- Paper selling prices for communication papers in Australia have remained under pressure, though some increases have occurred as we endeavour to recovery higher input costs



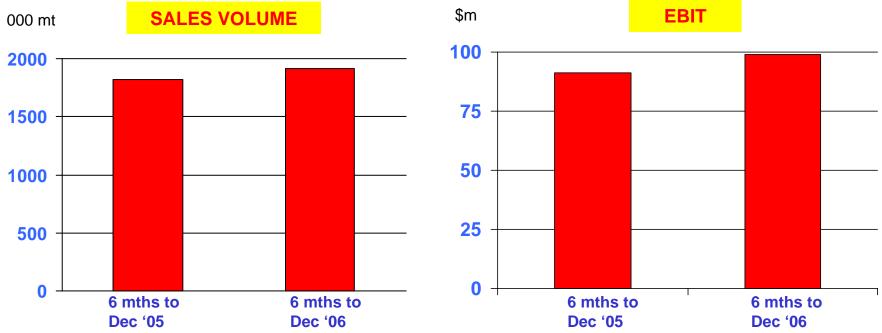
#### Australian Paper – Project updates

- The pulp and bleach plant upgrade at Maryvale to improve paper quality, reduce pulp costs and improve environmental performance announced in August 2005, remains on track for targeted returns. This reflects the risk to final steel and labour costs mitigated by expected higher savings on pulp costs versus current levels
- The wood yard outsourcing contracts at the Maryvale Mill are completed and oneoff costs have been included in the six months just completed. Project completion will match the pulp mill upgrade
- The benefits of the closure of Shoalhaven number 1 paper machine can be seen in this result. Additionally, production at the number 2 paper machine has been consolidated on to the number 3 machine, further enhancing productivity
- Increased usage of recycled water (12%) planned and improved water efficiency implemented (10%)
- The integration of PaperlinX Office was completed successfully and has contributed positively during this six months. All one-off costs associated with the integration have been included

**PaperlinX** 

# Paper Merchanting – Consolidated Result

		6 months Dec 05	6 months Dec 06	Change <u>%</u>
Sales Volume	'000 tonnes	1,823	1,910	5
Sales Revenue	\$m	3,224	3,618	12
Earnings before Interest & Tax	\$m	91.3	99.1	9
EBIT/Sales Revenue	%	2.8	2.7	-0.1pts
Return on Average Funds Employed	%	10.9	11.4	+0.5pts



# Merchanting - Europe

		6 months Dec 05	6 months Dec 06	Change <u>%</u>
NW Europe	'000 tonnes	383	382	0
UK & Ireland	'000 tonnes	602	601	0
Central &Southern Europe	'000 tonnes	<u>241</u>	<u>258</u>	7
Total Sales Volume	'000 tonnes	1,226	1,241	1
Sales Revenue	€m	1,363	1,399	3
Earnings before Interest & Tax	€m	38.4	38.8	1
EBIT/Sales Revenue	%	2.8	2.8	nc

- European market remained challenging, particularly in France and Germany, while demand in the UK has yet to show any sign of recovery
- Reported EBIT was in line with pcp, underlying EBIT up 6%
- Despite the soft markets, branded volumes continued to grow, up 16% on pcp
- Stock to indent ratio improved
- Total net operating costs benefited from the continued focus on expenses and from restructuring initiatives
- While working capital showed a seasonal increase, working capital to sales ratio unchanged



# Merchanting - Europe

- Proposed sale of Axelium in France and purchase of Italian paper merchant, Antalis, Italy, strengthens and builds on existing platform, improving scale in Italy and exiting a sub scale position in France. Transactions expected to settle in three to four months, if they meet all conditions
- Mill closures underway at present in Europe have yet to be fully reflected in market supply, but are beginning to be implemented
- Paper price increases implemented towards the end of period in the UK for all grades. CWF pricing on the Continent currently underway. UCWF prices increased Q1 with new pricing announced
- Pricing driven largely by input cost pressures on manufacturers
  - Indent prices need to rise first
  - Buyer resistance slows implementation and increases volatility
  - Margin recovery possible when pricing becomes more supply/demand driven (versus current mix of supply/demand and input cost recovery driven)



### **Merchanting - North America**

		6 months Dec 05	6 months Dec 06	Change <u>%</u>
Sales Volume	'000 tonnes	218	315	44
Sales Revenue	US\$m	347	547	58
Earnings before Interest & Tax	US\$m	11.7	20.2	73
EBIT/Sales Revenue	%	3.4	3.7	0.3 pts

- North American paper selling prices continued to be supported by capacity reductions, up 3-4% on pcp, with only modest market demand
- Proprietary branded volumes were up 19% across North America, with good growth in all operating companies
- Expenses contained (ex sales commission flow on)
- EBIT/sales up further to 3.7%
- Total earnings are up 73% on pcp, and have doubled over the past two years reflecting leverage to the upside
- Solid improvement in returns for all businesses, with Spicers Canada (included for the full period) exceeding year 3 return target in year 1 due to both earnings and strong working capital management



# Merchanting – ANZ/Asia

		6 months Dec 05	6 months Dec 06	Change <u>%</u>
Sales Volume	'000 tonnes	379	355	(6)
Sales Revenue	A\$m	537	511	(5)
Earnings before Interest & Tax	A\$m	13.1	6.3	(52)
EBIT/Sales Revenue	%	2.4	1.2	(1.2) pts

- Overall volumes were down 6% with lower volumes in New Zealand and in Paper Trading
- Australia continued to see pricing pressure, with average realisations down
  1.5% impacting on margins and returns
- Other markets saw positive pricing impacts
- New Zealand EBIT negatively impacted by \$(3) million by accounting treatment of paper purchases, expected to reverse in second half
- Australia impacted by a net \$(2.1) million property restructuring charges
- Expenses have been reduced in all businesses
- Further progress was made on working capital, down 7%
- Asian EBIT up 8% and up 35% over two years



#### PaperlinX 2007 Interim Result Summary

- Net profit of \$32.7 million including net \$(10) million of after tax one-off costs
- Underlying EBIT of \$96.0 million (up 24% on pcp) reflects positive contributions from strategic initiatives, mix and effective cost management, with minimal benefit realised from improving market conditions
  - Net positive EBIT contribution of \$16 million from Maryvale M1 upgrade,
    Spicers Canada acquisition, Shoalhaven closures and PaperlinX Office
  - Strong productivity and some pricing mitigated by higher input costs
- Australian Paper underlying EBIT benefits from internal initiatives and efficiency gains despite input cost increases
- Potential European portfolio changes follows current strategy
- Hybrid issue will allow greater flexibility
- Lift in return on average funds employed



#### **Business Outlook**

- UK, North America and Australia/NZ demand remains modest, though balanced by only modest capacity increases net of mill closures.
- Manufacturing input costs remain high but are stabilizing
- Strategic initiatives are on-track to exceed \$23 million/\$100 million net EBIT benefits in 2007/2009
- Seasonal improvement in working capital and on-going focus on working capital % sales is targeted in a climate of higher revenue
- Minimal "market improvement" benefits expected in the second half
- Hybrid funding to be pursued
- Growth opportunities to leverage existing global platform will be addressed
- Focus remains on improved competitiveness, economic profit and shareholder returns through the cycle



# **Appendices**



# Australian Paper – Segmental Split

#### Australian Paper: Communication Papers

		6 months Dec 06	6 months Jun 06	6 months Dec 05
Sales Volume	'000 tonnes	254	260	270
- Australia/New Zealand	%	83	78	81
Sales Revenue	A\$M	383	377	402
Earnings before Interest & Tax	A\$M	0.1	(9.9)	1.3

#### Australian Paper: Packaging Papers

		6 months Dec 06	6 months Jun 06	6 months Dec 05
Sales Volume	'000 tonnes	159	157	159
- Australia/New Zealand	%	74	67	79
Sales Revenue	A\$M	127	119	123
Earnings before Interest & Tax	A\$M	2.9	2.4	2.8



# **Operating Earnings (A\$)**

	EBIT		Sales R	Sales Revenue		Assets
	Dec 2006 <u>\$M</u>	Dec 2005 <u>\$M</u>	Dec 2006 <u>\$M</u>	Dec 2005 <u>\$M</u>	Dec 2006 <u>\$M</u>	Dec 2005 <u>\$M</u>
Industry Segments						
Europe	66.2	62.5	2,388	2,221	2,101	2,038
North America	26.6	15.7	719	466	480	400
ANZ/Asia <sup>(1)</sup>	<u>6.3</u>	<u>13.1</u>	<u>511</u>	<u>537</u>	<u>470</u>	<u>471</u>
Total Paper Merchanting	99.1	91.3	3,618	3,224	3,051	2,909
Communication Papers (1)	0.1	1.3	383	402	749	731
Packaging Papers	<u>2.9</u>	<u>2.8</u>	<u>127</u>	<u>123</u>	<u>304</u>	<u>295</u>
Total Australian Paper <sup>(1)</sup>	3.0	4.1	510	525	1,053	1,026
Corporate <sup>(1)</sup>	(15.0)	(16.2)			25	60
Operating earnings before interest & income tax	87.1	79.2				
Net Interest	(36.4)	(32.9)				
Income Tax Expense	(18.0)	(11.0)				
Outside Equity Interests						
Inter-segment Sales			(179)	(175)		
Unallocated Assets (deferred tax assets)					64	83
Total	32.7	35.3	3,949	3,574	4,193	4,078



#### Reconciliation of one-off items for 1H 07

		First Half 06/07 EBIT (A\$mils)							
	As Reported	Net Property Actions	Business Restructuring	Net One-Offs	Underlying				
Paper Merchanting									
Australasia	6.3	(2.1)	0.0	(2.1)	8.4				
Europe	66.2	2.9	(0.7)	2.2	64.0				
North America	26.6	0.6	0.0	0.6	26.0				
Total Paper Merchanting	99.1	1.4	(0.7)	0.7	98.4				
Communication Papers	0.1	0.9	(7.0)	(6.1)	6.2				
Packaging Papers	2.9	0.0	(3.5)	(3.5)	6.4				
Total Australian Paper	3.0	0.9	(10.5)	(9.6)	12.6				
Corporate & Other	(15.0)	0.0	0.0	0.0	(15.0)				
Total PaperlinX	87.1	2.3	(11.2)	(8.9)	· 96.0				

<sup>\*</sup> due to Australian tax losses, Net One-offs = \$(9.8) million PAT





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PaperlinX Limited - 307 Ferntree Gully Rd, Mt Waverley, Victoria 3149, Australia - ABN 70 005 146 350

