Annual Shareholders' Meeting 2009

10.30 am Wednesday 11 November 2009

Dunedin Centre
Dunedin

Chief Executive Officer's Address

FLETCHER BUILDING LIMITED

Annual Shareholders' Meeting 2009

Good morning ladies and gentlemen.

May I also say what a pleasure it is to be here in Dunedin as we celebrate one hundred years of Fletchers in New Zealand.

As Roderick has already noted, the past year has been an exceptionally difficult one given the very depressed global economic picture.

In this context, we have sought to manage effectively through the downturn, and to emerge from it strongly, with the business lean and fit, and the balance sheet in good shape. I am confident that we have achieved these things.

Results overview

Sales were steady at just over $7 billion for the year, which was a good result given the decline in volumes. Strong performances in construction, and in our steel division were key in achieving this sales effort.

Operating earnings before unusual items were $ 558 million, down from $768 million in the prior year. The second half was noticeably tougher than the first half, and the run rate for the second half was around $230 million compared with $328 million in the first half.

In looking at our results, it is vital to stress that very few of our markets were untouched by the global economic crisis. Typically, we saw residential housing and commercial construction markets weaken throughout the year regardless of geography. The notable exception to this was Asia which saw growth for our Formica business in some parts.

Australia, whilst avoiding recession, was not immune from the downturn. New housing activity was down in key states such as Queensland, and commercial activity slowed throughout the year.

By way of illustration, this slide shows the trend in some of our key markets which are exposed to residential house building activities. The two year trend is even more stark in the US and Spain.

A notable exception was in government sponsored infrastructure spending. In New Zealand and Australia, activity levels in infrastructure, continued to help underpin many parts of our business.

In addition to the decline in activity levels, many of our businesses sustained significant increases in input costs, particularly in the first half of the year. Resin costs, energy and fuel costs all impacted earnings.

Building Products

The Building Products division lifted sales by 4 percent to $771 million, but operating earnings were down 28 percent to $106 million.

This division's earnings have a strong correlation with the residential housing market, and the weak New Zealand marketplace had a marked impact on the plasterboard and insulation businesses. Towards the end of the year, the benefit of government stimulus packages was seen on both sides of the Tasman in the insulation business, and the sale of Pink Batts and other products in Australia are now outstripping our production capacity. Metal roof tiles experienced good growth in export markets but this was offset by the weak New Zealand domestic housing market.

Distribution

PlaceMakers is highly correlated with the New Zealand housing market and its earnings continued to be impacted by the residential construction slowdown.

Sales were down by 18 percent against a decline in residential building consents of 39 percent. Operating earnings excluding unusual items were 59 percent lower at $30 million, due to the lower turnover and competitive pressures on margins. Overall PlaceMakers held or grew its market share in its key target markets of trade builders and serious DIY.

Infrastructure

Sales in the Infrastructure division were up 11 percent due to the increase in construction activity, offset in part by lower concrete sales. Operating earnings excluding unusual items declined by $105 million to $203 million, with the most significant component the decline in earnings from property related activities. These were $80 million in the 2008 year, compared with $18 million in 2009.

In New Zealand most concrete related activities saw a reduction in volumes – cement, aggregates, readymix, masonry, and concrete pipes, all recorded lower sales.

The Australian pipeline and quarry businesses performed well with growth in operating earnings boosted by strong demand for non-pipe products.

The construction business increased operating earnings to $43 million. The current backlog stands at $1.2 billion including the Victoria Park Tunnel project in Auckland which was won in July.

Laminates & Panels

Operating earnings for Laminates & Panels were $74 million, compared with $141 million in the previous year, with sales 3 percent lower at just over $2 billion.

Operating earnings in the Laminex business fell to $56 million from $125 million in the prior year. This reflected tough trading conditions in Australia and New Zealand, and the impact of sharply higher resin costs. Performance was also adversely affected by the West Australian gas crisis in the first half of the year. As Roderick has already noted, the decision was taken to close two export plants which had become unviable due to the deterioration in export markets, one in Auckland and one in Western Australia.

Formica's operating earnings before unusual items were up 11 percent on the prior year to $18 million. This was despite a further weakening in the North American housing and commercial construction markets, and a rapid deterioration in European markets. Formica Asia recorded another year of solid growth although this was lower than in previous years.

As you can see from the table, there was a significant improvement in the performance of Formica's North American operations, and the turnaround is especially pleasing given the deterioration in the market there. What is also evident from the table, is the decline in the performance of operations in Europe. Markets there have declined significantly – you may recall the 80 percent reduction in housing construction in Spain that was in an early overhead – and this is impacting performance in that region currently.

A priority for the management team is to address European performance including closure of part of the Bilbao plant in Spain.

In both Laminex and Formica, further cost reduction initiatives are under way, and these are expected to benefit operating earnings by $50 to $60 million per annum within the next two years.

Steel

The Steel division was the standout performer in the past year, with operating earnings up 52 percent to $154 million.

This performance was driven by high demand for steel coupled with steel supply shortages, and volatility in international pricing. The market dropped away rapidly in the second half and sales were 30 percent lower than for the first half due to lower volumes and pricing. Strong demand from infrastructure spending offset weakness in the residential and commercial markets. The rollforming and coated steel business experienced volume declines over the prior year due to the weakness in the residential and light commercial markets.

We do not expect the operating earnings in Steel in 2009 to carry through to 2010, although expectations are for a return of operating earnings to the more typical range of $80 to $100 million.

Health and safety

In health and safety, we continued to make good progress in 2009 with a reduced injury rate across the group. This year we introduced total recordable injury frequency rate as the primary performance indicator for safety. Recordable injuries are defined as both lost time and medical treatment injuries. By this measure, there was a pleasing 15% reduction in recordable injuries over the previous year.

Our health and safety vision continues to be “zero harm”, based on the principle that all accidents are preventable. We will continue to invest significant resources in safety education and training, to reinforce our commitment to the health and safety of our employees.

Current operating climate

That brings me to a close on last year’s operating performance. Let me now spend a few minutes updating you on current trading conditions and how Fletcher Building is placed for the next part of the cycle.

While financial markets internationally have become excited about the end of the recession, and the prospect of a recovery in economic conditions globally, we are currently seeing no significant pick-up in activity in our businesses around the world. There are some exceptions to this – such as the insulation business in NZ and Australia, and certain markets for metal roof tiles, for instance – but overall we have seen volumes stabilise at current low levels for the past few months.

The downturn in new residential housing has been clearly highlighted, but we have greater concerns over the slowdown in the commercial building sector. We are starting to see new housing consents pick up from the current low level, particularly in markets like New Zealand and Australia where there is no overhang of existing housing stock. We believe that commercial activity will, however, take longer to recover. As a prerequisite, such a recovery will require increased bank capacity, and appetite for exposure to new developments.

Increased government spending on infrastructure has been beneficial to Fletcher Building in New Zealand and Australia. However, this is not sufficient to offset the slowdown in residential and commercial as we have seen in the past year.

So overall we remain cautious about the immediate outlook for our businesses and the pace and timing of any significant recovery in volumes and revenues.

Positioned for the future

Given this cautious stance, it has been imperative that we position the business to perform strongly in an environment of cyclically low volumes.

We have already outlined a number of restructuring and capacity reduction initiatives, that have been undertaken to ensure all divisions are able to trade profitably in the current environment. In addition to these, we have a number of programmes underway across the group, examining product profitability and customer cost-to-serve. These have already identified further areas of efficiency gain, and we will be rolling out the changes that have been identified through these programmes, in the current financial year and into the next.

Pleasingly, the strong cashflow performance we saw in the last financial year has continued into the first three months of the current year. On top of this, we expect capital expenditure to be well down on the $289 million recorded last year. We are targeting stay-in-business capital expenditure of around $130 million this year compared with a depreciation rate of $211 million in 2009.

The strength of our cashflow, coupled with the equity raising, we completed earlier this year, has placed the group in a sound financial position. As you can see from this graph, near term refinancing requirements are modest, and all bank lines are presently undrawn with the exception of working capital facilities. We presently have over $1 billion of undrawn bank facilities available to the group.

Looking to the future

With the restructuring and manufacturing capacity reduction initiatives largely completed, and the balance sheet in a strong position, the next imperative is to prepare for the upturn when it comes. Currently we are preparing plans in all of the divisions, addressing how manufacturing volumes could be ramped up when demand improves. We are looking to learn from our insulation business, which earlier this year saw a very sudden increase in demand due to the government stimulus packages. Their experience in dealing with a rapid surge in volumes is helping other parts of the group in planning how to increase output efficiently.

Strategy

Let me turn now to our long term strategic priorities.

Fletcher Building's long term strategy continues to be, to improve earnings reliability through geographical and product diversification, to maintain and improve internal capabilities, and to pursue acquisition opportunities where these meet our key investment criteria.

In New Zealand, we will continue to maintain and grow our existing businesses and pursue means of strengthening our distribution capability.

Australia remains the key geography for pursuit of our growth aspirations. We will continue to build on our existing positions in the building products and construction materials sectors over time.

Beyond Australasia, we will continue to develop our laminates and panels businesses, and in particular seek to extend Formica's footprint in Asia. While Australasia is our principal area of focus, we do see Fletcher Building maintaining a leading position globally in laminates and panels through Formica and Laminex.

That concludes my review of the performance of the business and its future strategies.

Thank you.