2014 Annual Shareholders' Meeting

10.30 am Tuesday 21 October 2014
Eden Park
Auckland

Chief Executive Officer's Speech

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Good morning ladies and gentlemen. What I would like to do this morning is outline the various strategies we have been pursuing, provide an update on the progress we have made, and set out the priorities for the coming year.

Before doing so, however, I'd like to briefly reflect on our operational performance over the past year.

2014 Overview

As Ralph has mentioned, we enjoyed buoyant conditions in New Zealand, and I am pleased with how the businesses responded. The strong uplift in our New Zealand earnings was due in part to the improved efficiency of our businesses, driven by the initiatives we have undertaken over the past several years to lift performance. To have achieved such strong earnings growth with the high currency and increased import competition speaks volumes about the strength of our businesses and their teams.

Conversely, many of our businesses in Australia faced tougher economic conditions, compounded by excess manufacturing capacity and market over-supply. Reduced demand and a weak pricing environment were two of the challenges faced by our businesses there. With such a backdrop, we have increasingly focused our attention on our Australian businesses, to determine what more we can do to lift our performance and which businesses might have a higher value under different ownership.

Overall, we were pleased to achieve operating earnings growth of 10 per cent, particularly in light of the currency headwinds that have already been referenced. Delivering year on year earnings growth is a clear priority for us, and managing this in the context of differing market conditions and changing industry economics is our ongoing challenge.

Strategic Priorities

To ensure we deliver growth in returns to our shareholders, we have continued to pursue the agreed set of strategic priorities.

Broadly, these can be divided into four categories:

The first is the set of productivity initiatives, centred on the FBUnite programme that I outlined last year.

Second is the active approach we are taking to the business portfolio including both divestments and potential acquisition opportunities.

Third is the set of organic growth opportunities that we have continued to pursue and invest in.

And fourth is a continued emphasis on investing in our people, lifting capability and building employee engagement.

Let me discuss each of these in turn.

Productivity

At this meeting a year ago, I outlined the FBUnite business transformation programme, a series of work streams that, in combination, will reduce operating costs through leveraging the group's scale and establishing functional centres of excellence. We have set ourselves the goal of delivering incremental operating earnings of $100 million by the end of the 2018 financial year from FBUnite and are on target to achieve this.

We made excellent progress during the year with FBUnite, and delivered $25 million in benefits, offset partly by increased operating costs of $10 million. The strongest contribution came from the procurement function, which was fully up and running at the start of the year and which addressed expenditure across a number of supplier categories.

Good early progress was made in the newly centralised property function, which has the responsibility for managing over a thousand leased and owned properties across Australia and New Zealand. We will see the financial benefits accrue over the next several years as we rationalise our property footprint.

The manufacturing excellence programme completed its establishment phase during the year. This programme seeks to lift the operating performance of our key plants across the group, and we expect significant cost savings and ongoing improvements in efficiency.

In terms of our IT strategy, the recruitment last year of Carl Powell as Chief Information Officer has been key in establishing the group-wide IT and digital priorities. Carl and his team now have a clear roadmap for modernising our core IT platforms, and how these will support the deployment of new digital capabilities. Key deliverables have included financial system upgrades in a number of business units, and deployment of the group intranet and the human resources management system Workday.

One aspect of FBUnite where we have slowed the pace of implementation is the financial shared services centre. Early in the year it became apparent that this programme was intrinsically linked to the upgrade of the financial systems in a number of business units. We therefore decided to align the phasing such that business units will transfer their finance functions into the shared services centre once planned IT upgrades have been completed.

Managing the business portfolio

Last year I signalled that we would be taking a more active approach to managing our existing portfolio of businesses. The most significant development in this regard during the year was the sale of the Pacific Steel long steel business to New Zealand Steel, the local subsidiary of BlueScope.

The sale followed a strategic review of the steel industry and Fletcher Building's participation in it. The review showed that, on average, returns from Pacific Steel were lower than our cost of capital. In addition, we could see significant cash costs in the medium term with extensive reinvestment required to keep the plant at Otahuhu operating. The sale of Pacific Steel to a local operator has ensured that steel manufacturing stays in New Zealand, and will provide the necessary scale economies. Pleasingly, most of the staff at Pacific Steel were offered roles with the new owner, and where this was not the case employment opportunities are being found elsewhere in the group.

More recently we completed the sale of the Hudson Building Supplies business to a Woolworth's subsidiary in Australia. Again, this sale followed an assessment of the fit of this business with the broader portfolio of assets in Australia, and we determined that it was not core to our strategy and, in particular, did not fit with the Tradelink plumbing distribution business, our core distribution activity in Australia.

Since balance date, we have made the tough decision to cease copper tube manufacturing at Crane Cooper Tube in Sydney. We had tried to sell the business as a going concern, but were unable to. We also couldn't see a way of returning the business to profitability, in fact, we believed that losses would likely increase, despite the best efforts of the team.

In terms of acquisitions, we have over the past year continued to consider opportunities to grow through acquiring businesses in the building products sector.

Our focus has been primarily on Australia and New Zealand, but we have been prepared to consider acquisitions beyond our home territories which would fit with our global Formica business.

It is fair to say that high quality opportunities, priced where we could see value, have been scarce and we feel no particular pressure to pursue acquisitions. However, we remain open to considering potential opportunities should they arise.

We will continue in the year ahead to actively review the portfolio and are likely to divest of further non-core businesses if conditions are sufficiently favourable.

Pursuing organic growth opportunities

A priority for me and the management team has been to pursue organic growth across our businesses. This has been delivered in a number of ways, including market share growth, margin expansion, product innovation, and geographic expansion.

The first priority has been to ensure we capture the growth inherent in the economic cycle. In New Zealand, the strong economy helped to further drive overall construction activity levels, positively impacting volumes for most products. As a result, operating earnings in New Zealand rose 27 per cent. We have tackled the challenge of responding to the increase in demand in a variety of ways. One of the factors we must balance is the need to meet the expectations of our customers but without committing significant investment in new manufacturing and distribution capacity to meet volumes that may only be sustained for a relatively short period of time.

One key area of organic growth for us has been in our residential development business here in New Zealand. With continued strong demand for housing across the country but particularly in Auckland and Christchurch, we are stepping up the number of houses we complete and bring onto the market each year.

Historically we have built and sold around 300 houses per annum. Our new approach has seen us broaden the types of homes we offer in the market, from apartments to terrace houses to stand alone dwellings. Beyond this, we have set ourselves the goal of more than trebling the number of homes we sell each year, and are creating a pathway to an annual rate of one thousand homes sold each year. To meet this goal we need to increase our investment in land and we have successfully negotiated a number of land purchases in the past year. We are mindful of the need to generate strong returns from our residential business through the cycle and the property purchases we have carried out have been achieved at valuations which we believe are prudent and will allow the requisite returns to be generated.

Beyond our own development activities, we have been exploring partnership opportunities with central government agencies in New Zealand to improve the quality of social housing, while at the same time delivering on the government's priority of increasing the supply of housing, especially in the Auckland region.

Our construction business has also expanded its operations, and this is evidenced by the record backlog of work which stood at $1.8 billion at the end of September, up from $1 billion a year earlier. Recent innovations in the market have included the advent of public private partnerships, or PPP's, and we have developed in-house capability to allow Fletchers to participate in these projects.

In Australia, we have committed significant management resource into lifting the performance of the Tradelink business, which services the trade plumber market. We have opened two new format stores in Sydney and Melbourne, a significant milestone for the team and a marker of future developments to come. We believe that Tradelink has significant potential to further lift its performance, and to build on the strong performance last year when operating earnings doubled.

Further afield, Formica commissioned their newest plant in JiuJiang, China late last year, and production has ramped up progressively. This plant will not only supply the domestic China market but will also support the strong growth we have experienced across South East Asia.

Investing in our people

A priority for me since I took on the role of chief executive two years ago has been to grow our people capability through investment in training and development, and to build employee engagement throughout Fletcher Building.

We have redesigned the core people development programme into four modules targeted at different levels of skill and seniority right across Fletcher Building. This has enabled us to standardise the quality and consistency of the development of our people regardless of where they work. In doing so, we have been able to dramatically improve on the efficiency with which our training programmes are delivered, and thereby expand their reach and increase the number of employees able to participate in them.

A particular highlight during the year was the recognition conferred on our senior leadership development programme, Leaders Edge. Run in conjunction with The University of Auckland Business School, the programme won a silver award in the executive development category of the 2014 European Foundation for Management Development Excellence. This was a particularly impressive achievement as the programme was competing against a formidable line up of leading business schools including Harvard and Oxford universities.

We have instituted an annual employee engagement survey right across the company. What has been especially pleasing this year has been the very high participation rate, with over 90 per cent of our people participating in the survey. The results provide clear insight into the areas our people would like to see improved or further developed. We have included in senior managers' short term incentive scheme a specific goal around lifting engagement, and there is a particular focus on teams where engagement is well below the average for the company.

Embedded in this focus on employee engagement is the belief that we can deliver outperformance through the quality of our people. Hiring and retaining the best people requires the company to offer appropriate training and development opportunities, the prospect of a rewarding long term career path, and a team environment which lets them fulfil their aspirations.

Health and Safety

Our biggest priority is always the health and wellbeing of our employees. In the past year, we continued to improve on our health and safety performance. The key measure, total recordable injury frequency rate, which measures total lost time and medical treatment injuries per million hours worked, reduced further from 6.8 to 6.0. In June 2005 this rate was over 60, so we have made huge progress in the past decade and continue to seek to further reduce injuries. Particular focus was given in the past year to fire and explosive risk in our high temperature manufacturing processes, and other areas of manufacturing identified as high risk. In addition, new standards were developed for traffic management, with further new standards for machine guarding and isolation underway.

Canterbury

The next few months will mark an important milestone in Canterbury as the home repair programme comes to an end. Upon completion, Fletcher Building will have managed the repair of nearly 70,000 homes in addition to 59,000 temporary repairs and winter heating installations. This has been an enormous undertaking over four years, and I am enormously proud of the contribution our people have made to the reconstruction of the region.

Elsewhere in Canterbury, much work remains to be done but progress is encouraging. The infrastructure repair programme, SCIRT, has passed the half way mark. Construction activity in the Christchurch city centre is gathering pace, and Fletcher Construction was pleased to be awarded the contract to build the new Christchurch Justice and Emergency Services Precinct on which work has already commenced.

Priorities for the year ahead

Looking ahead to the next twelve months and beyond, our priorities will be to continue to capture the growth from the cyclical upturn in construction in New Zealand. In Australia, we will seek to lift earnings despite mixed market conditions.

As always, safety will be the number one priority. While the company has made excellent progress in recent years, we must maintain the philosophy of continuous improvement to ensure that our people get home safely every day.

Across the group, we will continue to improve the performance of each of our businesses as we further extend the operations excellence programme, particularly in the areas of manufacturing and supply chain.

In addition, we will expand the resources we have committed around marketing excellence, with a view to substantially lifting the effectiveness of our sales and marketing activities.

Other work programmes within FBUnite will be further progressed, as we seek to deliver an additional $25 million improvement in operating earnings for the 2015 financial year, and move towards our target of $100 million by 2018.

We will renew our focus on delivering better cash outcomes, through targeted reductions in working capital and further structure and process around capital investment decisions.

Finally, we will continue to actively manage our business portfolio, through actively seeking to divest businesses that no longer fit within our strategy, and through consideration of businesses acquisitions to augment our existing operations.

Tribute to Ralph Waters

Ladies and gentlemen, before I hand back to the chairman, I would like on your behalf to officially acknowledge Ralph's time here at Fletcher Building. This meeting is Ralph's last official duty as a director of the company and I think it appropriate at this point to reflect on the enormous contribution Ralph has made to the company over the past 13 years. Ralph, on a personal note I have greatly enjoyed my interactions with you, particularly over the past two years as we have collaborated as Chairman and CEO, and I look forward to our ongoing friendship. While your departure from the board doesn't mean an end to your working career, it does denote the end of an era. We wish you and your wife Helen all the best for the future and thank you for your long service to Fletcher Building.

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