# FLETCHER BUILDING LIMITED

**Annual Shareholders’ Meeting 2016**

**Chairman and Chief Executive Officer Speeches**

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**CHAIRMAN**

**Welcome**

Good morning ladies and gentlemen. Welcome to the 2016 annual shareholders’ meeting of Fletcher Building Limited.

We are delighted to be holding this year’s meeting in Christchurch in the beautiful Great Hall of the Christchurch Arts Centre, which was reopened just four months ago.

I advise that a quorum is present and the meeting is duly constituted.

This meeting is being webcast and I extend a warm welcome to those who are watching proceedings online.

# Directors

Before commencing the business of the meeting, let me introduce my fellow directors.

Tony Carter joined the board in 2010. He was previously managing director of Foodstuffs (Auckland) and Foodstuffs (New Zealand) and has extensive experience in retailing, including as a previous director and later chairman of Mitre 10 New Zealand. Tony is chairman of Fisher & Paykel Healthcare, Air New Zealand, and the Blues LLP, and is a director of ANZ Bank New Zealand and Avonhead Mall.

Alan Jackson was appointed to the board in 2009. He has been an international consultant since 1987 and was until 2009 chairman Australasia and a director of The Boston Consulting Group. He has proven experience at the most senior levels of international and government business. He is a director of Delegat Group and Chairman of NZ Thoroughbred Racing.

John Judge has considerable experience in Australasian business including most recently as the Chief Executive of Ernst & Young New Zealand. He is chairman of the ANZ Bank New Zealand and the Auckland Arts Festival Trust, a director of The New Zealand Initiative, and a member of the Otago University Business School Board of Advisors.

Mark Adamson was appointed Chief Executive Officer and Managing Director with effect from 1 October 2012. He joined the Formica Group in 1998 and became president of Formica Europe in 2004. Mark was appointed chief executive of Formica Corporation in 2008 and of the Laminates & Panels division in 2011. Mark is a member of the Institute of Chartered Accountants in England and Wales and the Institute of Taxation.

Kate Spargo was appointed to the board in March 2012. She has extensive business experience from advisory roles on strategic and governance issues following a career in legal practice in both the public and private sectors. She is Chairman of UGL, and a director of Adairs, Sigma Pharmaceuticals, Sonic Healthcare and SMEC Holdings (Australia). She is a fellow of the Australian Institute of Directors.

Cecilia Tarrant joined the board in 2011. She has over 20 years’ experience in international banking and finance in the United States and Europe. Cecilia is a director of Annuitas Management and Payments NZ, and deputy chairman of the Government Superannuation Fund Authority. Cecilia is also an executive-in-residence at The University of Auckland Business School.

Steve Vamos joined the board in 2015. He has more than thirty years’ experience in the Information Technology and online Media industry and has lived and worked in Australia, the USA and Asia. Steve currently serves as a non-executive Director of Telstra and is a member of the Advisory Board of the University of Technology Sydney Business School.

On my immediate left is Charles Bolt, our Company Secretary and General Counsel.

# Meeting Agenda

I will shortly provide an overview of the company’s financial performance for the year ended 30 June 2016. Mark Adamson will then address you and discuss the operating performance and progress against the company’s strategic priorities, and outline the key areas of focus for the year ahead.

At the conclusion of Mark’s presentation we will then take the opportunity for questions and discussion from the floor. I will outline the procedure for that part of the meeting when we reach it.

The formal proceedings this year comprise four resolutions, which are outlined in the notice of meeting. The resolutions will be decided by poll. Any questions from the floor will be dealt with before they are voted on.

# Fletcher Building in Canterbury

# Before I review the financial performance for the year I wanted to reflect on the reason we are holding our annual meeting in Christchurch this year. In choosing to come here this year, we wanted to acknowledge the progress that has been made in repairing and rebuilding the city following the earthquakes of 2010 and 2011.

# Each time I return to Christchurch I am impressed by the resilience of the Canterbury spirit and the increasing vitality of the city.

# The restoration of the Arts Centre is one of the highlights of the rebuild and the Arts Centre management and board are to be congratulated for returning this campus of Gothic Revival buildings to its former glory. Fletcher Building was pleased to contribute $4 million towards the renewal. Our construction division has been associated with this site since 2004 when it undertook strengthening work and more recently it led restoration of the Clock Tower and College Hall.

# Over the past six years, Fletcher Building has donated $8 million to Christchurch initiatives including the Mayoral Fund, the Canterbury Earthquake Heritage Buildings Fund, the University of Canterbury Earthquake Centre, and the McKenzie Willis façade.

# In addition to these heritage and research projects, we are proud to have played our part in supporting the arts and culture in Canterbury. Since the earthquakes, our construction, building products, and distribution divisions have supported the Christchurch Arts Festival, the Court Theatre, Art Boxes, Ilam Arts School, Christchurch Stands Tall, and the Centre of Contemporary Art.

# Our commitment to returning vibrancy to the city does not stop here. Our Residential and Land Development Division has committed $1 million for temporary use activities within the East Frame. As this development of 900 homes takes shape over the next few years, vacant lots within the development will be used for sporting, cultural and family focused activities.

# Fletcher Building’s involvement in large-scale rebuild projects such as the Canterbury Home Repair Programme, the Justice Precinct, and SCIRT is well known. We are equally pleased to have built 4 health care facilities, 3 supermarkets and 2 hotels for the city, in addition to over 50 new homes in Hornby and Farringdon.

# Fletcher Building is proud of its Southern roots which extend back to our first project in Canterbury that we undertook in Ashburton in 1920. We look forward to continuing our involvement in the rejuvenation of Canterbury.

# Review of 2016 Performance

Let me now briefly review the financial performance of Fletcher Building over the past year.

Net earnings for the year ended 30 June 2016 were $462 million, compared with $270 million in the 2015 financial year. This result included significant items totalling $37 million. Net earnings before significant items were $418 million, which was 5 per cent higher than the $399 million recorded in the prior year.

Operating earnings, that is, earnings before interest and tax, were $719 million, compared with $503 million in the prior year. Operating earnings excluding significant items were $682 million, up 4 per cent on the prior year and towards the top end of our earnings guidance range of $650 to $690 million which we provided at last year’s annual shareholders meeting.

Overall this was a good performance, and the growth in earnings was achieved despite declines in earnings from businesses we divested during the year as well as lower contributions from Fletcher EQR and the Stonefields residential development as these projects started to wind down.

Our cash flow performance was a particular highlight of the year, with cash flow from operations up by 15 per cent to $660 million. This increase was driven by higher earnings and reductions in working capital. We benefitted in particular from the cash realisation of working capital in our long steel manufacturing business, Pacific Steel, which ceased operations during the year. The growth in operating cash flow was despite increased investment in residential land in Fletcher Living.

Looking at our operating earnings performance on a geographical basis, and excluding corporate costs, New Zealand was up 6 per cent, Australia was up 31 per cent, while the Rest of World was 16 per cent lower.

In terms of the geographical spread of our revenue and earnings, a particularly pleasing aspect of the result has been the turn-around in our Australia operations, which contributed 23 per cent of operating earnings versus 18 per cent last year.

**Market conditions in key geographies**

Here in New Zealand, market conditions have continued to be very supportive. The past year has seen residential consents continue to rise, against a backdrop of rising net migration into New Zealand, and house price appreciation across most parts of New Zealand. Total construction activity in New Zealand has now surpassed the previous peak level experienced in the mid-2000s, and we expect this heightened level of activity to continue for several years.

In Australia, residential consents reached record levels, driven by further growth in consents for apartments. These have been running at record levels although in recent months they have tracked slightly lower, particularly in the multi-residential category.

In contrast to this trend the Western Australia new housing market weakened considerably during the year.

Operating earnings from our businesses beyond Australia and New Zealand were down 11 per cent, due mainly to performance issues with our Formica plant in the United Kingdom which offset higher reported earnings in North America and Asia. With a refreshed management team and good progress achieved during the year in improving manufacturing operations, we are confident of a significant turn-around in performance in 2017.

# Dividend

The total dividend for the year increased to 39 cents per share, up from 37 cents per share last year, and the increase was consistent with the growth in net earnings for the year. This corresponds to a pay-out ratio of 64 per cent of net earnings, which is within the target pay out range of 50 to 75 per cent. We continue to target a dividend pay-out ratio in this range, which has been set with the objective of allowing dividends to be maintained through changing market conditions over an economic cycle.

The final dividend was fully imputed for New Zealand taxation purposes. For the 2017 financial year, on the basis of current estimates, we expect to be able to fully impute both the interim and final dividends for New Zealand taxation purposes. At this stage we do not have sufficient franking credits to be able to frank the dividend for Australian tax purposes. We expect to be in a position to fully impute the interim and final dividends in New Zealand for the next three years.

# Total shareholder returns

# The total return to shareholders for the year to 30 June 2016 was 11 per cent, representing a combination of positive share price appreciation over the year and dividends paid. This past year has been one of exceptional volatility in equity markets which has at times impacted Fletcher Building’s share price dramatically despite a steady financial and operating performance. Looking back over the four past years since the new management team were appointed, total shareholder returns in aggregate have been 78 percent.

# Balance Sheet

In terms of our approach to capital management, there has essentially been no change. We continue to target credit metrics consistent with a strong BBB rating, although we don’t have a formal credit rating. We finished the year with significantly lower net debt; this was due mainly to the timing of the sale of the Rocla Quarry Products assets which we completed in January. With the completion of the Higgins acquisition at the end of July, this position has largely reversed and our gearing and leverage are in line with previous levels. This was a pleasing outcome given the additional investment we made in residential land during the year, and was a result of the good operating cash flows generated across the company. We expect to continue to maintain a sound financial position in the year ahead.

**Health and safety**

# Fletcher Building’s safety performance was stable during the year, and we are continuing our efforts to further improve our performance with an increased emphasis on the identification of risks and the elimination of serious incidents. We are determined to make further progress to reduce the incidence of safety-related events.

Our approach to managing the safety and health of our employees and contractors is governed by a board oversight process. In addition, we have an external assurance programme whose findings on our broad sustainability performance including health and safety are reported through to the board. Our leadership team and individual business managers are responsible for continuing to reduce risk and improving our performance in these areas. Senior managers short term incentive payments are partly linked to their health and safety performance.

During the year, our Construction division chief executive Graham Darlow was awarded Executive Leader of the Year at the New Zealand Annual Safeguard Awards for the work he led in the Christchurch recovery programme. Graham was recognised for forging a new safety culture with the work programmes we undertook for the Government and Christchurch City Council, in response to the earthquakes.

# Progress on Strategic Priorities

Over the past year we have made further progress in rationalising our portfolio of businesses.

In addition to the Higgins road contracting acquisition, the divestment of Rocla Quarry Products in Australia, and our new aluminium windows and doors joint venture with NALCO, we have also combined a number of businesses and revised our group structure, which we announced in February.

Looking forward our focus will be on pursuing our growth strategies and delivering further performance uplifts from our portfolio of businesses.

The organic growth areas we are prioritising include our residential development business in New Zealand, our civil and engineering construction business, and our distribution businesses in both Australia and New Zealand. While we remain open to further investment through acquisitions where we can see good returns and where such investments are sufficiently linked to our chosen growth priorities, these opportunities are likely to be limited in number.

Mark will provide further detail on our strategic direction shortly. In summary, we recognise that we must deliver further value from our existing operations, through revenue growth and market share gains, and through effective cost control and margin enhancement. This remains the number one priority for the board and management.

Let me now hand over to Fletcher Building’s Chief Executive, Mark Adamson, who will address you.

# CHIEF EXECUTIVE

Thank you, Chairman, and good morning ladies and gentlemen.

Sir Ralph has already discussed our 2016 financial performance. What I would like to do is review some of the operational highlights for the past year, and then discuss our priorities for the future.

I‘ll discuss our performance region by region, starting first here in New Zealand.

**2016 Operational Review**

As Sir Ralph has already mentioned conditions in New Zealand were very supportive for us and growth in the construction sector has been a major contributor to New Zealand’s overall GDP growth.

Volumes in most of our manufacturing businesses have tracked the growth in market activity overall.

The Building Products division is predominantly exposed to the New Zealand Construction cycle, and we saw good volume growth in most product categories:

Cement volumes were up 6 per cent, ready-mix concrete volumes rose 7 per cent, and plasterboard volumes were 11 per cent up on the prior year. Insulation volumes grew by 13 per cent.

Market shares in all other product categories were stable or slightly higher.

Our distribution businesses recorded good revenue growth, with PlaceMakers revenues up 10 per cent and Mico Plumbing and Bathrooms up 12 per cent and overall operating earnings up 13 per cent. Steel Distribution recorded operating earnings growth of 22 per cent, driven by good performances in Pacific Coil Coaters and Easysteel.

All of our New Zealand distribution businesses have benefitted from the strength of the construction cycle, but performance has also been driven by the focus on customer service, product range expansion, and cost control through initiatives such as the co-location of Mico and PlaceMakers stores.

Fletcher Construction had a record year, with revenue growth of 29 per cent. Total revenue for the division exceeded $1.5 billion for the first time, and the backlog at 30 June 2016 stood at $2.7billion, not including the Puhoi to Warkworth project for which we have been named preferred bidder as part of the Northern Express Group consortium. Construction earnings were up 5 per cent overall, with New Zealand 14 per cent higher and South Pacific 13 per cent lower.

Our residential development business, Fletcher Living, recorded 12 per cent growth in operating earnings, which was impressive given the reduced contribution from the Stonefields development in Auckland. We were able to accelerate the build out of other sites around Auckland and have benefitted from the strength of house prices. In addition, the team have made good progress in achieving the land supply we need for the next 3 years. Earnings also included a $10 million contribution from the development of surplus land holdings, and we expect ongoing earnings of around $25 million per annum on average over the next 5 years from this activity

Conditions in the Australian construction industry have been more mixed over the past year. While new housing construction was running at record levels, the industry has had to digest the impact of the slow-down in capital expenditure in the mining and resources sectors and a marked reduction in activity levels in Western Australia in particular.

Against this backdrop, we recorded a significant uplift in the performance of our Australian operations, with the 31 per cent growth in operating earnings a key feature. This growth rate was achieved through improved performances in a number of our businesses.

Three business recovery stories worth highlighting are Iplex Pipelines, Fletcher Insulation, and Stramit.

The turn-around of Iplex has gone really well, and the business finished the year ahead of budget, and was profitable in the second half. This improvement has been driven by increased manufacturing efficiencies, higher levels of customer service, and cost reduction measures. We expect to achieve further improvements in performance in the current financial year.

We’ve also had considerable success in lifting the performance of our insulation businesses in New Zealand and Australia, with earnings across this category doubling over the past year. We have re-opened our second Australian insulation plant at Rooty Hill in Sydney. You may recall this plant was mothballed five years ago when the government insulation scheme was abruptly terminated. We have made significant gains in market share in our Australian insulation business in the past year, mirroring the success we have had in New Zealand.

Stramit performed better this year with operating earnings up 43 per cent, and revenue up 1 per cent. We are seeing the restructuring and cost out programmes we initiated two years ago really bear fruit, as well as the focus on customers and delivering on the Customer Services Promise.

Tradelink recorded increased operating earnings, and as we flagged in April this was driven by the sale of their property in Waterloo, Sydney.

Looking at our international businesses, while operating earnings were down year on year, we did see good progress made in a number of regions.

Firstly, we have had a focus on addressing the manufacturing issues with Formica’s UK operations. The team have a clear plan to lift performance over the next few years, and we have already started to see operational improvements. Formica Europe traded at a breakeven level in the second half, after the operating loss in the first half.

North America recorded 4 per cent revenue growth in local currency terms, with 2 per cent growth in volumes, and continued earnings growth.

In Asia, we experienced good volume growth in China, and utilisation of our second plant in JiuJiang continued to rise, although we still have spare capacity.

Laminex achieved modest earnings growth in Australia after two years of double digit growth and good underlying growth in New Zealand. Earnings in the Roof Tile Group were stable, with growth in key markets offset by a significant decline in demand from key African markets.

**Strategic Priorities**

As we outlined in the annual report, we have over the past year been delivering on our priority areas of focus.

I have already touched on the progress we have made in our New Zealand businesses to capture the growth in the construction market. Similarly you now have a sense of the performance improvements we have generated in our Australian business portfolio.

At last year’s annual meeting we outlined the areas we had identified as offering the most opportunity. These were New Zealand residential development, construction in New Zealand and the South Pacific, and trade distribution in New Zealand and Australia. In each of these businesses we have differentiated capabilities, cost positions and customer relationships, and end-markets that offer substantial room for growth.

**Pursuing Organic Growth**

**1. Residential**

As we have already heard, Fletcher Living, our residential development business, had a record year in 2016.

We have ambitious plans to expand this business, with the ultimate goal of lifting the number of homes we bring to market each year from an historical average of 300 to 1500. To achieve this, we are working on three fronts.

The first is a continuation of our traditional activity where we buy completed lots from land developers. The second is the purchase of bare land for development with which we master- plan whole new communities. Third are our partnerships with the government to develop existing land with increased density to cater for a wider range of housing needs. Great examples of these can be found right here in Christchurch with our developments including Awatea Green, and the East Frame.

The expansion of our residential development business continues to require investment in land inventory to enable us to meet the goal of delivering 1500 homes a year. Last year we invested a further $89 million in land and work in progress, and expect to invest a further $160 million in the 2017 financial year.

**2. Construction**

Our Construction business continues to offer further growth potential.

We had signalled for some time our desire to extend our activities into the road construction and maintenance sector, where we have identified significant opportunity. With the completion in July of the acquisition of the Higgins contracting business in New Zealand and Fiji, we are now in a position to fulfil this aspiration. Higgins was a logical choice for Fletcher Building, as we have partnered with them on road construction projects for over 25 years and have forged a close working relationship.

The acquisition included the Higgins aggregates business in New Zealand, and the total purchase price was $303 million. We believe that a combination of Fletcher Building and Higgins will provide our customers with a more compelling proposition for both new road projects and maintenance contracts. We also see further benefits for a number of group businesses in being able to work more closely with Higgins, and believe that we can derive further value through operational synergies.

Higgins has achieved good growth in Fiji, and this business complements our existing South Pacific construction activities. We will be looking to extend the sphere of operations beyond Fiji into other South Pacific territories over the next few years

**3. Distribution**

The third area of growth is in our New Zealand and Australian distribution businesses. In New Zealand, we have seen PlaceMakers achieve record retained earnings, and Mico plumbing and bathrooms go from loss making two years ago to strongly profitable this year. In addition, we have seen further gains in our steel distribution businesses.

In Australia, we have continued to implement the turn-around of Tradelink. While underlying trading earnings were broadly flat on the prior year significant progress was made in executing against the strategy we put in place two years ago. The focus has been on cost-effectively expanding the store footprint, implementing a service guarantee oriented around the core requirements of the trade plumber, and on lifting the capability of people within the business.

In many ways our distribution businesses are at the heart of our desire to better serve our customers. Across all our distribution businesses, we have identified further organic growth opportunities, from improving our store footprint, developing complete customer solutions and expanding our product range into adjacent categories. We intend to invest in online platforms, and increasingly leverage our procurement capabilities to further source from low cost countries. Our portfolio of distribution brands provide us with the opportunity to drive deeper customer connections through the services and products we procure or supply.

**Efficiency**

During the year we completed a review to identify the potential to further grow shareholder value from our existing portfolio of businesses. Following on from this analysis, we developed a new approach that would enable us to deliver on the opportunity we had identified, over a three year timeframe and beyond. We have established clear targets for each business unit, grouped around the following three categories:

• Commercial – which consists of both revenue and product margin growth;

• Cost reduction – including both external expenditure and overhead costs; and

• Manufacturing and operational efficiency – including manufactured products, distribution costs and construction delivered margins. Called Accelerate, the programme leverages the capability that we built with FBUnite, particularly around procurement, property management, information technology, manufacturing excellence, and sales and marketing centres of excellence.

We have also established a Transformation Office to oversee the governance of the Accelerate programme, provide support and tools to each business unit, and coordinate resources. To date, over one thousand seven hundred initiatives have been started.

The success of the Accelerate programme will be seen in the results of each business unit over the next 3 years, and will potentially include higher revenue growth, improved gross margins and lower operating costs.

**Building our people capability**

The final strategic priority I want to touch on is our investment in people capability. We understand that, in order to better serve our customers and grow shareholder returns, we must continue to invest in our people and capability. This past year has seen a continuation of our mission to make Fletcher Building a great company to work for. This means ensuring that our people return to their homes safely every day, and that we build deep leadership talent pipelines for the future. It also entails investing to build capability across all levels of the organisation in an environment that fosters both high performance and high levels of engagement across all of our teams.

I’d like to make a special note of welcome to the 1,200 Higgins employees who joined Fletcher Building at the end of July, with the completion of that acquisition. Critical to the success of the Higgins businesses within Fletcher Building will be the integration of the newly acquired business with our existing construction and quarrying activities.

# Outlook

Let me now conclude by discussing the outlook for our key markets.

In New Zealand, every indicator points to another good year in the construction sector, with residential, commercial and infrastructure work expected to continue at record levels.

In Australia, we expect stand-alone housing construction in Eastern States to remain steady at current levels, while apartment construction may start to ease. We see the non-residential markets remaining steady but expect low growth in the commercial and government infrastructure sectors. Activity levels in Western Australia are likely to remain well down on previous years.

Further afield, we expect reasonable growth to continue in Asia and North America, while Europe is likely to remain mixed but with reasonable prospects for the key UK market.

In terms of financial guidance, there is no change to the earnings outlook we provided in August when we announced our full year results. Operating earnings for the 2017 financial year are expected to be in the range of $720 to $760 million, versus the $682 million we delivered in the 2016 financial year. The incremental earnings from Higgins are expected to fully offset the loss of earnings from Pacific Steel, Rocla Quarries and Fletcher EQR. One factor which may impact the final result is the New Zealand dollar. This has been relatively high in recent months and is currently trading above budgeted levels against both the Australian and US dollars, which is adversely impacting the translation of overseas earnings at present.

Thank you for your attention ladies and gentlemen, let me now hand back to the chairman.

# CHAIRMAN

Thank you, Mark.

# General business

Ladies and gentlemen, I would now invite you to raise any matters in relation to the activities of the company on which you would like to hear our views. Mark or I will attempt to answer your questions, but if necessary we have the other board members, senior company executives and the auditors present.