

# Formica Europe – Presentation to Analysts

**September 2010**

# Agenda

## **Business Environment**

- Locations & Workforce
- Product Portfolio
- Geographies, Channels and Market Shares
- Industry Structure

## **Regional Economics**

- Current Scenario
- Regional Analysis

## **Situational Assessment**

- Current Financials
- Restructuring
- Situation Analysis

## **Strategic Outlook**

- Strategic Options

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# Formica Europe manufactures at five plants and operates across Europe, India & the Middle East with 80% revenue coming from UK, France, Holland, Spain & Scandinavia

## Europe

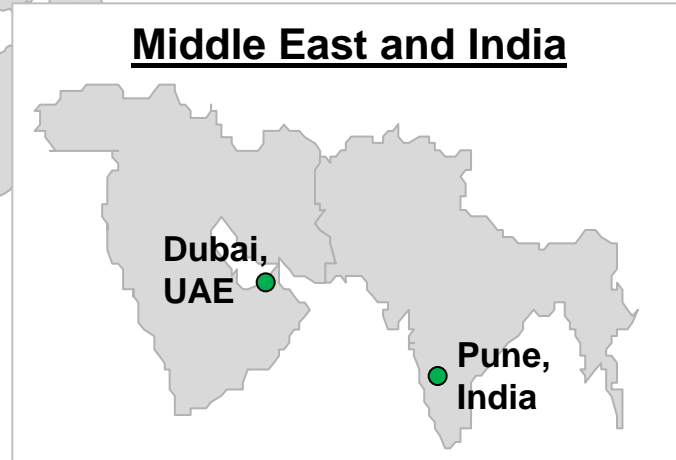
- Manufacturing, Warehouse & Sales Office
- Warehouse
- Sales Office



- Headcount:
 

Direct Manufacturing	700
Indirect	500
<b>Total</b>	<b>1,200</b>
- Major Product Lines:
  - HPL, CPL, Compact, Worktops

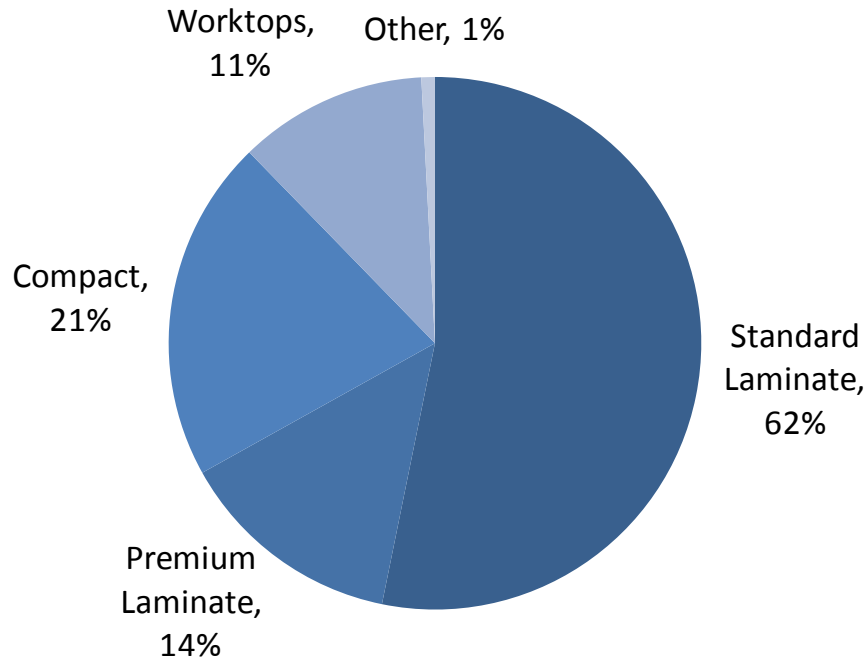
## Middle East and India



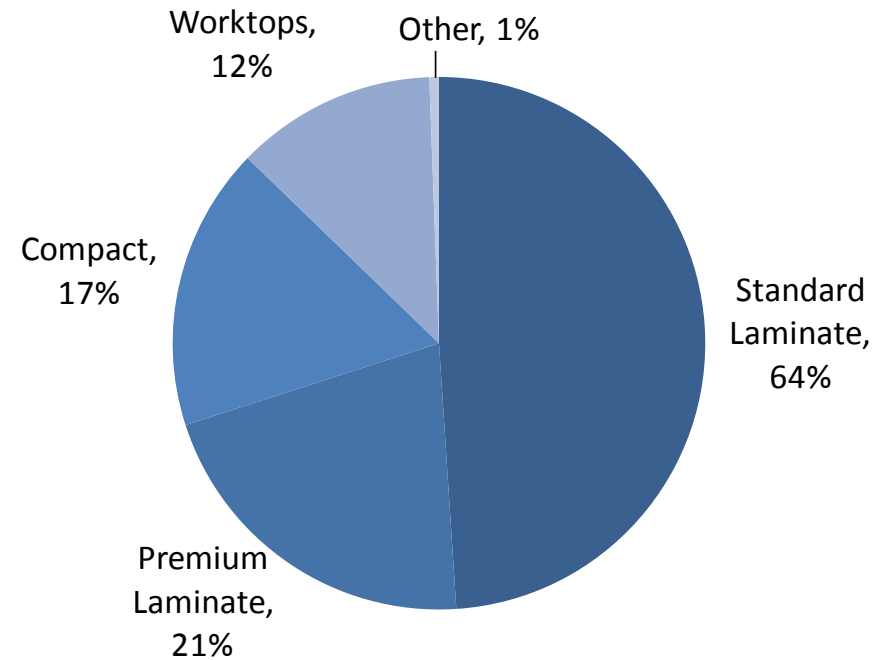
Source: Formica operations data, Formica Financials

# Sales revenue is principally derived from HPL, CPL, Compact and Worktops with the majority of revenue & margin delivered from HPL

## Revenue % by Product Line



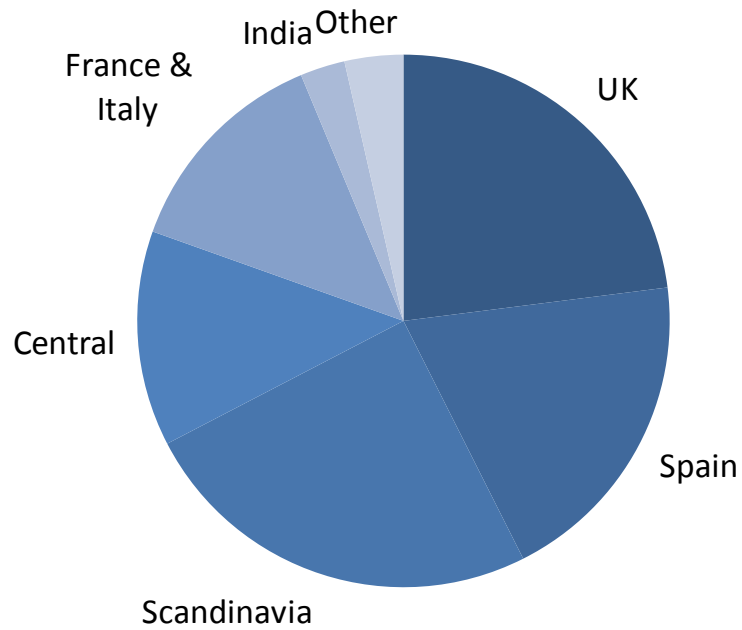
## Gross Margin % by Product Line



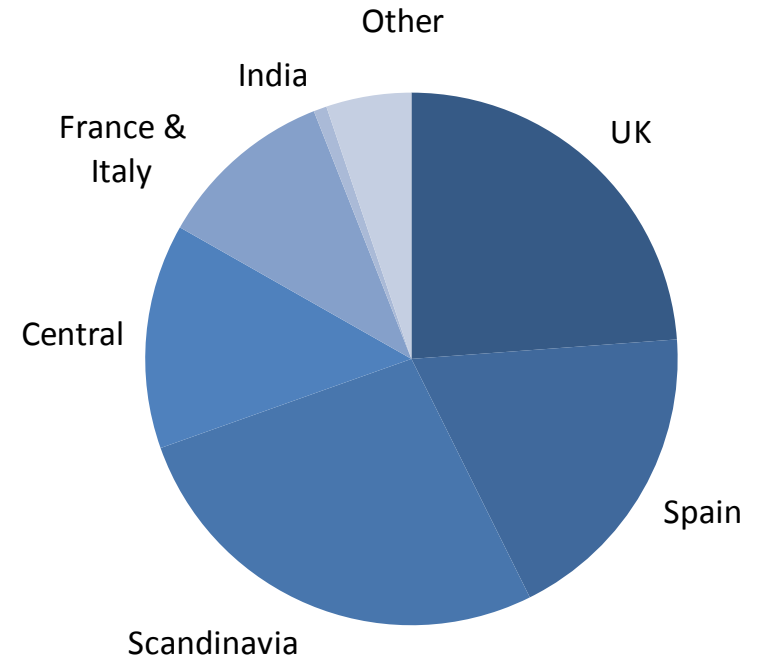
- **Standard laminate** is where the majority of earnings originate, in 1) the specification market, high margin but high supporting costs or 2) the fabrication channel, lower margins but limited costs
- **Premium laminate** (Metallics, ColorCore & Premium finishes) is a revenue stream with strong margins
- Bonded **Worktops** are a strong EBIT generator in the UK & Scandinavia
- Current **Compact** volumes are split 80% Interior and 20% Exterior with the Exterior business currently only in Scandinavia and Spain.

# Both Revenue & Margin streams are spread over a large number of countries

Revenue % by Region



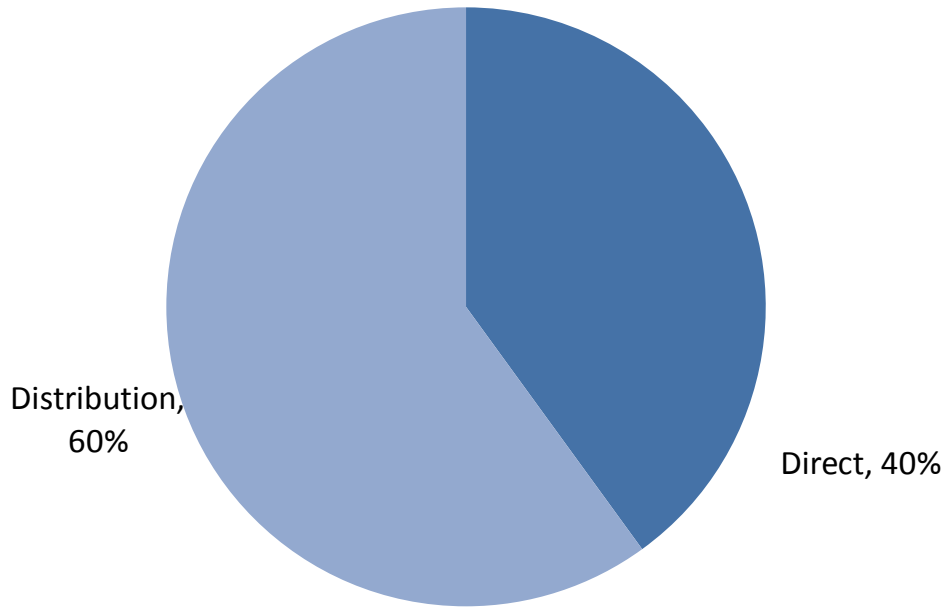
Gross Margin % by Region



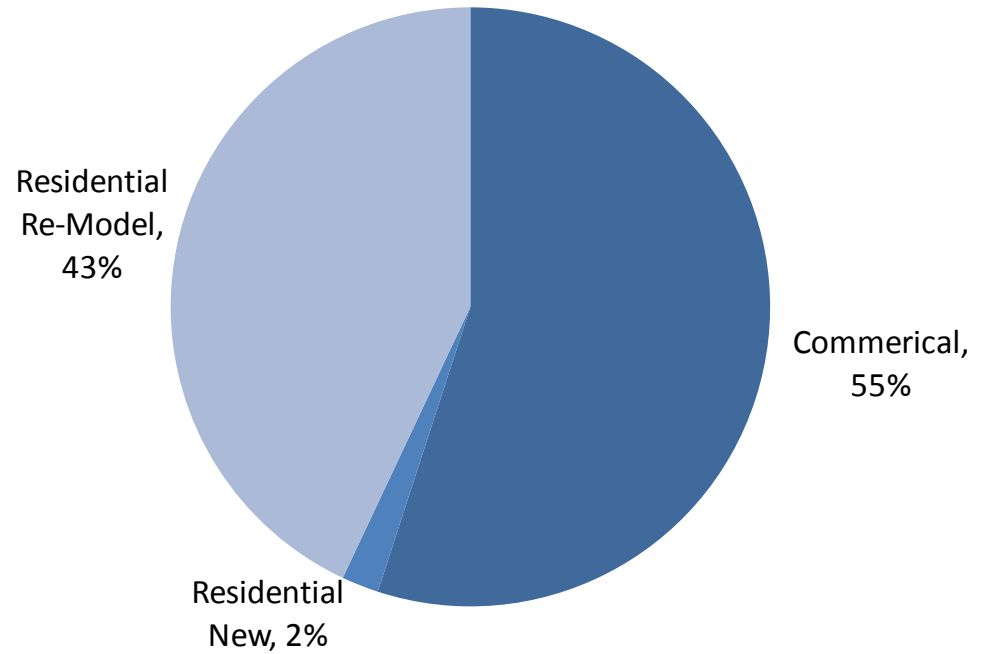
Source: Formica FY11 Plan

# Product moves predominantly through Distribution and is sold primarily into the commercial specification sector—new housing is just 2% of the business

Revenue % by Channel



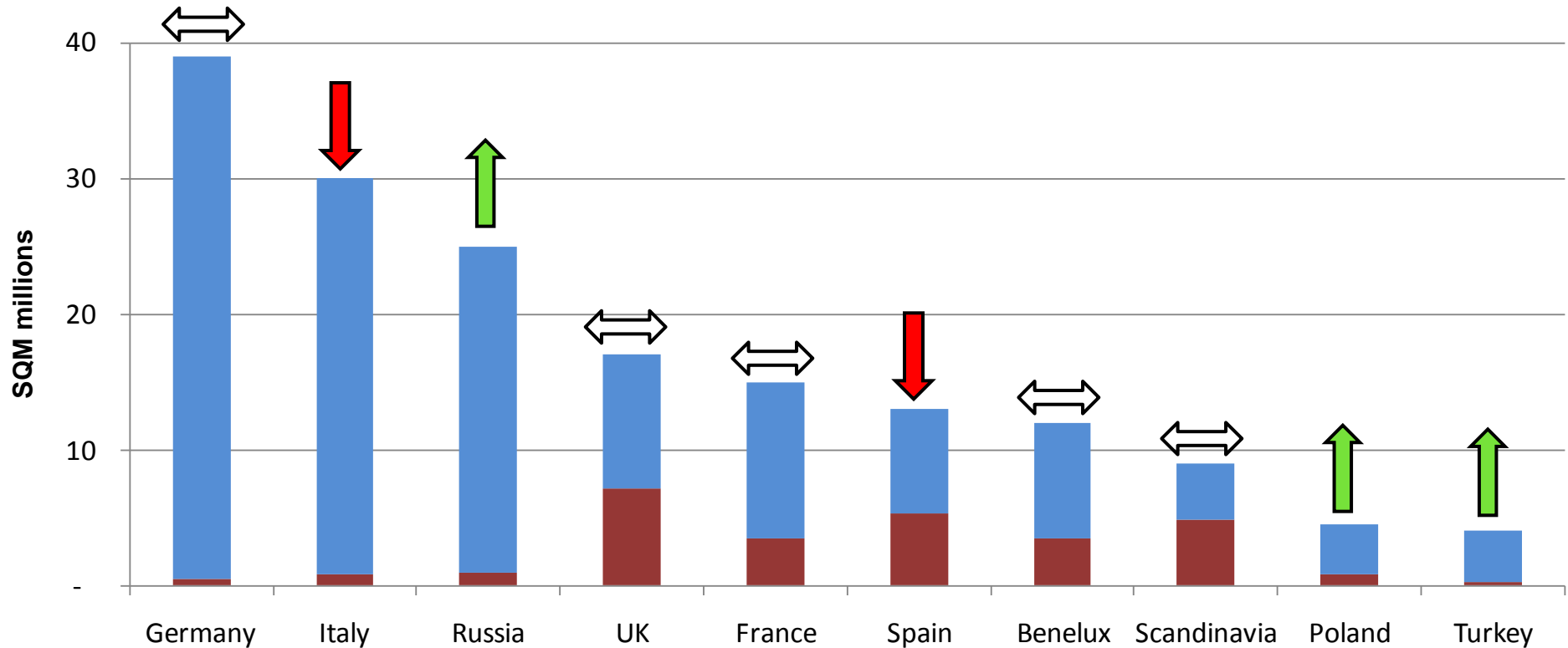
Revenue % by Sector



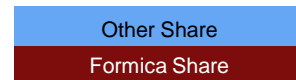
Source: Formica FY11 Plan

Market shares have been mainly stable over the past five years and vary from +40% in the UK and Northern Europe to low single digit shares in Russia, Italy and Germany

### European Market Sizes and Formica Shares



Formica Manufacturing



Source: Formica Management Estimates, Industry Reports



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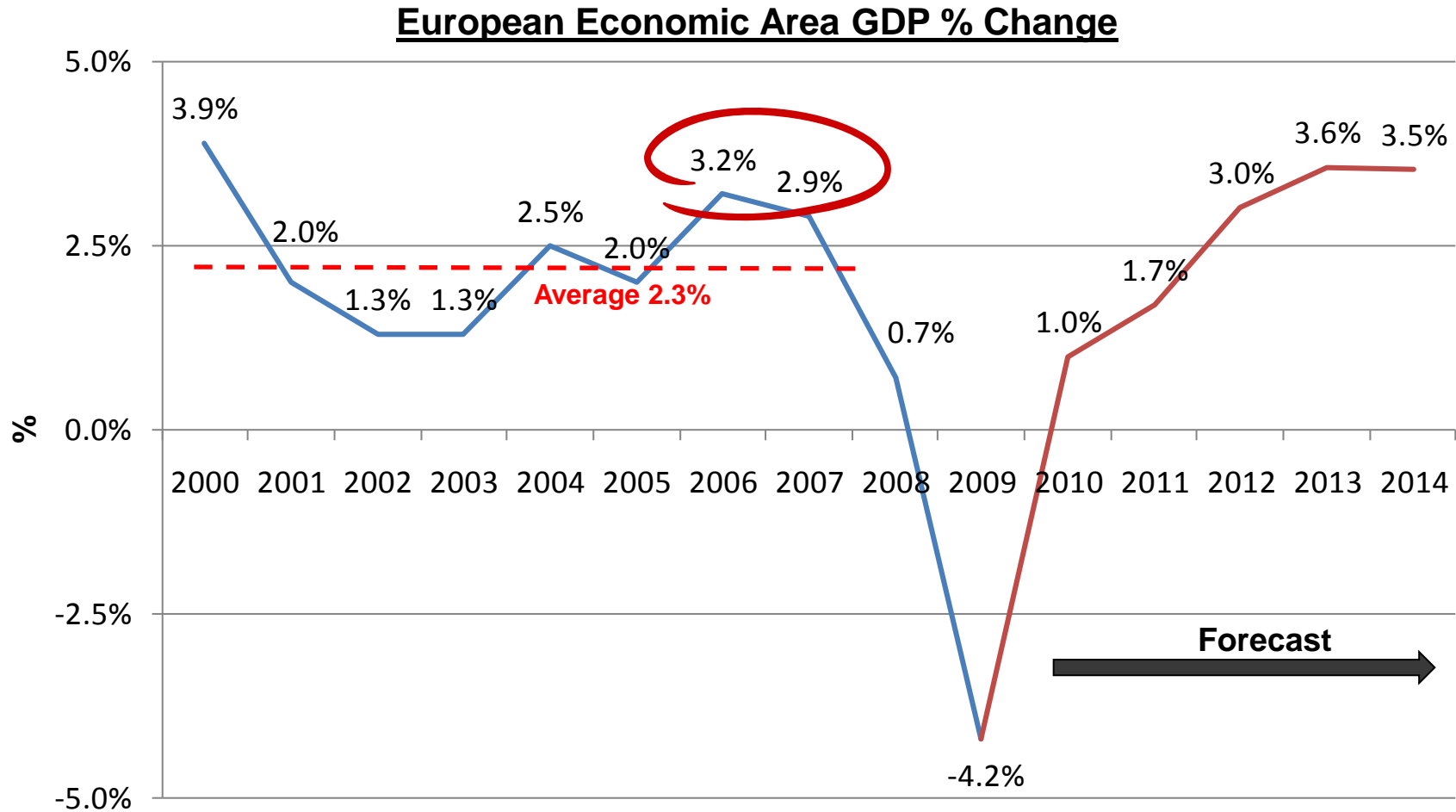
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Since 2000 the European economy has grown steadily at an average of ~2.3%. Europe was hit by the Global downturn in 2009, however, GDP recovery has started



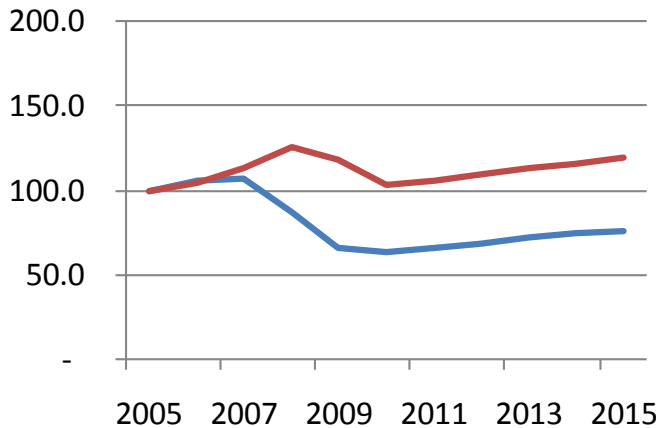
The growth predictions vary widely by market, Eastern & Central Europe are forecast to recover and grow quickly, with Spain lagging by ~1 year.

Source: Eurostat, EU stats body, <http://epp.eurostat.ec.europa.eu/tgm/download.do?tab=table&plugin=0&language=en&pcode=tsieb020>

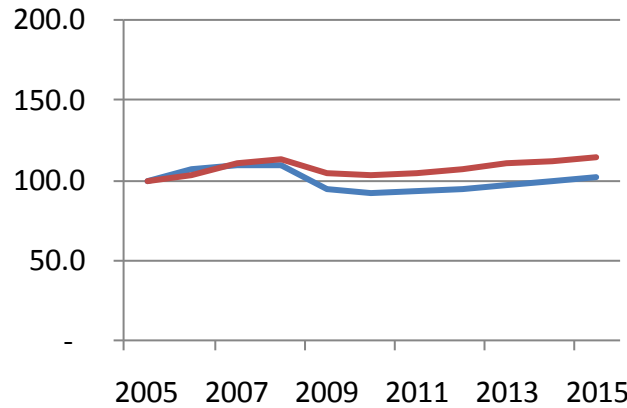
Recoveries in spending occur in all markets by 2012, however, given the lag between construction & laminate demand, major volume growth looks unlikely in the short term

**Construction Spending Index (2005 = 100)**

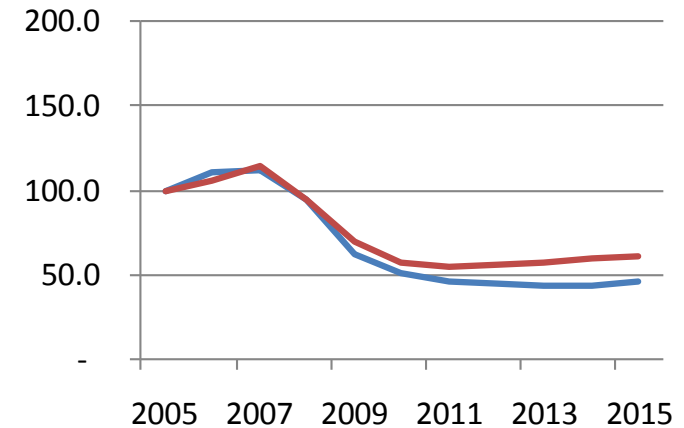
**UK & Ireland**



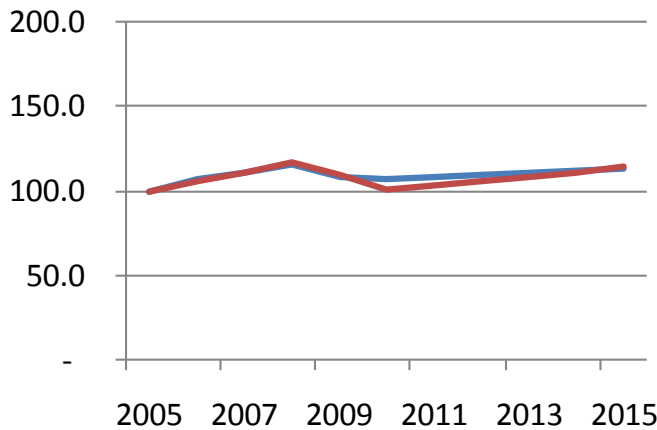
**France & Italy**



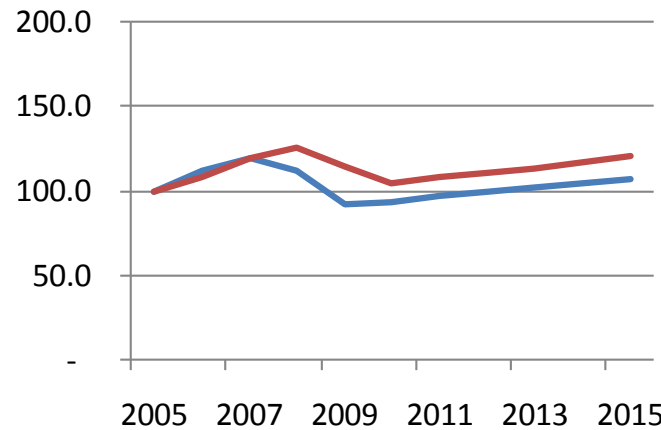
**Spain**



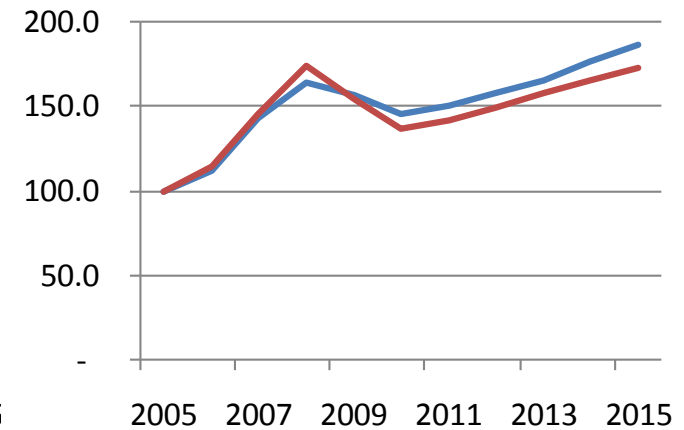
**Central Europe**



**Northern Europe**



**Eastern Europe**



— Residential — Non Residential

Source: Global Insight, August 2010

# Targeting growth in the developing markets will offset flat trading conditions forecast for the developed markets

## Developing Markets – growth opportunities

<u>Country</u>	<u>GDP</u>	<u>Laminate Market</u>	<u>Actions</u>
India	+8% in 2010 double digit forecast in 2011	Four times the size of the German market	Market entry strategy established
Russia	+15% over 3 years	Set to double in 5 years	New distributor appointed New country director appointed Increased resource
Poland	+25% over 5 years	Set to double in 7 years	Develop market growth strategy

## Developed Markets – market share gain

- Re focus on specification channel through new Collection
- Maintain residential positions
- Use cost to serve model to improve margin
- Share gain in the German market via a new distribution model
- New product launches

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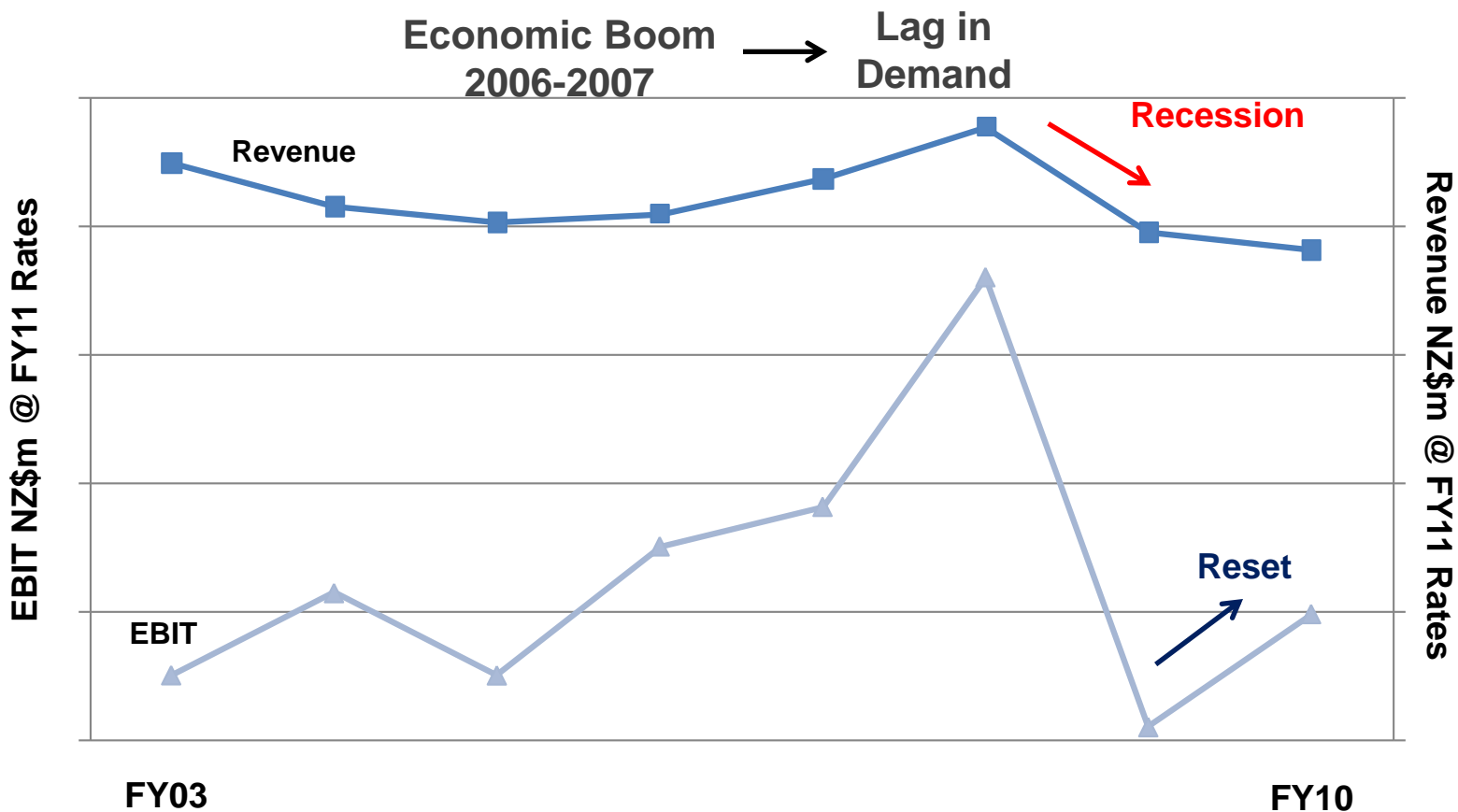
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# FY08 saw a substantial increase in EBIT due to strong revenue growth and the 1<sup>st</sup> phase of the European restructuring programme

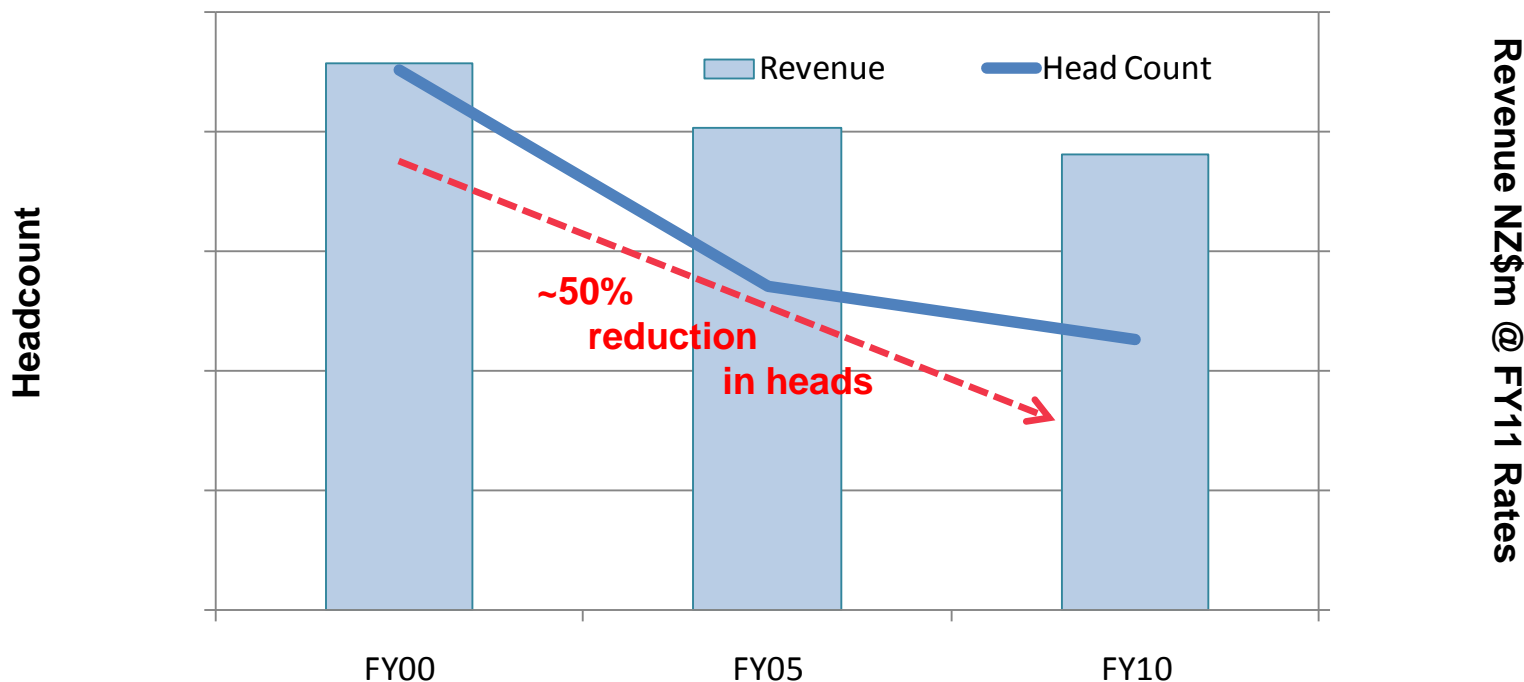


With major cost reductions completed, EBIT growth will be driven by capturing new revenue streams and further restructuring of the footprint

Source; Formica FY11 Plan, EBIT excludes any restructuring charges

# The European business has gone through numerous restructuring programmes aimed at cost reduction & centralisation in order to create a unified European business

## FY00 – FY10 European Headcount v Revenue



- As well as the closure of 3 facilities, Burstadt (Germany), Christchurch (UK) and Quillan (France) aggressive headcount reduction has taken place
- A centralisation project has also been completed with the functions of Finance, Customer Service, Logistics, HR and IT now based at the European head office in the UK

**In addition to headcount reduction projects, in 2009 the Reset project was launched to deal with inherent profitability issues**

Source; Management Information

# The Reset Project has realigned the product offering, shifted the focus to profitability by customer and altered the mentality around all aspects of procurement

## Reset Programme

### Direct Procurement

- Rationalisation of the décor pool completed with a 61% reduction in the décor offering and large cost savings
- All orders now placed centrally with all Formica facilities grouping

### Indirect Procurement

- Procurement function established with key commodity managers in place
- Restructuring of the freight routes around Europe with a tender process completed to reduce freight costs

### Customer Profitability

- New commercial policies have been introduced with strong acceptance from the customer base
- A project to implement a live “Cost to Serve” is also complete, giving the sales teams access to level and SKU level profitability
- A customer by customer profitability exercise was completed with actions in place and delivering results

### Product Profitability

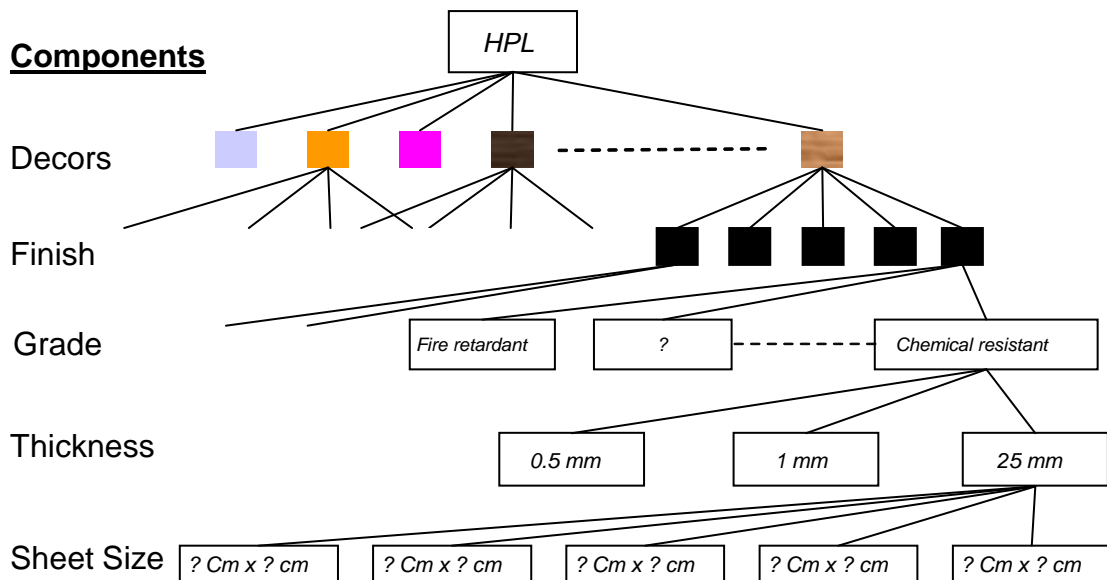
- Withdrawal from loss making products such as Solid Surfacing & Veneers
- Rationalisation of the grades, finishes, thicknesses and sizes offered to customers, reducing most of these variations by half
- Reduction in SKU's from 220,000 to less than 40,000, targeting a further reduction in FY11

### Manufacturing

- Realignment of production volumes and head count across all European facilities completed
- Restructuring of the logistics functions in Europe



# Complexity has grown over the years due in part to the almost infinite number and combination of product permutations leading to increased costs that erode EBIT



*Number of SKU's*

Original	Current	% change
3,004	1,179	-61%
106	25	-76%
82	20	-76%
86	25	-70%
262	100	-61%
225,765	25,000	-89%

## Proliferation = Operational Complexity & Inefficiencies

**Decors** – Increases raw paper obsolescence and impedes procurement efficiencies

**Surface Finish** – Increases maintenance costs and consumes excessive capital for plates

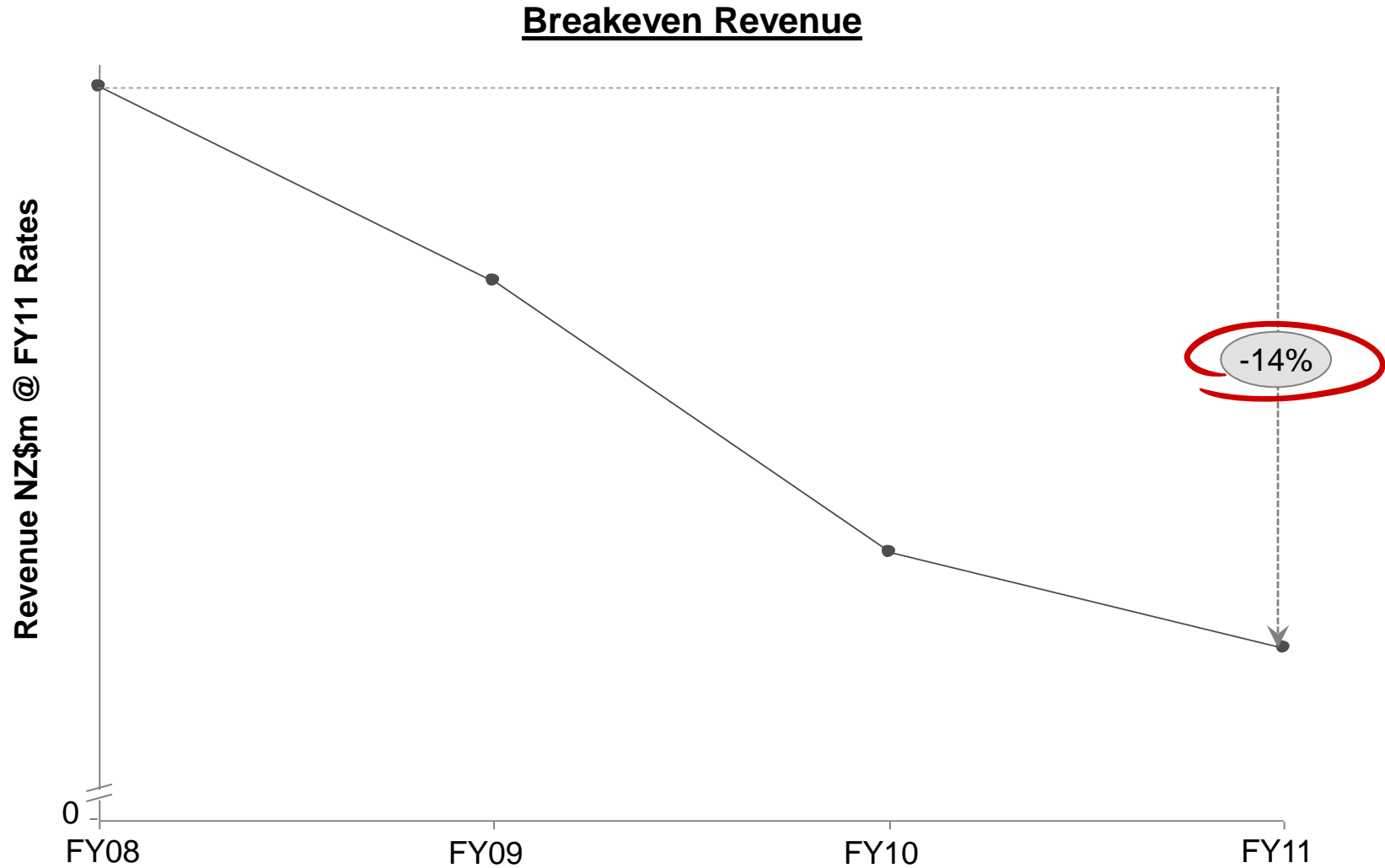
**Product Grades** – Drives extra inventories, and unnecessary slow moving products

**Laminate Thickness** – Produces unnecessary variations and adds cost while negatively impacting service

**Sheet Size** – Adverse impact on press yields, and complicates production scheduling

In addition to reducing and restricting the number of components, a key element of SKU rationalisation has been to limit the combinations in which these components are offered

# The centralisation projects and the reset programme has helped drive the break even point down by 14%



Source; Formica normalised Financials, excluding restructuring costs, pension costs and JV income, not including India sales and costs

# There is now a clear path to long term profitability through an aggressive revenue growth strategy

	Completed so far.....	Strategic options.....	
Revenue Growth	<p>Initial expansion into developing markets, e.g. Russia, Poland, Middle East &amp; India</p> <p>Product development in core product line e.g. new collection, new finishes etc</p>	<p>Re-position product offer to gain share of new trends</p> <p>Build on the success of bonded components</p> <p>Acquisitions</p> <p>Exterior Compact</p>	<p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p>
Variable Cost	<p>Global procurement of all major raw materials and centralisation of controls around spending</p>	<p>Additional step change in variable costs requires a significant capital investment</p>	
Factory Fixed Costs	<p>Completed closure of three manufacturing facilities</p> <p>Major indirect headcount restructuring program</p>	<p>Realignment of manufacturing footprint to meet market demands</p>	<p>✓</p>
SG&A	<p>Centralisation of all back office functions</p> <p>Lean cost management through all departments</p> <p>Closure of regional sales offices</p>	<p>Limited scope for further major cost reductions</p>	<p>✗</p>

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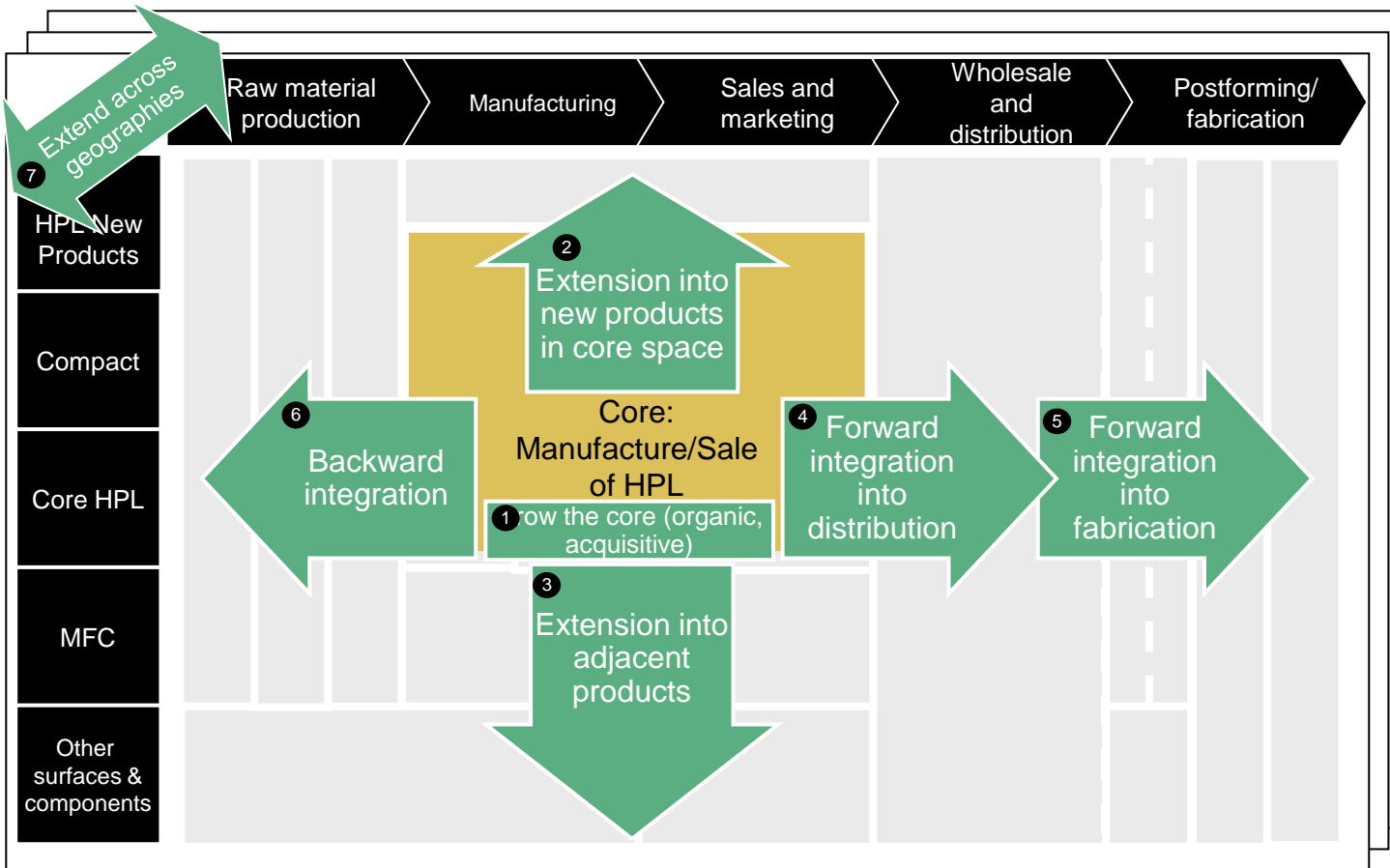
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# There are a strong set of strategic options for Formica Europe to consider



Note: Areas do not represent size

- 1** Primary focus of growing the Core both organically and through selective acquisitions
- 2** Continued leveraging of HPL innovation, particularly in Developed markets to drive share gain
- 3** Exterior compact
- 5** Exploit worktop opportunities
- 7** Geographic expansion as market development permits (i.e., into Russia, Turkey etc)

# Over the next 3 years, Formica Europe will implement the following projects to deliver the strategies below that will ensure long term profitability and strong returns

- 1 **Revenue Growth Strategy:** *Several opportunities exist to grow revenue and market share*
  - Exterior Compact
  - Worktops
  - Extra Large Format Laminate
- 2 **Manufacturing Footprint Optimisation**
- 3 **Geographic Expansion**
- 4 **Industry Consolidation**

Once these strategies are successfully completed, the European business will deliver strong shareholder returns

# The revenue growth strategy is three fold

1

## Exterior Compact

- Large opportunity
- Routes to market established
- Range defined

2

## Worktops

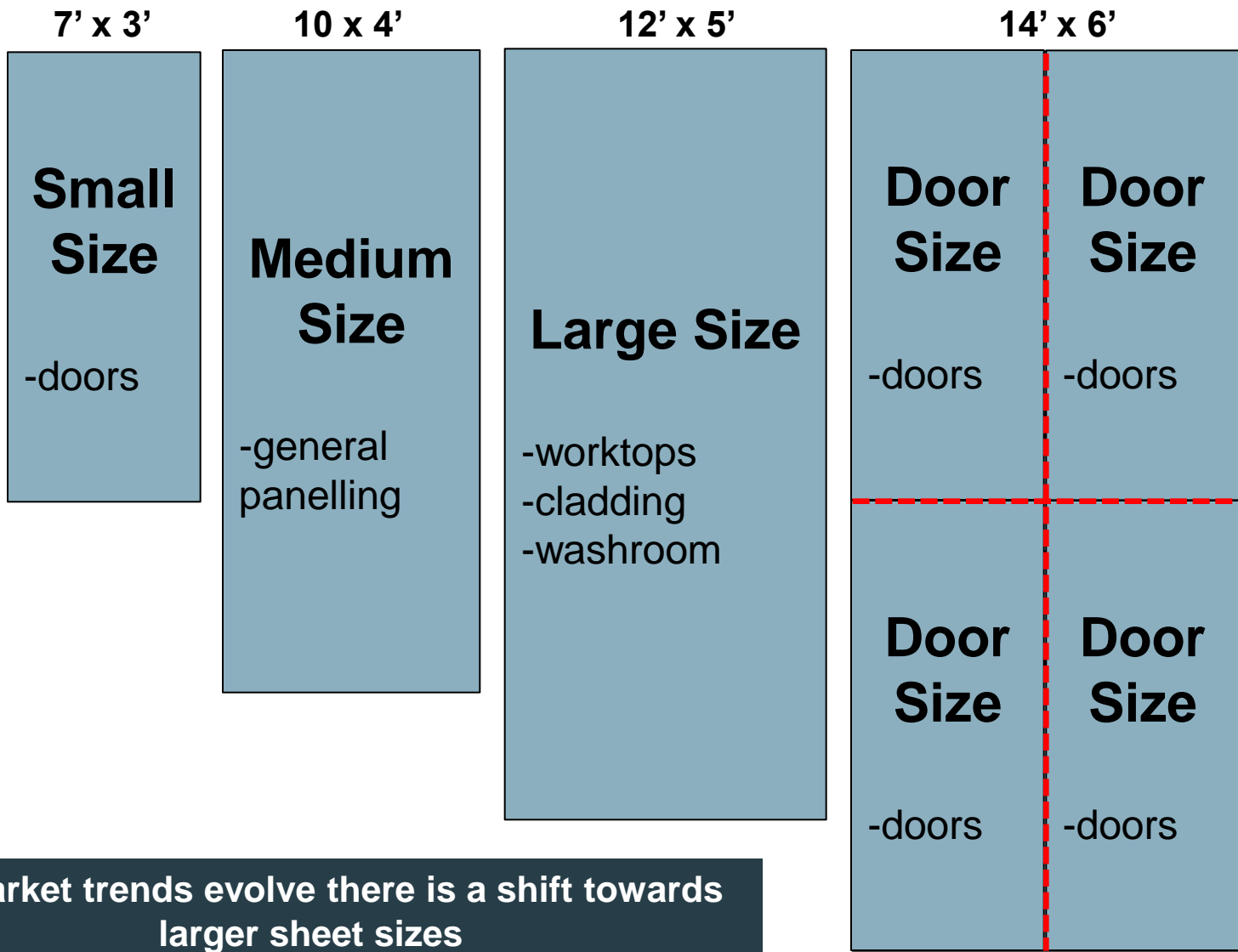
- Routes to market identified
- Brand established in the UK
- Significant opportunity to role UK model into Europe

3

## Extra Large Format Laminate

- Would need major investment
- Substantial opportunities exist

**1.3** The laminate industry supplies four main sheet sizes which relate to particular applications



As market trends evolve there is a shift towards larger sheet sizes



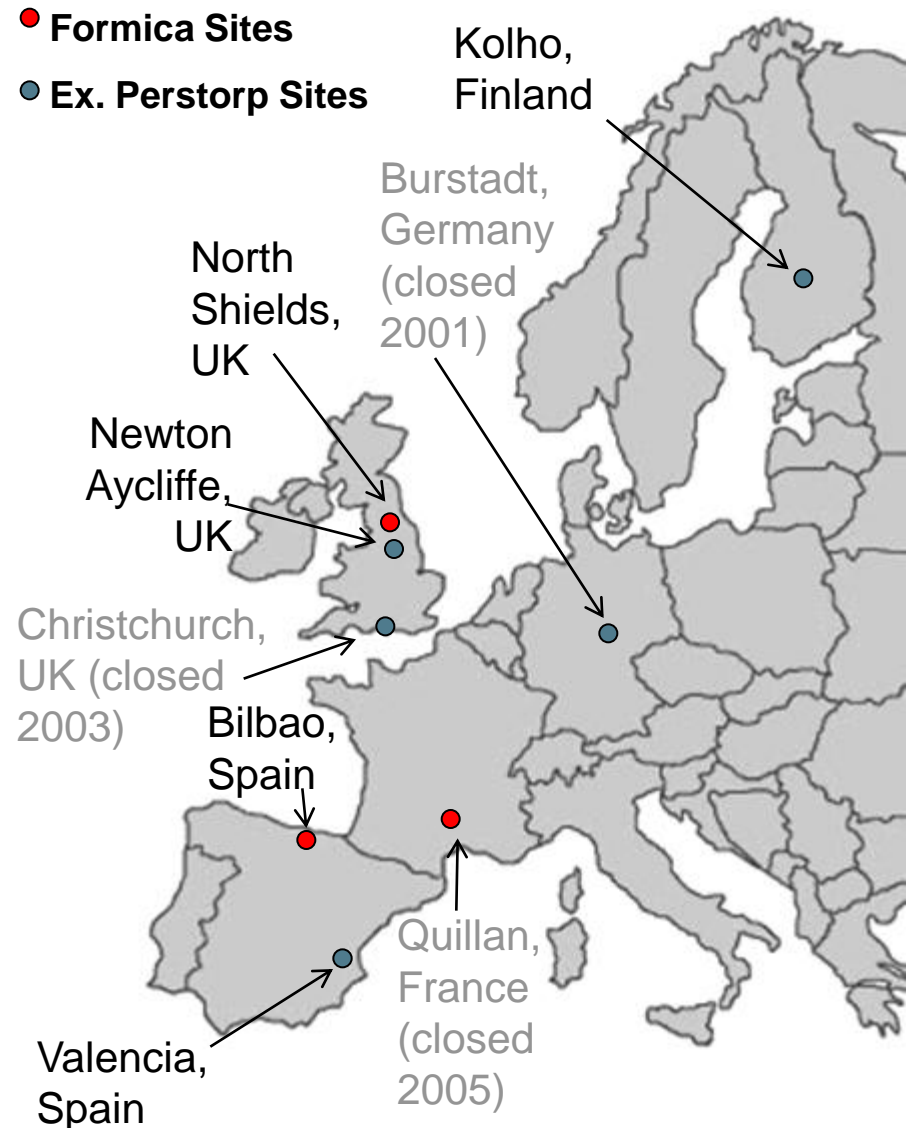
**1.3** There is a significant market for extra large sized laminate mainly focused around washroom cubicles, cladding and kitchen work surfaces in our core markets

	Doors	Cladding	Kitchen Worktops	Washroom
Extra Large	Reduce manufacturing costs	Extra larges sizes give design flexibility & cutting optimisation	Industrial channel demands 4.2m length. CPL production limits texture	Legislation & design driving towards deeper full height cubicles
Large		Our largest existing size is smallest competitor size	Trend to thicker & wider tops demands wider tops	Demand influenced by cubicle design & manufacturers' processes
Medium		Reducing demand as trends shift	Mainly focused on the big box market	
Small	Migration to 2350x1300 for specialist applications & physical changes			

Source: market surveys, management estimates

## 2 The merger of Formica & Perstorp in 2000 created an unbalanced manufacturing footprint that has partially been addressed through the closure of 3 facilities

- Although volumes dipped significantly during the economic crisis, **all presses are still required to meet the complexity of sheet size and product finish demanded.**
- The recent economic downturn has exposed the high fixed costs base of having 5 sites.
- However, the alignment of production volumes and head count across all European facilities has been addressed through the downturn
- To penetrate untapped market opportunities and to further increase our flexibility, we are conducting a study on introducing extra large format capability



## The Indian laminate market represents a significant opportunity for growth

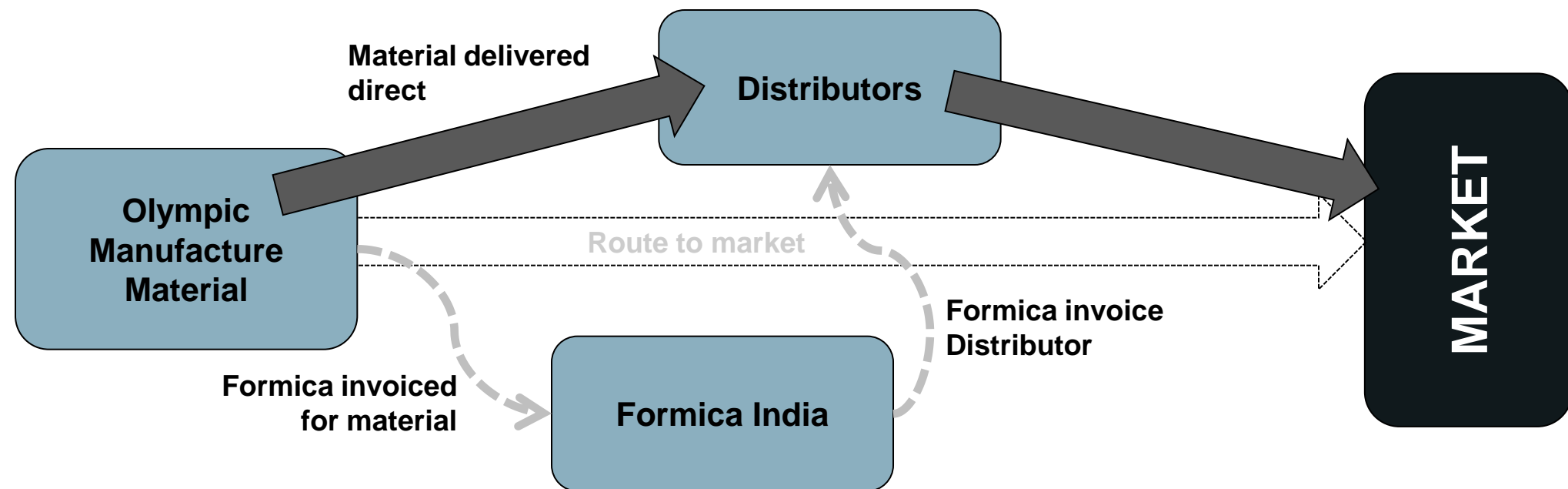
### Market Overview

- India is one of the **fastest growing** world economies with a healthy and developing laminate market
- The market is estimated at around **200m SQM**, with 40% low price & quality product that does not represent an attractive market but 60% is “structured” with **good opportunities for earnings**
- There is **no one dominant player** in the market with a large number of small producers
- Under licence, the Formica brand has been active in India for **over 45 years**, with that licence ending in 2009, we have now setup a trading entity in India



### 3 Formica is supported by a local Indian manufacturer with a strong supply chain, we have also directly employed strong local management to drive growth

- Laminate is sourced from a local supplier Olympic Laminates which is a well established manufacturer with over **30 years experience** in the industry. Both the **quality and service** from the supplier has been excellent
- **No volume guarantees** or liabilities regarding any raw materials have been given.
- The business was launched in spring 2010 with a series of marketing road shows around India to launch the **new specification collection** to architects and designers



# 3 As well as the promotion of local Indian manufactured laminate, there is also an opportunity to sell European produced premium products into the market

- Living standards increasing rapidly with strong GDP growth
- Early market entrants can guarantee share and market position
- Therefore, introducing products such as ColorCore, Compact, Metallics and Veneers represents a significant market positioning opportunity

**Metallic Laminate**



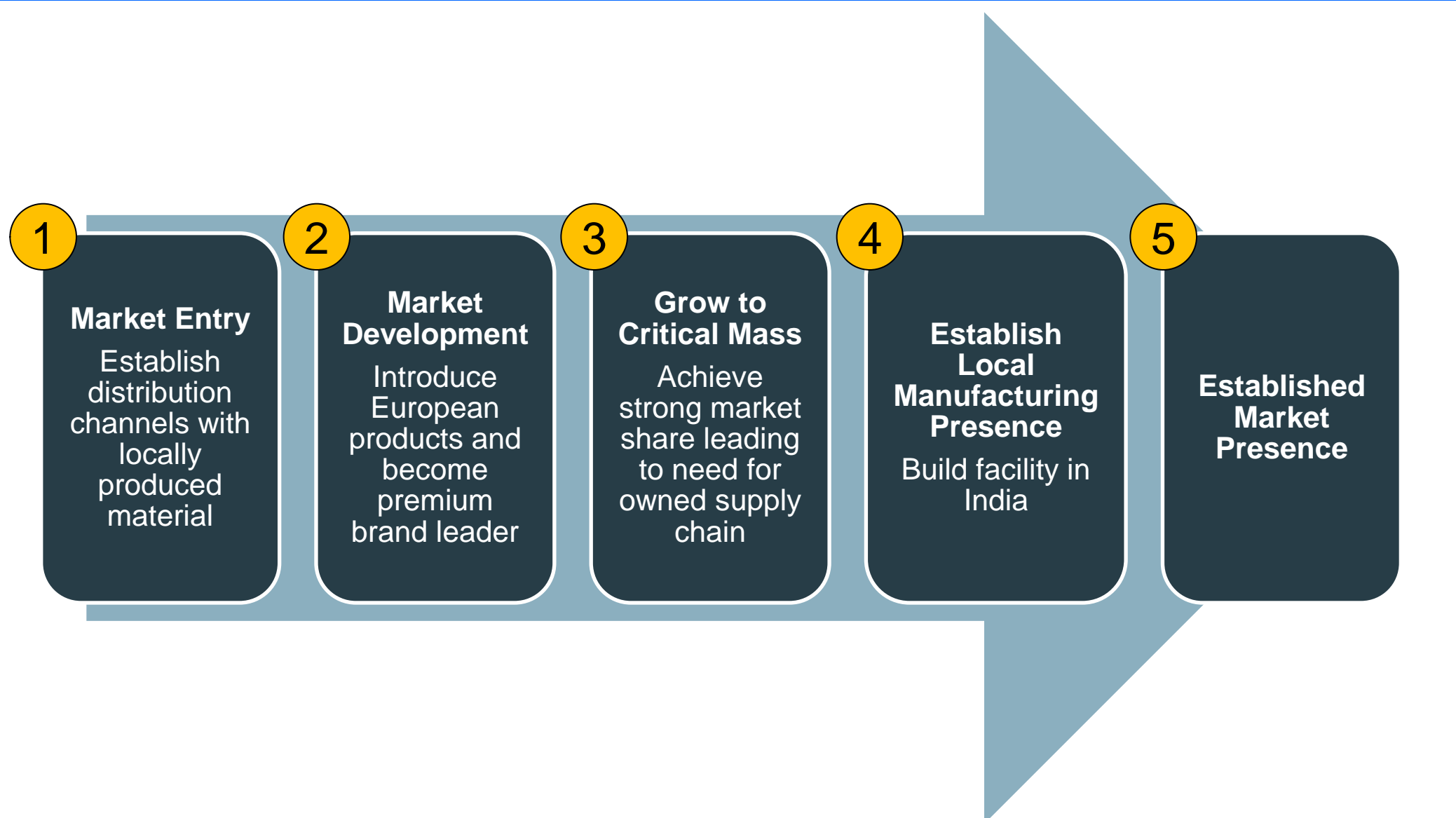
**Compact**



**ColorCore Laminate**



**3 Growth projections show that a local manufacturing presence will be required as a critical volume mass is reached to achieve a dominant market position**



**4** The European laminate industry is highly fragmented with little opportunity for consolidation

