Salmat Limited results for the year ended 30 June 2008

Presentation speech, August 2008

<u>Phil Salter:</u>

Title slide

Good morning and welcome to our presentation today, covering Salmat's results for the year ended 30 June 2008.

I'm Phil Salter and I'll be presenting along with Peter Mattick and our Chief Financial Officer, Colin Wright.

We've got attendees both here in person as well as on the teleconference line. We'll provide an opportunity for everyone to ask questions at the end of the presentation, so I'd ask that you all hold any questions until that time.

Highlights slide

The past year has been one of the most significant on record for Salmat.

We've continued our long history of year on year top line growth to once again post record sales revenue of $812 million.

This was achieved thanks to increased operational volumes in each of our three key divisions. That's a great achievement, especially in some of our traditional markets which remain under competitive pressure.

This was also a landmark year in terms of us making our largest ever acquisition, with the purchase of HPA. There was a great effort made to get this deal over the line and it was successfully completed in November 2007. There's also been a lot of work done since to bring HPA and our former BPO division together. It's been a really positive initiative and we'll be covering the integration in more detail later in the presentation.

We also launched our new Lasoo website in November 2007. We've had a very encouraging response to the site and the related online services offered under the DigitalForce banner. Lasoo fast became Australia's number one pre-shop website and has consolidated that position ever since, with massive growth in both visitor numbers and time spent on the site.

In our catalogue business, we entered into a joint venture during the year with New Zealand Post to strengthen our presence and capabilities in the NZ market. Reach Media is now coming together onto a common operating platform and we expect good results over the next two years as the joint venture develops its full potential.

In the contact centre field, we opened two new centres: one additional local facility in Melbourne and a new facility in Malaysia.

The offshore centre and the @Home model we rolled out during the year really complement our other services. We now offer clients an unrivalled choice along the full spectrum, from low-cost, low-complexity services to highly sophisticated solutions.

Following the $300 million purchase of HPA, we are also very happy to have brought our debt down to $219 million at year end. This was due to working capital initiatives and a capital raising. Our gearing is now within our targeted range of 40-45%.

Finally, with all the new acquisitions and service launches over the past few years, we decided to review our branding and bring all of our various divisions together under a consistent visual standard during the year. We've supported this with an advertising campaign, communicating Salmat's market-leading abilities and overall strength as a group.

Rebranding divisions slide

You can see here that we've got the three key divisions and four brands under the Salmat group.

A key part of Salmat's value proposition for clients is that they can draw on the services of any number and combination of these divisions to achieve their communication objectives. We can help them design and implement a totally integrated program that combines, for instance, contact centres, face to face sales staff, online and offline targeted catalogues, personalised essential and direct mail, email and SMS communication and the receipt and processing of inbound customer responses. This is total communication outsourcing and is unique to Salmat.

Financial summary slide

Looking at a summary of our key financial movements, you can see we've recorded strong increases in sales revenue and earnings before interest, tax and amortisation. Our EBITA before significant items is at the mid-point of the $55–60 million guidance first provided in February 2008 and reaffirmed in July.

Our net profit after tax result was also in line with the guidance provided last month. This result was impacted by several one off factors, primarily relating to Lasoo development costs; costs incurred through the integration of HPA into our BusinessForce division; and restructuring costs in our MediaForce division. The comparative difference in net profit after significant items was also exaggerated by the $25 million one-off gain contained in last year's results, on the sale of our Philippines JV interest.

Given the improved run rate of the past few months and board confidence in our future prospects, the board has declared a final dividend of 10.5 cents per share fully franked. This brings the total regular dividend for the year to 18.5 cents per share, an increase of 2.8% on the previous year. The board has resolved to suspend the dividend reinvestment program for the time being.

In summary, we have invested wisely for the future, both through acquisition and by further developing our own capabilities. We've got an unbeatable range of communication services and we look forward to building on this strong offering.

I'll now hand over to Colin Wright to present our full year financials in more detail.

Colin Wright:

Thanks, Phil. Good morning everyone.

Group result slide

Overall, Salmat delivered a sound underlying result in the 2008 financial year. Group revenue and EBITA before significant items both increased considerably over the prior year, and each division posted good sales growth.

Revenue and EBITA were of course boosted by the eight months of contribution from HPA.

Both amortisation and interest costs were much higher than in the previous year, mainly due to the acquisition of HPA. Following assessment of the fair value of HPA assets, an amortisation charge of approximately $7 million has been recognised in the second half of the year. We expect that amortisation next year will total around $12 million.

Our tax expense was slightly down on 2007, due to the comparatively lower profit. The income tax expense this year is a higher percentage of profit before tax and significant items owing to the non-deductible amortisation incurred this year.

Significant items brought the final NPAT figure to $12.8 million, which was in line with our expectations.

Though the total regular dividend increased slightly, earnings per share is obviously lower for 2008. This is due to the profit impact of the significant items and the higher interest and amortisation charges, as well as the increased number of shares on issue this year.

Significant items slide

As you'll recall, last year's results were positively impacted by a significant one-off gain of approximately $25 million from the sale of the Philippines joint venture.

This year, nearly all of the significant items were costs, and the impact of these is shown here.

The main item was the integration, restructuring and redundancy costs across the group of $5.8 million. This included integration of HPA into the business.

We also incurred $5.2 million in Lasoo development costs.

Finally, we had gains of $1.8 million. Of this, $1.1 million related to the sale of our Deltarg business in New Zealand and the balance related to the close out of our interest rate hedges.

In the year ahead we see continued integration costs in the order of $3 million post tax, but these will be more than offset by integration savings.

We also expect to incur some further costs in the Lasoo business as it progresses towards break-even over the next year. Lasoo costs from 1 July 2008 will be treated as normal costs rather than significant items.

Revenue growth slide

Revenue growth from all divisions contributed to the overall result.

BusinessForce was the key contributor, with an additional $128.8 million over the previous year. This was largely due to the initial eight-month contribution from HPA but underlying growth also contributed, notably in the area of laser impression volumes.

MediaForce revenue was up $49.8 million, thanks to good increases in catalogue volumes and the first full year impact of the growing Dialect business.

SalesForce revenue grew by $31.5 million. This increase resulted from a combination of increased sales activity across its various businesses and higher contact centre volumes.

EBITA growth slide

EBITA performance prior to significant items improved in the second half and by year end was up 22.6% on the previous year to $57.6 million.

Again, the BusinessForce result was primarily influenced by the initial contribution from HPA.

The MediaForce result was impacted by pricing and field cost pressures in the catalogue business. While competitive pressures in the catalogue business are easing, it will take some time to see the full effect on results. The Reach Media joint venture also incurred some restructure costs.

SalesForce EBITA was on par with the previous year's result, following a stronger second half. Margin decreases in some of the mature areas of operation were offset by margin increases and new business in the emerging sectors.

Corporate costs increased by $7.8 million due to a number of factors. These included:

- Equity profits from ClientLogic were included in last year's corporate costs.
- Ongoing costs associated with improving organisational efficiency and lowering risk that were previously shown as a significant item. Note that these costs will continue

to be shown as corporate costs whereas the benefits will be reflected as lower costs in the divisional results.

- Increased costs in group human resources and IT.
- Increased corporate costs stemming from the HPA acquisition.

We are working to reduce corporate costs over the next year.

Cash flow slide

Net operating cash flow almost doubled to $60.6 million, reflecting the increased scale of our business and a focus on improving cash flow. Borrowings were reduced by $40 million from the half year, primarily due to a strong focus on improving working capital management.

Capital expenditure was up 27.1% on the previous year in line with the growth in revenue.

We incurred joint venture funding costs of $1.4 million in connection with our New Zealand joint venture, Reach Media.

And the largest cash flow items by far were the purchase of business and proceeds from borrowings relating to the HPA acquisition. The subsequent part repayment of borrowings amounted to $110 million. A successful equity raising of $75 million was also completed.

The total dividend payment was lower this year due to the payment of a special dividend last year.

Capital expenditure slide

Capital expenditure of $20.2 million was slightly below the normal range at 2.5% of sales revenue.

Although we've seen some higher capex over the past five years, we believe that our capital expenditure needs will average 3-4% of sales over the longer period.

Finance facilities slide

At year end we had a longer term debt facility of $200 million expiring in October 2010 and a smaller short term facility.

To provide longer term finance more appropriate to our needs, we repaid the short term facility in August 2008 and took out a new working capital facility of $50 million, which expires in August 2010. This means that we now have adequate finance facilities for at least the next two years.

We have also taken out interest rate hedges to protect us against increases in interest rates over the period of our borrowings.

I'll now hand over to Peter Mattick who will take you through the strategic review for each of our divisions and provide a market update.

<u>Peter Mattick:</u>

Thanks, Colin. Good morning everyone.

BusinessForce slide

It's been a very busy year for BusinessForce, which is the new brand for the amalgamation of the BPO division and HPA.

Given the demands of such a major integration, it's gratifying to see that the business is progressing very well and we are confident of its future prospects. Following the merger, BusinessForce is now the largest division of the Salmat group and the largest supplier of specialised business process outsourcing services in the Asia Pacific region.

We've been pleased to maintain all of our key relationships and we certainly feel that there are benefits for both clients and staff flowing on from our increased scale.

Progress has already been made in terms of rationalisation in areas including corporate expenses, suppliers and equipment. We've also brought together some of our smaller branch facilities and we've identified some further consolidation opportunities over the coming two years.

Even with these sorts of changes, the whole project has run very smoothly and we've avoided any major disruptions for our clients and our production teams.

A key advantage of the recent integration has been the opportunity to enhance our service portfolio with the complementary strengths and capabilities of both organisations. The combined sales team has been working closely to identify cross-selling opportunities in our client base as well as new opportunities in different markets, including growing our business in Asia. We'll also be further integrating our print on demand business - which was recently rebranded as PrintZoo - in the coming year.

We are on target to substantially complete the integration program by the end of calendar 2009 - as originally anticipated - and we are also on target to achieve synergy savings at the upper end of our original estimate.

Integration costs and savings slide

When we first looked at the potential to achieve cost savings by putting the two businesses together, we thought we could save $10-15 million per annum. We are now confident that the savings will be at the upper end of this range and that they should be achieved over a relatively short timeframe.

This table shows the offsetting impact of integration costs in the initial stages. We expect these costs will be wound down by 2010, when the full impact of the annual savings will be reflected in our P&L.

SalesForce slide

SalesForce showed good revenue growth in 2008, though EBITA was relatively flat and our full year margins decreased slightly.

The margin decrease reflects a catch-up in costs following significant growth over the previous two years, as well as expensing start up costs in relation to the @Home business.

What was particularly good about the result was that the areas of strongest growth were in our new businesses. While this growth was achieved from a relatively small base, it certainly reassures us that our long-term strategy is sound.

We saw new channel and category growth in the direct sales area, alongside steady ongoing growth in mainstream channels. Importantly, the growth in direct sales was achieved without a commensurate increase in fixed overheads.

Our e-Learning division – Aframe - achieved outstanding year on year revenue growth through a number of new clients.

And in the exciting field of speech recognition services, significant new wins contributed to strong revenue and EBITA growth in our VeCommerce business.

In our traditional contact centre business, the @Home contact centre model - trialled on a small scale last year - was rolled out on a larger scale during 2008, growing to 350 contractors and achieving profitability within the first five months of operation.

We also successfully launched a new 150 seat facility in Kuala Lumpur in December 2007. These new models complement Salmat's traditional contact centre business by offering clients an increased range of price and complexity options for different market segments.

We'll continue to look at ways of maximising operating efficiencies in each area within SalesForce, as we increasingly diversify into the consulting and technology-provider role.

MediaForce slide

MediaForce is another area where we are integrating our traditional business with new technology offerings. The past year was largely characterised by a reengineering and revitalisation of the traditional business alongside some exciting growth in our newer segments. The 2008 top line result showed a pleasing improvement after a challenging previous year.

Of course, a highlight for this year was the November 2007 launch of our new Lasoo website. Consumers and retailers alike quickly recognised the superior proposition offered by the Lasoo site and the Dynamic Catalogue product. New functionality continues to be added to both services.

Now that the key development and start up costs for Lasoo have been expensed, this business should reach run rate break even in the second half of the year with a reduced loss for the full year in the order of $4 million.

We increased traditional catalogue sales by more than 10%, which was a great achievement in the current environment. We also continued to innovate our offering in the area of job tracking and reporting, completing the roll out of our total accountability model on a national basis. This model is the most sophisticated of its type in the world and offers clients an unbeatable range of reporting options, which are supported by extensive independent auditing.

Our new joint venture with New Zealand Post commenced last November and continues to gain ground as the two businesses are brought together. While we won't see the benefits right away, we are confident that this enterprise positions us at the top of the NZ market.

The Dialect business, acquired in December 2006, has shown strong growth in 2008. The business recorded full year profit, benefiting from new mobile content applications and higher Interactive Voice Response volumes. We expect continued growth and good results next year.

In the catalogue business, costs relating to freight, fuel and contractors in some regions increased during the year. There is a lag in recovering these costs from clients with long-term contract arrangements.

While pricing and costs impacted our traditional business margins in 2008, we expect the combination of a continued productivity review program, price increases and the growing contribution of our new technology businesses to improve the overall margin in 2009.

Summary slide

We are extremely pleased with the progress made this year, from both a performance and a strategic viewpoint.

As we move into our thirtieth year in the business, it's exciting to mark another year of increased sales, with good prospects for continued strong growth.

This sort of growth only stems from a sound strategic balance – and we are confident that we've further strengthened the business with acquisitions, new service launches and the re-investment that we've undertaken over the past few years.

We are happy that everything is set in place for improved sales and profitability in the next few years and won't be actively seeking any further acquisitions at this stage. Instead, we'll be focussed on maximising performance across all of our divisions and leveraging our unique capabilities.

Our improved run rate over the past four months augurs well for our prospects next year. Additionally, we do not anticipate the same impact from significant item costs in the next 12 months.

As such, the board is confident that Salmat will deliver an improved result in 2009 and this is reflected in the decision to increase the full year dividend.

In terms of 2009 performance, we are comfortable with the current market consensus of around $75-80 million for EBITA. We'll provide a further market update at the AGM in November.

Thank you for your interest today.

We'll now take questions regarding our results and operations. Please state your name and the organisation you represent before asking your question.