2012 Annual Shareholders' Meeting

10.30 am Wednesday 20 November 2012
Eden Park
Auckland

Chairman's Address

Chairman

Good morning ladies and gentlemen. Welcome to the 2012 annual shareholders' meeting of Fletcher Building Limited.

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

This meeting is being webcast via the Internet. 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) Limited and Foodstuffs (New Zealand) Limited and has extensive experience in retailing, including as a previous director and later chairman of Mitre 10 New Zealand Limited. Mr Carter is chairman of Fisher & Paykel Healthcare and is also a director of ANZ Bank, Air New Zealand and Fletcher Building Industries, co-chair of the NZ Initiative and a trustee of the Maurice Carter Charitable Trust.

Alan Jackson was appointed to the board in 2009. He has been an international consultant since 1987 with the Boston Consulting Group and has proven experience at the most senior levels of international and government business. He is chairman of Housing New Zealand Corporation and New Zealand Racing Board, a director of Delegats Wines, and a trustee of The Icehouse Auckland.

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 and the Auckland Art Gallery Foundation, and a member of the Otago University Business School advisory board.

Mark Adamson was appointed Chief Executive Officer and Managing Director with effect from 1 October 2012.He joined the Formica Group in 1998 as chief financial officer of the European division 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 English Institute of Chartered Accountants and the Institute of Taxation.

Cecilia Tarrant joined the board in 2011. She is an Executive-in-Residence at The University of Auckland Business School and has over 20 years' experience in international banking and finance in the United States and Europe. She has worked as a real estate finance lawyer and as an investment banker, and was a managing director in Morgan Stanley's Global Capital Market Group in London. Cecilia is a Trustee of The University of Auckland Foundation, and a director of the Government Superannuation Fund Authority.

Kathryn 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 a non-executive director of UGL, Sonic Healthcare, SMEC, and Investec Bank (Australia). She is currently chair of the Australian Accounting Professional and Ethical Standards Board and a fellow of the Australian Institute of Directors.

Gene Tilbrook was appointed to the board in 2009. Until his retirement in May 2009 he was Finance Director at Wesfarmers Limited and he led Wesfarmers' business development group. He is chairman of Transpacific Industries Group and a director of QR National and the GPT Group and a councillor of Curtin University of Technology.

On my immediate right is Martin Farrell, our Company Secretary and General Counsel.

Meeting Agenda

I will shortly give you my overview of the company's performance and the key areas of board focus during the 2012 financial year.

Mark Adamson will then address you and outline the company's strategy and his priorities. After that I will provide an update on how we expect the company to perform in the 2013 financial year, and 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 seven 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.

Overview Remarks

Before reviewing the company's performance for the 2012 financial year, I would first like to comment on the major economies in which Fletcher Building operates.

In New Zealand, economic conditions were difficult in the first half of the year but there was an improvement in the second half. In particular, we saw a sustained improvement in new housing consents. This was driven in part by a strong pick up in residential house building work in Canterbury, and also by increased activity in the Auckland region. Whilst the increase in housing consents was pleasing, the improvement needs to be seen in a wider context. Housing consents for the year to June were 15,414, a 14 per cent improvement on the prior year, but still down approximately 30 per cent from the long term average. Meanwhile the value of the commercial construction market declined a further 7 per cent and there was little recovery evident during the year. Government spending on infrastructure continued to underpin the construction market overall.

In Australia, we experienced a continued decline in residential construction activity throughout the year. New residential consents were down 12 per cent on the prior year and continued to weaken as the year progressed. Total consented commercial construction work fell by 9 per cent. Infrastructure construction work was up strongly, driven by the mining and resources sector and continued government investment. However, it is unlikely that this will be sustained given recent announcements on new mining project deferrals.

Beyond Australasia, a modest recovery in US housing starts assisted our Formica business in that market, but most European markets remained depressed. Continued growth in Asia was pleasing given the interruption to our business in Thailand from the floods there a year ago.

Highlights of 2012 Financial Year

Despite the economic challenges we faced, there were a number of key achievements during the year which are worthy of a mention.

We continued to make excellent progress in Canterbury with the house repair programme for the EQC. Since its inception, over 26,000 permanent house repairs have been completed, in addition to 47,000 emergency repairs and 18,000 winter heat installations.

Crane delivered earnings growth in its first full year under Fletcher Building ownership. The corporate cost synergies we identified at acquisition have been fully achieved and Iplex Pipelines performed strongly. We have in recent months divested several Crane businesses which we had identified as being non-core.

During the year, we completed a strategic review of our Australian insulation business. This review concluded that the best outcome would be to retain the business. However, given the high Australian dollar and lower activity levels, we took the decision to write off the goodwill arising on the acquisition of the business, to write down stock, and to reduce the carrying value of the brands. I am pleased to report that the operational performance of this business has improved although market conditions remain tough.

In our Laminex business we embarked on a major restructuring programme to better position the business for the lower volumes and to exit unprofitable lines of business. We expect to incur further costs this year as the restructuring programme is completed.

Also during the year, we announced our intention to close Formica's plant in Bilbao, Spain. This closure has been made necessary by the collapse in construction activity in Spain, which is down almost 90 per cent from its peak.

Financial Performance

There is no doubt that 2012 was a difficult year, with poor economic conditions significantly impacting our financial performance. At the start of the year we were very cautious about how the key economies to which we are exposed would perform and, as it transpires, we were right to be cautious. Continued global uncertainty, a weak recovery in New Zealand and declining activity levels in Australia all contributed to a very tough operating environment. As a result, we were forced to undertake the restructuring I have just mentioned to ensure we remained competitive and sized appropriately for underlying demand levels.

For the 2012 financial year, net earnings were $185 million compared with $283 million in 2011. Included in this were restructuring and impairment charges of $132 million after tax incurred in the Laminex, Formica and Insulation businesses.

Net earnings excluding these restructuring and impairment charges were $317 million, 12 per cent lower than the comparable figure for the prior year.

Operating earnings, that is, earnings before interest and tax, were $403 million, 18 per cent lower than the $492 million achieved in the prior year. Operating earnings before restructuring and impairment charges were $556 million, 7 per cent lower than for the prior year.

Earnings per share before restructuring and impairment charges were 47 cents per share compared with 57 cents per share in 2011.

Total group revenues for the year were $8,873 million, 20 per cent higher due to the inclusion of a full year of Crane revenues for the first time.

Despite the lower operating earnings, we were pleased to report stronger cash flow from operations, which increased by 11 per cent to $448 million. This was driven by stronger cash contributions from a number of our businesses including Formica, and the Crane, Construction and Steel divisions.

Divisional earnings

Let me now briefly review the performance of each of our divisions.

The Building Products division reported operating earnings excluding restructuring and impairment charges of $72 million, down 35 per cent on the prior year.

Operating earnings in the plasterboard and insulation businesses were down as a result of lower volumes, while the insulation business was also impacted by the continued over-supply of insulation products in Australia and increased imports.

Operating earnings in the Concrete division increased by $5 million to $130 million.

In New Zealand most product volumes were similar or slightly stronger than last year except for cement and masonry.

In Australia, the pipeline and quarry businesses performed well. The pipeline products business benefitted from two newly acquired businesses while the quarry business in Australia recorded a strong result from a favourable sales mix and improved margins.

The Construction division's operating earnings for the year were $50 million, down 17 per cent on the prior year. The construction backlog at the end of October was $1.3 billion compared with $1.1 billion at the same time last year. During the year we were pleased to announce that we had won the tender for two key construction contracts – the Waterview motorway extension and tunnel here in Auckland, and the new men's prison to be built at Wiri in South Auckland. Earnings from residential house sales were up as a result of increased house sales, predominantly in our Stonefields development in Auckland.

As I have already mentioned, Crane delivered increased operating earnings in its first full year of ownership of $106 million. The pipelines business had a particularly strong year with significant increases in revenues from the coal seam gas, resources, civil and rural sectors off-setting the broader decline in building activity. However, the lower activity levels impacted the trade distribution businesses in Australia and New Zealand.

Good progress has been made in divesting several businesses in Crane which we had identified as non-core. In September we announced the conditional sale of the Cory's Electrical distribution business. Once completed, this sale will mean that Fletcher Building has realised almost $90 million in total through the divestment of Corys Electrical and Crane's two metals distribution businesses, which we announced in July.

With these divestments completed, we now have in Crane a leading position in plastic pipes manufacturing across Australia and New Zealand, and an equivalent pipes and plumbing supplies distribution footprint in both markets.

In the Distribution division, PlaceMakers' revenues were 5 per cent lower than the prior year's. Earnings were impacted by the low level of residential house building and increased competitor activity which negatively impacted gross margins.

Formica's operating earnings before restructuring and impairment charges were $71 million, 27 per cent higher than the prior year. The improved result was due to on-going operational improvements and efficiency gains in all key areas of the business, plus increased revenue in North America and Asia.

Laminex's operating earnings before restructuring and impairment charges were $68 million, 39 per cent lower than the prior year. Australian revenues were 7 per cent lower, driven by a slowdown in new residential activity and continued weak conditions in the commercial sector.

The Steel division recorded operating earnings for the year of $48 million, down 41 per cent on the prior year.

The rollforming and coated businesses in both Australia and New Zealand experienced volume declines. Market conditions in the long steel businesses were extremely difficult. New Zealand domestic volumes were up as a result of market share gains but margins were lower, and the high Australian dollar led to intense import competition in the Australian market and poor margins on exports from New Zealand.

Dividend

The total dividend for the year was 34 cents, compared with 33 cents in the prior year. Our dividend guidelines remain unchanged and it is the board's intention to at least maintain the dividend each year, with the aim that dividends will rise over time commensurate with further earnings growth. For the next several years we anticipate that the dividend will grow at a slower rate than earnings, as we seek to return the dividend pay-out ratio to between 50 and 60 per cent of earnings.

Total Shareholder Returns

Total return to shareholders for the year to 30 June 2012 was minus 27 per cent, driven by a reduction in the share price over the course of the 2012 year, partly offset by the 34 cents in dividends paid. While this rate of return was disappointing, it was due in part to a negative change in sentiment to the building materials sector by investors that affected not only Fletcher Building but all of our Australian peers.

Interestingly, in recent weeks we have seen a change in sentiment towards the building materials sector. By illustration, if we were to measure total return to shareholders for the 12 months to 31 October 2012, that figure would be positive at plus 10 per cent. Such wild swings in returns are indicative of the volatility in financial markets we have all experienced in recent times. Despite such volatility, our goals remain unchanged. We seek to grow shareholder value over time, and to manage the portfolio of businesses as best we can given the prevailing economic conditions. We must by necessity shrug off the gyrations of the global financial markets, and instead focus on operational excellence and on serving our customers.

Board changes

This year we have had further changes to the composition of the board.
Kate Spargo joined the Board in March. In her short time with Fletcher Building she has brought a breadth of business experience, and a legal and governance focus, to board considerations. Kate will address you shortly when she comes up for election to the board.

At the end of September Jonathan Ling retired from the board contemporaneous with his retirement as chief executive. Sadly Jonathan couldn't attend today's meeting, but nonetheless I would like to take this opportunity to publicly thank him for everything that he did for Fletcher Building over his six years as chief executive. Under Jonathan's leadership the size and scope of the company was transformed, and he successfully steered Fletcher Building through exceptionally tough economic conditions. The strength of the company today, its sound financial position and its quality management team all bear strong testament to Jonathan's stewardship.

The end of September also marked the end of another era when Hugh Fletcher retired from the board. Hugh's retirement ended a formal link with the Fletcher family that stretches back 103 years to the very origins of the company. This connection with the Fletcher family has given Fletcher Building a special character, and a set of values that have sustained the business for over a century. Hugh himself was first appointed to the board of Fletcher Holdings some 34 years ago, and I doubt that there is anyone in New Zealand today who could claim such length of service as a public company director. Hugh is with us here today, and on your behalf I would like to publicly acknowledge his long association with the company and thank him for his wise counsel and enormous contribution to the strategic debate around the board table.

People

On behalf of the board, I would like to especially thank all of our people for their commitment and hard work over the past year. Whichever business they are in, and whichever part of the world, all our people have had to truly apply themselves this year to deliver to our customers and to meet our financial targets.

This year I would particularly like to thank those who have worked so hard in Canterbury helping to rebuild the city. Despite the setbacks of further earthquakes and numerous practical difficulties, great progress has been made in restoring homes and services across the region. While there remains much to be done, we are proud of what has been achieved thus far due to the extraordinary efforts of our people.

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

Let me now provide an update on the outlook for the 2013 financial year.

Outlook

Having now completed the first four trading months, we have seen a fairly clear picture emerge of conditions in our core markets.

In New Zealand, the improvement in residential house building activity has been maintained. Seismic activity in Canterbury has reduced to the extent that substantial progress can now be made. Activity levels in Christchurch have continued to gain momentum with infrastructure repairs now underway together with increased levels of new house building activity. The re-entry into the market of insurance companies prepared to write fresh polices for housing has been key with regard to the improvement in housing activity. In July this year the plan for the new City centre was unveiled, and with the completion of demolition work in mid-2013, the stage will be set for rebuilding work in the CBD to begin in earnest.

Beyond Canterbury, a sustained improvement in new house building in Auckland has been evident over the course of the past seven months, but other parts of New Zealand have shown only limited improvement to date. The outlook for commercial construction activity remains subdued in the short term, and a sustained recovery would typically lag any improvement in the residential market. Government spending on infrastructure is expected to continue to underpin overall construction activity levels, but with financial contributions from the large infrastructure construction projects not expected to materially boost earnings until the next financial year.

In Australia, we have noted a continued decline in new housing consents, and are seeing this negatively impact all of our businesses that are exposed to the residential house building market. Whether the market will stabilise at these levels or decline further remains unclear. We do not believe that the easing of interest rates by the Reserve Bank of Australia will be sufficient, in and of itself, to significantly improve consumer confidence in the short term. A sustained improvement in consumer confidence is, in our view, a necessary pre-requisite for a substantial pick-up in new home construction. As in New Zealand, the commercial construction market remains weak. While infrastructure spending has continued to be strong, driven by the resources and mining sectors along with state and federal government investment, growing uncertainty around the timing and likelihood of future mining projects is of concern.

In North America, the increase in new housing construction in the US has benefitted the Formica business, although only 15 per cent of its revenues are derived from new housing construction so the impact is not as direct as for other building materials companies. No improvement in the commercial market is evident yet. Certain parts of Europe remain difficult, particularly Spain, and we do not foresee any marked improvement in that region overall in the near future. Asia has continued to grow satisfactorily but evidence of a slowdown in growth in China is a concern.
In terms of the earnings outlook for the year, we would reiterate the guidance given at the time of the full year result. We noted that a significant increase in earnings from the current level would require a marked improvement in residential and commercial construction levels, particularly in New Zealand and Australia.

One change to signal at this point is that, going forward, all restructuring costs will be treated as normal expense items arising in the ordinary course of business. As such, restructuring costs will be included in the EBIT or operating earnings number and not shown “below the line” as an unusual item as was our practice previously. To allow for valid comparison we have restated last year’s earnings to be consistent with this new policy. On this basis, operating earnings for 2012 were $502 million after the inclusion of $54 million in restructuring costs that were incurred last year in Laminex, compared with a figure of $556 million that we reported in August.

On the basis of trading conditions in the first four months of the year, and the plans developed by the business to counter areas of weakness in demand, we expect operating earnings for the full year to be in the range of $560 million to $610 million. Included in this range is an estimated $20 million in restructuring costs that will be incurred primarily in Laminex which we indicated at the time of the annual results announcement. This represents growth in operating earnings, on the restated basis which I have just outlined, of between 12 and 22 per cent over the previous year.

In terms of the split between the first and second halves, operating earnings in the first half are forecast to be broadly in line with those achieved in the same period in the prior year. This implies a stronger performance in the second half to deliver operating earnings within the guidance range. The board believe that this is achievable, on the basis of the momentum seen in New Zealand recently which is expected to continue for the whole of the year. A caveat to note, however, is that any further deterioration in the Australian market in particular, or in other key markets in which Formica operates, may necessitate a revision to this guidance.