MILTON CORPORATION LIMITED
2015 ANNUAL GENERAL MEETING
TO BE HELD THURSDAY, 15 OCTOBER 2015 AT 3 PM
AT SOFITEL SYDNEY WENTWORTH,
LEVEL 4, ADELAIDE ROOM,
61-101 PHILLIP STREET, SYDNEY

WELCOME

Good afternoon ladies and gentlemen.

My name is Robert Millner and it is my pleasure to welcome you to the 77th Annual General Meeting of shareholders of Milton Corporation Limited.

As it is now 3pm I declare the meeting open.

Before we turn to the official business for the day I would like to introduce you to the non executive directors and senior executives of Milton.

Starting from the far end we have the non executive directors: John Church, Graeme Crampton, Kevin Eley and Ian Pollard.

In front of me we have Nishantha Seneviratne, the company's secretary and then Frank Gooch, the managing director.

In addition, the company's auditor, Melissa Alexander from Moore Stephens Sydney is in attendance.

The notice of annual general meeting has been circulated to all shareholders. The holders of over 181 million shares or approximately 28 per cent of the company's ordinary shares have either lodged their proxy or voted on-line.

Following my report to the meeting Frank will provide an overview of the 2015 financial results of Milton and comment on the investment portfolio.

CHAIRMAN'S ADDRESS

Milton's net profit for the 2015 financial year was a record $128 million including $3 million of special fully franked dividends.

Importantly the main driver of the increased profit was a lift in ordinary dividends and distributions received from Milton's portfolio of investments in Australian listed companies and trusts and not only from an increase in capital.

Consequently underlying earnings per share grew by 4.3% to 19.6 cents and the ordinary fully franked dividends paid to shareholders were increased by 4.5% to 18.4 cents per share. Milton also paid a special fully franked dividend of 0.4 cents per share.

Total dividends paid for the year, including the special dividend, amounted to $120 million. The ordinary fully franked dividends paid by Milton represented 94.2% of its underlying operating profit whilst the special fully franked dividend represented 85% of the special revenue received.

Milton has now paid a special dividend in four of the last five years and the current intention is to pass on the benefit of the special dividends in the year in which they are earned by Milton.

Milton's dividend history graph illustrates the reliability of Milton's dividend and that Milton has been successful in meeting the first of its objectives, which is to pay increasing dividends over the long term.

This graph shows the dividends per share since listing in 1958. In the period to 1995 Milton had a lower payout ratio and issued bonus shares periodically. Since 1995 the payout ratio has increased and with sound growth in earnings the dividend per share has quadrupled.

Milton's second objective is to provide capital growth in the value of the shareholders' investments.

It's strategy to achieve these objectives is to invest for the long term in Australian listed equities, property joint ventures and liquid assets, including interest bearing securities. At the end of June 2015 the equity portfolio represented 94% of total assets.

This strategy has proved to be successful over the long term. For example if you had invested £1,000 or, for the younger shareholders here today, $2,000 in 1958 that investment would have been worth $128,389 at 30 June 2015 and it would be providing annual ordinary dividend income of $5,250 plus franking credits.

There are probably not many of us here that were able to make that investment in 1958 so I would like to consider the performance since the turn of the century. That is for the 15 years since 2000.

In this 15 year period, the annual ordinary fully franked dividend has increased by 114% to 18.4 cents per share from 8.6 cents per share and a total of 15.9 cents per share has been paid as special fully franked dividends.

Over that same period of time the NTA, before provision for tax on unrealised capital gains, has grown by 127% to $4.39 per share from $1.93.

If we assume the dividends were reinvested into shares, then the total return based on the movement in NTA over the 15 years would have been 10.3% per annum compounded. This is what we refer to as the Total Portfolio Return.

The share price tends to track the NTA so it is no surprise to see the returns based on share price are similar. If you had invested $1,000 on 30 June 2000 that same parcel of shares would have more than doubled in value to $2,520 and, in addition, you would have received $1,247 in fully franked dividends.

Again assuming the dividends were reinvested into shares, the total return based on the share price movement over the 15 years would have been 11.1% per annum compounded. This is what we refer to as the Total Shareholder Return.

For comparison purposes the total return of the All Ordinaries Index over the 15 year period was 7.8% per annum.

Whilst the share price does tend to track the NTA they are rarely equal. Following the GFC Milton's shares, like many LICs, traded at a discount to NTA.

A number of initiatives were put in place by Milton to reduce the discount.
The shares were split into five in October 2013, the Share Purchase Plan was reinstated and a Dividend Reinvestment Plan was implemented.
The Share Purchase Plan and the DRP have also provided additional funds to be invested without any material dilution to shareholders. In October last year the SPP raised $36 million and a further $32 million was raised in October this year.

The DRP is also gaining in popularity with 3,170 shareholders participating in the DRP for the 2015 final and special dividends. This effectively provided a further $4 million for Milton to invest.

As the LIC sector has expanded with a number of new LICs coming to the market, the profile of LICs has been raised significantly and the benefits of the LIC structure are now better understood by both advisers and investors.

I think it is a combination of all of the above factors as well as ongoing sound performance that have positively influenced Milton's market price relative to its NTA with Milton's shares having traded at a premium more often than a discount over the last 18 months.

Over the last 18 months Milton's shares have traded at a premium more often than a discount.

In March this year the government released the Tax White paper and invited submissions from interested parties. One of the discussion points related to the retention of the dividend imputation system which we believe has played a critical role in delivering a strong capital market in Australia and is likely to continue to do so. A submission was lodged by Milton encouraging the retention of imputation.

I am sure that tax reform is very much on the new prime minister's agenda and we will continue to monitor these developments and urge shareholders to do the same.

The majority of companies in the portfolio have now reported and declared dividends for this half year.

Overall we were pleased with the level of dividend income arising and Milton's underlying investment income for the quarter to 30 September 15 is ahead of the previous corresponding period.

Whilst five of Milton's Top 20 investments are yet to report the directors expect to be able to at least maintain the interim dividend at 8.5 cents per share.

MANAGING DIRECTOR'S ADDRESS

The 2015 financial year was another interesting year for investors.

This graph shows the movement in the All Ordinaries index over the year. It is easy to see why some investors thought they were on a roller coaster ride.

Within the first six months the market increased by 5.4% in August and then fell by 9.7% in December only to finish the calendar year roughly where it started. In the second half it reached new heights of 5963 on 13 April but then dropped to 5451 by 30 June. Over the year the market finished up by just 1.3%.

Importantly Milton's ability to pay dividends to its shareholders is unaffected by these market price movements and as a long term investor Milton can use the down days as opportunities to invest in companies that we expect will pay increasing dividends over time.

In 2015 Milton's investment portfolio provided $113 million in fully franked dividends, including special dividends, nearly $9 million in unfranked dividends and $3.5 million in trust distributions. The distinction between the franked and unfranked dividends is very important as Milton does not pay any tax on the franked dividends.

It is worth noting at this point that, in accordance with tax transparency laws, in mid December this year the ATO will publish on its website details of Milton's taxable income and tax paid for the 2014 financial year. As more than 90% of Milton's pre tax profit is comprised of fully franked dividends on which it pays no tax, its effective tax rate is less than 5%, which is substantially below the corporate tax rate of 30%. I only hope that no misinformed media represents that Milton has engaged in aggressive tax avoidance.

Interest income in 2015 was approximately $600,000 less than the prior year mainly due to lower interest rates available on deposits.

Milton's share of net profits of property joint ventures was marginally lower at $6.3 million. Increases in earnings from the Ellenbrook joint ventures were offset by start up losses incurred on a new residential development in the Hunter region. This is a twenty year project which commenced selling in 2015. The project manager at Ellenbrook is also responsible for the development of the Hunter project.
The Ellenbrook development has won multiple awards here in Australia and this year it won the 2015 FIABCI World Prix d'Excellence Award for the best master planned community in the world.

We anticipate increasing profits from the new Hunter project will offset lower earnings from Ellenbrook as it approaches completion and the investment is repaid.

Administration expenses remained well controlled and they represented 0.12% of average total assets for the 2015 year.

The underlying operating profit, which excluded the $3 million in special dividends received in the 2015 year, was $125 million, 6.5% higher than the prior year.

Milton's balance sheet remains in a sound condition with no debt and with total assets valued at $2.8 billion at 30 June 2015. The investment portfolio was valued at $2.7 billion.

During the year an additional 9.4 million shares were issued, increasing capital by $42 million. In October 2014, 3,400 shareholders subscribed for shares with a total value of $35.7 million under the share purchase plan and shareholders that participated in the DRP during the year reinvested $6.4 million of their dividends.

Earlier this month the 3,200 shareholders who participated in the share purchase plan subscribed for shares with a total value of $32.4 million. This has provided additional funds to be deployed as the opportunities arise.

Following the payment of the final dividend and the completion of the share purchase plan Milton now has 649 million shares on issue to almost 23,000 shareholders.

Over the 2015 financial year the net asset backing, before provision for tax on unrealised capital gains, grew by 0.9% to be $4.39 per share but the Milton share price closed the year 0.9% lower at $4.50. Effectively the premium to NTA at which the Milton shares were trading reduced from 4.3% to 2.5%.

The movement in the NTA is generally reflective of the change in value of the portfolio but it is also affected by dividends paid, as well as income, expenses and tax payments during the period and so it is not directly comparable to the movement in the All Ordinaries index, which is unaffected by all of the above.

The Accumulation Return of the All Ordinaries index assumes all dividends paid are reinvested in shares so that the resultant compound return combines capital growth and dividend payments. Milton uses a similar calculation to determine its Total Portfolio Return and we often compare the two returns to provide a guide to relative performance.

The investment portfolio has delivered sound returns in terms of income and capital growth to its shareholders over many years.

Milton's one year Total Portfolio Return, or TPR, to 30 June 2015 was 5.1% per annum, marginally below the benchmark return of 5.7% per annum. Over longer time periods Milton's TPR shows consistent outperformance. The compound annual return of the TPR over fifteen years to 30 June 2015 was 10.3% per annum compared to the accumulation return of the All Ordinaries Index for the same period of 7.8% per annum. Milton's relative performance would be enhanced if the value of franking credits were included in the calculations, as the average dividends paid by the companies in the All Ordinaries Index is only partly franked.

During the year $115 million was invested in 44 companies and trusts. Most of this was directed towards increasing the investment in existing holdings but there were also three new companies added to the portfolio.

This slide shows you the portfolio movements by sectors. I do not intend to go through each of these, however I would like to touch on the larger movements.

In the Transport sector $11.8 million were received from Japan Post for the takeover of Toll Holdings and a total of $16.8 million was invested across four companies in the same sector: Lindsay Australia, Qube Logistics, Sydney Airports and Transurban Group.
In the Materials sector additional funds were invested in Adelaide Brighton, BHP Billiton and Duluxgroup.

In the Diversified Financials sector investments were made in ASX Limited, BT Investment Management Limited, Equity Trustees through participation in its rights issue, IOOF Holdings, and Macquarie Group.

In the Bank sector Milton added $2.5 million to its ANZ exposure and by accepting its rights Milton invested $10 million in NAB.

Whilst not on this slide I note in September 15 Milton participated fully in the CBA rights issue as well as the ANZ placement.

The movements in the Consumer staples sector include Metcash, which Milton continued to sell down and it disposed of that investment altogether. Some of the funds from that disposal were reinvested in Woolworths and Wesfarmers.

The new companies added to the portfolio were:

- the fund manager, BT Investment Management Limited, with an initial investment of $2.1 million,
- the travel insurance provider, Cover-More Group, with an initial investment of $3.6 million and
- the provider of residential aged care services, Regis Healthcare, with an initial investment of $2.1 million.

Whilst the size of each investment was modest in the context of the overall portfolio size we expect to increase these holdings over time.

In addition to the Toll Holdings takeover, other corporate transactions that affected Milton during the year included:

- Australand Property Group, which was taken over by Frasers Centrepoint Limited, and
- David Jones which was acquired by Woolworths Holdings Limited.

Milton also reduced its holdings in GWA and ALS and sold out of Seven West Media entirely.

The current weightings of companies in the portfolio have resulted from consistent application of the company's long held investment philosophy over many years and therefore may be quite different to their weightings in the market indices.

To illustrate this point let's look at Milton's Top 20 investments as at 30 September 15. The top 20 made up 70% of Milton's total assets whereas these same stocks only make up 50% of the S&P/ASX 200 index.

This graph shows Milton has larger overweight positions in nine of the Top 20 companies.

In the Banks Milton has relatively larger holdings in Westpac, Bank Of Queensland, and Bendigo and Adelaide Bank. In other sectors W H Soul Pattinson, AP Eagers, Perpetual, Blackmores, Brickworks and ALS are above the index weighting. It is worth noting that in September this year Blackmores was included in the S&P/ASX 200 Index and Brickworks was added to the S&P/ASX 300 Index however Milton has been a long term holder of both of these companies.

Milton has underweight positions in ANZ, BHP Billiton and Telstra.

This chart shows Milton's weighting in other companies that are in the Index top 20 but not in Milton's top 20.

You can see here that Milton is underweight: Woodside Petroleum, Scentre Group, Westfield, Rio Tinto, AMP, Brambles and Amcor.

Approximately 34.9% of Milton's assets are in the bank sector. These investments have provided significant dividends and capital growth over many years. We are alert to the threats of disruption in this sector and we follow very closely the developments in APRA's 'unquestionably strong' capital adequacy requirements.

Whilst the additional capital will strengthen the banks' balance sheets it is likely to lower the future return on capital that the banks can earn and we expect bank dividends will be relatively flat in the short term at least.

As the chairman has reported the majority of companies in the portfolio have announced their results and we know what dividends we will receive from them in the six months to December 2015. Overall the outcome was a little better than anticipated by our analysts and Milton's investment income year to date is ahead of that for the previous corresponding period.

I should note however there are five companies within the top 20 holdings, ALS, ANZ, NAB, Macquarie Group and Westpac, that are yet to report and their dividends will obviously affect the overall result for the first half. Macquarie Group and Westpac have provided an indication of their next dividend and these are higher than the previous corresponding period.

The Australian economy is still adjusting to declining mining investment as a result of lower commodity prices. It is being assisted by improving residential construction and a lower exchange rate which has helped our exporters.

In a relatively low growth environment many companies have opted to return excess cash to shareholders rather than invest for further growth. Corporates have generally restructured their operations and are running lean. There is now limited growth in earnings to be derived through restructuring and payout ratios are unlikely to be pushed much higher.

With this in mind I expect marginal improvement in earnings and dividends per share over the year ahead from the market as a whole.

I expect the volatility in the share market to continue throughout the 2016 financial year with many global factors and domestic concerns weighing on the market.

News is disseminated very quickly these days and often we find the market over reacts to short term issues and I think this adds to the volatility we see in the markets at the moment.

As a long term investor with a strong balance sheet and cash available to invest Milton is well placed to take advantage of these conditions to continue to invest in companies with sound business models and reliable earnings and dividends.

Finally I would like to thank all six of my staff, who are totally shareholder focussed, for their commitment and support during the year. I would also like to acknowledge the contribution of each of the non executive directors. Their support and guidance is much appreciated.