Salmat Limited results for the year ended 30 June 2009

Presentation speech, August 2009

<u>Grant Harrod:</u>

Agenda slide

Good morning and welcome to our presentation today covering Salmat's results for the year ended 30 June 2009.

I'm Grant Harrod and I'll be presenting along with our Chief Financial Officer, Colin Wright.

Also in the audience are outgoing Joint Managing Directors, Peter Mattick & Phil Salter and our new CFO, Chad Barton, who will be replacing Colin who is retiring after our AGM in November.

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.

Today we'd like to take you through our results for the year ended 30 June 2009; the performance of each of our business divisions and our growth focus and strategic insights moving forward.

Financial summary slide

As you can see from this summary of our financial performance for the year, Salmat has recorded a strong result.

Sales were $890.8 million which was 9.7% up on last year. EBITA before significant items was up 34.3% on the prior year and in line with guidance provided in February 2009.

Net profit after tax but before significant items was up 49.7%. Net profit after tax and after significant items was up 168.2% leading to an EPS increase of 141.1%.

The Board's confidence in our future prospects has led them to declare a final dividend of 11.0 cents per share fully franked. This brings the total dividend for the year to 20 cents per share, representing an increase of 8.1% on the previous year.

In summary, 2009 has been a year of consolidation and strengthening our company as an outright leader in its markets and it is ideally positioned moving forward with a comprehensive range of services to assist our clients in growing their businesses.

One Salmat slide

Salmat is Australia's leading outsourced services provider specialising in targeted customer communications solutions. Our current offering backs up this statement. Our future offering will reinforce this even further.

This slide illustrates the concept of 'One Salmat', which is essentially the ability for us to provide all of our clients' customer communication needs under the one roof.

Salmat has developed over the years through a combination of organic growth and acquisitions. The acquisitions in particular had led to a range of disparate businesses and brands under the Salmat banner.

'One Salmat' has been a strategy to bring all our services together under a singular Salmat brand, philosophy, attitude and identity.

We are working to link the various sub-businesses to enhance our ability to provide seamless cross-company solutions. Rather than targeting clients according to their individual needs, we are going to provide a comprehensive suite of relevant services to different vertical markets.

Business scorecard slide

At the end of last year we set ourselves some objectives. It is important that we hold ourselves accountable to the successful execution of these and I would like to go through them in more detail.

Firstly, we planned for growth across all of our divisions. I am pleased to report that BusinessForce achieved revenue growth of 21.2%, mainly due to the full twelve months inclusion of the HPA acquisition from November 2007 and organic growth. Our SalesForce division grew organically in the order of 6.9%. MediaForce declined by 2.2% with our decision to exit non-catalogue work in the distribution of newspapers and directories, both of which are low margin activities consuming valuable capacity in our network. In addition, with changes in legislation we no longer captured pass through telco revenue in our Interactive division relating to the SMS marketing work we do. Both activities reduced our revenue contribution but likewise improved our return on sales. The underlying revenue growth in MediaForce excluding newspapers and directories was 4.7%.

Our second key area of focus for the year was the integration of HPA. We planned to have the integration substantially underway by the end of FY09 and this has been achieved. There are still things that need to be done but these tasks are more in the nature of business as usual than large scale integration projects.

We recently completed a full external review of our IT infrastructure that has highlighted further opportunities to streamline activities and improve productivity. We are currently hiring a new CIO who will be responsible for leading these changes.

As discussed previously, we are progressing on our strategy to promote our one-to-one service offering, in particular consolidating all our activities under One Salmat. We will therefore move to the next phase of the rebranding of our divisions. This is currently taking place and I will talk about it in more detail a little later in the presentation.

Our fourth key objective for the year was to reduce our debt to $180 million by the end of FY09 and this has been exceeded. Debt was reduced from $219 million at the end of last year to $167 million in June of this year.

We targeted organic growth and improved productivity. This has been achieved and our EBITA growth has exceeded our revenue growth.

Our extensive client base provides significant opportunity for organic growth, particularly as we focus on extending our services throughout these organisations. By providing an enterprise wide solution we can maximise synergies, lifting customer engagement and reducing costs. We are moving from a transaction-based to a solutions-based business which will derive extensive efficiencies.

We provided guidance during the year that EBITA before significant items would be between $75 and $80 million. We are pleased to report that we achieved EBITA of $78 million for the full year.

In terms of the CEO succession process, it is well underway. I have now been in this role for 4.5 months and Peter and Phil have continued in their positions as joint Managing Directors. As of October 1, 2009 they will step down to take on Non Executive Director roles and I will assume the position of Managing Director from this time.

All in all we believe that we delivered on our objectives in an economic climate that deteriorated from the time that we set these objectives.

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

Colin Wright:

Thanks Grant. Good morning everyone.

Group result for year ended 30 June 2009 slide

As previously mentioned our sales were up 9.7% and EBITDA before significant items increased by 27.1% as we focused on improving efficiencies and extracting synergies from the HPA acquisition.

EBITA increased by 34.3% as depreciation increased but at a lower rate.

The share of equity losses relates mainly to our Reach Media joint venture in New Zealand. The business is slowly improving in a difficult economic climate.

Interest expense increased slightly recognising that our borrowings balance peaked in November 2007 to accommodate the HPA acquisition. Although our borrowings have declined substantially since then, we have still had a full twelve months of relatively high borrowings for FY09 relative to FY08.

Tax expense before significant items increased from $10.9 million to $14.9 million on higher profit.

Significant items turned around from a negative last year to a positive this year. They will be discussed in more detail later but represent the gain from the sale of two properties offset by one-off property costs in Hong Kong.

Our final dividend has increased as mentioned and our EPS has risen from 9 cents to 21.7 cents representing an increase of 141.1%.

Balance sheet slide

The main changes in our balance sheet reflect the sale of our two properties in Sydney and Brisbane. Our fixed assets have reduced by $13.8 million.

Our total liabilities have reduced by $32.1 million mainly reflecting the reduction in borrowings.

As mentioned earlier, our borrowings have declined by $51.9 million due largely to the sale of our two properties.

Revenue growth slide

This waterfall slide visually shows the contributors to our revenue improvement this year. As you can see, MediaForce revenue declined for the reasons previously mentioned, while SalesForce and BusinessForce both contributed positively. The largest contribution came from the full 12 months revenue from HPA.

EBITA (before significant items) slide

All divisions contributed positively to the EBITA growth. The MediaForce EBITA result is noteworthy as it increased by $1.6 million despite the drop in revenue and it also included a $5.8 million loss from Lasoo. Last year the Lasoo cost was shown as a significant item.

SalesForce and BusinessForce both made good contributions to EBITA and corporate costs at the EBITA level were $2 million lower than last year.

Significant items (post tax) slide

As previously mentioned, we have shown the sale of properties and the Hong Kong property costs as significant items due to their magnitude and the one-off nature of the costs. The sale of properties contributed $4.5 million and due to the fact that we leased back the properties, there will also be a contribution in 2010 and 2011 of $1.7m and $1.1m respectively.

There will be no further costs relating to the Hong Kong property rationalisation.

Last year there was a significant item cost of $9.2 million after tax relating mainly to integration costs and the Lasoo start-up. This was one of the main reasons for the large percentage increase in net profit after tax relative to last year. Investment in Lasoo is now being treated as an operating item.

Cash flow slide

Net operating cash flow increased by $20 million due to the increased EBITDA for the year.

Net capital spend out of cash flow declined by $2 million but this was offset by finance leases.

The sale of our two properties generated $24 million in cash.

The dividend payment during the year was $31 million which was higher than last year due to the dividend reinvestment programme that was in place.

This year we repaid borrowings of $47.1 million and increased our cash on hand by $8.5 million. We benefitted from the timing of some receipts at year end.

Net capital expenditure slide

Capital expenditure as a percent of sales is consistent with last year. We expect it to continue at around this level that some capex might be leased rather than purchased .

Finance facilities slide

Our senior debt of $200 million is due for renewal in October next year. We also have a $50 million working capital facility expiring in August 2010 that we do not need to renew.

We have been discussing refinancing with our banks and intend to start the renewal process well before our facilities are due to mature. We have had positive indications from our banks and do not foresee any problems in renewing our loans. The interest rates have come down but the margins have gone up. Our interest costs for next year will be affected by the combination of the unhedged rates, our hedged rates and the timing of our facility renewal.

As at the end of the year, we had $160 million of our borrowings hedged until June 2010 and a further $110 million hedged until our loan maturity in October 2010.

Key ratios slide

All of the key ratios listed have shown signs of improvement as a result of our good result this year and our improved borrowing position.

Our return on capital employed has improved from 8% to 14.5%.

Our EBITDA margin as a percentage of sales has increased from 9.9% to 11.4% reflecting the advances that we have made in containing costs.
Our EBITA margin has also increased from 7.2% to 8.8% even though the Lasoo costs have moved from significant items last year to normal EBITA this year.

Our NPAT margin has improved from 1.6% to 3.9%. EPS has increased by 141.1% from 9 cents to 21.7 cents.

As a result of our improved operating performance and the property sales our debt to equity ratio has improved from 77.3% to 59.6% and our gearing ratio or debt to debt plus equity has improved from 43.6% to 37.3%.

Integration costs and savings slide

The integration of HPA into the Salmat business has proceeded according to plan. The initial savings that were achieved in FY08, which included the combination of the Perth sites as well as other smaller sites together with the removal of the duplication in corporate costs, have been reflected in savings in this year's cost base.

There has been some site consolidation during this financial year and we have combined some administrative functions. In terms of the comparison with the two businesses before they came together, we have saved in the order of $9 million this year. The costs that were incurred in achieving these savings were mainly one off in nature and amounted to approximately $4 million. This meant that the EBITA improved by about $5 million compared to pre-merger and the savings run rate is now approximately $12 million per annum.

Next year we expect to achieve net savings of $10 million. This will mean that the cost base for FY10 is expected to be $13 million less than the two pre-merger businesses, with the savings run rate being $15 million.

There are more savings to be realised as leases expire and as the IT functions draw more closely together over time. However, by then the businesses will be regarded as integrated and the savings will not be separately reported as integration savings.

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

Grant Harrod:

Thanks, Colin.

BusinessForce scorecard slide

Following the integration of HPA into BusinessForce, the retention of key clients and staff for both businesses was a key objective. I am pleased to report that this has been achieved and all major clients have been retained in the integration process. The former head of BusinessForce, Terry Daly, announced his retirement during the year and the former NSW and QLD State Manager of BusinessForce, Peter Hartley is now heading up the division.

We have addressed property consolidation issues in Hong Kong and taken all future costs to the P&L this year as a significant item.

We planned to enhance the service portfolio of our data solutions and workflow management businesses. Whilst this is progressing, it has not been as fast as we would have liked.

As already mentioned, we planned to achieve integration savings of $15 million by 2010 and we remain confident of achieving this, with further opportunities to extract cost efficiencies. Savings are now running at $12 million per annum and this means that we are on track with this objective as well.

BusinessForce financials slide

In terms of BusinessForce's performance, sales revenue was up 21.2% to $370.8 million and this was due both to the full 12 months revenue contribution from the HPA acquisition and some organic growth.

EBITDA increased by 29.5% due to higher revenue and integration savings which were offset to some extent by EBA increases.

EBITA before significant items increased by 37.3% and the EBITA margin increased from 9.8% last year to 11.1% this year.

SalesForce scorecard slide

All SalesForce objectives for the year were achieved.

There were improved volumes and cost containment across the portfolio with our traditional contact centre business growing and our field sales area increasing. New client wins extended our capability into outbound financial services selling and IT help desk work. In addition, our outsourced field and outbound phone sales business grew revenue, as we increased the number of kiosks and expanded our presence into NZ.

Our emerging services including speech, learning solutions and field sales enjoyed solid growth.

During the year we also opened a new contact centre in the Philippines providing an off shoring capability to compliment our extensive on shore offering and we expanded the Malaysian call centre facility.

SalesForce financials slide

In terms of financial performance, sales revenue increased by 6.9% during the year to $294.2 million. EBITA before significant items was up 30.4% to $21.8 million. Due to a focus on costs and revenue growth, the EBITA margin increased from 6.1% last year to 7.4% this year.

MediaForce scorecard slide

Some, but not all of our MediaForce objectives were met.

We grew the Lasoo website and decreased the EBITA loss. However we did not achieve the run rate break-even position that we were hoping for by the end of FY09.

We are averaging over 800 thousand clicks per month to the Lasoo website. Much of our ongoing investment is in building the Lasoo brand as the premier pre-shopping portal. Our volume of traffic is testament to its growing support and recognition. To assist in managing our expense base we are now providing content management services both for Lasoo and our Dynamic catalogue service via our newly established Philippines business process outsourcing infrastructure.

The letterbox distribution joint venture with NZ Post was bedded down in what was a difficult economic environment. We appointed a new leader and restructured the business during the year and we are pleased to confirm that it is now EBITA and cash flow positive and we are well positioned for that business to improve in line with the economy.

From a sales perspective, MediaForce's revenue was down 2.2% to $225.7 million, as previously mentioned due to a strategic decision to exit from non-catalogue work together with the removal of pass-through telco revenue in the SMS business.

Our catalogue distribution volumes were stable in the period with major retail customers up, but we did see a decline across 2nd tier retailers and smaller customers.

MediaForce financials slide

MediaForce's EBITA margin increased from 11.5% to 12.5% in the period with the removal of low margin activities. EBITA before significant items improved by 6.3% despite the inclusion of the Lasoo loss of $5.8 million this year. The Lasoo loss last year was regarded as a start-up and classified in significant items.

Salmat divisions and services slide

Salmat today has been formed from the acquisition of a range of companies together with internal product and service development. As we acquired companies such as Dialect, AFrame, HPA and VeCommerce, these brands were taken under the Salmat umbrella and allocated into their relevant business division.

Four key brands were then created to fall under the Salmat group – BusinessForce, MediaForce, SalesForce and DigitalForce.

However, it has become very evident that the value of this strategy has been achieved and we now have the opportunity to leverage the tremendous goodwill the Salmat brand has in the marketplace across all its business activities.

Our customers are telling us they want to deal with one Salmat. Therefore we will be phasing out completely the sub-brands and our divisions will now be classified according to their service offering.

BusinessForce will become Business Process Outsourcing, which offers services including transactional & direct marketing services, e-solutions, print on demand and business process automation.

SalesForce will become Customer Contact Solutions, which offer services including contact centres, field sales & marketing, speech, consulting & support services and learning & development solutions.

MediaForce and DigitalForce will become Targeted Media Solutions, offering letterbox distribution, digital, interactive, customer targeting solutions and Lasoo.com.au.

Clients engaging Salmat can select some or all of these services to customise a communications solution specific to their requirements.

Strategic insights slide

As discussed previously, we have a strong business model with a highly diversified product offering. Our unique mix of services and technology absolutely helps our clients achieve real business efficiencies.

The formation of our new senior leadership team and our sales and marketing focus will allow us to better link our divisions across a common platform, so that our clients can benefit from our broad range of services, rather than perhaps one or two services from within a division.

Improving the quality of service offering to our clients has the potential to extend the scope of work that we conduct for each of them. Our current service levels already engender a high degree of client satisfaction and trust. We intend to continue working on improvements in this area to grow revenue and drive client retention and competitive differentiation.

Increasingly clients recognise the importance of utilising targeted communication channels with their customers to enhance loyalty and satisfaction. One of the key ways to achieve this is by treating them as an individual, rather than as a number. Salmat's services provide the conduit to allow this interaction to take place and clients can select from phone, email, post or face-to-face delivery mechanisms to suit their specific communications objectives or all thereof.

For organisations, the ability to commission one outsourced services provider to access this range of channels is appealing. For Salmat, the ability to leverage our relationship with these clients by selecting services from across our divisions to offer a bundled solution to meet their specific needs is a significant opportunity.

Salmat is largely in the business of working with essential, rather than discretionary type communication which makes for a sound business model. We are excited about the opportunities that exist amongst our current client base and also across the mid-tier sector, where we do not have a significant presence.

As with any business, there are risks which we try and mitigate as far as possible. The loss of a major contract or impacts associated with the broader economy naturally has the potential to affect our business. Fostering client and employee relationships to maximise their loyalty is an important mechanism to guard against this including building a strong new business focus to retain a healthy pipeline of opportunities.

Earnings growth forecast – BPO slide

We are anticipating that print and mail volumes in the essential mail area are likely to remain flat in the upcoming year and discretionary mail volumes will continue to be affected by a weaker economy. Electronic delivery is predicted to continue to grow at double digit rates but this is off a low base.

Further integration savings and reductions in overheads will continue to contribute to profitability. Some of these will come from general business initiatives and further benefits will flow from the HPA integration with a continued focus on overhead costs and site consolidation activity. Revenue integrity, labour management, integration and further site consolidation are key improvement programs moving forward. We have already made changes to a number of our sites and are reassessing our footprint to ensure we have the best model moving forward.

Our Print on Demand services have suffered in the past year as it is considered to be a more discretionary spend. Moving forward, given our unique national offering we aim to push into more national customers who can use this service as a fast turnaround print solution and we have restructured the business more in line with the changed environment.

Our Philippines operation offers offshoring opportunity for clients wishing to send data entry, scanning, programming and contact centre work overseas and we are targeting this as a growth area for the company.

Earnings growth forecast – Customer contact slide

In the past year, the majority of the revenue growth in this area has continued to come from opportunities across our existing client base. Our ability to offer a more aligned suite of capabilities than our competitors based on existing relationships and offerings has provided us with a competitive edge and we expect this will continue.

Emerging services within this division continue to have aggressive growth targets. The @Home network is positioned as a bolt-on to our bricks and mortar call centre solution and as a very cost effective and scalable offering. Its success has been driven by excellent market acceptance.

Our learning & development division is an important component within Salmat's suite of services. It has been used as an induction and skills development tool by retail clients improving the selling skills and competencies of their sales teams with an extremely cost effective and flexible solution. We anticipate this service will be another area of growth moving forward but coming off a low base.

Speech solutions are also predicted to have continued growth in the next year, particularly in light of issues surrounding data fraud and security within the financial services sector where our voice biometric systems offers real security solutions to help customers manage and reduce their exposure to fraud and identity theft. Likewise, this platform is providing clients with the opportunity to segment their customer base by routing calls to specialist service agents based on the individual's profile, reducing their service costs and enhancing the customer experience.

Earnings growth forecast – Targeted Media solutions slide

There are significant prospects within the retail sector, reflective of the shift in the way this industry chooses to communicate with its customers.

Increasingly clients require a multi-channel communication capability so that they can link paper-based, mobile, SMS, voice and email technologies – Salmat is ideally positioned to bundle these solutions accordingly.

We aim to break even on Lasoo by the end of 2011 as we continue to invest in building both the brand and content. We are also evolving a complete digital communications solution across on-line, SMS, email and social networking platforms.

In the catalogue area, we are foreseeing growth through a combination of organic and new business wins as we leverage our highly unique delivery model and competency.

Outlook slide

Moving forward, we are anticipating continued positive performance. In my short time with Salmat, we have made a number of important strategic changes which will provide the springboard for this continued growth.

Having almost completed the appointment of the new senior leadership team, we are focused on the consolidation of our one to one communications model to capitalise on the significant opportunities for organic growth amongst our existing client base.

As such, the board is confident that Salmat will deliver an improved result in 2010 and this is reflected in the decision to increase the full year dividend.

We anticipate a stable economic environment and competitive market environment and we will provide an update to our 2010 year at our 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.