

Title : Open Briefing. Wesfarmers CEO on 29 per cent profit rise

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Wesfarmers Limited announced a 29 per cent increase in profit after tax to \$251 million for the year to June 2001. You forecast profit after tax of \$323 million for FY2002. What profit growth do you expect beyond that year and which divisions have most upside?

CEO Michael Chaney

We haven't yet stated publicly any growth expectations beyond this year but our five year plans give us some confidence that we'll have reasonable growth. Profit growth is likely to come from the hardware business, from energy, in particular coal, and from the rural and insurance businesses.

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The final dividend of 60 cents per share fully franked brings the full year to 87 cps compared to last year's 73 cps and represents a 98 per cent payout ratio. Do you plan to maintain this payout ratio?

CEO Michael Chaney

Yes. We plan to maintain our policy of paying out all our after tax profits, subject to adequate franking credits being available. The after-tax profits are after goodwill amortisation.

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Wesfarmers' hardware & forest products business achieved a 4 per cent increase in EBIT to \$146 million. What was the underlying performance of Bunnings after adjusting for forest products?

CEO Michael Chaney

EBIT for the Bunnings hardware business increased by 13 per cent.

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The hardware sector within the retail market has been growing faster than average retail sales. Can it be maintained?

CEO Michael Chaney

There's been about a five per cent per annum growth in the DIY market and we're projecting that will continue.

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Bunnings stores average annual sales of over \$25 million compared with around \$17 million for BBC stores. Bunnings stores have a profit margin of around 30 per cent more than BBC stores and the return on capital employed of more than 20 per cent is double that of BBC stores. What strategies will you employ to improve the financial performance of BBC stores?

CEO Michael Chaney

We aim to lift the financial performance of the BBC stores through a number of initiatives. We will spend some capital on the stores to get them set up to Bunnings' standards. Then it's a question of adopting the appropriate product mix, pricing strategy, advertising strategy, store layout and service levels. We will be increasing the number of employees in the warehouse stores.

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How long will it take to complete that program?

CEO Michael Chaney

It should take us about three years to do all the conversions.

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After the takeover of Howard Smith, the total number of Bunnings and BBC Hardware stores is about 279 with 10 stores overlapping. Do you still aim to roll out around 8-12 new warehouse stores per year and what number of store closures do you expect from the merger?

CEO Michael Chaney

Yes, we still expect to rollout about eight to twelve new warehouses each year. There will be a large number of closures of conventional stores and that could total 80 or 90 but we really have to analyse and understand the performance of the individual stores before we make those decisions.

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Bunnings main markets are in Western Australia, South Australia and Victoria while BBC's are in New South Wales, Queensland and New Zealand. Does the BBC acquisition solve the problem of Bunnings trying to penetrate the Sydney hardware market?

CEO Michael Chaney

The great thing about the acquisition is that it's a near perfect fit geographically so it does give us a better representation in the Sydney market.

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Does BBC have an adequate presence in Sydney already?

CEO Michael Chaney

There are more things that can be done.

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What annual cost savings and volume purchasing discounts do you expect from merging Bunnings and BBC?

CEO Michael Chaney

We've stated a synergy benefit of \$40 million in the first year, increasing somewhat after that. There's been talk in the market of much larger synergies but we think the figures we've put forward are realistic.

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What are the forecast rationalisation costs of the merger?

CEO Michael Chaney

The costs of rationalisation including store closures should be \$80 to \$90 million. We aim to capitalise those costs.

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Presumably, the market share of Wesfarmers' warehouse stores will reach a limit. Although, the superbarn/warehouse concept originated in the United States do you have plans to expand overseas?

CEO Michael Chaney

We think there's capacity to grow within Australia for quite some years and at this stage we don't have plans to expand overseas except, of course, in New Zealand.

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What plans do you have for the Blackwoods industrial distribution business acquired in the Howard Smith takeover?

CEO Michael Chaney

After we acquire Howard Smith we will undertake a full operating and strategic analysis of Blackwoods so that we understand the company and the industry better.

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Wesfarmers' Energy business achieved a 77 per cent increase in EBIT to \$190 million. You received strong price increases from April 1, 2001 for annual thermal and coking coal contracts. What other potential for earnings growth exist at your Premier (Wesfarmers 100 per cent), Curragh (Wesfarmers 100 per cent) and Bengalla (Wesfarmers 40 per cent) coal mines?

CEO Michael Chaney

Coal production across the three mines should increase by about a million tonnes overall this year. There's potential for further increases. At Bengalla, we'll have an opportunity to switch low-priced domestic coal to export coal after 2002 and the sales mix at Curragh will also become more favourable. We are doubling the size of the wash plant capacity at Bengalla by building a duplicate plant and we are upgrading the wash plant technology at Curragh, which will increase the yield of export quality coal.

At Premier there is some potential for continued productivity improvement but Bengalla and Curragh are already operating efficiently.

We've now renegotiated our rail arrangements with Queensland Rail and that will give us some bottom line boost in 2002.

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LPG prices averaged just over US\$300 per tonne last year but have since fallen to around US\$250 per tonne. What is the likely earnings impact of that price fall on your domestic LPG business, Kleenheat and on the export sales of LPG from your Kwinana extraction plant?

CEO Michael Chaney

Falling international gas prices help Kleenheat's margins but give us less earnings on the export side. Overall, higher international prices have helped the bottom line but there's not a lot in it. The optimum is to have high LPG prices during the Australian summer and low prices during the Australian winter because it's during the Australian winter that Kleenheat experiences greatest demand; but this is the opposite of the normal seasonal price pattern.

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Wesfarmers CSBP, your fertilisers and chemicals business, achieved a 17 per cent increase in EBIT to \$53 million. What impact did the drought in Western Australia have on fertiliser volumes in FY2001 and what do you expect this year?

CEO Michael Chaney

Fertiliser volumes were down 14 per cent. We had expected a recovery in the current year but the very dry start to the season probably means that fertiliser sales volumes won't be much different to 2001.

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What has been the recent trend for Wesfarmers CSBP in market share and margins for fertilisers?

CEO Michael Chaney

In 2001, CSBP appears to have picked up about one per cent in market share and margins improved by a reasonable amount. We had a strong margin squeeze in 2000 and we were able to recover some of that despite the difficult seasonal conditions.

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Chemical earnings have been constrained by operating difficulties at the Kwinana ammonia plant and Queensland nitrates project. Are these plants now operating satisfactorily?

CEO Michael Chaney

The Kwinana ammonia plant certainly is. QNP is operating much better but still has some problems which we expect to be resolved soon.

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So you'll get an earnings boost from chemicals this year?

CEO Michael Chaney

Yes.

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Wesfarmers Landmark, your agribusiness products and services subsidiary, achieved a 42 per cent increase in EBIT to \$57 million following EBIT of \$40 million in FY00 and \$25 million in FY99. Where has the improvement come from?

CEO Michael Chaney

It's really across a range of areas. Firstly, it's important to note that there was a \$3 million goodwill charge in 2001 with four months of ownership of IAMA which wasn't there the previous year so you could add that to the underlying earnings growth.

We had improvements in livestock earnings, mainly price driven, higher fertiliser earnings and a significant increase in merchandise earnings with both sales and gross profit margins increasing.

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Wesfarmers Landmark was formed out of the merger between Wesfarmers Dalgety and IAMA Limited. To what extent have earnings risen due to the integration of IAMA and to an improvement in trading conditions?

CEO Michael Chaney

Not much from the former yet. It was more to do with trading conditions.

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What annual cost savings do you expect following the integration of IAMA?

CEO Michael Chaney

It's too early to tell but it's in the region of tens of millions of dollars.

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The Western Australian grain harvest fell around 40 per cent at the end of 2000 and is expected to fall significantly again this year because of drought conditions. How serious are the ramifications for the drought on Wesfarmers Landmark, Wesfarmers CSBP and Wesfarmers Transport?

CEO Michael Chaney

Overall, in the group sense, the ramifications aren't large. We had significant rainfall throughout the agricultural area in the last two weeks and that's made a big difference. Wesfarmers Landmark's chemicals sales suffered in July as a result of the drought but they now should be stronger. CSBP, as I mentioned earlier, will sell less fertiliser than it was budgeting, but it shouldn't be greatly problematic.

The Australian Railroad Group (Wesfarmers 50 per cent) will be affected by the drought because we expect the grain task this year to be about six million tonnes instead of the budgeted ten and a half million tonnes. The EBIT affect of that for Wesfarmers is in the lower single digits. The drought won't affect the remaining parts of Wesfarmers Transport.

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During the year, the Australian Railroad Group (Wesfarmers 50 per cent) acquired 50 per cent of the Western Australian government's rail freight business. Is the business performing satisfactorily?

CEO Michael Chaney

Yes, it's going well.

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Australia's freight industry is likely to move more towards rail transport and away from road transport. Although that may benefit your Australian Railroad Group (Wesfarmers 50 per cent), might it be to the detriment of your road transport business?

CEO Michael Chaney

No. Our road transport business is diminishing and is only a small part of the Wesfarmers group now.

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Thank you Michael.