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The content of this Open Briefing® reflects management and analyst discussion at the Wesfarmers Briefing Day held in Sydney on Tuesday, 15 November 2005.

General Corporate Issues

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Wesfarmers has stated previously that one advantage of investing in a conglomerate such as Wesfarmers is that earnings are likely to be smoothed because each business would usually be at different stages of the earnings cycle. However, it looks like the risk profile of your earnings has increased now that you have a much greater reliance on Curragh. Would you consider selling Curragh to reduce that earnings risk?

Richard Goyder, Managing Director Wesfarmers
Would we be as happy if coking coal prices hadn't risen to US$125 per tonne? The answer of course is no because our shareholders have benefited greatly. Even if prices fall in the next 12 months they will still be high compared with historical levels.

If coal prices fall then we've said that our earnings and dividends will also fall in the absence of an acquisition. However, Curragh has been a fantastic investment and volatile earnings are just the nature of the coal industry. Longer term we believe it is a really good asset to have in the group.

The question about selling it is academic in the sense that no one has made an offer worthwhile considering. It is not a liquid asset and frankly it would have to be a large price for us to sell. Our focus is to run the business as best we can so that it is profitable at any coal price. Sure, Curragh increases the volatility of our earnings, but we're enjoying a strong kick up in earnings because of it.

corporatefile.com.au
Following on from that theme, is there an inclination to look at non-coal acquisitions because Curragh has made your earnings more volatile?

Richard Goyder
We don't have a portfolio theory approach to investment so we haven't decided that we can't look at any more coal assets, but sub-consciously we would probably like to make an investment that will generate increasing profits and returns if coal prices come off. However, that's a perfect world and we don't live in it.

We don't feel compelled to make an acquisition at the moment and even if coal prices fell quite substantially we wouldn't feel huge pressure. We will continue to be very diligent in our evaluation of potential investments and we won't be forced into doing anything unless it meets our investment criteria.

Some people have argued that we should use scrip to make acquisitions because we're trading at a relatively high PE multiple. Although that strategy might be good for our current shareholders it might not necessarily be good for the shareholders of the company we acquire.

We've got a lot of investments under review but who knows whether we'll do anything with them.

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It used to be the case that if you modelled Wesfarmers out a few years, you would spin off a lot of cash and dividends, but the gearing ratio would also decrease fairly quickly over time. It seems that when we do our modelling now we forecast that the gearing levels will only gradually reduce. I know it's an objective to distribute franking credits to shareholders, but there doesn't seem to be the capacity to make a large acquisition. Can you comment on that?

Richard Goyder
We look at our capital expenditure and acquisitions quite separately from our capital management and dividend policy. If we think a new investment meets our hurdles then we would look at how we would fund it whether it's by debt or equity or a combination. We also have the option of reintroducing the dividend reinvestment plan. We don't feel constrained at all from a funding perspective.

Our cash flow continues to be very strong. However, we have a huge capital expenditure program this year and because of our policy of paying out franking credits we won't have a sharply reduced gearing level at the end of the year. We're not unhappy about that because we're happy to have an efficient level of gearing.

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With so many capital expenditure initiatives throughout the company, is it possible that the FY07 capital expenditure budget could approach the $900 million set down for this year?

Richard Goyder
We don't have a good feel for that yet. We think we'll have a pretty strong capital expenditure program for FY07 but we don't know the level yet. We're investing in very attractive growth projects. We hope that we have strong capital programs for a while to come.

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Can you comment on the success of the Howard Smith acquisition including integrating BBC into Bunnings?

Richard Goyder
I think we handled the BBC integration very well. We extracted the cost synergies quickly. We integrated Industrial & Safety pretty well also. We did the initial stages of the integration pretty well, but one difficult issue with acquisitions is melding the different cultures. We've only just started to sound upbeat about Bunnings in NSW. There were a lot of cultural issues there and those issues always take a lot longer to address and there are still some to address in Industrial & Safety. I think that many of the Howard Smith employees had cause to pause and contemplate their new owners, particularly when we publicly compared the performance of BBC stores against Bunnings stores.

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Will the change in gearing due to adopting IFRS alter your target gearing range?

Richard Goyder
We're currently doing a wider review to determine our appropriate gearing range. We're discussing our lending arrangements with our banks and it's a more in-depth review than just the impact of IFRS.

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Can you expand on the discussion of the relevance of private equity investments in the Wesfarmers group?

Richard Goyder
As Gene mentioned, private equity investments will have challenges because a lot of money is finding its way into the sector. Gresham may establish Private Equity Fund 3 in another year or two and so our commitment will potentially increase and some of the volatility in our investment returns from private equity will decrease. We see it as an area with increasing importance for the group providing it continues to make satisfactory investment returns.

Industrial & Safety

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You've had the Industrial & Safety business for about four years now but its performance has recently gone backwards and the return on capital is below your target. Is this a business that should be in Wesfarmers? Can you reach that hurdle rate?

Terry Bowen, Managing Director Wesfarmers Industrial & Safety
I think it is certainly a business that should be part of Wesfarmers - it is a very good business. While, it is unlikely that Industrial and Safety will achieve a return on capital of 20% in the next 18 months or so, over the longer term I do believe that sort of return is achievable. We must, however, focus on improving our capital management, as well as how we go to market with our products. These kind of returns though are achievable as evidenced by some of our competitors who achieve a return on capital of more than 50%. It all depends on whether we have the right business model and that is something we are reviewing.

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You mentioned that the manufacturing segment is weak. What is your exposure to manufacturing?

Terry Bowen
Manufacturing is currently our largest business segment. While we will continue to treat this segment as very important and look after our manufacturing customers well, we are also looking at opportunities and ways to widen our exposure to those segments which are growing and we have a smaller exposure to, such as the infrastructure and resource sector.

corporatefile.com.au
You mentioned that you've surveyed some of your staff and customers. Can you detail the feedback you've received?

Terry Bowen
It's too early as yet as I've only received formal responses from a fraction of our staff who I asked to come back to me with business opportunities. I can however say that early indications are that there appears to be common themes in their responses, which are positive, and note a variety of capital management and specific growth opportunities.

corporatefile.com.au
Can you apply any aspects of Corporate Express's strategy to your business?

Terry Bowen
There are always elements you can learn from successful companies. They understand the customer segments they operate in and they've proven that you can get good returns in a highly competitive industry if you get your model right.

corporatefile.com.au
You've only just joined Wesfarmers as Managing Director of Industrial & Safety. Can you outline your experience prior to taking this role?

Terry Bowen
My background was initially manufacturing. I spent 11 years with Tubemakers of Australia, which is now OneSteel. I then spent seven years in Wesfarmers Landmark with the last three and a half as CFO, which included operational responsibilities for the banking and insurance parts of this business as well as typical accounting, strategy and information technology responsibilities. Finally, I spent nearly two years as CFO with Jetstar from its start-up after leaving Landmark when it was acquired by AWB.

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What explains the cash generation levels say over the last three years? Are customers putting pressure on you to hold more inventory?

Terry Bowen
This is a good cash flow business. In respect of consignment stock, that does not appear to be happening at large. In fact our consignment stock levels have been reducing across the business of late. What our customers are saying though, is that they want our sales staff to give advice on their business to help them reduce their overall costs rather than just selling them a product. They really want to build a knowledgeable relationship and that's why staff retention I think is really important for us.

corporatefile.com.au
What cash is the business generating each year?

Terry Bowen
We're generating cash of around $120 million per annum and after capital expenditure around $100 million, so it's a good cash-generating business. My focus is to improve this over time and improve the return on capital in the business.

corporatefile.com.au
Are you in danger of worsening the business performance if you try to push it too hard?

Terry Bowen
That's a good point. We could probably achieve a 20% return on capital within 18 months if that was our only goal, but that could require us to sell large parts of the business and would reduce our earnings overall. We have to be careful that we improve the business across the board.

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Most of your capital employed is within distribution fit out and inventory. You have a very wide product range. Where are the opportunities to improve the return

on capital? Are you going to narrow the product range? Are you going to wind back the distribution hub?

Terry Bowen
There are opportunities certainly for us to improve our return on capital and our staff recognise this as reflected in their feedback to me. It's too early to give a detailed answer on where the improvements will come from other than to say we will be taking a wide view of the opportunities and not merely walking away from market segments.

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We've understood for years that the strategy for Industrial & Safety was to become the specialist in several segments. Is that still the key to getting more business?

Terry Bowen
We've got to make sure that our specialist businesses are seen as true specialists in the market place with everything that that entails, but I wouldn't say that these businesses are our only opportunity for growth. Over time we also have good general industrial product growth opportunities as well. Again in respect of our future strategic direction, it's too early to say, but clearly this is how our main competition operates.

corporatefile.com.au
Would it be fair to say from early initial observations that size is not an advantage in this business?

Terry Bowen
It depends on the customers. You've got to make sure you've got the right distribution model and offering for each part of your customer range.

CSBP

corporatefile.com.au
Can you explain your long term ammonium nitrate contracts and whether these set both volumes and prices?

Keith Gordon, Managing Director CSBP
Our ammonium nitrate contracts generally have a take or pay volume and a price with an escalator. In our case, the escalator relates to input costs.

corporatefile.com.au
Is it correct in saying that, with spot ammonium nitrate prices currently very strong, when you are importing product to meet customer contracts it has a significant negative earnings impact?

Keith Gordon
That issue applies to QNP, but not to Kwinana. Product from QNP was actually slightly oversold when the plant was commissioned. At the moment that is the key issue facing QNP and if the expansion goes ahead we would be able to supply all contracts from our own production.

corporatefile.com.au
To what extent is QNP production oversold?

Keith Gordon
About 5-10% of capacity.

corporatefile.com.au
Wesfarmers' strategy has always been that it won't inject capital into a business until it achieves an acceptable Return on Capital (ROC). QNP is returning well below your target ROC. Can you explain the logic in expanding the plant?

Keith Gordon
We haven't taken the decision to expand yet. We're currently evaluating it. It won't go ahead unless we can achieve firm contracts and pricing agreements with customers. The current performance of QNP is a concern for us. We've started to address that by employing new management and focusing on getting the fundamentals of the business right.

The other issue we need to understand is the change in supply/demand dynamics after the Dyno/Orica deal. Orica will pick up supply capacity in south east Asia and we have to work out what it all means in terms of the supply/demand balance in Queensland. We have thoroughly committed to evaluate an expansion of QNP and that includes speaking to all our customers. We'll make a decision on the expansion in the first quarter next year, but we haven't pre-determined the outcome. It will have to be a "customer-led" expansion if it is to go ahead

corporatefile.com.au
You've said that half the additional output from Kwinana will be taken by Dyno. Do you know if that is all their requirements?

Keith Gordon
That's not correct. A small number of customers will take the output from the expanded facility.

One of the issues we focussed on in our offtake strategy was to make sure we had secure supply arrangements. We don't think that there will be enough demand in north west Western Australia to justify a new ammonium nitrate project in addition to our expansion.

corporatefile.com.au
What timetable is possible if you proceeded with an expansion at QNP?

Keith Gordon
First production from the expanded plant would be around mid 2008. This could be impacted by the tight construction market.

corporatefile.com.au
You mentioned that your long term ammonium nitrate contracts have escalation clauses relating to input costs and that you'll be short ammonia going forward. I assume the contracts have "pass through" for ammonia?

Keith Gordon
We will have a "pass through" for the ammonia on ammonium nitrate going into the explosives market. In the fertiliser market, the price for our Flexi-N product follows the urea price which has a linkage to ammonia

corporatefile.com.au
Will you continue with the de-bottlenecking exercise at QNP if the expansion does not proceed?

Keith Gordon
That would certainly become a priority to evaluate again and would more than cover the current production shortfall against our contracts.

corporatefile.com.au
Can you explain the current price environment in the context of your expansion plans?

Keith Gordon
We will need a significant increase in price for the QNP expansion to be viable. There is a trade off in price that comes with securing long term take or pay contracts and we have to recognise that when we're negotiating prices.

We're negotiating price contracts for any additional output from QNP at the moment and prices have been finalised with new customers for the expanded output at Kwinana.

corporatefile.com.au
Why haven't you undertaken an ammonia expansion at Kwinana?

Keith Gordon
We de-bottlenecked the ammonia plant in 2004 which increased it to around 260,000 tpa . There's no significant opportunity to de-bottleneck it further. The most competitive world ammonia plants now have capacity around 800,000 tpa so it wouldn't make sense to expand our plant to supply the shortfall in our current requirements of around 100,000 tpa. Ammonia imports are available and we've been able to manage the price risk.

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Do you still have domestic ammonia products?

Keith Gordon
We still have a number of domestic ammonia contracts. The intention is to maintain those sales and import all our additional ammonia requirements when the new ammonium nitrate plant is commissioned.

Insurance

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Is it accurate to say that the Lumley business has been hard to integrate?

Bob Buckley, Managing Director Wesfarmers Insurance
When we bought Lumley it wasn't so much an issue of integrating its business because it runs under a different model to WFI. We would never take a "direct" model and try to integrate it with a "broker" model because the first thing that would happen is we would have all the brokers protesting that we're competing with them. We're running Lumley separately from our other businesses. However, if we acquired another insurance company it would either be a direct model or a broker model and we could therefore either integrate it with Lumley or WFI.

corporatefile.com.au
How do you view the value of other insurance businesses?

Bob Buckley
They still look pretty expensive, but there could be all sorts of reasons why one or two competitors decide to quit the market whether it is because of losses from the hurricanes or whatever.

corporatefile.com.au
You mentioned that the reinsurance market is tightening. Is there any evidence of that coming through in the commercial market?

Bob Buckley
It won't just come through in particular parts of the business. It will be across the board, but it's hard to tell precisely what impact it will have. December is a big reinsurance renewal period, followed by a smaller period in March and another large one in June. We will only notice any movements in pricing in reinsurance at those times. One principle of the insurance industry is that many pay for the few. The losses in the hurricanes were substantial. Reinsurers will probably have to put their prices up and it will flow through to the primary market.

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Can you indicate in which area of insurance you're considering the small acquisitions you mentioned?

Bob Buckley
Not really because they are all confidential. We're looking at niche businesses that have been running for some time with good results and where the owner wants

to quit the business for various reasons. There are probably a dozen or so of these businesses around at the moment.

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Acquisitions aside, do you expect to reduce the amount of capital employed in the business?

Bob Buckley
I don't think so because we already operate at the lowest possible level of capital. We need a minimum amount of capital to support the business according to an APRA formula and we also need a minimum amount of capital to maintain our Standard & Poor's rating of A-. If we fall below that rating many brokers won't deal with us.

corporatefile.com.au
Can you explain the impact you expect from the anticipated increase in reinsurance rates?

Bob Buckley
In the past, insurance rates in the industry have increased after reinsurance rates have gone up. Historically, most increases in insurance rates have emanated from the reinsurance market after there have been large international catastrophes. There is some tolerance to absorb small increases but it won't hold for these recent large reinsurance losses. The reinsurers will have to put their rates up.

corporatefile.com.au
You showed a chart of the Gross Earned Premiums for Australian General Insurers. It showed that you're very small compared with the larger players, yet your expenses are quite competitive. How do you manage that?

Bob Buckley
We've always had a strong focus on expenses. One thing that helps us is our direct business which we source without paying large commissions and we also haven't had any failures with our large IT programs. We've always had a careful approach to IT. We're rolling out new systems now and we think they will give us further advantages in running our business profitably.

corporatefile.com.au
Can you explain the $5 million of EBITA from Non-Insurance Activities earned in FY05?

Bob Buckley
It is an aggregate of our financing businesses. It should be ongoing.

corporatefile.com.au
How much of your business is long tail?

Bob Buckley
I'd say about 20% although I can't be exact.

corporatefile.com.au
Where do you stand in the commercial motor market?

Bob Buckley
We're the number one insurer for commercial motor market and fleet management in Australia and New Zealand. Fleet management includes things like total risk management and maintenance and so it's a fairly hard model to replicate.

corporatefile.com.au
Have the returns come down in that class?

Bob Buckley
It has become more competitive because new entrants have been attracted to this segment after we had a run of dry roads and low level of accidents.

Business Development, ARG, Gresham

corporatefile.com.au
What is the carrying value for Gresham Private Equity (GEP) Fund 1 and GEP Fund 2?

Gene Tilbrook, Finance Director Wesfarmers
We have about $38 million in Fund 1 and a little under $20 million in Fund 2.

corporatefile.com.au
Do you expect returns from these investments of more than 20%?

Gene Tilbrook
We expect some very high internal rates of return from a couple of those investments but they are relatively small investments.

corporatefile.com.au
Do you have any involvement in the management of these businesses? What value do you add to the management?

Gene Tilbrook
We have management involvement in some of the investments such as retailing and distribution; mainly at the time of investment or any significant change to the business.

corporatefile.com.au
What is the purpose of these private equity investments when you consider the market capitalisation of Wesfarmers relative to these small investments?

Gene Tilbrook
We've committed $150 million to Fund 2 which is significant for Wesfarmers. Our primary goal is to make satisfactory returns on investments. That has certainly

been the case for Fund 1 and the indications are that that will continue to be the case as the remaining investments in Fund 1 are realised. The environment for private equity is such that the returns over the last five years won't necessarily be repeated over the next five years, but we still expect to get returns in line with our targets.

corporatefile.com.au
If you exclude Repco, are the rest of the investments in Fund 1 making an acceptable return?

Gene Tilbrook
The very first investment, Eurogestion, which we divested out of Fund 1 returned 2.5 times the investment in less than two years. We expect to at least double our money from our investment in EROC.

Impact of International Financial Reporting Standards

corporatefile.com.au
You stated that liabilities of $151 million had been recognised in accounting for the Stanwell rebate. Can you outline the components of that number?

David Moroney, General Manager, Group Business Services
There were a number of concessions we gave when purchasing Curragh North. These were the export price rebate, the volume rebate and a discount on steaming coal prices to Stanwell. That liability relates to those three components. The amount relating to the export price rebate only for 2006 is approximately $80 million and that is the amortisation amount that we'll be recognising. The $80 million approximates the cash payment under the Stanwell rebate. Due to the price rebate being determined on a rolling 12 month basis, there is a time lag impact on the amount paid. If coal prices stay at the same level next year you would expect that number to go up.

Energy

corporatefile.com.au
You mentioned that total annual cash production costs at Curragh had increased in absolute terms by 24% based on a comparison of October 2005 against October 2004. What is the general outlook for costs?

David Robb, Managing Director Wesfarmers Energy
Although we are clearly seeing an increase in total cash costs, driven by both production volume increases and unit rate increases in business inputs such as fuel and contractor charges, we don't believe these increases are structural. Fuel prices will probably eventually fall and that will reduce both contractor rates and the cost of operating our own equipment. Contractor margins will also presumably fall as the scramble to secure contractors subsides. The same outlook can be envisaged for many of the inputs that are currently in high demand.

That said, there are some aspects of our current mode of operation which will impact costs for a while to come. For example, we are using a higher proportion of truck and shovel than we would in our steady state operation because Curragh North is currently all contractor and all truck and shovel. Over the next couple of years we will commission (in the fourth quarter of calendar 2006) the conveyor from Curragh North to Curragh and also relocate two of our draglines up there, which will reduce unit production costs.

Of course, these cost pressures are industry-wide and we are currently going through an exercise as part of our normal corporate planning process to update our estimate of where we sit on the industry cost curve. I don't have the results of that yet.

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Can you give an indication of the relative pricing of semi-hard coking coal compared with hard coking coal?

David Robb
I won't answer it specifically, but we were successful in the negotiations for prices to apply in the current contract period in linking semi-hard coking coal price outcomes to hard coking coal outcomes. While demand for high quality coking coal remains firm, we have seen some slow down of crude steel production in Europe and Japan and I think it is logical to assume that suppliers generally will find it harder to maintain those coal price relativities, if the supply/demand balance changes in favour of buyers.

corporatefile.com.au
Can you remind us what your long term coking coal price assumptions are in those hedging numbers you gave us?

David Robb
We assume that prices will revert to long run historic levels which average around the low US$50s per tonne. I wouldn't suggest that that will necessarily prove to be the long run level in the future but the one thing we don't want to be is over hedged. We are therefore conservative on a number of fronts when we forecast revenues as part of our hedging.

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How confident are you of achieving your forecast of 6.4 to 6.8 million tonnes of production from Curragh in FY06? How are you going to get the big increase in the second half of the year? Is the infrastructure in place to handle that sort of production?

David Robb
The infrastructure is in place to support that volume, unless there is an unforseen event such as a port closure or train derailment. Our job is to have coal available to match our sales plan and to load every train - which is something that we haven't done consistently over the first half.

We expect to produce just over 3 million tonnes for the December half and then run at a rate of around 7mtpa for the June half which should give us the forecast 6.4 to 6.8 mt for the year.

corporatefile.com.au
Given it has so many moving parts, is the wash plant capable of delivering those tonnes?

David Robb
We expect that the plant will be able to operate more reliably in future and produce the required coal to support our sales targets.

corporatefile.com.au
There are conflicting reports about the future of Mt Pleasant and how it could affect the operation of Bengalla (WES 40%) considering Rio owns 100% of Mt Pleasant, but only 60% of Bengalla. Is there a risk that Rio will operate Mt Pleasant to the detriment of Bengalla? Are you in a vulnerable position?

David Robb
We're in competition with everyone in the Hunter Valley, including a number of new mines. The development of Mt Pleasant doesn't change that dynamic materially in terms of winning export and domestic sales volumes.

It will be interesting to see what Rio's decision is on Mt Pleasant. My understanding is that they are working through a feasibility study with a decision due in the first half of calendar 2006.

A number of industry analysts have observed that it would make sense, when Mt Pleasant does go ahead, that the development leverage existing infrastructure at Bengalla. Wesfarmers is willing to discuss any mutually beneficial proposition that may be put to the Bengalla Joint Venture.

In the unlikely event that material conflicts of interest emerge, there are solutions available to the venturers under the terms of the joint venture agreement to deal with them.

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You stated that your export sales volumes from Curragh are typically in the proportion of 60% hard coking coal, 20% semi-hard coking coal and 20% PCI. Is it possible that any of your hard coking coal could be re-classified as semi-hard coking coal and therefore receive a lower price?

David Robb
No, although bear in mind that not all hard coking coal products are identical. Customers have different tolerances for particular specifications - ash levels for example - and this is reflected in prices received by suppliers. We expect to maintain approximately that proportion of hard coking coal exports as part of a total export sales volume of around 7 mt.

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What proportion of LPG production do you expect to export?

David Robb
Last year we produced 310,000 tonnes of LPG, of which slightly more than 100,000 tonnes was sold domestically. This year, as always, the domestic market will be satisfied first and any production above that level will be exported. Daily LPG content has been very volatile this year, but if the current average content levels continue we would expect LPG production this year to be roughly half that of last year.

corporatefile.com.au
What earnings does the LPG extraction plant generate?

David Robb
We've never commented on the profitability of the plant.

corporatefile.com.au
You mentioned that it's impossible to recover fully the increases in input costs within the Kleenheat distribution business. Is that comment applicable to both the auto gas market and the industrial gas market?

David Robb
It's usually easier to pass on input cost increases in markets where you have customers who have higher costs to switch fuels. The auto gas market is particularly tough, but despite that Unigas has actually increased ROC in recent times through a focus on capital employed as well as margin management. Although business conditions are in many ways currently very tough for Kleenheat, cost differentials between LPG and LNG and other transport fuels are positive for our business longer term.

corporatefile.com.au
You've spoken about Curragh costs. Can you speak about the cost issues at Bengalla and Premier?

David Robb
Bengalla is subject to similar pressures as Curragh in areas such as contractor labour, fuel, electricity, contractor rates, maintenance and spare parts. It's an industry wide issue.

Premier is a bit different. Premier does not have Curragh's volume growth challenge and short term dependence on contractors and we expect cost increases would therefore be somewhat less than those at Curragh.

Bunnings

corporatefile.com.au
Can you explain your comments that there is strong competition for the discretionary spend?

John Gillam, Managing Director Bunnings
There are two points I wanted to make here. The number of home improvement type shows on TV has decreased and we now need to provide more inspiration for people to spend on their homes. You'll see us do more on that front over the next 12 months. Secondly, in the current tighter retail climate we're seeing retailers in other market segments, such as electronics, offering deep discounts to try to increase their turnover and that has an affect on our business because it takes away some of the available discretionary dollars. We simply won't take that deep discounting approach because we think it would be damaging to our business over the longer term.

corporatefile.com.au
You stated that July to October cash store on store growth was 1.1%. Can you give an indication of the underlying cash store on store growth for a store that has been trading for a few years?

John Gillam
I can't answer that directly but I'll try to give some guidance on a few relevant factors. The overall comp store number is obviously made up from all our trading regions and each trading region has quite different drivers. For example, South Australia, which is not an overly large part of our business, is trading poorly and Victoria has also been doing it tough for some time. The Western Australian and Queensland markets, on the other hand, appear to be responding to the positive resources related economic activity.

We've been happier with the way the overall market has been responding in more recent times, but conditions have certainly been tighter for us over the past two quarters and we just have to keep focussed on presenting our offer as best we can.

corporatefile.com.au
Do you expect EBITA/Sales margins to grow when you consider the positive impact from store refurbishments and the reduction in shrinkage?

John Gillam
We would be concerned if our EBITA/Sales margin grew markedly because we think it would attract more competition. If you look at our business across a range of benchmarks, one of the areas we perform best in is the EBITA/Sales margin and we think the 10% mark is a pretty good performance. We certainly don't model it going higher, although there can be short term spikes as business improvement strategies or economies of scale benefits kick in.

In addition, within our business we've seen positive margin shifts as we have lifted the ratio of our retail sales over our trade sales and through another sales mix shift as the volume of sales from builders, which is our largest but lowest margin category, has declined.

These factors allow us to lower prices and by holding the EBITA/Sales margin at around the current levels, we can reward our customers with lower prices and reward our shareholders with good returns.

corporatefile.com.au
How do the margins in the smaller format stores compare with the margins in the larger stores?

John Gillam
This depends on the characteristics of the individual store. Some of the smaller format stores have fairly large trade volumes and therefore smaller margins, but others like those in some inner city locations can have higher margins than our average.

corporatefile.com.au
What are the latest trends in basket size per customer?

John Gillam
This is not something on which we comment in detail but we are keen to grow our basket size in terms of product units and dollar value and there is more emphasis on that at store level.

corporatefile.com.au
Can you talk about the success of some initiatives such as cross-docking trials? Do you expect big cost savings?

John Gillam
Yes we do expect cost savings from a number of initiatives that we are pursuing across our stock processes and within our supply chain, but not in the near term from cross-docking. Our supply chain is a little different to more conventional retailers. A large chunk of our business comes direct to our stores because of its extreme size and/or weight or because of its organic nature. We also have product that we import ourselves that already goes through a DC, leaving around 50% to 60% of our volumes which could go through a cross-docking style operation. Within those volumes, some of our suppliers have already optimised their distribution and there is not the level of savings from a cross-docking set-up that might appear from a quick look. We did complete a two month trial of cross-docking within one region and this was very useful in terms of what we learnt.

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Can you explain the split-level store concept? Will it change the style of stores you're rolling out?

John Gillam
The economics of a possible multi-level store are a little different to our normal store as they have a much higher capital cost. And the work we are doing won't

change the type of stores we are currently rolling out as we still prefer the large single level store because it's a lot easier to run and to shop in. However, multi-level stores may be suitable in inner city areas where we currently only have smaller, traditional format stores and where we have struggled to secure the land we need for our warehouse format.

We've invested quite a bit in study tours over the last 12 months looking at the best performing multi-level store models in other parts of the world and we have worked up plans on a site in Hawthorn in Victoria on which we are currently seeking planning approval. One concern we have addressed to ensure there is connectivity between levels and we think a large cutaway will achieve that and allow our customers to navigate such a store much more easily.

It's early days as we haven't secured planning approval as yet but it is likely that we'll open one of these multi-level stores in the next 24 months. If it performs well, we'll be looking to roll out this new format pretty quickly.

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You mentioned that you were doing a total revamp of special orders. Can you give more detail on what you expect from this program?

John Gillam
As I mentioned in the presentation, last month we launched in our Victorian stores a new approach to special orders. We have started with three categories and by March we aim to lift that to six or seven categories and to extend the new offer into the Sydney market as well. That'll give us a good indication of how our customers and suppliers are responding to this. In the longer term, we would like to see special orders grow to represent a high single digit percentage of our total sales, with a low single digit level of cannibalisation. We see it as a big add-on opportunity, but every product segment is a bit different and we'll have to work hard with our suppliers to get it right.

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Is there a strong correlation between the performance of your business and the housing market?

John Gillam
Our market conditions become more challenging when the housing market drops off. One possible exception is NSW where we have a relatively smaller market share. We're actually achieving good growth in that market and we look to 2006 with some confidence.

corporatefile.com.au
You talked earlier of needing to do more to inspire customers. Will this mean we will see more TVC's or things like sponsorship opportunities?

John Gillam
I don't think you'll see our brand name on a football jumper or a sports stadium anytime soon, nor will you see an increase in TVC's. We'll be spending our

marketing dollars through mediums aimed directly at attracting people to our stores and a large amount of our marketing effort will continue to be directed at the local community level.

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