Paperlinx

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PAPERLINX 2015 INTERIM RESULTS

PaperlinX Limited (PaperlinX) today announced a statutory loss after tax of $(90.8) million for the six months to 31 December 2014 compared to a loss of $(28.4) million for the prior corresponding period (pcp). Included in the loss is an impairment charge of $(63) million relating to impairments of goodwill in Canada and Asia and other non-current assets in Europe. The underlying EBIT loss(1) for the six month period was $(12.7) million (compared to $(9.6) million pcp).

In the second quarter, the market demand for paper in Europe fell significantly more than expected. At the same time, the market in the UK and Benelux changed significantly with some major suppliers (mills) selling directly to our customers at unsustainably low prices. As a consequence, the UK and Benelux businesses in particular experienced a poor second quarter that led to trading results well below expectations which has put pressure on the Group's cash position. As the UK is our largest operation, this has a significant impact on the Group's operations.

Given these market conditions, the Directors chose to pursue a Strategic Review ('Review') in late December 2014, which has focused on the European, Asian and Canadian assets.

The Company recently announced the sale of its Canadian operations (Spicers Canada) and for the purposes of these results, the business will be classified as a continuing operation as at 31 December 2014. Competition clearance has been received and this transaction is now expected to close on Monday 2nd March 2015. Gross proceeds from the sale are anticipated to be C$63 million.

As part of the Review, the Company continues to engage with interested parties with regard to the sale or restructuring of all or part of the European operations. Negotiations are progressing in a positive direction with certain parties in relation to a whole of Europe transaction or the sale of certain operations in Europe.

The key features of the 2015 Interim results are:

- Continuing revenue of $1.30 billion, fell 12% from $1.48 billion pcp (fell by 13% in constant currency(1))
- Underlying EBIT loss(1) of $(12.7) million for the Group was adverse to the prior period loss of $(9.6) million
- Impairment charges of $(63) million, include write downs of goodwill for the Canadian business of $(31.7) million related to the sale process, and further write downs of non current assets in the European and Asian businesses
- The Australia, New Zealand and Asia (ANZA) business delivered a positive underlying EBIT(1) of $9.1 million (down 1% pcp)

(1) Non-IFRS measure – refer Appendix 2

- Canada improved its performance, delivering a positive underlying EBIT[1] of C$7.4 million (up 4% on pcp)
- The European business reported an underlying EBIT loss(1) of €(14.9) million (an increase of 13% from pcp) mainly due to a shortfall in earnings from Commercial Print divisions in the UK and the Benelux
- Growth continues in our diversified businesses but still not at the levels required to offset the diminishing Commercial Print segment. Total gross margin for Sign & Display/Visual Technology Solutions (VTS) increased by 5.1% and Packaging gross margin increased by 5.4%. The recent Total Supply signage acquisition in New Zealand performed well.
- Trading expenses decreased by 8.5% compared to pcp
- Pre-tax restructuring charges of $(6.3) million represent a slow down in restructuring activities due to funding constraints linked to poor trading performance. In the half, FTEs reduced from 3,459 to 3,309.
- Negative operating cash flow of $(54.0) million versus cash outflow of $(29.9) million pcp was an unfavourable movement relating to poor trading performance and tightening of supplier trading terms
- Net debt of $158 million is an increase from the June 2014 balance, and reflects unfavourable trading results, additional cash commitments to restructuring plans and unfavourable foreign currency translation movements
- The 31 December 2014 financial covenants relating to the main European facility were waived by the lender

Commenting on the result, PaperlinX Chairman, Robert Kaye SC said, “Despite consistently positive performances from Spicers ANZA and Spicers Canada, the Interim results are negatively skewed by the underperformance of the European business which experienced a very tough six months and in particular the second quarter.”

“We have continued to lower our cost base through restructuring and cost reduction initiatives and achieved a drop in trading expenses but this has not been enough to offset the fall in sales in Europe which has impacted the Group’s performance. This also led to pressure being placed on our European lending covenants.”

“This is a disappointing result out of Europe. In December when we announced the Strategic Review the Board flagged it was taking a more cautious stance on the outlook for the European business and we had no choice but to consider the position regarding non-ANZA assets.”

“The sale of Spicers Canada provides liquidity into the Group to ensure the Strategic Review can continue and ultimately can deliver the best outcomes for shareholders. The Review is progressing and we remain positive about the prospects of securing transactions with one or more interested parties in relation to our European businesses.”

“Once the Review is finalised and the recommendations are implemented, it is likely that PaperlinX will have a reduced portfolio of assets with greater prospects for financial stability.”

(1) Non-IFRS measure – refer Appendix 2

“The Board is confident that the newly appointed Managing Director and Chief Executive Officer, Andy Preece, will lead the Group forward with a renewed focus for growing our diversified offer and managing the structural shift in Commercial Print. Andy has a track record of building positive relationships with key stakeholders and delivering strong results despite difficult trading conditions.” said Mr Kaye.

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(1) Non-IFRS measure – refer Appendix 2

<u>**RESULTS FOR THE SIX MONTHS TO 31 DECEMBER 2014**</u>

PaperlinX Limited has reported a statutory loss after tax of $(90.8) million for the six months to 31 December 2014.

Results Summary		Actual Dec 2014	Constant currency *(1)* Dec 2014	Actual Dec 2013	% Change v Actual	% Change v Constant currency *(1)*
Net sales revenue - continuing	$000	1,296,659	1,281,264	1,475,497	(12)	(13)
Earnings before interest and tax - continuing	$000	(82,001)	(81,238)	(18,798)	(336)	(332)
Underlying earnings before interest and tax *(1)*	$000	(12,692)	(11,892)	(9,583)	(32)	(24)
Profit/(loss) before tax - continuing	$000	(87,421)	(86,858)	(25,276)	(246)	(244)
Profit/(loss) after income tax - continuing	$000	(90,088)	(89,536)	(28,204)	(219)	(217)
Statutory profit/(loss) after tax	$000	(90,804)	(90,158)	(28,441)	(219)	(217)
Net working capital	$000	442,845	445,630	546,507	(19)	(18)
Net operating cash flow	$000	(54,026)	(52,557)	(29,905)	(81)	(76)
Net debt / net debt & equity	%	46.5	46.0	33.5	1300 bpts	1250 bpts
Basic earnings per share	cps	(13.7)	(13.6)	(4.7)	(191)	(189)
Dividend per ordinary share	cps	nil		nil		
FTEs - continuing		3,309		3,824	(13)	

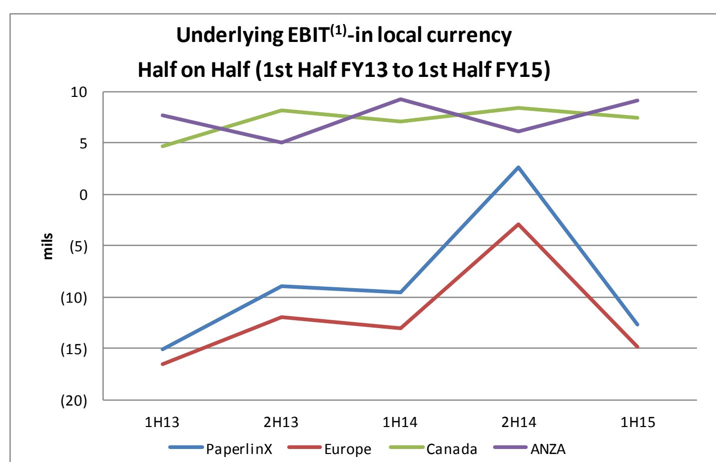
OPERATING PERFORMANCE

Revenue

Continuing sales revenue for the Group fell by 12 per cent from $1.48 billion to $1.3 billion, largely on the back of lower paper volumes in our key markets and changing market dynamics in Europe that caused a loss of market share in the Benelux and the UK. The impact of technology continues to reduce the demand for Commercial Print products as the permanent structural decline in this segment is felt in all regions. Our strategy to boost revenue involves continuing to improve our margin management and shifting our focus to growth segments other than Commercial Print.

Earnings

The Group reported an underlying EBIT loss(1) of $(12.7) million which is adverse to the prior period loss of $(9.6) million and primarily reflects the impact of losses from our European business in the past six months. The ANZA region delivered a positive underlying EBIT(1) result of $9.1 million, (1 per cent down on pcp) due to a solid performance from Spicers in Australia and Total Supply in New Zealand. The Canadian business improved its performance, delivering growth of 4 per cent at the underlying EBIT(1) level compared to the prior period. Europe reported losses of $(21.5) million at the underlying EBIT(1) level, an increase of 13 per cent on the prior period loss showing the need to continue adjusting the cost base and growing a higher margin product mix.



(1) Non-IFRS measure – refer Appendix 2

Restructuring activities

Commitments to restructuring activities slowed in the first six months of FY15 mainly due to the commencement of the Strategic Review and due to funding constraints. Europe had the majority of the HY15 restructuring charges reflecting efforts to reduce fixed costs in the UK and the Benelux. Predominantly, this has involved lowering headcount (reduced FTEs by 4.3 per cent since 30 June 2014) and we expect to see some benefits of the cost savings flow through in FY15 and beyond.

Restructuring charges (pre-tax)		Dec 2014	Dec 2013	% Change
Europe	€000	(3,453)	(5,104)	32
Canada	C$000	(113)	(405)	72
ANZA	A$000	(997)	(412)	(142)
Unallocated	A$000	(208)	(946)	78
Total	**A$000**	**(6,314)**	**(9,215)**	**31**

Diversifying product mix

The impact of technology on traditional forms of communication continues to reduce the global demand for commercial print. This reality is the platform of our strategy to develop alternative segments in Sign & Display/VTS, Packaging, and Graphic Supplies which have relatively higher margin opportunities. We have focused on driving organic growth in these segments, but will seek appropriate bolt-on acquisitions to more effectively accelerate expansion in the future if funding is available. For instance, in October 2014 the Company acquired Total Supply, a leading sign industry supplier in New Zealand.

Our Sign & Display/VTS business represents 12.1 per cent of total sales and this market continues to grow. We supply screen, wide and grand format printing and finishing, including consumables, hardware, software and accessories. From point-of-sale and vehicle graphics, through to exhibition stand construction and shop fit-out, we distribute an extensive range of substrates including banners, synthetics, self-adhesives and rigid materials like thermoplastics.

Our Packaging business, which now represents 10.8 per cent of total sales, is showing further potential for growth. Our industrial supplies and packaging materials range from cartons and adhesive tapes, to protective packaging and shipping supplies and we can also provide customised packaging solutions.

We also offer a range of graphic supplies and systems for traditional printing press rooms, such as plates, inks, software, varnishes, coatings, chemistry and cleaning supplies. This business represents 2.9 per cent of total sales.

(1) Non-IFRS measure – refer Appendix 2

OPERATING PERFORMANCE BY REGION

The following table shows underlying EBIT[1] and sales revenue by regional segment for the six months to 31 December 2014.

Operating Summary		Sales Revenue Dec 2014	Sales Revenue Dec 2013	Underlying EBIT (1) Dec 2014	Underlying EBIT (1) Dec 2013
Segment:					
Europe	$000	883,943	1,042,340	(21,493)	(19,092)
Canada	$000	205,215	213,551	7,495	7,375
Australia, New Zealand, Asia	$000	209,016	221,393	9,122	9,235
Corporate/Unallocated	$000	(1,515)	(1,787)	(7,816)	(7,101)
Total continuing operations	**$000**	**1,296,659**	**1,475,497**	**(12,692)**	**(9,583)**
Discontinued operations	$000	-	-		
Total	**$000**	**1,296,659**	**1,475,497**		

PaperlinX Europe

Europe - Continuing		Dec 2014	Dec 2013	% Change
Net sales revenue	€000	610,893	715,462	(15)
Profit/(loss) before interest and tax	€000	(35,259)	(18,209)	(94)
Underlying EBIT *(1)*	€000	(14,854)	(13,105)	(13)
Underlying EBIT/sales revenue *(1)*	%	(2.4)	(1.8)	(60) bpts
Expense/sales revenue	%	21.8	20.5	130 bpts
Average working capital/sales revenue	%	17.5	19.0	(150) bpts
Diversified revenue (gross)	€000	195,715	193,838	1
Diversified margin	€000	43,241	41,303	5
Diversified margin/total margin	%	43.4	37.0	640 bpts

In Europe, PaperlinX businesses operate across 11 countries that provide a range of products to thousands of customers in the commercial print, office, packaging and display markets. The focus is a ‘customer-centric approach’ backed by technical support services and efficient local logistics. Sales teams have an in-depth knowledge and strong expertise in the industry. The largest business in the region is in the United Kingdom.

Revenue from continuing operations in local currency is down 15 per cent compared to the pcp. The market demand for paper in Europe fell significantly more than expected in the second quarter. This, combined with structural changes in the competitive landscape, had a significant impact on our sales in the region.

For instance, in the UK, the Commercial Print market is changing rapidly with European mills and merchants now competing for the same business and price cutting to win customers. The outlook for the Commercial Print industry in Europe and particularly in the UK for the next 6 months remains challenging.

The underlying EBIT loss[1] of €(14.9) million increased from a loss of €(13.1) million pcp.

Whilst the VTS saw a slight revenue fall, importantly the gross margin improved slightly on pcp as we focused on more profitable segments of the market.

The Packaging segment saw an increase in revenue and margin compared to pcp, after organic growth in Poland and Scandinavia.

(1) Non-IFRS measure – refer Appendix 2

Spicers Australia, New Zealand and Asia

ANZA		Dec 2014	Dec 2013	% Change
Net sales revenue	A$000	209,016	221,393	(6)
Profit/(loss) before interest and tax	A$000	1,350	8,823	(85)
Underlying EBIT *(1)*	A$000	9,122	9,235	(1)
Underlying EBIT/sales revenue *(1)*	%	4.4	4.2	20 bpts
Expense/sales revenue	%	17.9	18.4	(50) bpts
Average working capital/sales revenue	%	22.6	20.9	170 bpts
Diversified revenue (gross)	A$000	29,193	22,760	28
Diversified margin	A$000	7,850	6,038	30
Diversified margin/total margin	%	17.8	12.4	540 bpts

In Australia, New Zealand and Asia, PaperlinX is structured across a variety of independent operating companies, united under the Spicers brand. Spicers is the leading merchant group in Australia and New Zealand, with sales offices and distribution capabilities in most major cities, and a focused position in Asia. The focus is on Commercial Print Products, Sign and Display, Industrial Packaging materials and Graphic Supplies and Systems.

While revenue was down 6 per cent, strong margin and expense control in Australia and New Zealand more than offset the shortfall. The ANZA region delivered a positive underlying EBIT(1) of A$9.1 million for the period broadly in line with prior against continued difficult trading conditions in the core Commercial Print segment. Gross margins were under pressure as adverse currency movements pushed the cost of sales higher.

Fixed costs continue to be reduced across the entire operation, including right-sizing logistics operations and property leases. For example, the Spicers site in Victoria will relocate from Scoresby to a new site in Dandenong South in mid 2015 as part of an ongoing initiative to right-size footprints that deliver flexibility and substantial cost reductions. The non-strategic and unprofitable sheeting operations at the Victorian site were closed in late November.

In New Zealand, the traditional paper business contracted sharply in the past six months while the acquisition of Total Supply in October 2014 boosted earnings and exceeded performance expectations in the period.

The Asian business continues to experience a marked slow down in demand for Commercial Print in its major markets of Malaysia and Singapore. A profit improvement program is underway in the businesses to reduce expenses and improve margins, and transition to a product mix with higher margin opportunities. Given the market weakness in this region, an impairment charge of $6.3 million related to goodwill was booked in the period

The ANZA region continues to experience growth within its diversified businesses. The acquisition of Total Supply helped to increase diversified revenue by 28 per cent compared to pcp. Bolt-on acquisitions remain a strategic priority for the region as it seeks to strengthen its share in the sign and display and packaging markets.

(1) Non-IFRS measure – refer Appendix 2

Spicers Canada

Canada		Dec 2014	Dec 2013	% Change
Net sales revenue	C$000	202,957	205,457	(1)
Profit/(loss) before interest and tax	C$000	(24,042)	6,690	(459)
Underlying EBIT *(1)*	C$000	7,413	7,095	4
Underlying EBIT/sales revenue *(1)*	%	3.7	3.5	20 bpts
Expense/sales revenue	%	16.6	16.6	0 bpts
Average working capital/sales revenue	%	11.4	12.1	(70) bpts
Diversified revenue (gross)	C$000	24,633	26,134	(6)
Diversified margin	C$000	5,414	5,623	(4)
Diversified margin/total margin	%	13.0	13.1	(10) bpts

On 11 February 2015, PaperlinX announced the agreement to sell its Canadian operations (Spicers Canada) to Central National-Gottesman Inc. (CNG) for C$63 million, subject to a customary post-completion working capital adjustment. Competition clearance has been received and the transaction is expected to close on Monday 2nd March 2015. The proceeds from the sale will be used to repay Canadian debt and assist the Group with its liquidity requirements.

As this announcement was made after the balance date of 31 December 2014, the favourable underlying EBIT(1) contribution of C$7.4 million (up 4 per cent on pcp) is classified as part of the Group's continuing operations. The operation will be restated as discontinued in the full year consolidated financial statements.

Corporate and other

Corporate / Unallocated		Dec 2014	Dec 2013	% Change
Corporate and other costs	A$000	(5,689)	(5,609)	(1)
Net other finance costs	A$000	(2,127)	(1,492)	(43)
Underlying EBIT *(1)*	A$000	(7,816)	(7,101)	(10)

Corporate costs for the period of $5.7 million were largely in line with pcp. Net finance costs of $2.1 million increased by 43 per cent from the pcp mainly due to higher borrowing costs in Europe.

FINANCIAL POSITION

Balance Sheet		As at 31 December 2014	As at 30 June 2014	As at 31 December 2013
Current assets	$000	916,915	919,904	1,072,625
Non current assets	$000	68,319	147,037	161,466
Total assets	$000	985,234	1,066,941	1,234,091
Current liabilities	$000	646,340	460,409	623,549
Non current liabilities	$000	157,515	293,223	258,643
Total liabilities	$000	803,855	753,632	882,192
Shareholders equity	$000	181,379	313,309	351,899
Funds employed (net debt + net assets)	$000	339,020	407,029	528,881
Net tangible assets attributable to ordinary shareholders and PaperlinX Step-up Preference Securities holders	$000	140,452	209,926	238,388
Net tangible assets per ordinary security	cps	(17.2)	(6.7)	(6.3)

(1) Non-IFRS measure – refer Appendix 2

Net assets decreased in the period from $313 million in June 2014 to $181 million. This reduction was largely due to the negative impacts of impairments of property, plant and equipment and intangibles, adverse movements in the defined benefit pension plan position, the de-recognition of deferred tax assets and trading losses in the period.

Working capital balances (trade receivables, payables and inventories) were up 7 per cent on June 2014 (3 per cent in constant currency) with the bulk of the increase in Canada and ANZA regions.

Non-current liabilities for employee benefits (primarily defined benefit pensions) moved adversely in the period due to actuarial losses of $31.3 million on the defined benefit pension plans in the UK, Continental Europe and Canada.

Working capital and cash flow

Negative operating cash flow of $(54.0) million versus cash outflow of $(29.9) million for the pcp is due to poor trading conditions and tightening of supplier trading terms. Capital expenditure of $6.5 million included the acquisition of Total Supply in New Zealand. Maintenance capital expenditure of $2.1 million was slightly lower than pcp and represents expenses relating to sites, fleet and enhancements to computer software systems.

Cash flow	Dec 2014 $000	Dec 2013 $000
Operating cash flow excl working capital and restructuring	**(18,648)**	**(14,516)**
Restructuring	(20,940)	(15,753)
Working capital movement	(14,438)	364
Operating cash flow	**(54,026)**	**(29,905)**
Capital expenditure	(6,515)	(2,195)
Proceeds from sale of assets & businesses	3,747	207
Borrowing costs paid	(988)	(957)
Transaction costs paid for takeover offer - SPS Units	-	(788)
Tas Paper closure	(97)	(584)
Net cash flow	**(57,879)**	**(34,222)**

Debt and Interest

Net debt since June 2014 has increased by $64 million due to unfavourable trading results, additional cash commitments to restructuring plans and unfavourable foreign currency translation movements (see table below).

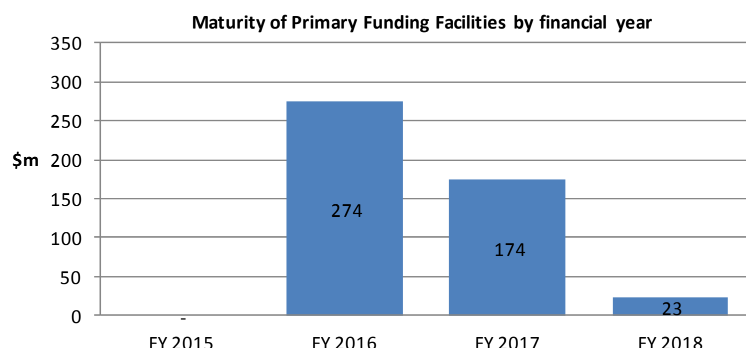
Debt		Dec 2014	Constant currency *(1)* Dec 2014	Jun 2014	% Change v Actual	% Change v Constant currency *(1)*
Gross debt	$000	243,574	242,840	200,738	21	21
Cash and cash equivalents	$000	85,932	86,692	107,018	(20)	(19)
Net Debt	**$000**	**157,642**	**156,148**	**93,720**	**68**	**67**

Interest expense		Dec 2014	Constant currency *(1)* Dec 2014	Dec 2013	% Change v Actual	% Change v Constant currency *(1)*
Cash net interest on bank debt	$000	5,214	5,323	6,336	(18)	(16)
Non-cash interest	$000	302	297	337	(10)	(12)
Net interest expense	**$000**	**5,516**	**5,620**	**6,673**	**(17)**	**(16)**
Avg daily gross debt	**$000**	**240,994**	**236,203**	**287,792**	**(16)**	**(18)**

(1) Non-IFRS measure – refer Appendix 2

Funding update

The Group's primary funding facilities are $471 million (see Maturity of Facilities graph below). The debt facility from our main lender in Europe is due to expire in September 2015. Discussions continue with the lender regarding an extension. The weighted average life of our working capital facilities is 1.2 years. Our funding facilities are linked to the regionally based business structures and are mainly based on the pledging of debtors and/or inventory.



Defined Benefit Pensions

The group defined pension deficit increased 28 per cent in the period to $138 million from $108 million at 30 June 2014. Declining discount rates in the major plans in the UK, Netherlands and Canada led to an actuarial loss of $31.3 million. Compounding this was an unfavourable foreign currency translation to Australian dollars of $5.9 million.

Dividends and distributions

There was no dividend paid on the Ordinary Shares for the six months ended 31 December 2014. No distributions relating to the PaperlinX Step-Up Preference securities were paid in the six months ended 31 December 2014.

Conclusion

The first half of the financial year 2015 saw strong performances from our businesses in ANZA and Canada, but there was a sharp downturn in the fortunes of our business in Europe, particularly in the second quarter. The weaker than expected market for paper in Europe, coupled with a significant change in supplier behaviour in our largest markets of the UK and the Benelux resulted in a loss of market share and poor trading results for the region.

The Strategic Review is progressing and we will be making further announcements in the near future.

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(1) Non-IFRS measure – refer Appendix 2

Appendix 1

The following table shows statutory earnings in Australian dollars.

Results for the half-year ended 31 December 2014	Dec 2014 $000	Dec 2013 $000
Group revenue	**1,296,659**	**1,475,497**
Earnings:		
Total continuing operations	(10,565)	(8,091)
Discontinued operations	(119)	(141)
Loss before net finance costs, tax and significant items	**(10,684)**	**(8,232)**
Net other finance costs	(2,127)	(1,492)
Significant items (pre-tax)	(69,810)	(9,116)
Loss before interest and tax	**(82,621)**	**(18,840)**
Net interest	(5,516)	(6,673)
Loss before tax	(88,137)	(25,513)
Tax relating to pre-significant items	(2,725)	(3,039)
Tax relating to significant items	58	111
Tax expense	(2,667)	(2,928)
Statutory loss for the period	**(90,804)**	**(28,441)**

The following table is a reconciliation of underlying EBIT[(1)].

Underlying earning reconciliation for the half-year ended 31 December 2014	Dec 2014 $000	Dec 2013 $000
Statutory loss for the period, after tax	**(90,804)**	**(28,441)**
Adjust for following (gains)/losses included in statutory profit:		
Impairment of property, plant and equipment	13,659	-
Impairment of intangible assets	49,336	-
Restructuring costs	6,256	9,104
Discontinued operations	716	237
Underlying loss for the period, after tax *(1)*	**(20,837)**	**(19,100)**
Continuing net interest	5,420	6,478
Continuing tax relating to pre-significant items	2,725	3,039
Underlying EBIT *(1)*	**(12,692)**	**(9,583)**

Appendix 2

Non-IFRS information

PaperlinX financial results are reported under International Financial Reporting Standards (IFRS). The tables and analysis provided in this document also include certain non-IFRS measures, including underlying statutory profit/(loss) after tax, underlying Earnings Before Interest and Tax (EBIT), and constant currency. These measures are presented to enable understanding of the underlying performance of the Company without non-trading items. Non-IFRS measures have not been subject to audit or review.
The non-IFRS measures used throughout this document are defined as:

- Underlying statutory profit/(loss) after tax: statutory profit/(loss) after tax before impairment of non-current assets, restructuring costs, and results from discontinued operations.
- Underlying Earnings Before Interest and Tax (EBIT): underlying statutory profit/(loss) before interest and tax for the continuing operations.
- Constant currency: constant currency assumes current and prior period earnings of foreign operations are translated at prior year exchange rates.

(1) Non-IFRS measure – refer Appendix 2