

## **CROSS RELEASE PXUPA ASX RELEASE**

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## **PAPERLINX 2011 AGM – CHAIRMAN’S AND MANAGING DIRECTOR’S ADDRESSES**

### **CHAIRMAN’S SPEECH**

#### **INTRODUCTION**

As indicated in the Annual report, worldwide demand for the core papers we distribute has continued to decline for the third successive year. In response to this ongoing structural change in global markets, we have taken the following actions to address the issues we are facing:

1. we have continued with an extensive restructuring programme to reduce costs and overheads throughout the organisation which will better align our businesses to current market conditions.
2. we are simplifying and streamlining the organisational structure around our core paper business to provide us with a more flexible cost base.
3. we have refocused on the key performance indicators that determine success in our sectors and these indicators are supported by specific initiatives to drive improved performance in margins, costs and working capital .
4. we have invested in our diversified product categories such as Sign and Display and Industrial Packaging where we can grow our business and achieve higher margins.
5. and we have commenced a Strategic Review of our business and capital structure.

Our CEO, Toby Marchant, will comment further on the restructuring program and strategic review as we work to regain relevance for PaperlinX. Today I will focus on the 2011 year, provide an update on other important matters as well as Board and management changes and the business outlook.

#### **REVIEW OF 2011**

Our results for 2011 show a significant statutory loss after tax of \$108 million. The biggest factor influencing this result was the further global deterioration in paper volumes, which were down 5.6% on last year. This volume decline and continued difficult trading conditions triggered the need to make an impairment charge of \$68.5 million after tax in Australia and Europe. Other non-recurring costs included internal restructuring charges of \$17.7 million after tax to resolve legacy issues and establish a platform for future growth and the non-cash valuation loss for a currency option of \$15.4 million after tax. After dealing with all these issues, the underlying loss for the PaperlinX Group of \$(22.6) million still showed an improvement over 2010's \$(27.6) million loss.

Our results were also impacted by the strong Australian dollar which contributed to the apparent revenue reduction of 11 per cent. This would have been only 2 per cent had currency remained constant. In fact, our revenue reflected stronger selling prices, up 8% on prior year which increased our dollar yield per tonne in local selling currencies. Overall, gross margins were held virtually flat with last year, which was a result of strong pricing disciplines and the continued development of our diversified business by our teams around the globe.

There were many good news stories hidden beneath this overall result. We gained share in a number of markets, although we gave up some share in Australia when we decided not to pursue high credit-risk business. We showed strong management of our controllable costs, with expense to sales down, average working capital to sales down, and operating cash flow up 136% on the prior year. Our diversified products contributed 20.9 per cent of the Group's gross margin which was up from 18.7 per cent last year.

The Board recognises that there is still a substantial way to go for your company to provide an acceptable return, with significant challenges still to be overcome. To that end, we are undertaking a Strategic Review of the business and capital structure.

### **STEP-UP PREFERENCE SECURITIES**

In relation to the Step-up Preference Securities (SPS), the Board has determined that the PaperlinX SPS distribution for December 2011 will not be paid. This reflects a prudent approach to cash management given the challenging trading conditions we have encountered in this first quarter and other ongoing demands for our cash, including our restructuring activities.

Whilst decisions on future SPS distributions will be made at the relevant time, until there is a significant improvement in trading conditions and the Company's financial performance, it is unlikely that further SPS distributions will be paid.

We are acutely aware that both ordinary shareholders and SPS holders are not seeing an

adequate return on their investment. One of the major drivers, and intended outcomes, of the strategic review is to create a more robust capital structure which will enable an improved return to investors. All aspects of the business and capital structure are being reviewed and a number of alternative actions are being considered and evaluated. This could include a possible divestment of certain assets, which would generate additional funds. With respect to the capital structure we have received significant commentary and queries around a possible buyback of the SPS prior to a Remarketing Date. Whilst no decision has been taken, it is one of the alternatives which is being considered.

## **BOARD AND MANAGEMENT**

In the past year, we have made significant changes in the Senior Management team, the global structure of our operations, and the Board.

In November 2010, the Board appointed Toby Marchant as Managing Director and Chief Executive Officer. Toby has already made major reductions and changes to the leadership group reporting to him, and there are now only two of the original eight members in the ongoing executive team.

With around 70 per cent of our business in the UK and Europe, and 20 per cent in North America, the Board decided to relocate the operating headquarters of the business to the UK, in order to be closer to the action. The statutory and corporate headquarters remains here in Melbourne.

The Board succession programme continued with the retirements of Barry Jackson and Jim Hall as Non-executive Directors, and David Meiklejohn as Chairman. Lindsay Yelland will retire at the end of this meeting. We thank them all for the contributions they made during their many years of service on the Board, particularly over the recent difficult years.

During the year Lyndsey Cattermole, Tony Clarke and Mike McConnell joined the Board to replace retiring directors. They bring a fresh view and perspective which will complement the Board and benefit the executive team. With Mike McConnell located in Los Angeles, the Company has its first overseas-based Non-executive Director, reflecting our global reach. Together, we are equipped to meet the challenges and seize the opportunities ahead as we determine the appropriate strategic direction for regaining relevance for PaperlinX.

## **OUTLOOK**

It is a tough environment to be operating in as general market confidence remains low in most of our key markets. The structural decline in core paper markets has continued and we are not

forecasting a recovery in overall volumes. While paper volumes continue to be very volatile, any forward projections are a matter of considerable uncertainty.

However, whilst many paper markets are down, there is real and continued growth in some geographies such as Asia and Central Europe, and in a number of niche paper sectors, such as Digital, that we are successfully focussing our attention on. Toby will provide further details in this regard.

Pricing is still generally moving in a positive direction. In Europe for example, paper manufacturers are currently increasing prices, which we are passing on, and this helps to offset the weak volumes.

Importantly, our diversified sectors are showing growth in all respects. We are growing our market shares, we are growing revenues and we are growing margins and they are starting to have a significant impact on our EBIT, as we move from a phase of organic investment to generating positive returns from key markets.

The benefits of the restructuring in 2011 will start to flow through to the bottom line in 2012, with full benefits in 2013. More than ever, we remain well positioned for any potential cyclical recovery, although no recovery is included in our internal forecast.

## **CONCLUSION**

The Board and management are committed to making PaperlinX a success. Significant changes have been made, but we know that more is required. The Strategic Review that is now underway will help us define the future direction for PaperlinX. We will act upon the results of the Strategic Review, and we are confident this will produce a stronger company over time.

Finally, I would like to acknowledge and thank the Company's excellent management and staff around the world for their ongoing dedication and efforts to make PaperlinX a better company during what has been an extraordinarily difficult period.

It is now my pleasure to hand over to our Managing Director and Chief Executive Officer Toby Marchant who will discuss the company's strategy and provide an update on the first quarter performance for 2012. I will then return to conduct the formal business of today's meeting.

Thank you ladies and gentlemen.

## **MANAGING DIRECTOR'S SPEECH**

### **INTRODUCTION**

Today I want to explain the company's strategy for regaining relevance, which comes in three parts.

### **REGAINING RELEVANCE**

The first is to resolve our legacy issues. The second is to manage the basics of this business and the third is to reshape our future. Let me talk you through each.

#### **1. RESOLVING LEGACY ISSUES**

During the year, we resolved two legacy issues that have hampered this business for some time. Firstly, we have now identified and fully provided for all known remediation issues associated with the closure of our Tasmanian manufacturing sites. Any sale of equipment or land now represents upside. Secondly, we have undertaken significant restructuring to reduce corporate overheads and recalibrate businesses to the markets they now operate in. The focus of this restructuring has been on those businesses that require and deserve the investment. Importantly, we are not simply taking out cost, but rather creating a more streamlined and flexible business that is better able to flex costs to match future conditions. This is in addition to the restructuring at the Melbourne corporate head office and the closure of the European head office in Amsterdam.

#### **2. OPTIMISING THE CORE AND ACCELERATING DIVERSIFICATION**

Managing the basics of this business is an ongoing task and involves optimising our core business and accelerating diversification into new sectors. The core of our business is paper distribution and this sector has seen another year of reduced demand due to a combination of structural and cyclical factors. In these circumstances we have driven our businesses around the achievement of the key performance indicators that determine success in this industry – margin to sales, expense to sales and working capital to sales. For each we have specific initiatives that range from data driven margin management to inventory optimisation through sales and operations planning. Across the business this focus on getting the basics right has had a positive impact during 2011. In specific operating companies, including Germany, Italy, Poland and Denmark, we have achieved real and sustainable turnarounds. We are also progressing with major reorganisation programmes in Australia, the UK and the Benelux that will change our business model for the long term to positively impact both our customers'

experience and our profitability.

Accelerating Diversification is a simple and logical development of our business, but one that requires skilful handling to ensure success.

Given the decline in our core paper volumes, the need to diversify our business is greater than it would otherwise have been, but the business principles behind our diversification strategy are essentially the same. We are basically diversifying PaperlinX in two ways. The first is to sell new products to our existing customers, primarily printers, and the second is to sell new and existing products, using the same logistics platform, to new customers, such as specialist sign makers and packaging convertors - and general consumers of these products in the industrial and corporate sectors. Our logistics platform is a significant differentiator in these diversified markets and it allows us to operate with healthier margins than are available in our core sector.

Our diversified products fall into four sectors: Sign and Display, Industrial Packaging, Graphics and Digital and each continues to grow in market share, revenue and margin. Overall the gross margin percentage in our diversified businesses increased from 22.6 to 23.2 per cent. This now represents 20.9 per cent of our total gross margin and importantly, we are seeing a significant impact on EBIT as we move from a phase of organic investment to generating real returns in key markets.

I will just take a minute to explain the product offering in each of these diversified sectors as some of them may not be familiar to you. The Sign and Display market is currently our largest diversified business. The products we sell comprise wide format printers and their ongoing requirement for inks and consumables as well as a broad range of signage material for internal and external usage such as cardboard, plastics, metal, vinyl, textile, vehicle graphics, banners, posters and LED lighting.

In the PaperlinX context, Industrial Packaging comprises primarily transit or “end of line” packaging. Our products include: packaging equipment such as shrink wrap machines, cardboard shipping cartons, shrink wrap, bubble wrap, strapping and tapes. In some markets we are also moving into primary packaging, in other words, the packaging that surrounds the actual product for sale and the outer or multi-pack secondary packaging.

Both sign and display and packaging products are sold to new AND existing customers. However, the Graphics market represents non-paper product offerings to our traditional customer base of printers and is therefore a new product to an existing customer. In Graphics we sell inks, chemicals, cleaning supplies, films, printing blankets, varnish as well as cutting and binding supplies. These images represent our “Total Print Supplies” brand which sells graphic

supplies to printers across the UK.

Finally, Digital refers to the sale of products for digital printing devices outside of our traditional commercial printer customer base. This represents a new and fast growing market into which we are selling a combination of new and existing products. The growth in Digital is based on an increasing trend of corporate end users such as small businesses, schools and churches to in-source their digital printing. The capabilities of these printers are generally way beyond the knowledge and understanding of the organisations who have acquired them and they soon develop an interest in learning how to get the most from these sophisticated printing devices. Our product offering is a broad range of branded products and we have also established partnerships with digital printer manufactures to work together in meeting the needs of these new customers. The images on the screen represent an example of our branded products “Spicers Digital” and “Kelly Digital” which are growing rapidly in North America. In support of this market Kelly Paper has recently launched its new American web store which can be found at [kellypaper.com](http://kellypaper.com). Additionally you can see a liveried vehicle from our recently launched New Zealand business called Paper Boy which is delivering digital products to new customers with the arresting slogan of “scream for a ream”.

### **3. RESHAPING OUR FUTURE**

The third component of regaining relevance comes from reshaping our future and whilst this year’s result shows some signs of improvement, it is clearly insufficient, particularly in the context of the difficult trading conditions that persist. Having dealt with a number of our legacy issues, secured our liquidity and appropriate covenants, we believe that now is the time for us to take a fresh look at how best to shape our future. We are therefore undertaking a Strategic Review of our business and capital structure. We will communicate the outcome of this review before the end of the 2012 financial year; however, we have defined the overall objective as being to create a company with a sound balance sheet, a sustainably profitable future and a regained relevance to our shareholders.

### **RECENT PERFORMANCE**

The start of this financial year has seen volumes below last year as demand is unchanged from the depressed levels experienced in quarter four of 2011. The macro economic pressures in the Euro zone are now depressing volumes in key markets such as the Benelux, Germany and Italy and the impact of this should be expected to continue for the rest of the financial year. The UK market appears to be stabilising, and pricing is positive. The North American market is starting to show signs of strengthening, as is Asia and New Zealand, but unfortunately we’re still

experiencing depressed conditions here in our home market of Australia.

Our September 2011 quarter results are tracking at a level similar to the second half of financial year 2011. Restructuring benefits are being realised and from quarter two we will start to see the cost savings from the various restructuring programs. As mentioned earlier, our diversified business is growing fast but is still insufficient to offset the decline in our core business in the short term.

Our forward performance in the core business relies on a continued focus on expense management, cost reduction initiatives and further optimising of our working capital. We do not expect demand to substantially improve in the near term, though it is certainly true to say we do maintain good leverage to any improvement.

## **CONCLUSION**

In conclusion, I have now been in the role for a nearly a year and can report the following: There is a huge appetite in this organisation to recover our fortunes. We have driven significant change this year in our business structure and cost base and in any year before 2008 that would probably have been sufficient, but we know that in this market we have to do more and the strategic review will address that. This has been fully communicated within the Company and we are therefore braced for further change with an attitude at all levels that is committed to doing whatever it takes to restore the pride, performance and future prospects of a fundamentally solid group of companies.

So in closing, I would like to thank all of our employees – for continuing to focus on the needs of our customers whilst managing unprecedented levels of change. It is the determination and professionalism of our people that gives me the certainty that we can emerge as a sustainably profitable company.

I would like to sincerely thank our retiring Chairman, David Meiklejohn, for his steady hand and ever present support. I would also like to thank Harry and all our Directors for their guidance and support this year. Finally, I would also like to thank our shareholders for their patience, support and, despite our recent performance, their continued belief in our future.