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Record of interview:

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Wesfarmers Limited announced a 2% decrease in profit after tax to $291 million for the half year ended 31 December 2004. This was down from the $297 million pcp which included after tax earnings of $45 million from the investment in Gresham PEF1. How did each of the Wesfarmers businesses perform relative to budget?

CEO Michael Chaney
Overall, the half year result was close to budget. We had below budget performances in energy, hardware, industrial and safety and above budget in insurance and chemicals and fertilisers.

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What main profit drivers do you expect in the second half?

CEO Michael Chaney
Obviously coal prices in the final quarter will have a significant impact, subject to achieving our budgeted delivery volumes. We expect continued growth in Bunnings' revenues.

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Can you explain the progress and timetable for the transition to International Financial Reporting Standards? Which areas do you expect to have the largest impact on Wesfarmers?

CEO Michael Chaney
In the half year accounts, we disclosed the likely impact on balance sheet items. The biggest impact on profit will be the removal of goodwill amortisation and that will add about $90 million to the full year result.

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Earnings before interest, tax and goodwill amortisation (EBITA) from the Bunnings hardware merchandising business increased by 10% over the same period last year to $230 million. You stated that solid progress has been made on major strategies. Can you reiterate these strategies?

CEO Michael Chaney
I was really referring to four things - the continued store development network, development of new trade distribution centres, upgrading the business systems and some business improvement initiatives, including a cross-docking feasibility study and a warehouse administration cost reduction project.

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Revenue for Bunnings increased by 7% to $2.14 billion. Cash store on store growth was around 7% and cash sales growth was 11%. Your outlook comment of continued retail sales growth is a little at odds with other retail commentary and comments from hardware competitors. What conditions did Bunnings experience in January? What is the recent experience with market share for Bunnings?

CEO Michael Chaney
I won't comment on the January performance because we really want to avoid a month by month analysis of our businesses. Given the aggregate ABS figures, it seems that Bunnings continues to increase its market share of the hardware industry.

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What impact have the softer housing conditions had on Bunnings? What about the impact from the new Mitre 10 MEGA store openings last year?

CEO Michael Chaney
The housing conditions have certainly flattened our performance in the trade sector and we expect that to continue.

Mitre 10 has four MEGA stores in Australia and six in New Zealand. While there have been some minor impacts, the overall impact has been negligible.

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Are you committed to your store refurbishment and upgrade program and your rollout program of 8-12 new warehouse stores per annum even if hardware markets soften substantially?

CEO Michael Chaney
Yes, because the economics of individual stores are strong.

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Bunnings is trialling a new business model for the trade sector in Queensland. What has that trial revealed so far?

CEO Michael Chaney
We've implemented the trade sector strategy at Morayfield in Queensland. Initial work has centred on the transfer and fulfilment of existing business from nearby warehouses and the focus is now shifting to new business development.

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Can you update progress on the feasibility study on the cross-docking trials for product supply at Bunnings stores? When do you expect it to be completed?

CEO Michael Chaney
We're currently planning preparatory work on a pilot cross-docking model. That will proceed over several months with a limited number of suppliers within the Melbourne store network, starting at the earliest in April 2005.

Our approach to this project is one of cautious haste. The theoretical savings and benefits appear attractive, but there are many practical issues that need to be worked through in detail with the buyers and the logistics provider to make sure that the benefits are real and importantly that there are no material business disruptions.

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EBITA from Wesfarmers' Energy business increased by 10% to $127 million. You now expect to produce export sales of less than 5mtpa from Curragh for FY05 after the extended shutdown of the coal plant to undertake a major upgrade. Production from Bengalla in the December quarter was also lower than expected. What are your production forecasts for the year across all three coal operations?

CEO Michael Chaney
The reduced tonnage from Curragh during December which resulted from upgrade works on the coal handling plant is likely to result in export sales from Curragh being below our previously estimated 5mt for the full year. It is also likely that some of the reduced tonnage will be priced at the lower, pre 1 April 2005 coal price until we meet certain minimum volume requirements under our contracts.

We don't generally provide forecasts of production, but suffice to say, we expect production volumes to increase at all three operations and in particular Curragh as we move into Curragh North in the fourth quarter.

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The mining industry has seen emerging cost pressures such as the price of labour, fuel, housing, explosives and steel and capacity constraints in rail and port infrastructure. In percentage terms, how much did operating costs per tonne increase at your operations? Are you on track for timing and capital budget for the expansion to 7mtpa at Curragh?

CEO Michael Chaney
Like all miners, we're feeling the effect of increasing supplier costs and each of the operations recorded higher per tonne product costs in the first half compared with a year earlier.

We're on track for the development of Curragh North. We're actually slightly ahead of the time schedule and while some capital items have come in above our original estimates, it's not very material.

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You stated that the FOB (US$) prices for Curragh coking coals have increased by an average of approximately 130%. You expect PCI prices to be settled shortly. Are you still hopeful of reducing its pricing differential relative to hard coking coal? What export thermal price increases have you received at Bengalla?

CEO Michael Chaney
We were pleased with the outcome of our coking coal negotiations with an average price increase for contracts settled to date across all coking coal products (excluding PCI) of 130%.

We haven't produced or sold PCI before so it would be difficult to comment on any pricing differential relative to coking coal. We're expecting to work through the issues on PCI pricing with suppliers over the next few months.

Export pricing on thermal coal at Bengalla is subject to a number of leads and lags as contracts are renewed on a calendar year basis, financial year basis and Japanese financial year basis. Overall, we expect to achieve price outcomes consistent with the market as contracts are renewed.

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What domestic coal price changes have you received? What proportion of Wesfarmers' coal is now sold domestically?

CEO Michael Chaney
We don't disclose domestic coal prices for commercial reasons. About 55% of our coal is sold domestically and 45% is exported.

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You were quoted in the press as saying that coal revenue could increase by as much as A$600 million in FY06. On reflection, is that accurate and what could change that expectation?

CEO Michael Chaney
I really just provided a ballpark estimate on the spot although it's probably not far off the mark. It will depend on several factors including the price we achieve for PCI coal. Of course not all that revenue would drop to the bottom line because we will have to make the Stanwell rebate payment and operating costs are likely to increase as prices increase.

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In FY06, you expect to pay between $80 to $100 million to Curragh's domestic customer under the export related price rebate. The customer gets a rebate equal to 25% of the increment that Curragh's export semi soft coking coal price exceeds approximately A$60/tonne, multiplied by Curragh's total export tonnage. Why was it necessary or beneficial for Wesfarmers to agree to this rebate?

CEO Michael Chaney
We were in a competitive tender and Stanwell wanted to share the benefits of increased coking coal prices. At the time of the bid none of us imagined that coal prices would increase as much as they have, but we're very happy with the overall outcome because we won the tender and we're receiving most of the benefits.

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EBITA for the industrial and safety business fell 3% to $51 million. Last year you engaged an external party to help review the structure of Wesfarmers industrial and safety (WIS). Can you outline the areas of the business which have improved and the strategies to improve the underperforming parts of the business?

CEO Michael Chaney
We haven't completed that review. It should occur towards the end of the third fiscal quarter and then we'll have a better understanding of what might be achieved.

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Revenue for WIS was up 2% but the EBIT/ Sales Ratio fell from 9.2% to 8.7%. What impact could the new strategies have on its margins?

CEO Michael Chaney
It's yet to be determined exactly what we will achieve, but we expect some improvement in profit margins following the implementation of the improvement initiatives.

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EBITA for the insurance division rose 93% to $69 million. In the previous corresponding period, Lumley contributed only two months of earnings. How much of the increase was due to the inclusion of Lumley for the full six months?

CEO Michael Chaney
The normalised growth in EBITA was 27% i.e. if we included Lumley for the whole of the previous corresponding period result.

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In your results presentation you quoted a number of divisional KPIs for the insurance division. Where can you improve on these KPIs? Are your capital reserves adequate?

CEO Michael Chaney
It will be difficult to improve on some of the KPIs given that our Combined Operating Ratio is at a record low level and our insurance margin is at a record high level. That's driven partly by favourable claims performance but also I think by pretty good risk management.

As far as capital reserves are concerned, the three companies - Lumley General Australia, Lumley General New Zealand and WFI - are operating well above their required solvency levels with an MCR around two in each case.

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The insurance industry had been experiencing peak cycle conditions but you have warned of increasing competition. What trends are emerging and to what extent could earnings come under pressure?

CEO Michael Chaney
The market has been tightening for the best part of last year and achieving sales growth is increasingly challenging. The impact of that won't flow through for another six to nine months because of the way you account progressively for insurance revenues.

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Wesfarmers CSBP, your fertilisers and chemicals business, achieved a 41% increase in EBITA to $29 million. Fertiliser volumes were up 53%. Can you indicate which area of the business had the greatest impact on the EBITA increase?

CEO Michael Chaney
Fertilisers contributed slightly more than chemicals to the increase in EBITA.

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In December 2004, AWB, Elders and WMC Resources announced that they had formed a strategic partnership in the fertiliser industry which will increase competition and drive cost savings in the supply chain. Although the partnership

will operate on the east coast, do you expect any pricing and margin pressure on your fertiliser business as a result?

CEO Michael Chaney
No we don't expect any impact. We have a very close relationship with Elders and Landmark and given the highly competitive nature of the market in Western Australia as it is, we don't think there will be any change as a result of that alliance.

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Thank you Michael.

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