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Wesfarmers Limited
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Title: Open Briefing®. Wesfarmers. MD Goyder on 24% Profit Rise

corporatefile.com.au
Wesfarmers Limited announced a 24% increase in net profit to $869 million (excluding an after tax profit of $179 million on the sale of ARG) for the year to 30 June 2006 compared with $702 million in FY05. Excluding the impact of the ARG sale, earnings per share of $2.36 was up 22.7%. Can you explain the main influences on the profit increase?

MD Richard Goyder
Earnings from our Energy division increased by $310 million which is around 98% on the previous year. That was largely due to an increase in metallurgical coal prices and in export coal sales from Curragh. Earnings from our home improvement division were marginally up on last year while earnings from the industrial and safety, insurance and chemicals and fertilisers businesses were down on the previous financial year.

corporatefile.com.au
Can you give a quick summary of the performance of each of the business segments over the year relative to your expectations – which ones outperformed or underperformed and why?

MD Richard Goyder
In general we feel the profit result was a reasonable outcome although a number of our businesses were affected by factors which adversely impacted their results. For example, our original expectation was to sell 7 million tonnes of export coal from Curragh, but due to both technical and logistics factors we sold 6 million tonnes. I'll touch on other specific aspects of business unit performance as we discuss each of our business units.

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Directors declared a final fully-franked dividend of $1.50 per share bringing the total dividend for the year to $2.15 per share, an increase of 19%. Ignoring the franking credits you will have available from the ARG sale, what payout ratio can shareholders expect for FY07?

MD Richard Goyder
The payout ratio for FY06 was around 94% and we expect that for FY07, based on our current earnings profile, we would have sufficient franking credits to pay fully franked dividends of about 90% of net profit after tax.

corporatefile.com.au
You've stated that a satisfactory profit will be achieved again in FY07, although at a lower level than that recorded in FY06. What FY06 profit number are you referring to for comparison? What is the general profit outlook across the various divisions?

MD Richard Goyder
The profit number we're referring to is the normalised net profit after tax of $869 million. Overall we're expecting improved contributions from most divisions in FY07, but offsetting those will be a fall in earnings in the energy division as a result of lower coal prices and the impact of industry-wide, high costs. Across all businesses higher interest rates and increasing fuel prices may have some impact on our customers' discretionary expenditure and our costs.

corporatefile.com.au
This time last year, Wesfarmers' capital expenditure estimate for FY06 was just over $900 million and it came in at $615 million. Why was FY06 actual so different to budget? What's the budget for FY07? What organic growth projects are proceeding?

MD Richard Goyder
We do our budgets some time before the beginning of the financial year so it's not surprising we didn't spend our budgeted capital expenditure because project timing can slip. The timing of the Kwinana ammonium nitrate expansion and some capital expenditure in our coal businesses have been pushed back.

The $615 million we spent in capital was still well in excess of depreciation. At this stage we're forecasting to spend over $800 million this year, but the same proviso applies. The major projects in addition to the Kwinana ammonium nitrate expansion are the construction of the conveyor system at Curragh North, the continued refurbishment and rollout of Bunnings stores and some investment in gas processing in the energy division.

Energy

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Earnings before interest and tax (EBIT) from Wesfarmers' energy business increased by 98% to $627 million. For FY06, coal production was 6.3mt of coking and 2.6mt of steaming at Curragh, 2.3mt of steaming at Bengalla (40%)

and 3.7mt of steaming at Premier. What coal production across your three operations do you expect in FY07? What is the latest with the possible expansion at Bengalla?

MD Richard Goyder
We don’t provide forecasts for coal production, however production should reflect the expected sales outcome and obviously we maintain sufficient production flexibility to take advantage of opportunities as they present. For FY07, at Curragh production will be geared to our estimated metallurgical coal sales of between 6.2 and 6.5 million tonnes, subject to infrastructure performance. Sales from Premier Coal will depend on demand from Verve Energy. Port capacity issues will limit Bengalla’s sales increases in the short term, but we continue to work on expansion opportunities with a view to obtaining necessary approvals to increase maximum annual run of mine production capacity from 8.7 million tonnes to 10.7 million tonnes. We expect to make a decision on this sometime in the next 6 months.

corporatefile.com.au
For FY06, coal sales at Curragh of 8.6 million tonnes were below forecast and below production. What impact will the transport infrastructure restrictions have on your coal sales in the future? What is the status of the projects to increase rail and port capacity?

MD Richard Goyder
We’ve been advised that the port capacity expansion should be completed by the end of calendar year 2006 and the rail capacity expansion by mid 2007. Our export sales forecast for FY07 of 6.2 to 6.5 million tonnes is based on the commitments our service providers have made regarding those expansions. Following completion of those projects by mid 2007 we will have contracted rail and port capacity of over 7 million tonnes per annum.

corporatefile.com.au
The proportion of hard coking coal produced at Curragh North is now lower than you expected at the time of purchasing the mine. How might you increase the proportion of hard coking coal?

MD Richard Goyder
Just to clarify the first part of the question - at the time we acquired the rights to mine Curragh North we expected the deposit to be 100% semi-soft coking coal. We think our sales mix this year will be around 50% hard coking coal and having that mix has significantly increased the value of the Curragh North deposit since we purchased it. The future sales mix will depend on the product demands of our customers and will also depend on the characteristics of the run of mine coal as we go through the mine sequences.

corporatefile.com.au
What cost pressures are your coal operations operating under? Have these eased at all?

MD Richard Goyder
The whole mining sector is under cost pressures at the moment particularly in areas such as fuel, labour which is scarce, contractor rates and tyres. In FY06, overall cash production costs per tonne across our three coal mines increased by 8% and we're not expecting any immediate easing of those cost pressures.

corporatefile.com.au
In FY06, Wesfarmers achieved LPG export volumes of 38,532 tonnes, 80.6% below last year's. Is Wesfarmers continuing to pursue options to replace the earnings lost from lower LPG volumes from its extraction plant?

MD Richard Goyder
We'd like to have higher LPG volumes coming down the Dampier to Bunbury Natural Gas Pipeline, but we're reliant on the content delivered into the pipeline by the gas producers. We're continuing discussions with gas producers to see if we can obtain more, but that is challenging. Our best estimate at the moment is for FY07 production to be at similar levels to FY06.

corporatefile.com.au
Kleenheat's earnings were in part lower because of record high international LPG prices. Up until recently Wesfarmers had a natural hedge against rising LPG prices because it benefited through its exports. Is Wesfarmers committed to the Kleenheat business given that the Group is now further exposed to rising LPG prices?

MD Richard Goyder
Kleenheat has always been a net buyer of LPG when looked at on a national basis so the hedge has never been complete. We remain committed to the business although it needs to further adapt to the higher cost structures in the industry.

Obviously the Federal Government's announcement on subsidies for conversion of vehicles to LPG is a positive for Kleenheat.

corporatefile.com.au
One growth strategy for Wesfarmers Energy has been to introduce new gas products, to enter new markets and to pursue remote power opportunities. Can you update the progress there?

MD Richard Goyder
We're looking at a number of initiatives across the division at the moment. We continue to look at opportunities on the LNG front, we continue to win tenders to build remote power stations and we've commenced construction of our demonstration char plant at Premier Coal.

Home Improvement

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EBIT from the Bunnings home improvement business increased by 1.1% to $421 million. For FY06, underlying store-on-store cash sales growth was 5.1%. How

did market conditions change during the year? What are current market conditions? How was Bunnings' performance relative to the sector?

MD Richard Goyder
Retail trading conditions for Bunnings during the first four months of FY06 were difficult across Australia and we reported low store-on-store growth numbers for that period. However, since November they have improved and Christmas trading was positive. That trend continued in the second half with store-on-store cash sales growth up 7.5% in the January to June period.

Public data and industry sources indicate that Bunnings appears to have outperformed the sector in FY06 and continues to win market share. It's very early in the new financial year, but Bunnings has experienced positive trading conditions in the year to date.

corporatefile.com.au
As you say, the Bunnings business continues to outperform the sector. Can you update the progress on your major strategies such as merchandising, advertising, systems and the supply chain?

MD Richard Goyder
We've seen a good response to our changed advertising format since its introduction last December and we'll continue to do new things in this area. We're seeing success from new and enhanced merchandise ranges including a revamped special orders offer and some good detailed range management work. Our supply chain performance improved across FY06 particularly in the area of product return management, direct import lines and store receivables. The progress on our business systems project has been a little slower than we'd hoped. We're on schedule with a number of parameters although the implementation of part of the new system will be delayed some months.

corporatefile.com.au
In FY06, Bunnings opened 12 warehouse stores and undertook 32 store upgrades. In addition to ongoing openings and upgrades, how will Bunnings grow its earnings?

MD Richard Goyder
Firstly, the store upgrades and rollouts are a very important part of Bunnings growing its earnings and we plan to rollout another 10-14 new stores this coming year and to continue with accelerated store upgrades. Beyond that, there are a number of areas where we have been, and will continue to grow earnings including lifting our performance in product categories where we have low market shares and introducing new service offers and new product ranges. This is driving better use of space, and associated returns, in the business.

corporatefile.com.au
You have established a network of stand-alone trade distribution sites. What are the benefits of that change?

MD Richard Goyder
The reason we've established a network of stand-alone trade distribution sites is to move heavy trade business out of our stores into more specialised and lower cost sites designed for the large builder market. The benefits are that these customers get better outcomes and, within the stores, we can provide a stronger range and a lift in service to walk-in trade customers and we also free up space to extend our overall offer. In addition, we see safety improvements in our stores.

Insurance

corporatefile.com.au
EBIT from Wesfarmers Insurance Division was $125 million, down 8% on the previous year. What is driving the weaker market conditions?

MD Richard Goyder
The weaker market conditions have resulted from increased competition and a return to more normal loss ratios. Margins have contracted although they remain relatively attractive.

corporatefile.com.au
June is usually a busy period for insurance companies because a lot of policies are renewed. Can you talk specifically about your success in client retention, gaining new clients and maintaining margins?

MD Richard Goyder
We had a reasonable result in terms of retention of clients although prices were under pressure. We have won some new business, but as I said earlier, the industry is pretty competitive at the moment.

corporatefile.com.au
Can you give more detail on the progress of Wesfarmers Insurance division's growth strategies?

MD Richard Goyder
We've had some success in reducing our reinsurance costs and reinsurance ceded, excluding AMO, fell from 28.2% to 23.5% during the year, and we continue to look at a number of growth initiatives across the division. We have acquired some small portfolios within Lumley General Australia and Wesfarmers Federation Insurance continues to form strong alliances particularly in regional areas.

Industrial and safety

corporatefile.com.au
EBIT from the industrial and safety businesses decreased by 11% to $97 million. Can you detail the financial impact from restructuring the division?

MD Richard Goyder
The EBIT figure included redundancy costs of $2.4 million, inventory write-downs of $5.1 million and provisions for long term uncollected debt of $2 million. These charges were partly offset by around $3.5 million in profits from asset sales.

This year's result was also adversely affected by the inclusion of employee share plan costs of $3.5 million and an adverse New Zealand exchange rate impact of $1.5 million.

corporatefile.com.au
What progress has been made in improving the business?

MD Richard Goyder
In February 2006, the division was restructured into distinct national business units to improve customer focus while also reducing support costs and improving support staff efficiencies. That resulted in the reduction of approximately 150 employees, mainly during the last quarter, and the closure of around 14 underperforming branches. Capital employed has been reduced due to working capital improvements of 7% from focused initiatives across all businesses. We've made very good progress in that area.

Following the restructure, each business has developed and begun implementing an improvement programme covering sales effectiveness, procurement and logistics processes as well as continuing to improve working capital management.

Chemicals & fertilisers

corporatefile.com.au
EBIT from the fertiliser and chemicals business segment decreased by 9% to $81 million. What impact did gas curtailments have on FY06 earnings from chemicals? What are possible solutions?

MD Richard Goyder
Gas supply constraints reduced ammonia production by around 15,000 tonnes in FY06 which necessitated a small import of ammonia to keep our plants operating. These factors combined reduced earnings by around $4.5 million. CSBP is attempting to negotiate supply arrangements which will provide greater certainty of gas supply.

corporatefile.com.au
In April 2006, CSBP and its joint venture partner elected not to proceed with an expansion of QNP due to a significant escalation in capital costs. What's the likelihood that QNP will be expanded at another time? Is the Kwinana expansion running within time and capital budget?

MD Richard Goyder
When we conducted the feasibility study on a duplication of QNP we decided not to proceed on the basis of economics at that time. That is not to say it could never happen, but we are now actively looking at debottlenecking the existing plant.

The capital expenditure forecast for the Kwinana ammonium nitrate expansion has increased by $60 million to $260 million. The increase relates substantially to the prill tower where detailed engineering work has shown that we need significantly higher quantities of structural steel piping and instrumentation. The other significant cost increase has been for storage requirements.

corporatefile.com.au
What impact did the dry conditions at the end of the financial year have on fertiliser sales in the fourth quarter which is usually the largest volume quarter? What have been recent weather conditions?

MD Richard Goyder
June across many regions of Western Australia was the driest on record and that resulted in June fertiliser sales being less than 50% of typical levels. June is traditionally our largest sales volume month of the year.

Recent rains have been helpful for farmers in some areas, but will not result in us making up lost fertiliser sales.

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Thank you Richard.

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