DuluxGroup Limited

ABN 42 133 404 065

# ASX Announcement

**14 November 2011**

## DULUXGROUP DELIVERS STRONG EARNINGS GROWTH

DuluxGroup today reported net profit after tax (NPAT) of $93.2 million, inclusive of a one-off tax consolidation adjustment of $12.5 million and a $4.5 million ($3.1 million after tax) uplift relating to insurance income associated with the Rocklea flood.

Excluding these items NPAT was $77.6 million, an increase of 8.5% over the 2010 pro forma NPAT, before one-off demerger costs, of $71.5 million.

Earnings before interest and tax (EBIT) increased 12.7% to $139.2 million. Excluding the $4.5 million insurance uplift, EBIT was $134.7 million, up 9.1% over 2010 pro forma EBIT.

Sales revenue increased by 3.4% to $996.4 million. This was achieved despite the estimated 2% sales loss as a result of the loss of production at Rocklea following the Queensland flood.

The Board has declared a final dividend of 7.5 cents per share fully franked, taking the full year dividend to 15.0 cents, which represents a 70% payout ratio on NPAT before the tax consolidation adjustment and flood insurance uplift.

DuluxGroup Managing Director and CEO Patrick Houlihan said the result was particularly pleasing, given mixed market conditions, rising input costs and the added challenge of the company's main Australian paint factory being completely shutdown for two months and not fully operational for six months due to damage from the Queensland flood.

"To deliver an 8.5% increase in profits, despite some significant headwinds this year, reflects the resilience of our strategy," said Mr Houlihan.

"We have continued to invest in DuluxGroup's premium branded products and services that are targeted at the home renovations and improvement segment, rather than more cyclical new housing. During the year we saw increased investment by our retail customers in the home improvement segment, catering to demand associated with high levels of home ownership in our core markets. We support our brand investment with a strong focus on customer service and industry leading supply chain performance, and it has proved an enduring formula for earnings growth.

"Overall, this year's result was reinforced by sound financial discipline which saw resilience in earnings margins, despite rising input costs. Trade working capital was also effectively managed, despite the need to build higher than normal stock levels to recover from the Queensland flood impact."

The Australian Paints business achieved a record result with sales up 4.3% and underlying earnings up 11.4% to $102.4 million. Sales growth was achieved despite flood related lost sales. This is estimated at 3% in lost sales for Paints Australia, which equates to 2% of overall DuluxGroup sales.

"To deliver such strong earnings growth, given the impact of the floods, is particularly pleasing and reflects effective risk mitigation and disaster recovery. Importantly, we have not lost any market share, and both our retail and trade businesses finished the year with strong momentum. This could not have been achieved without the strong support of our retail and trade customers and we thank them for that," said Mr Houlihan.

The New Zealand Paints business was heavily impacted by the continued slowdown in consumer spending generally across the economy. Negative consumer sentiment was further exacerbated by the Christchurch earthquakes earlier in the year. The decorative paints market in New Zealand was down by an estimated 4% in volume terms for the year. While sales revenue increased 3.9% to $82.5 million and earnings declined 5.8% to $9.7 million, this was boosted by increased production to support the Paints Australia business while the Rocklea factory was offline. Earnings were also negatively affected by increased costs and depreciation associated with the significant upgrade of the 70 year old paint factory in Wellington and the transfer of the manufacture of protective coatings products to the new Dandenong manufacturing site in Australia.

The Selleys Yates business delivered earnings of $30.5 million, up 5.5%. The positive result reflects profitable market share growth, along with the benefits of ongoing productivity initiatives. Selleys sales were assisted by a strong new product development pipeline and range review gains with key customers in Australia. Favourable gardening conditions in Australia and New Zealand saw revenue increases for the Yates business.

DuluxGroup's Offshore and Other business segment – comprising Dulux Powder, Refinish and Industrial Coatings, Dulux Papua New Guinea (PNG), and the South East Asia and China businesses (known as DGL International) – delivered earnings of $7.7 million, down $2.2 million or 22.2%. Volumes in the core Shanghai wood coatings market were impacted by government constraints being imposed to regulate growth within the residential property. However there were signs of improvement in the final 2011 quarter, with revenue growth above the prior year. The Powders, Refinish and Industrial Coatings business was impacted by the slowdown in new housing and commercial construction in both Australia and New Zealand. The PNG business grew earnings in local currency, however the magnitude of growth was reduced on translation due to the strong Australian dollar.

"This year DuluxGroup continued to focus on delivering profitable growth, effectively managing margins and productivity, while reinvesting for the longer term," said Mr Houlihan.

"During the year we invested in the infrastructure to support growth in our core domestic markets. The significant upgrade of our paint factory in Wellington New Zealand and the commissioning of a new protective coatings plant at Dandenong South in Victoria were successfully completed. We also purchased a smaller scale paint factory in Glen Waverley in Victoria, which will provide greater flexibility and risk mitigation in our manufacturing and supply chain.

"We have also strengthened our platform for long term growth in China with the merger of our DGL International business with Hong Kong based Camelpaint. DuluxGroup holds 51% of DGL Camel International.

"This new joint venture is a low risk growth option, providing increased scale and greater geographic reach into Hong Kong and Southern China. There are opportunities to leverage the expertise and customer relationships in each company's respective markets. In addition to this we are also seeking other growth opportunities, including building on the Selleys position developed in South East Asia over the past decade.

"During 2012 we will continue to build on our key capabilities to grow DuluxGroup's market leading positions in Australia and New Zealand. In addition, we will seek growth, both organically and through bolt-on acquisitions, in adjacent product categories in these core markets. We will also look to build upon our strengthened platform in targeted segments of high growth markets in Asia, in a measured way, for the longer term."

Subject to economic conditions, we expect 2012 DuluxGroup underlying net profit after tax to be higher than that reported in 2011 ($77.6 million).

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DuluxGroup Limited

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# DuluxGroup Limited results for the financial year ended 30 September 2011

**Please Note:**

1. **The 2011 result has been impacted by the supply disruption at our Rocklea decorative paint factory due to the Queensland Floods in January 2011.**
2. **The results for the prior period (2010) as outlined in the Financial Report are impacted by the restructuring activities in preparation for the demerger from Orica. In general, the prior year figures in this report are 'pro forma' to present a full 12 months' performance of the businesses regardless of when they were acquired as part of this restructuring.**

**Please refer to the Appendix 4E Financial Report for further information.**

| **Results** | **Year ended 30 September** | | |
|---|---|---|---|
| **A$M** | **2011 Actual** | **2010 Pro forma** | **% Change** |
| Sales revenue | 996.4 | 963.9 | 3.4% |
| EBIT before insurance uplift | 134.7 | 123.5 | 9.1% |
| **Total EBIT** | **139.2** | **123.5** | **12.7%** |
| Net interest expense | (23.1) | (22.1) | (4.5%) |
| Tax expense | (22.9) | (29.9) | 23.4% |
| **NPAT** | **93.2** | **68.7** | **35.7%** |
| NPAT before one-off items * | 77.6 | 71.5 | 8.5% |
| Operating cash flow, excl. tax and interest | 137.3 | 149.3 | (8.1%) |
| Net debt (closing) | 222.1 | 204.9 | (8.4%) |
| Diluted earnings per ordinary share (cents) | 25.7 | 19.7 | 30.4% |
| Final dividend per share (cents) | 7.5 | 3.0 | nm |

** The one-off items in 2011 consist of a tax consolidation adjustment ($12.5M) and insurance uplift ($3.1M net of tax); the one-off item in 2010 consists of demerger costs ($2.8M net of tax).*

## Result Highlights

- **Sales revenue** of $996.4M increased by $32.5M (+3.4%). This growth was achieved despite the loss of production at Rocklea following the Queensland floods, which we estimate adversely impacted sales by approximately 2%.
- **EBIT** of $139.2M, inclusive of a $4.5M uplift from insurance following the Queensland floods (refer later). Excluding this amount, EBIT increased 9.1% to $134.7M.
- **Net Profit after Tax (NPAT)** was $93.2M, inclusive of a one-off tax consolidation benefit of $12.5M and the $4.5M insurance uplift ($3.1M after tax). Excluding these items, NPAT was $77.6M, an increase of $6.1M (8.5%) over pro forma 2010 NPAT (excluding one-off demerger costs) of $71.5M.
- **Operating Cash Flow** (before tax, interest and dividends) of $137.3M, decreased by $12.0M (8.1%), adversely impacted by timing of insurance recoveries and post-flood stock build.
- **Net Debt** at $222.1M, up from $204.9M at September 2010.

## Outlook

Subject to economic conditions, we expect 2012 DuluxGroup underlying net profit after tax to be higher than that reported in 2011 ($77.6M).

Note: Numbers in this profit report are subject to rounding.

## Profit and Loss

**Sales revenue** of $996.4M increased by $32.5M (+3.4%) on last year. The sales result was driven by:

- Continued momentum in Paints Australia across both retail and trade businesses; and
- Strong growth in Selleys Yates due to market share gains within Selleys following success in new product development, positive outcomes from major retailer range reviews and growth in Yates, largely due to a stronger start to the financial year and improved gardening conditions in both Australia and New Zealand.

Partly offset by:

- Lost sales as a result of the loss of production at Rocklea following the Queensland floods (estimated at approximately 2% of DuluxGroup sales);
- Continued poor market conditions in New Zealand;
- Challenging conditions in our core Shanghai woodcare market; and
- Adverse impact on translation of foreign revenue to A$ (approximately $8M).

**EBIT** of $134.7M (before the flood insurance uplift) increased by $11.2M (+9.1%) on the previous year's pro forma EBIT, due to:

- Flow through effects of sales revenue variances in all businesses; and
- Disciplined cost and margin management, despite input cost pressures, particularly in paint, and ongoing investment in marketing, innovation and sales initiatives.

Segment results are discussed in more detail later in this profit report.

### Queensland Flood Impact

We estimate sales lost as a result of the loss of production at Rocklea following the Queensland floods was approximately 2% of DuluxGroup sales. These lost sales impacted the Paints Australia segment.

The table below summarises the key flood impacts and insurance recovery amounts:

| | $M |
|---|---|
| **Flood Loss recognised in 2011 (before insurance income)** | |
| 2011 Profit and Loss impact (P&L costs + profit on lost sales) | 60.5 |
| *less ...* Fixed asset write-off (non cash) | (6.6) |
| *add...* 2011 Capital expenditure on replaced assets | 17.5 |
| Total 2011 Loss | 71.4 |
| | |
| **Insurance Income recognised in 2011** | |
| Insurance Income received in cash | 53.5 |
| *add ...* Insurance receivable | 11.5 |
| Insurance Income recognised in 2011 Profit and Loss | 65.0 |
| | |
| **Insurance uplift calculation** | |
| Insurance Income recognised in 2011 Profit and Loss | 65.0 |
| *less ...* 2011 Profit and Loss impact | 60.5 |
| Net Profit and Loss Insurance uplift | 4.5 |
| | |
| Estimated 2011 net cash flow impact (refer later) | (34.8) |

## Profit and Loss (continued)

The estimated profit and loss impact of the flood in 2011 was approximately $60.5M, of which approximately 85% related to direct costs (e.g. tolling costs, stock and asset write-off, clean-up and repair costs) and approximately 15% related to the profit impact of the lost sales. However, the profit and loss impact alone does not capture the entire loss, as the insurance policy replaces assets at replacement cost, which is typically higher than the written down value. The replacement cost spent in 2011 on replacing damaged assets at Rocklea was $17.5M, an excess of $10.9M over profit and loss cost, being the written off book value of $6.6M. The total flood-related loss for the 2011 year was, therefore, approximately $71.4M ($60.5M profit and loss impact plus $10.9M difference between replacement cost and written down value for replaced assets).

The profit result for 2011 includes insurance income of $65M (recognised as other income). Of the $65M, $53.5M was received in cash at year end, with the remainder of $11.5M recognised as a receivable.

The recognition of $65M of insurance income results in an uplift of $4.5M over the estimated profit and loss impact of $60.5M. In assessing the underlying performance of DuluxGroup and the Paints Australia business, this $4.5M uplift has been deducted.

The overall cash flow impact is estimated at $34.8M for 2011. This is discussed later in this report.

Whilst the flood-related recovery activity was largely complete at year end, we expect a modest amount of further expenditure to impact 2012, mainly due to the completion and final payment of capital-related items.

Our insurance processes are well advanced, and we remain confident that the total claim will be satisfactorily finalised in the first half of 2012. Additional insurance income is expected to be booked in 2012 to cover the difference between the final total loss and the $65M booked in 2011. Importantly, from a cash flow perspective, we expect that this additional income plus the $11.5M receivable will be received in cash in the first half of 2012.

### Other items

**Corporate Costs**, at $15.6M, were $1.9M lower than pro forma 2010 costs ($17.5M). This favourable variance reflects savings achieved throughout the year, some minor favourable non-recurring variances, as well as differences between our estimate of $13M incremental standalone costs and actual costs incurred (partially timing-driven). We expect that on an ongoing basis, full year total corporate costs will be approximately $17M.

**Net interest expense** of $23.1M reflects an average cost of debt of approximately 9%. Interest expense was $1.0M higher than the 2010 pro forma net interest expense, due to higher average debt levels throughout the year caused by the adverse cash flow impact of the Rocklea flood (refer later).

**Income tax expense** of $22.9M includes a one-off tax consolidation benefit of $12.5M (an increase of $3.1M over the $9.4M recognised in the first half), which relates to the tax effect of recognising a deferred tax asset on the formation of the Australian tax consolidated group upon demerger. Excluding this amount, the effective tax rate was 30.5%.

**Net Profit after Tax (NPAT)** was $93.2M. Excluding the one-off tax consolidation adjustment of $12.5M benefit and uplift from flood insurance of $4.5M ($3.1M after tax), NPAT was $77.6M, which was $6.1M or 8.5% higher than 2010 pro forma NPAT (excluding one-off demerger costs) of $71.5M.

**Final Dividend** of 7.5 cents per share fully franked, taking the full year total to 15.0 cents, which represents a 70% payout ratio on NPAT before the tax consolidation adjustment and flood insurance uplift.

# Balance Sheet

| Balance Sheet<br>A$M | Sept<br>2011<br>Actual | March<br>2011<br>Actual | Sept<br>2010<br>Actual |
|---|---|---|---|
| Inventories | 135.7 | 121.2 | 113.4 |
| Trade debtors | 155.9 | 126.3 | 137.8 |
| Trade creditors | (159.5) | (141.3) | (138.0) |
| Total trade working capital | 132.1 | 106.2 | 113.2 |
| Non trade debtors | 16.8 | 20.8 | 6.7 |
| Tax balances (DTA, ITP and DTL) | 24.2 | 23.0 | 18.3 |
| Net property, plant & equipment | 196.4 | 159.9 | 153.9 |
| Intangible assets | 87.0 | 86.3 | 89.0 |
| Non trade creditors | (34.2) | (35.2) | (41.3) |
| Defined benefit fund liability | (22.6) | (10.4) | (13.3) |
| Provisions (excluding tax) | (42.5) | (40.3) | (40.1) |
| Net debt | (222.1) | (190.6) | (204.9) |
| Net other assets | 3.4 | 3.5 | 3.5 |
| **Net Assets** | **138.5** | **123.2** | **85.0** |
| **Shareholders' Equity** | **138.5** | **123.2** | **85.0** |

Key movements in the Balance Sheet since **September 2010** are:

- **Trade working capital** (TWC) has increased by $18.9M, largely as a result of the recovery activity following the Rocklea flood:
  - Inventory increased by $22.3M from September 2010, primarily due to additional stock built as part of the Rocklea flood recovery program and the impact of having to hold inventory of a wider range of products to support recent range review successes; and
  - Trade Debtors and Creditors movements largely reflected business growth.
- **Rolling TWC to rolling sales** (on a 12 month basis) at 12.1%, was consistent with September 2010 (12.0%).
- **Non trade debtors** increased by $10.1M, largely due to the recognition of the $11.5M insurance receivable relating to the Queensland floods.
- **Tax balances** as a whole have increased by $5.9M, mainly due to the tax consolidation adjustment.
- **Net property, plant and equipment** increased by $42.5M from last year, largely due to spend on the New Zealand factory upgrade, the new protective coatings factory in Melbourne, replacement assets at Rocklea as a result of the flood and sustenance capital expenditure, offset by depreciation and assets written off at the Rocklea site in Queensland following the flood.
- **Non trade creditors** were down by $7.1M, mainly due to the utilisation of the final earn out payments attributable to the acquisition of SOPEL in China in November 2008 and Envirosolutions in March 2008; and the timing of interest payments.
- **Defined benefit fund liability** has increased by $9.3M due to actuarial adjustments to the fund liability at September 2011.
- **Net debt** has increased by $17.2M (refer cash flow for explanation).

# Cash Flow

| Statement of Cash Flows * | Year ended 30 September | | |
|---|---|---|---|
| A$M | 2011 Actual | 2010 Pro forma | % Change |
| **Net operating cash flows** | | | |
| EBIT | 139.2 | 123.5 | 12.7% |
| Add: Depreciation | 18.1 | 17.5 | 3.4% |
| Add: Amortisation | 1.9 | 2.0 | (7.3%) |
| EBITDA | 159.2 | 143.0 | 11.3% |
| Trade working capital movement | (18.9) | (0.6) | nm |
| Non trade working capital movement | (10.6) | 5.4 | nm |
| Other non cash | 7.5 | 1.5 | nm |
| **Operating cash flows (excl. tax and interest)** | **137.3** | **149.3** | (8.1%) |
| Income taxes paid | (25.6) | * | |
| Net interest paid | (25.6) | * | |
| **Operating cash flows** | **86.1** | * | |
| **Net investing cash flows** | | | |
| Capital expenditure | (62.0) | (33.6) | (84.6%) |
| Acquisitions/disposals | (4.3) | - | nm |
| Dividends from associates | 0.5 | 0.5 | 0.0% |
| **Investing cash flows** | **(65.9)** | **(33.1)** | (99.0%) |
| **Net financing cash flows** | | | |
| Proceeds from issue of ordinary shares | 1.3 | * | |
| Dividends paid | (38.6) | * | |
| **Financing cash flows before debt movement** | **(37.3)** | * | |
| **Total cash flow before debt movement** | **(17.1)** | | |
| **Cash conversion** [1] | **77.7%** | **92.3%** | |

** Due to the demerger in the second half of 2010, the prior year (2010) cash flow only includes operating items presented on a pro forma basis. A comparison of the key line items between the prior year (2010) pro forma cash flows and the statutory cash flow statement is included as an appendix to this report.*

[1] Cash conversion is calculated as EBITDA add/less movement in working capital and other non cash, less minor capital spend (excluding flood-related capital spend), as a percentage of EBITDA.

- Net operating cash flows before interest and tax payments decreased by $12.0M (-8.1%):
  - EBITDA increased by $16.2M, reflecting the continued growth in cash profit;
  - Trade and non-trade working capital movements reflect the Balance Sheet movements discussed earlier; and
  - Other non cash primarily represents the write-off ($6.6M) of flood damaged fixed assets included within the EBITDA result.
- Total capital expenditure of $62M consisted of:
  - Minor capital expenditure ($13.5M);
  - Major capital expenditure ($23.1M), relating to the New Zealand upgrade and new Protective Coatings factory. Final payments totalling $4M will occur in 2012;
  - Acquisition of the Glen Waverley site ($7.9M); and
  - Replacement of flood-damaged assets at Rocklea ($17.5M).
- Acquisition/disposals of $4.3M in 2011. This mainly relates to the final earn out payment attributable to the 2008 acquisition of SOPEL in China.

## Cash Flow (continued)

- Cash conversion has dropped from the prior year level of 92.3%, predominantly due to the flood related items (refer below).
- We estimate that the cash flow impact due to the flood is $34.8M (adverse), per the schedule below:

| | A$M | |
|---|---|---|
| EBITDA | 4.5 | Insurance uplift |
| Trade working capital | (9.0) | Additional inventory build |
| Non-trade working capital | (11.5) | Insurance receivable |
| Other non cash | 6.6 | Fixed asset write-off |
| Subtotal – operating cash | (9.4) | |
| Capital expenditure | (25.4) | Rocklea capital ($17.5M) + Glen Waverley ($7.9M) |
| **Total** | **(34.8)** | |

- The expected finalisation of our insurance claim in 2012 will have a positive cash flow impact.

# Segment Commentary – Paints Australia

**Paints Australia EBIT $106.9M; excluding flood insurance uplift, EBIT up 11.4% to $102.4M**

**Very strong result, despite the impact of the Queensland floods**

| **Paints Australia** | **Year ended 30 September** | | |
|---|---|---|---|
| **A$M** | **2011 Actual** | **2010 Pro forma** | **% Change** |
| Sales revenue | 580.6 | 556.5 | 4.3% |
| EBIT | 106.9 | 91.9 | 16.3% |
| EBIT before flood insurance uplift | 102.4 | 91.9 | 11.4% |
| *Normalised EBIT % Sales ** | *~ 17.0%* | *16.5%* | |

** Normalised EBIT % Sales has been calculated by taking the EBIT before insurance uplift, divided by Actual Sales revenue plus the estimated lost sales due to the flood. This provides a more accurate assessment of underlying margin performance because it removes the distortion effect of flood insurance accounting.*

**Sales revenue up $24.1M (+4.3%)**

- Underlying decorative paint market showed resilience, with market volumes growing over prior year (slightly faster than the long term average growth rate).
- Share gains over the year achieved despite flood impacts, with strong performances across all retail (decorative paint and woodcare) and trade (decorative paint, texture coatings and protective coatings) parts of the business.
- Lost sales due to the flood damage at Rocklea estimated at approximately 2% of DuluxGroup sales, which equates to approximately 3% within Paints Australia.
- The business has maintained broad distribution with good ranging across all major retail channels and through our trade network.

**EBIT growth of $10.5M (+11.4%) before flood insurance uplift**

- Continued pressure on input costs, with double digit titanium dioxide increases the most significant. However, after taking account of the positive effect from the strong Australian dollar and cost saving initiatives, overall input cost increases were slightly greater than inflation.
- Pricing discipline, innovation, cost control and productivity assisted in maintaining overall EBIT margins.
- Marketing investment increased, particularly in the second half once Rocklea supply was restored.

**Flood Recovery**

- Rocklea is now fully operational. Some minor non-operational works (e.g. offices) are in final stages of completion.
- Our flood related third party tolling arrangements have now all been completed. We acquired the Freeworld site in Glen Waverley, which will add greater flexibility to our supply recovery in the event of a future Rocklea incident.

**Paints Australia – Outlook**

- Modest market growth expected in 2012.
- Raw material prices are expected to further increase, with 2011 ‘exit rates’ well above prior year. Further double digit increases in titanium dioxide are expected, but initiatives to mitigate (including cost savings) are well underway.
- Depreciation charge is expected to increase by approximately $3M due to the new protective coatings factory and the replaced assets at Rocklea.
- We continue to see opportunities for profitable share growth within this business.

# Segment Commentary – Paints New Zealand

**Paints New Zealand EBIT down 5.8% to $9.7M**

**Weak market conditions and input cost increases affect underlying result, partially offset by revenue and EBIT from manufacture to support Australian operations post-Queensland flood**

| **Paints New Zealand** | **Year ended 30 September** | | |
|---|---|---|---|
| **A$M** | **2011 Actual** | **2010 Pro forma** | **% Change** |
| Sales revenue | 82.5 | 79.4 | 3.9% |
| EBIT | 9.7 | 10.3 | (5.8%) |
| *EBIT % Sales* | *11.8%* | *13.0%* | |

**Sales revenue up $3.1M (+3.9%)**

- Sales revenue was boosted by the New Zealand business providing production support for Paints Australia following the Queensland floods and adversely impacted by transfer of protective coatings manufacture to the new factory in Australia and foreign exchange translation.
- The New Zealand decorative paint market remained weak and is estimated to have declined approximately 4% in volume terms during the financial year. Most of the market decline has been experienced in the retail segment where discretionary spend remains weak in the face of rising cost of living. The Christchurch earthquakes in September 2010 and February 2011 have also contributed to the market weakness.
- Our business held share in this weak market and underlying revenue (excluding production for Australia and protective coatings exports) was flat.

**EBIT decline of $0.6M (-5.8%)**

- EBIT was impacted positively by the flood-related production for Australia, and adversely by the transfer of protective coatings manufacture to Australia, higher depreciation and non-recurring fixed costs due to the factory upgrade, costs associated with the Christchurch earthquake and on translation due to the stronger Australian dollar. Excluding these effects, like-for-like EBITDA declined by approximately 8%.
- Underlying margins contracted as net input cost increases (driven by titanium dioxide) were greater than in Australia, due to a lesser foreign exchange offset. Price increases were realised across all major sectors. Fixed costs increased modestly due largely to the investment in two new trade stores, with other costs well-contained. Margins were also adversely impacted by increased depreciation following the completion of the factory upgrade.

**Paints New Zealand – Outlook**

- Weak market conditions are expected to continue for the remainder of calendar 2011 with some improvement expected in early 2012.
- The reconstruction activity in Christchurch is moving quite slowly given continued aftershocks, though a positive 2012 impact is expected.
- As per the Paints Australia outlook, input costs are expected to come under continued pressure.
- Excluding the revenue associated with manufacture for Australia (flood recovery and protective coatings), which will not form part of the business in 2012, the 2011 like for like sales base is approximately A$70M. This is a reasonable base from which to build 2012 projections.

# Segment Commentary – Selleys Yates

**Selleys Yates EBIT up 5.5% to $30.5M**

**Growth driven by market share gains in Selleys and ongoing improvement in Yates business performance**

| Selleys Yates | Year ended 30 September | | |
|---|---|---|---|
| A$M | 2011 Actual | 2010 Pro forma | % Change |
| Sales revenue | 248.9 | 230.8 | 7.8% |
| EBIT | 30.5 | 28.9 | 5.5% |
| *EBIT % Sales* | *12.3%* | *12.5%* | |

**Sales revenue up $18.2M (+7.8%)**

- Sales revenue for Selleys grew as a result of a strong new product development program and market share gains with key customers in Australia.
- Yates revenue grew and was supported by improved gardening conditions and a strong marketing campaign.

**EBIT growth of $1.6M (+5.5%)**

- Earnings growth in both Selleys and Yates. Slight overall margin contraction was predominantly due to sales mix following range reviews.
- Return on sales declined in Selleys as a result of one-off costs associated with new customer ranging and a mix effect, as this extended range now includes lower priced 'entry level' products.
- Yates profit growth continued to be supported by ongoing improvement initiatives.

**Selleys Yates – Outlook**

- Further moderate market growth is expected in Australia, while the New Zealand market is expected to begin to recover during 2012.
- Focus will remain on stimulating consumer demand and growing profitable market share through increased new product development and customer share growth activity.
- We will continue to seek adjacent bolt on acquisition opportunities to support organic growth plans for both Selleys and Yates.

# Segment Commentary – Offshore and Other

**Offshore and Other EBIT down 22.2% to $7.7M**

**Softness in China and Powder Coatings dilutes earnings**

| Offshore and Other | Year ended 30 September | | |
|---|---|---|---|
| A$M | 2011 Actual | 2010 Pro forma | % Change |
| Sales revenue | 113.8 | 123.5 | (7.9%) |
| EBIT | 7.7 | 9.9 | (22.2%) |
| *EBIT % Sales* | *6.8%* | *8.0%* | |

The Offshore and Other segment consists of the Dulux Powder, Refinish and Industrial Coatings Australia and New Zealand business ('Powder Coatings'), the Dulux Papua New Guinea business and the South East Asian and China businesses (known as DGL International).

**Sales revenue down $9.7M (-7.9%)**

- The ***DGL International Asia*** business in China experienced a challenging trading environment during the year, particularly in the core Shanghai woodcare market:
  - Volumes impacted by government constraints being imposed to regulate growth within the residential property sector, increased price competition and Shanghai Expo (which increased the previous corresponding period); and
  - Signs of improvement in the last quarter of 2011, with revenue growth above prior year.
- PNG revenue continued to grow in local currency, largely due to market growth driven by investment in the gas, oil and mining sectors.
- Powder Coatings declined marginally, given its exposure to the new housing sector.
- Total segment revenue was adversely impacted by the translation of foreign revenue to A$ (approximately $5M).

**EBIT decline of $2.2M (-22.2%)**

- A weaker result in China, driven by revenue softness, raw material price increases and ongoing investment in capability for longer term growth.
- PNG earnings grew in local currency, though the quantum of growth was lower on translation due to the strong Australian dollar.
- A weaker result for Powder Coatings, largely attributable to the decline in sales.

**China Strategy Update**

- DuluxGroup announced on 2 November 2011 the merger of the DGL International business in China and Hong Kong with Camelpaint of Hong Kong to create DGL Camel International Limited. Refer below for further details.

**Offshore and Other - Outlook**

- Market conditions are expected to improve moderately in 2012. We have seen signs of improvement in China in the last quarter of 2011.
- We continue to seek opportunities to build on our Selleys positions in South-East Asia.

# Other Items

**China Merger**

DuluxGroup Limited announced on 2 November 2011 the merger of its DGL International business in China and Hong Kong with Camelpaint of Hong Kong to create DGL Camel International Limited.

Camelpaint was established in Hong Kong in 1932. It is a leading manufacturer and marketer of a range of coatings products in Hong Kong and mainland China, mainly focussed on the trade painter and industrial markets. DuluxGroup and Camelpaint have a successful history of working together, having been joint venture partners in DGL Camel Powder Coatings in mainland China since 2004.

DuluxGroup will hold 51% of DGL Camel International and the current General Manager of DGL International, Alan Preston, will be the General Manager of DGL Camel International. Kerwin Yan, current CEO of Camelpaint, will continue as a full-time employee and Director of DGL Camel International.

The newly formed company will manufacture, market and distribute coatings and associated products, including the Opel, Levene, Selleys, AcraTex and Camel product ranges.

The transaction involves a payment by DuluxGroup to Camelpaint to secure board and management control of the new company. The amount is not material to DuluxGroup. There are a number of conditions to be met prior to completion of the transaction, which is expected to occur by the end of the 2011 calendar year.

**Debt Facility Renewal**

DuluxGroup has recently renewed its $400M syndicated debt facility. Whilst the existing facility did not expire until April 2013 ($300M) and April 2015 ($100M), the Company felt that it was appropriate to capitalise on favourable borrowing conditions and renew early. The borrowing rate will be more than 1% lower than under the previous facility. In addition, the tenure of the facility is now more evenly spread with $100M expiring in one year (but with a DuluxGroup option to extend for a further three years), $150M expiring in three years and $150M in five years.

**Depreciation**

Due to the capital expenditure program in 2011 (including Rocklea post-flood renewal), depreciation and amortisation will increase in 2012 by approximately $3-4M.

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# Appendix: Prior Year comparison between Statutory (Appendix 4E) and Pro forma Figures

| Profit and Loss comparison (A$M) | Appendix 4E 2010 | Pro forma 2010 | % |
|---|---|---|---|
| Revenue | 775.7 | 963.9 | 80.5% |
| EBIT | 103.1 | 123.5 | 83.5% |
| Net Interest | (13.4) | (22.1) | 60.8% |
| Tax expense (pre one-off demerger cost) | (25.6) | (29.9) | 85.7% |
| NPAT pre one-off demerger costs | 64.1 | 71.5 | 89.7% |
| One-off demerger costs (net of tax) | (2.8) | (2.8) | 100.0% |
| NPAT post one-off demerger costs | 61.3 | 68.7 | 89.2% |

As stated earlier, the 2010 results in the Appendix 4E include the progressive transfer of DuluxGroup's operations into the DuluxGroup Limited ownership structure, and therefore do not reflect a full 12 month operating result. The Australian and New Zealand businesses were transferred in on 1 December 2009 and the others were progressively transferred over the remainder of the year, as outlined at the front of this report. Therefore, for revenue and EBIT, the variation between statutory Appendix 4E numbers and the pro forma numbers is predominantly due to the trading results before the businesses were transferred (e.g. October and November results for Australian and New Zealand businesses). In relation to net interest expense, the Appendix 4E figures include a blend of inter-company interest (pre-demerger) and external interest (post-demerger). The pro forma figures reflect management's estimate of the net external interest expense that would have been incurred if DuluxGroup had been a standalone listed company with external borrowings for the full 12 months. Appendix 4E tax expense reflects the lower income (for the reasons outlined above) plus various demerger related one-off adjustments. The effective tax rate per the Appendix 4E is 28.5%. Pro forma Tax has been calculated using an effective tax rate of 29.5%.

# Appendix: Prior Year comparison between Statutory (Appendix 4E) and Pro forma Figures

| Cash flow comparison (A$M) | Appendix 4E 2010 | Pro forma 2010 |
|---|---|---|
| **Cash flows from operating activities** | | |
| EBITDA | 119.5 | 143.0 |
| Movement in trade working capital | (81.9) | (0.6) |
| Movement in non-trade working capital | 7.1 | 5.4 |
| Interest received | 0.2 | * |
| Interest paid | (9.2) | * |
| Income taxes paid | (25.1) | * |
| Other | - | 1.5 |
| **Net cash inflow from operating activities** | **10.7** | **149.3** |
| **Cash flows from investing activities** | | |
| Payments for property, plant and equipment | (29.8) | (33.6) |
| Payments for intangibles | (0.7) | * |
| Payments for purchase of businesses and controlled entities | (310.7) | * |
| Proceeds from joint venture distributions | 0.5 | 0.5 |
| Proceeds from sale of property, plant and equipment | 0.7 | * |
| **Net cash outflow from investing activities** | **(340.1)** | **(33.1)** |
| **Net cash inflow from financing activities** | **371.9** | * |

* Not calculated in 2010 for pro forma.

The above table is provided to compare key line items between the statutory cash flow in the Appendix 4E and the abbreviated pro forma cash flow.

The abbreviated pro forma cash flow has been based on the underlying operating figures of the DuluxGroup businesses as if they were owned by DuluxGroup Limited for the full 12 months. However, the pro forma cash flow has not been adjusted to reflect the impact of a capital structure. Therefore, interest, tax, debt and equity movements (including dividends) have not been included. In addition, one-off demerger costs and ongoing standalone costs have been excluded. For any other items where there is a value in the Appendix 4E cash flow and no corresponding value in the pro forma cash flow, this typically reflects demerger related transactions.

The EBITDA difference is due to the same drivers as outlined in the profit and loss comparison on the previous page. The significant adverse trade working capital movement in the statutory cash flow reflects the structuring within the demerger itself, predominantly relating to the transfer of working capital balances for the Australian businesses in December 2009.

For all other items where there is a comparison, the differences primarily relate to the progressive transfer of the assets from Orica to DuluxGroup.