Salmat – Results Presentation FY2006

[Phil Salter]

Title Slide

Good morning and welcome to this presentation of Salmat's results for the year to 30 June 2006.

Thank you for joining us today either in person or by conference call.

I'm Phil Salter and with me are Peter Mattick and Ashley Fenton, our CFO.

This has been a challenging year for Salmat and it's pleasing that we finished the year better than we expected, with our earnings $1 million ahead of our guidance.

Today I will give you an overview of the result and a run down on what we have achieved during the year in each of the businesses. Then Ashley will provide you with more detail on the numbers.

Peter will then address the operational aspects of each business and the strategies we have to move them forward. He will also talk a little about our recent bid for VECommerce and how the deeper technology skills and intellectual property will fit with our strategies.

The presentation will last for about 30 minutes and we'll take questions at the end.

During the presentation we will refer to the slides that were lodged with the ASX this morning. At the end of those slides, we have an information pack which will include any financial information, not already covered.

If you don't have the slides or the information pack yet, they are available on our website www.salmat.com.au or else we have some extra copies at the back of the room.

Key messages/overview slide

This was a challenging year for Salmat, as we contended with some tough market conditions, in BPO in particular. We incurred necessary costs as we implemented new technology, integrated recent acquisitions and restructured our operations to improve overall efficiency.

In 2006 we achieved strong revenue growth across all divisions – with a standout result from call centres, taking full year revenues to $527 million – up 29.3%.

Our Profit After Tax was better than our most recent guidance at, $26.2 million, as the second half turned out better than expected.

It was our first full year with SalesForce on board and the integration is complete. The combined Call Centre Division has produced excellent results with strong growth in new clients, seats, revenues and profits. And we're still growing - we have recently opened our new 300 seat Geelong Call Centre which has expanded our proven regional model. Our Genesys technology roll out is complete across all our centres and we're using our technology in smart ways, which have helped us to win complex work, such as the recent national census.

Targeted Media delivered a good result in a soft advertising market. We had continuing volume growth in the second half and our ongoing focus on cost control has meant that our margins have held up. Overall we were pleased to achieve the same growth rates in revenue and EBITA as the first half. The new excess print capacity in the industry will create opportunities going forward.

Our data analytics and targeting tools are having continued success in attracting non-traditional users of catalogues. Our new software distribution system has now been rolled out nationally and this year we will be looking to get some benefits from the platform through improved processes.

It's been a challenging year for our BPO division, following the recent price resets on major contract renewals. The Division's result was disappointing, being well down on last year. However, we've done a lot in restructuring, upgrading of facilities and equipment and lowering the cost base of the business going forward. We've also secured some new contracts in Asia which will provide that business with much needed scale.

ClientLogic, our Joint Venture Call Centre business in the Philippines, produced a good result with strong growth in revenues and earnings. This has enabled us to equity account for the first time.

During the year we've restructured our operations to improve efficiencies and manage growth and this has included the moves of our largest Targeted Media and BPO facilities from Chester Hill to Moorebank in NSW and our Hong Kong BPO operations to their new, state-of-the-art premises.

The Board has demonstrated its confidence in the business by declaring a fully franked final dividend of 9.5 cents, up 5.6% on the previous year, payable on 3 October to shareholders on the register at 12 September.

This will bring dividends for the year to 16.5 cents fully franked, an increase of 6.5% over 2005.

Overall, it has been a busy and important year for us. As we said at the half year, we have three divisions of similar revenue size, which means our exposure to industry cycles is more balanced and our future growth opportunities are wider. The work we've done in investing in our business gives us a strong growth platform for the future.

I will now hand over to Ashley to talk about our financial results in more detail.

[Ashley Fenton]

Thanks Phil. Good morning everyone.

The key features of this result are the very strong revenue growth, the growth in underlying EBITA despite our soft BPO results, and the better than expected second half result which led to the overall result being $1 million better than the guidance we provided in may.

I'll run through the make up of the revenue growth and you will see the excellent contribution from our call centre division. Then I'll take you through the EBITA and highlight the underlying growth of the business. I'll cover off the group result and then take you through the cash flow.

Sales revenue was $526.8 million, up 29.3% due to organic growth in all divisions and a full year's contribution from the SalesForce and NSW Print-on-Demand acquisitions.

The standout result came from our call centre division, with revenue up 85.1% to $180 million and like-for-like growth in the second half of 31%. You can see this impact on this slide.

Revenue waterfall slide

You can also see the $11 million or 6.5% increase in Targeted Media's revenue which came mainly from the 4.7% growth in advertising catalogue volumes.

BPO's revenue grew by 18.1% or $25.6 million, mainly due to the impact of the print-on-demand acquisition, which added $22 million. Australian revenues were flat but in Asia we've had strong revenue growth of 30%, albeit from a relatively small base.

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EBITDA was up 1.7% to $60.3 million. However excluding significant items, EBITDA growth was 12.8%, mostly due to the strong contribution from the SalesForce contact centres and the first equity-accounted profit from the ClientLogic Philippines Joint Venture.

Depreciation increased by $0.6 million to $16.0 million. However last year's $2.2 million write down of software assets masks an underlying increase in depreciation of 21.2% which reflects our higher capex spend.

Total EBITA was $44.4 million, an increase of 1.1% on prior year. Excluding the impact of significant items, EBITA growth was 10.0%, with second half growth of 18.9%.

The significant items, which are detailed in the information pack, totalled a negative $1.6 million, compared to a positive $2.1 million last year, and mainly related to redundancy and restructure costs, with last years credit being mainly the writeback of loan provisions.

The underlying business growth of 10% was solid and is in line with the compound average growth rate of underlying EBITA of 11.8% since listing, which you can see on the graph.

EBITA pre significants

The largest growth contributor to our growth this year was contact centres, whose EBITA contribution, increased by $7 million to $10.5 million for the year. You can see the significance of this on the graph.

EBITA waterfall slide

The contact centre result includes a full year of the SalesForce results versus 6 months in 2005, and the maiden equity accounted profit of $2.1 million from the ClientLogic Joint Venture. The second half results from the SalesForce contact centres show particularly strong organic growth in the underlying business with EBITA growth of 77%.

Targeted Media's EBITA also grew, but by a more modest 7.5% to $38.5 million. Margins, at 21.4 % for the year, were up slightly on last year. This is mostly due to the benefits from our continued focus on costs and improved management of freight expenses.

BPO's EBITA results, whilst disappointing with a drop of $5.7 million or 42.2% on the prior year to $7.8 million, were pretty much as we flagged at the first half – with second half performance broadly in line with the first half. Reduced pricing on major contract renewals cost over $7 million, whilst higher depreciation following the substantial capex reinvestment added $1 million to costs. Major new contracts and improved cost efficiencies helped restrict these negative impacts.

Group result slide

Goodwill amortisation was $1.4 million, up from $700,000 in the prior year due to the full year effect of the AIFRS amortisation on the SalesForce long term contracts.

Net interest expense of $4.5 million, up from $500,000 in the prior year, reflects the full year effect of the $64 million debt to fund the acquisition of SalesForce and increased working capital needs associated with the increased size of the business.

Our tax expense was higher than the prior year's, due predominantly to the non-taxable write-back of $5.4 million of the ClientLogic loan provision last year. We would normally expect an effective tax rate of about 33% due to non-deductible items, however this year's rate was lower, at 32% mainly due to the non-assessable ClientLogic Philippines equity result.

Second half profit was $13.1 million and took the Full Year Profit After Tax to $26.2 million down 16%.

The final dividend of 9.5 cents takes the total dividend for the year to 16.5 cents fully franked, which represents a pay-out ratio of 74%.

Cash flow slide

Operating cash flow was down 9.9% to $28.1 million, reflecting the increase in interest paid on the back of higher borrowings.

Capital expenditure of $26.7 million brought our yearly spend to 5% of sales, a little higher than our target range of 4.0 to 4.5 % of sales. It was a big year for capex, at $10.7 million higher than last year, with our major BPO machinery refresh program, the significant expansion of our call centre capacity, major new offices in NSW and Hong Kong, technology upgrades in a number of areas and our new call centre in geelong coming on line earlier than planned. We expect capital expenditure for the year ahead to come back within our target range.

The $4.5 million for acquisitions mainly relates to the final payment of retention monies on the SalesForce acquisition.

Joint Venture loans of $4.9 million were repaid during the year by ClientLogic. At 30 June, outstanding loans to ClientLogic totalled $5.0 million and are expected to be repaid in full in the year ahead.

Net debt at 30 June was $67.9 million, representing a net debt: equity ratio of 63.6%.

Annualised interest cover, at more than 13 times, calculated on the EBITDA line, remains strong which means we can comfortably manage the acquisition of VECommerce.

Our return on capital was lower than the previous year, but was still an impressive 25%.

I will now hand over to Peter Mattick, who will review the operational aspects of the divisions and the strategies we have to move them forward.

[Peter Mattick]

Thanks, Ashley. Good morning, everyone.

Moving on to the operations and strategies for the Targeted Media business.

We have had another solid year in this business despite a soft advertising market, the recent loss of the Coles brands (Target, BiLo and supermarkets) is a disappointment. This work is currently transitioning progressively through to April 2007. We have made good progress in replacing the volumes with new business, which will broaden our customer base and reduce our reliance on any one customer for future growth. We are confident that our service offering and solutions are competitive and provide results, flexibility, innovation and responsiveness to meet the needs of our customers.

During the year we have been introducing new strategies to improve the way we deliver advertising catalogues. We have also improved our targeting tools with the introduction of new product enhancements aimed at the home improvement and retail property sectors. These enhancements will improve targeting based on demographic information such as spend on renovations, development applications, and other lifestage and lifestyle variables.

Our multi-tiered accountability model for distribution is focused on proof of delivery and speed to market. Pleasingly, a recent independent audit by Morgan Research has confirmed that our model is already generating over 94% on time deliverability for individual catalogues distributed.

The industry outlook is competitive, overlayed with a continuing soft advertising market. We remain concerned that we may come under pricing pressure. However on the up side we have seen the print industry capacity constraints of the last two years removed by substantial new investment by the industry, with demand to fill new presses likely to provide a slow stimulus for additional catalogue work.

Business Process Outsourcing

It's been a challenging year for this division and whilst the EBITA results have been disappointing, we've done a lot of work restructuring, upgrading facilities and equipment and lowering the cost base. The division has borne a number of costs relating to new business and customer integration, the implementation of new technology and the moves to new sites in NSW and Hong Kong.

The industry environment has been competitive and led to a number of contract renewals being reset at lower prices, impacting our margins. Despite this, volume growth has remained sound, and pricing levels for new business have stabilised.

Take up of our new products and services has been pleasing, and continues to be a key focus area for us.

Our digital print on demand offerings have been enhanced through the recent rollout of our web based front end ordering systems.

Digital colour is providing an attractive capability for customers, whilst our electronic products are also growing in acceptance and we've had many new customers taking on our Streamserve product.

BPO is concentrating on redesigning its processes and investing in technology, to optimise efficiencies in the Australian business, and on moving the Asian operations into profitability.

Contact Centres

Contact centres has had a strong year across the board.

The growth has been faster than we expected. We've grown our seats by 14.4% to 2,744 as a result of expanding operations in Sydney, Melbourne and Auckland. During the second half, increased demand pushed utilisation to 90%, which prompted the recent opening of our new call centre in Geelong, adding a further 300 seats.

We have seen an increased take-up of outsourcing across the industry as companies embrace the model of improved customer service, increased sales and better quality at a lower cost.

We're also pleased to see the improvement in our EBITA margin up nearly 1% to 4.8%, particularly in a year when we've expanded our infrastructure and built a substantial business. We still consider a 10% target for this business is achievable in the medium term, but on a much larger revenue base than we originally forecast.

We continue to see a strong pipeline for new business, particularly in the areas of government, infrastructure, entertainment and telecommunications.

During the year SalesForce won the Hewitt Award for the Best Employer in Australia and New Zealand for the second year running. SalesForce is the first and only company to have achieved this accolade – a testament to the strong culture that is so critical in running a real people business.

Much has been made of the recent introduction of the do not call legislation. This may trouble some of the smaller outbound work focused players. For us it is not a major concern as we positioned our business a while ago away from the type of outbound cold calling work which will be impacted. Our mix of inbound work remains at 65%.

Our increased scale is providing our prospects considering outsourcing with the confidence they need to be comfortable in handing over their call centre operations to us. The growth in the outsourcing market can be seen on this chart.

Outsourced contact centres market slide

As you can see, the outsourced call centre market has grown to 13% and we believe that this trend will continue, following the lead of established overseas markets.

We are now the market leader with approximately 24% market share.

Our use of world-class technology is setting us apart from our competitors, and provides our customers with superior services. Our takeover bid for VECommerce, a speech solutions provider was announced on 27 July 2006. The acquisition will further strengthen our technical capabilities and customer appeal. VECommerce provides voice self-service solutions using speech recognition and verification technology. This allows for calls to be serviced in the most cost efficient way and gets customers who need to talk to a call centre agent through to one more quickly. We expect to lodge our bidder statement shortly.

Summary slide

In summary, this has been a challenging but important year for Salmat. Our revenue growth has been terrific, and gives us a solid base to grow from, and our underlying EBITA continues to grow. However, with this growth we can see that our costs and processes have needed attention.

We are now addressing this through project optimise – a full review and reshaping of all our processes, systems, products and services, which will provide us with a platform for continued sales and profit growth across the company. Optimise is a long term initiative that will provide transformational change in the businesses.

It’s too early to be talking about the current year’s outlook with only a month and a half gone. We’ll talk more about market conditions and trading at our annual general meeting in November.

We are confident, however, that we have a complementary business mix that will drive considerable long term growth potential.

We shall now be pleased to answer any questions. Please say who you are and the firm you represent.

Disclaimer

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Forward-looking statements involve inherent risks and uncertainties. We caution you that a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors include but are not limited to: competition and product pricing in the markets in which we operate; general economic and market conditions; compliance with, and possible changes in, environmental and health and safety laws; dependence on cyclical markets; the supply and cost of materials; exposure to environmental or other legal proceedings; and risks of conducting business internationally. We caution you that the foregoing list of factors is not exclusive and that other risks and uncertainties may cause actual results to differ materially from those contained in forward-looking statements. Forward-looking statements speak only as of the date they are made.