

Looking to the fundamentals

The following projects were completed during the year:

- relocation of the Thames branch
- the opening of a new depot facility at Ohakune
- the establishment of a new frame and truss manufacturing facility in Christchurch
- upgrades at the Huntly, Wairau Park, Dunedin and Cranford St stores

In addition, a site was purchased in Warkworth for a new depot facility and construction began for a new facility in New Plymouth.

As in the past, the branch upgrade programme provided much improved retail facilities, but continues to be focused principally on improving yard access and drive-through facilities, which are a service to the division's trade customers.

Infrastructure

The division is a vertically integrated business supplying aggregates, cement, readymix concrete and a range of concrete products in New Zealand; and concrete pipeline products and a range of aggregate sands throughout Australia. It is the largest construction contractor and residential builder in New Zealand.

Performance

Operating earnings grew for the seventh successive year despite lower demand for most construction products in New Zealand, a significant decline in the number of houses sold and ongoing weakness in the New South Wales market. The key operations all performed well given their market conditions.

Operating earnings grew by \$37 million to \$308 million, including earnings from property related activities of \$80 million from the residential business, quarry end use, and surplus asset sales, up from \$49 million in the prior year.

The concrete business increased operating earnings by \$1 million to \$189 million. Construction earnings also increased, from \$34 million to \$39 million. The property and residential operations accounted for most of the earnings improvement for the year, increasing \$31 million to \$80 million.

Operating earnings from the cement business were lower despite significant benefits flowing from the upgrade of the plant. Domestic cement volumes were 3 percent lower than for the previous year and 8 percent for the 2006 year. Export sales increased but margins were low. Completion of the plant upgrade enabled record production of clinker, avoiding the extra cost of imports for the first time in six years. Cement production was also at record levels. Prices were 4 percent above those for the previous year, but this did not fully recover increased production and distribution costs. The impact of cost increases in the new year – particularly for coal, diesel and electricity – will be substantial. A further cement price increase of \$11 per tonne has been announced, but will not be sufficient to cover cost increases.

Aggregates recorded lower operating earnings due to reduced volumes of core products, and competitive pressures that restricted the ability to pass on all cost increases. While overall sales volumes were similar to those for the previous year, the sales mix was unfavourable and weakness in the Auckland market resulted in a sharp decline in earnings in that region. Unit costs increased significantly due to the compounding impact of a high fixed cost base and significant increases in input costs.

Sales	\$1,857 million
Operating earnings	\$308 million
Funds	\$1,027 million
Employees	5,846
Key Brands	Firth Fletcher Construction Fletcher Residential Golden Bay Humes Rocla Winstone Aggregates

Readymix and masonry operating earnings were lower. The impact of a softening residential construction market gained momentum in the second six months, but strong demand in rural areas reduced the impact on earnings. Concrete sales volumes were only 4 percent below those for the previous year due to investment in new sites. A focus on margin maintenance ensured that the contribution per cubic metre of concrete was similar to that for the previous year despite significant increases in costs. Masonry volumes were 6 percent lower, with significant declines recorded in the latter part of the year, although margins were maintained.

The concrete pipe market was softer, but good growth in precast concrete product sales and a small acquisition resulted in improved earnings. Concrete pipe volumes were down 6 percent, but precast volumes were 24 percent higher due to market development initiatives. Overall margins were lower, primarily due to mix, and to a lesser extent increased input costs.

Construction had a strong year, with improved operating earnings and all business units performing above expectations. The construction backlog at year-end was \$1.3 billion, up from \$775 million one year earlier. The business continues to hold significant opportunities for the next year. Major contracts won during the year were the Mt Eden Prison Upgrade (\$150 million), the Eden Park Redevelopment (\$150 million), the Manukau Harbour Crossing (\$132 million) and New Lynn Rail Trench (\$140 million). The backlog, and continued infrastructure spending, suggests that the workload will remain strong in both the commercial building and the civil engineering operations. In the South Pacific, earnings were solid with Papua New Guinea offsetting the more muted tone of the market in Fiji. Turnover is forecast to be higher in the current year, but this will be dependent on the timing of major projects expected to commence during the year.

Earnings from property related activities include those from quarry end use and the residential business. Earnings from the residential business declined by \$16 million due to the significant drop in house sales. Housing starts declined in the second half and prices fell. While land stocks have grown, the land has been acquired at good prices and carrying values are not considered to be at risk. Good results were obtained this year from development opportunities for land previously used in the aggregates business, with these activities expected to provide further earnings in future years.

In Australia, the pipeline and quarry businesses performed well, recording combined operating earnings of \$59 million compared with \$47 million for the previous year. The quarry products business recorded improved results in all states except Western Australia, where earnings were still strong but lower due to recent reserve depletion. Two pieces of land were acquired in Perth for quarry development to address the situation. The pipeline products business recorded a substantial increase in sales volumes of non-pipe products, resulting in earnings significantly ahead of those for the previous year.

Looking to the fundamentals

The primary focus of the capital investment programme is on high-returning organic growth opportunities. This has contributed significantly to the earnings growth achieved in recent years and is expected to continue to do so. The \$158 million invested in the 2008 year was an increase of \$50 million on the prior year. Strategic and growth projects accounted for \$87 million, including the new cement port facility in Auckland (\$10 million); new quarry land, reserves and consents (\$36 million); new concrete plants, an upgrade to a concrete pipe plant and the acquisition of a motorway barrier business (\$18 million); pole and sleeper plant upgrades (\$13 million); and major construction plant (\$10 million).

Golden Bay Cement secured a long-term site to replace its Auckland port facilities. The new facilities will cost \$45 million and are due for completion in December 2009. The investment secures long-term, low-cost access to the major New Zealand market.

Further investment was made of \$17 million in New Zealand, and \$19 million in Australia, to enhance aggregates supply.

The readymix business improved its competitive position in a number of markets by investing \$10 million to acquire and upgrade concrete and masonry plants. The New Zealand pipeline business committed to upgrade to new technology at its Auckland manufacturing facility. The Australian business invested \$13 million in upgrading and expanding its pole and railway sleeper operations and acquiring a small water quality business.

The construction business was required to increase its investment in a range of plant as a consequence of the substantial lift in backlog.

Further progress has been made in divesting low-returning businesses and surplus assets, with \$45 million of cash generated during the year, compared to \$28 million in the previous year. This brought the total amount of cash generated over the past seven years from asset reductions to \$154 million. The operating earnings impact on future years is negligible. While the division will continue to fine tune its portfolio, material divestments are not expected during the current year.

Quarry end use

Over the years the aggregates business has developed significant skills in resource management planning and is applying these skills to develop the highest and best use alternatives for excess land while protecting the existing quarry activities.

AUCKLAND'S THREE KINGS QUARRY, WHERE DISCUSSIONS HAVE COMMENCED WITH STAKEHOLDERS WITH A VIEW TO IDENTIFYING THE APPROPRIATE END USE FOR THE ASSET



In the last financial year the aggregates business has advanced two opportunities in the Auckland area. At Pokeno it is working with a consortium of developers with a view to creating an integrated residential, commercial and industrial designation. In the South Auckland suburb of Wiri it has completed a transaction that frees up 35 hectares of industrial land for development. Both opportunities have been years in the planning and reflect the focus to ensure that the return from the business's asset base is maximised, while still protecting the core quarrying business.

Over the next few years there will be a number of quarries coming to the end of their productive lives and assessment is underway with regard to their best end use. This involves not only potential development but also use for cleanfill purposes, a use that already makes a contribution to profitability and reflects the whole of life approach to these assets.

The other major initiative is the change of use for the Three Kings quarry in suburban Auckland. In conjunction with the community and Auckland City Council the business will conceptualise the end use for 15 hectares of land that will be

available upon the completion of the quarry filling process, which will take some eight to 12 years.

Recognition of an earnings stream from more intensive land use is a natural progression. While earnings can be variable, it is hoped that, subject to market demand, these developments will provide average earnings of around \$10 million per annum for the 10 years from the financial year ended June 2010.

