# GUD Holdings Limited

## Chairman's Address

## 59th Annual General Meeting

Tuesday 25th October 2016

RACV Club

501 Bourke Street, Melbourne

Ladies and gentlemen, my address to you at today's meeting will cover three key topics. The first of these is the customary overview of financial performance for the last completed financial year – that ending 30th June 2016. The Annual Report and Annual Review covering that year were recently mailed to you or, if you have chosen, their availability electronically has been advised to you.

The second item I will cover relates to our business portfolio and the changes we have made to it since we gathered here at this time last year. Finally, following a review of operations from Managing Director, Jonathan Ling, I will provide some commentary on the outlook for the current financial year.

However, prior to addressing all these issues I wanted to provide a perspective on workplace health and safety at GUD, as this remains an overarching management matter to which significant attention is directed on a daily basis.

Our recent priority in relation to safety has been to improve safety performance through the introduction of a number of new programs and initiatives. These have included increasing employee engagement, improving the safety culture at each business unit and site and developing safety campaigns encouraging staff to be more aware of their surroundings and the immediate resolution of identified safety risks.

GUD established a Safety Excellence Awards program in the 2014-15 financial year and continued with this in the 2015-16 year. The Awards are directed at promoting, encouraging, recognising and rewarding businesses, teams and individuals who have placed a high emphasis on accident prevention and have promoted a safety culture in the workplace.

While significant progress has been made it has recently been recognised that the GUD group's primary safety risks now reside in remote sites and with employees whose role requires a significant time spent on the road. It is fair to state that while the culture and safety performance has improved at all major sites within GUD this hasn't translated fully to our more distant operations, such as interstate offices and warehouses. This is being actively addressed in the current financial year.

In relation to mobile worker safety we are actively managing driver performance through the installation of telematics systems in all tool of trade vehicles supplied to mobile staff to enable them to do their jobs. This allows poor driving behaviour, which elevates the safety risk, to be identified and rectified and effectively places the same safety culture into the mobile office as it does the traditional office.

While GUD operates across industries that are not as inherently risky as, for example mining or construction, we recognise that providing a safe workplace for our employees and contractors is essential and our safety programs are structured around improving safety performance year-on-year.

Pleasingly, this unyielding focus on workplace safety is reflected in the high ratings achieved on the safety questions included in the group's annual employee engagement survey. More importantly, our safety performance improved in the 2015-16 year as evidenced by the group's total injury frequency rate, as measured by the total number of recordable injuries per million hours worked, more than halving over the last two years to 7.1 injuries.

I will now turn to outlining the primary factors underpinning the financial results we reported in late July for the year ending 30th June 2016.

Whilst the headline result was a loss of $43 million, this clouds the underlying operating result which was boosted by the full year inclusion of Brown & Watson, further outstanding returns from the established Ryco and Wesfil automotive businesses and a substantial uplift in profitability at Davey.

Underlying net profit after tax from the continuing businesses in GUD's stable, increased by 36% to $44.4 million. It is important to note that with the impending sale of GUD's remaining interests in the Sunbeam joint ventures, the financial results for Sunbeam have been removed from comparisons of performance with the prior year.

It is important that you have an appreciation for the decision to write down the value of GUD's investment in the Dexion business by a total $75.7 million pre-tax. This impairment was taken following a review of Dexion's trading performance, particularly in the second half, and its then near term outlook. Some of this was recognised at the time of our first half results announcement but as conditions for Dexion didn't materially improve in the second half further impairments were necessary.

Included in this non-cash write down was just over $59 million of goodwill, $10 million in brand name values, $4 million in inventory and $2 million in capitalised product development costs. I will comment shortly on Dexion's trading performance in the year and the factors behind these write-downs.

In addition to the Dexion impairment two other one-off items affected financial performance after the operating line. The first of these was related to the payment of the maximum earn-out for the previous shareholders of Brown &Watson, following its exceptional financial performance in the year. $10.6 million, representing half of the earn out, was taken as a one-off expense

The last item included in the one-off costs for the year was an impairment of Davey's inventory, valued at $1 million, which was included with the first half's results.

However, underlying earnings before interest and tax for the continuing businesses improved by 52% to just under $79 million, with growth in Automotive and Davey offsetting declines in Oates, Dexion and Lock Focus.

By business the major points to note around FY16's trading performance were as follows.

Profit growth in the established Ryco and Wesfil automotive businesses was impressive and was generated by strong sales growth. This came from a combination of introducing new product categories, range extension in existing categories, growth in the user base and the activation of a number of innovative marketing programs to support the new product activities.

Additionally, financial performance in the Automotive segment of GUD was boosted by the inclusion of Brown & Watson's trading for the full year. Sales and profit from Brown & Watson exceeded all expectations and resulted in the maximum earn out being paid, as already noted.

Davey's 27% improvement in earnings before interest and tax came from a combination of sales growth and internal efficiency improvements. These improvements included substantial savings being generated on domestic freight and further contributions from Davey's leading sales force effectiveness program, centred on improving share of wallet with established customers and on reducing the cost to serve across the customer base.

Disappointingly, Dexion reported a loss of nearly $4 million following a $5 million profit in the prior year. This result came from a combination of lower sales especially in the Australian warehouse racking market. This lower demand led to reduced throughout at the Dexion's Malaysian factory, causing the factory to operate at below break-even volumes. Whilst it was expected that factory volumes would improve in the second half this didn't occur, as demand remained relatively soft and Dexion implemented an inventory reduction program to release cash, further affecting factory performance.

Despite this sub-par operating performance, the one positive to come from Dexion was its improvement in cash generation, coming from a combination of the inventory reduction and from increased collections from customers, especially in the second half.

While reporting a growth in revenue, profitability at Oates declined 11% on the prior year. The main reason for this decline was the difficulty in obtaining price increases in the retail channel, including supermarket and hardware customers, to offset the higher cost of product stemming from the devaluation of the Australian dollar. Both the grocery and hardware sectors remain extremely competitive and under significant pressure, as the demise of Masters reflects. These pressures fall back on suppliers in many instances, as the primary focus of retailers is on price to gain and retain retail customers.

To wrap up my commentary on the year I want to focus on cash generation. A significant improvement in cash generation was recorded in the year following a structured program, that was directed at working capital reduction, being deployed across all businesses. Operating cash generated improved to $70 million from $30 million previously with higher receipts from customers and lower inventories being the primary drivers of this improvement. Much of the gain occurred in the second half and the focus on cash generation remains strong into the current financial year.

All of these factors allowed us to increase the total dividend paid for the year to 43 cents per share from 42 cents previously.

In addition, the actions we have taken to reposition GUD, through both portfolio changes, which I will address shortly, and business improvement, have been well accepted by the market, as reflected by the share price moving from below $10 at the time of the annual results announcement to around $11 per share recently.

Prior to inviting Jonathan Ling to provide you with a review of operations I wanted to talk about GUD's portfolio.

As you are aware we have made significant changes to the portfolio in recent times with the acquisition of Brown & Watson on 1st July 2015 followed by the sale of our remaining interests in the Sunbeam joint ventures, a year later.

The rationale for quitting the small appliance business has been well documented and I can advise that the Sunbeam sale transaction is now fully settled following completion of all acquisition adjustment accounts in September.

The wash up of the Sunbeam sale is that we will have a gain on the book value of the assets of around $2.5 million, which will be recognised in the current year's results.

Sunbeam is now with its natural owner – Jarden Consumer Solutions - the owner of the Sunbeam brand internationally. This ownership gives Sunbeam access to world scale product development capabilities and internationally competitive product sourcing arrangements, something it couldn't achieve in GUD's ownership.

It is interesting to reflect on Sunbeam's history in GUD. We acquired the business in 1996 when GUD bought Sunbeam Victa Corporation and, following a much needed reinvigoration of the product range, Sunbeam was the market leader in Australia with around 24% market share.

At that time, early in the 21st Century, Sunbeam was the major contributor to GUD's profitability. But the external environment changed rapidly following the global financial crisis with many competitors entering the Australian appliance market, seeking growth as their local markets were stagnating. Simultaneously, the retail trade underwent significant upheaval with traditional operators such as Retravision disappearing under the competitive onslaught from mass merchants, in particular.

Consequently, Sunbeam lost market share and its earnings profile became unstable. The brand remains a major force in the industry and, from the last information we had access to, was still the single largest brand in the Australian market, but with a much lower market share.

These are important lessons for our remaining businesses and are topics we discuss at our annual strategy day. The Sunbeam story illustrates how rapidly competitive conditions and the external environment can change in these days of globalisation and digitisation. The speed of these changes can, as seen with Sunbeam, have a dramatic impact on a business's ability to generate financial returns that are consistent with shareholders' expectations.

The other significant change to GUD's portfolio in the 2015-16 year was the acquisition of Brown & Watson. I spoke at length in this forum last year on the reasoning behind our interest in this business. It is pleasing to be able to state that the contribution from Brown & Watson in its first year of GUD ownership significantly exceeded our initial expectations.

The new product momentum in the business continued following the acquisition, and led to strong sales growth on the prior year. Sales were further boosted by new product introductions associated with Narva catalogue publication in February 2016, a pattern that is typical in this segment of the industry.

Brown & Watson's integration into GUD's purchasing arrangements commenced, resulting in an EBIT boost from better buying of ocean freight, local freight and insurance. In addition the bringing of Brown & Watson into GUD management systems and philosophies commenced with activities around profitability analysis, high performance culture and innovation.

Opportunities to leverage customer-focused marketing and sales activities with the Ryco business, in particular, were also identified and actioned, to the benefit of both businesses.

The early indications are that this acquisition will be value creating for GUD. Brown & Watson was a well-managed business, with a strong track record of performance coming from having market leading brands with a strong record of innovation. The results to date confirm our view that the automotive aftermarket is an attractive industry in which to have a presence. Consequently, we are seeking other significant opportunities in that sector.

Finally, I wanted to mention Dexion. We flagged at the annual results announcement that we are reviewing all strategic options for this business, including divestment. Whilst I have nothing to report on that front I can reassure you that we are extremely active in progressing the financial turnaround of this business. This won't come overnight but the management team has a well-documented action plan of improvement initiatives that is reviewed on a weekly basis and that is being worked through methodically.

That concludes my commentary on the results and the portfolio matters. Prior to speaking about the current year's outlook, I invite GUD's Managing Director, Jonathan Ling, to provide you with some more perspectives on his and the business units' current challenges.

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Thank you, Jonathan, for providing that operational overview, including further details on our group-wide innovation initiative.

Prior to turning to the business of the meeting I wanted to talk about the outlook for the current financial year.

Traditionally GUD has been quite reliant on performance in the first half to underpin the full year's result, but with the sale of Sunbeam and the expansion of our activities in the automotive aftermarket this is no longer the case.

Davey exhibits some spring seasonality while Brown & Watson has a slight seasonal inclination to winter, due to its comprehensive range of lighting products. In the context of the GUD group overall the effect of these influences is relatively minor.

Following completion of the first quarter's trading, just over three weeks ago, I am pleased to convey that the automotive businesses in the portfolio are continuing to exhibit the sales and profit growth momentum that was evident in the previous financial year.

Davey's performance over the same period has been constrained by the extremely wet and cool weather conditions that existed across Australia over late winter and into spring. Indeed, many parts of the country experienced the wettest September on record and, in this context, it is not surprising that demand for farm pumps and swimming pool products has not been as high as expected. However, we remain confident, given the programs Davey has in place, that this business will recover over the balance of the year.

Our Oates cleaning products business remains under margin pressure due to its difficulty in securing price increases in the retail segment of its business, as we have flagged previously, while Dexion is on target to deliver a close to break-even result in the current year.

In considering all these varying performances and the factors that we think will shape financial performance in this year we expect to be able to report a full year level of earnings before interest and tax of around $85 million.

Thank you for your continued interest in, and support of, GUD. We will now turn to conducting the business of the meeting.