

# Fisher & Paykel Appliances Holdings Limited

---

FPA Stock Exchange Release ASX/NZX 18 August 2008

## Chairman's Address to Shareholders

For the year ended 31 March 2008, the Company recorded a Normalised Group profit after taxation of \$65.5 million, up 4.3% over the previous year. An increase in profit was in sharp contrast to competitors' performances in the global appliance industry.

After one-off costs, Group profit after taxation was \$54.2 million.

The one-off costs were associated with relocating New Zealand based manufacturing operations to Thailand and Mexico and the proposed sale of the Finance business. To date these have totalled \$15.9 million after tax, but were partially offset by the profit on sale of land and buildings of \$4.6 million.

Appliances' revenue during the year was constrained by the appreciation of the New Zealand dollar. Currency translation effects reduced sales revenues by \$74.9 million compared with the previous year and concealed sales growth of 4.5% in local currency terms. Record Appliance sales revenues were recorded in Australia and Europe.

The Finance business contributed a normalised operating profit of \$26.9 million before interest and taxation. Given the market conditions in which it operated, this was a robust performance.

The Company maintained its dividend of 18 cents per share.

For Appliances the New Zealand market remained static during the year; however increased revenue resulted from a move towards higher value and featured products being sold. The Company retained its 50%-55% market share. The Australian market remained buoyant throughout the year with sales finishing up 11.3% on the previous year in local currency terms. Strong sales of AquaSmart washers and the Ice and Water refrigeration offering, ensured the brand out-performed the market, gaining market share as a result and lifting sales to record levels.

Our brands continue to make share gains in North America. In the face of a further declining market, the combined brands of Fisher & Paykel and DCS increased revenue by 5.5%. This was achieved against a backdrop of a market downturn of between 10%-15%. An increased marketing spend, raised the brands profiles, and along with expanded product offerings, contributed to the continued growth.

European and Rest of World market sales grew at a satisfactory rate. Softening market conditions in Europe along with a strong Euro relative to the British Pound were compensated by increased revenues. Our Asian markets, particularly Singapore and Hong Kong, showed consistent growth.

Operating conditions remained difficult throughout the year. High raw material prices along with a strong New Zealand currency, supported by high interest rates, hindered growth and as a result margins were constrained. Our internal cost down programme,

however, continues to perform well with excellent results. This negated some of the increased costs incurred by the business during the year.

The move of our Laundry operation from Auckland to Thailand has been successfully completed. The decision taken by the Board last year to relocate was a difficult, but necessary one. Our major competitors are already supplying Laundry products to the Australasian market from low cost countries like China, Thailand and India. As a result Laundry margins have been under increasing pressure for a number of years.

I am pleased to advise that the relocation has been completed on time and within budget. The first dryer was produced in Thailand in March this year, with washers coming on stream in May. We are on target to realise the cost savings indicated at the time of the announcement of the shift.

In October last year we entered into a strategic partnership with Arcelik from Turkey. Although it is still early days, we are excited by the prospects this agreement brings. John Bongard, our CEO, will update you on progress to date in his address.

Last year saw the Company produce our one millionth DishDrawer. This comes 10 years after its first release in 1997. From its inception in Dunedin, this product has been the catalyst for launching the Fisher & Paykel brand name in many of our international markets including the USA and the UK. We donated the 1 millionth product manufactured in June to the local Otago Community Hospice.

The Company is committed to sustainable and environmentally responsible processes, right across its operations. Production procedures are constantly reviewed to ensure the cleanest and most efficient of processes.

Furthermore, Fisher & Paykel has operated a full recycling plant in New Zealand since 1993, where it breaks down and recycles products from all over the North Island. This has recently been extended into the South Island through the use of contractors. The Auckland recycling centre employs 6 people and processes around 25,000 old appliances a year, including competitor brands. Packing from home deliveries is returned to the factory for re-use.

This environmental commitment is carried through to our products where energy and water consumption are key components in the functional design of the product.

You will be aware that in March this year, the Company withdrew the Finance business from sale after an assessment of interest from bidders.

Finance remains a well funded, robust business. It has diverse funding sources notably retail debentures, commercial paper and wholesale bank facilities. Although reinvestment rates for retail debentures had reduced in the months leading up to March 31st, strong support from banks together with sound governance have ensured that the Finance business has maintained a steady and solid funding position through this period of uncertainty.

Finance receivables increased by 9% during the year driven by strong growth in Q Card and Farmers Finance Card. The number of retailers accepting Q Card increased during

the year, to 4000, contributing to the overall earnings of the Finance business. Active cardholders also increased to over 143,000.

The Finance business has its own separate Board of Directors to monitor and review performance and compliance. This structure provides additional Corporate Governance over the affairs of the business and ensures Trust Deed ratios and prudential policies are appropriately maintained and adhered with. The identified risks are regularly reviewed by management and the Audit and Risk Management Committee of the Board.

The Finance business continues to maintain its Standard & Poors A1 credit rating for its Commercial Paper programme and the A M Best A- Excellent rating for its Insurance businesses.

As the Company expands globally, it is important we remunerate our executive management competitively. This is the responsibility of the Remuneration Committee. The Committee takes advice from outside agencies for all countries in which we operate.

The Company's increasing global footprint has made us acutely aware for the need to maintain the high standards of governance and risk and compliance management that have been set. This is primarily the responsibility of the Audit and Risk Management Committee which is ably chaired by our Deputy Chairman, John Gilks. The Committee met on 5 occasions during the year to monitor and review progress against the approved internal audit and compliance plan.

I will now invite John Bongard to update you on progress that the Company has made since balance date.

### **Chief Executive Officer's Address to Shareholders**

As the Chairman has mentioned, the headwinds the Company has faced over the past 3 years have continued. High interest rates and a strong New Zealand currency have tempered growth. Raw material prices, particularly stainless steel, pre-painted steel and copper, remain at high levels. The cost of seafreight and inland transportation, fuelled by increasing global oil prices, has also increased the cost of doing business

We do, nevertheless, continue to make good progress in partially countering these increases. Our cost down programme continues to be a priority focus within the Company and has achieved excellent results. Everyone has contributed and the results of their efforts are evident in last year's performance, where we have managed to negate a percentage of these price rises.

We believe that any abatement of these cost increases will not occur in the short term. A price increase for our appliances will be implemented in all of our markets over the next 2 months. This is expected to partially offset raw material increases the Company has had to absorb.

I would now like to update you on the two sectors of the business in detail since balance date.

Firstly Finance.

The Finance business has not been immune from the slow down in the New Zealand economy. Interest costs for all funding sources have increased as the effects of the global credit crunch have intensified and confidence in the New Zealand financial sector has been undermined. As a consequence of this we have increased the interest rates for our products. Debenture reinvestment rates have stabilised and are currently at 60-65%.

As households have come under increasing financial pressure, bad debts have risen in selected categories, particularly Q Card. However Farmers Finance card delinquencies have been stable.

We have recently launched the “your rewards” loyalty programme to participating Farmers Finance cardholders. This scheme is targeted at high spend consumers and provides an additional incentive to use Farmers Finance card. Initial acceptance of “your rewards” has been encouraging.

The Finance business has a broad based consumer loan portfolio. It has no related party, motor vehicle or property loan exposures. The business has significant cash flow with payments from customers exceeding \$600 million per annum. This strong level of cash flow together with the ongoing support from investors and banks underpins the business.

And now Appliances

The Appliances business has a very busy and exciting year planned. As the Chairman mentioned, we have completed the first part of our new Global Manufacturing Strategy. I am exceptionally pleased with the way the relocation of the Laundry operation to Rayong, Thailand has been completed. The transition from manufacturing in Auckland to Thailand has gone smoothly, with little disruption to supply. I have been impressed with the speed and accuracy in which the project has been completed. As you can see from these photos, from a bare piece of land in August 2007, the factory building was constructed so as we were able to start installing equipment in February 2008 and commence production of dryers in March.

I am also pleased with the quality and the cost of the products we are producing from that site.

The knowledge that we have gained from this relocation gives me confidence that the further moves announced earlier in the year will transition just as efficiently.

The Electronics component factory in East Tamaki is currently in the process of transfer to Thailand. Various individual production lines have already been shipped and are up and running, with the remaining ones vacating the Auckland site by October.

Our DCS cooking plant in Huntington Beach, California is also in the process of relocation. We have already moved and started producing outdoor grills and cooktops in our newly purchased Mexican premises. The remaining DCS production lines will be shifted progressively between now and October this year.

The Mexican plant has proven so far to be an excellent acquisition. Not only have we purchased a 3 year old facility, comprising 2 buildings on 60 acres of land, but also a side-by-side refrigeration factory. This month saw us produce and sell our first side-by-side product in the United States. This is a product category that we have not previously distributed in the North American market and represents 35% of all refrigerators sold in the USA.

The Dishdrawer plant in Dunedin and the Cleveland refrigeration plant in Brisbane, are due for relocation starting March next year. The disassembly, shipping and recommissioning period for these two plants will be approximately 4 months. The DishDrawer line and Cleveland refrigeration plant will be housed in a purpose-built facility adjacent to our existing site in Thailand. Construction of this building is expected to commence later this year. Once fully complete, the Rayong facility will be Fisher & Paykel's single largest manufacturing site.

In addition to this, a new purpose built DishDrawer line is under construction for delivery to our Mexican plant later this year. This line will produce a new range of DishDrawers designed specifically for the North American market. Production is on time to commence in December.

The remaining cooking production in Dunedin, will be transferred to Italy and Mexico. Production will cease in December this year and the lines shifted thereafter.

This Global Manufacturing Strategy is a key component in Appliances prospects moving forward. It is imperative, in these times of globalisation, high cost of production and slowing markets, that we as a Company advance to ensure our competitiveness in the global market. Our advantage of being a small, transportable manufacturer has enabled us to move our plants with relative ease to lower cost countries, close to our major markets.

The savings that will be realised by these moves are significant. As globalisation advancement occurs, we must be prepared to fine-tune our business further if necessary to cope with the changing landscape.

Innovation remains our competitive advantage. Our new product platform releases over the years have seen the Fisher & Paykel brand recognised as a world leader in appliance innovation. In recent times we have actively sought to shorten the time it has taken from product conception through to development and marketing of the product. This has seen a number of ground breaking products released to the markets in a short period of time.

This year is no exception. Following on from the AquaSmart washer range, which has dominated the Australian top loading laundry market, and our Ice and Water refrigeration models, including the French Door development, we are in the process of releasing the Izone range of products to our major markets.

Izone is an elite range of products that are positioned at the ultra high end of the market. These products will be released to all markets in the coming months and be the catalyst to further enhance the Fisher & Paykel brand globally.

The initial offering in the Izone range is limited to 3 new products.

The CookSurface, formally known as the Luna Cooktop, has been released in New Zealand and Australia. This revolutionary product has been eagerly awaited since its early showing in the Kitchen & Bathroom Show in Chicago. It has been complemented by the VentSurface, an innovative auto-sensing rangehood.

Completing the Izone range is CoolDrawer. This is a world first refrigerator/freezer, but in a drawer concept. Its unique feature allows the user to select one of 5 different operating functions, depending on their individual needs. It can be converted from a freezer or refrigerator mode, to a wine chiller or pantry mode, at the touch of a button.

Initial reaction to these products from designers and specifiers has been tremendous. By releasing these concepts to designers and architects first, they are then able to specify them into future new high-end kitchens and homes.

These products will be on display after the meeting and we will have our people on hand to answer any questions you may have about them.

The markets around the world generally remain in downturn.

The New Zealand market in April to July this year has fallen between 7% and 10%, when compared to the previous period. This is a direct result of the tightening economy. Market shares have been retained and sales levels are slightly better than the market environment.

The release of the Elba brand in New Zealand has been well accepted. The advertising campaign, first aired in March this year, has proved successful with consumer awareness of the brand at very high levels. This approach provides an entry level brand that offers our retail base greater variety of products and models in which to market. Elba now represents approximately 50% of our domestic New Zealand sales.

Fisher & Paykel has again been voted the 3<sup>rd</sup> most trusted brand in New Zealand. This is a noteworthy achievement and important for the year ahead. As markets contract, it is the well trusted and known brands that consumers favour.

The Australian market remains uncertain. Interest rate rises along with an increasing cost of living have tempered consumer confidence. This has been reflected more recently in a slowing market. I am pleased to report, however, that the Fisher & Paykel brand, in the first 4 months of the fiscal year, is up 5% in local currency terms over the previous corresponding period.

The recent launch of the Izone range of products in Australia has reinforced Fisher & Paykel as an industry leader and raised the profile of the Company and the brand. This is especially so amongst architects and specifiers.

There has been no general improvement in the USA market. Industry statistics indicate a total market decline of between 10-15% year-on-year. Fisher & Paykel total revenue, including OEM and components, is down 4% in local currency terms. The Fisher & Paykel and DCS brands on the other hand continue to outperform the market, being down just 1.4% on the previous year.

The continuing high costs of raw materials have forced our mainstream competitors to increase selling prices in this market. We plan to follow suit and increase prices within the next month.

Our ongoing business with the independent retailers in the US remains strong. We continue to offer a point of difference from the major manufacturers by way of product offerings, terms of trade and profitability opportunities.

The planned product releases for the current year, including side by side refrigerators, the Izone range of products and the new DishDrawer configuration, should continue to see the brand out-perform the market.

Our European sales remain steady against a backdrop of uncertainty in most markets. We do have in place strategies to increase revenue for the second half of the year.

We have recently started an OEM selling arrangement with Arcelik of Turkey. This opportunity, arising from the strategic partnership signed last year, has seen our first shipment of Arcelik branded DishDrawers bound for the Turkish domestic market. Arcelik enjoys a 50% market share in its home country and will sell the DishDrawers through its franchised retailers. Dishwashers are one of the fastest growing categories in appliances in Turkey, a country with a population of 69 million people.

Arcelik's intention is to expand our product range offering in Turkey and take the Fisher & Paykel brand into a further 5 Eastern European block countries this calendar year.

The European sales office has recently increased its distribution in the United Kingdom. Retailer Marks and Spencer commenced distribution of our products from August 14<sup>th</sup> this year. Marks & Spencer is one of the world's most prestigious high end large retail chains.

Our Rest of World appliances sales year to date are up on the previous year. Asian markets including Singapore continue to perform strongly. The strength of the NZ dollar has delayed growth in some markets.

We have taken the opportunity to relocate the Rest of World sales office to Rayong, Thailand. From this new base we will be able to better serve our Asian markets.

I am pleased to announce that the Matsushita Corporation of Japan has approved Fisher & Paykel as a supplier of chest freezers from our Auckland refrigeration plant. These products will be branded Panasonic and distributed in the Japanese market. The contract, which is in the final stages of being signed, will commence in the second half of the fiscal year. We have a long-standing relationship with Matsushita dating back to our first transaction in 1964.

Following a review of the Groups funding, it has been decided to examine an issue of Capital Notes into the New Zealand market. Depending on market demand, an offer could be made later this year and the funding would provide greater diversity to the Groups funding profile.

I would now like to comment on the outlook for the Company.

The Finance business remains a well funded, robust operation with a widespread portfolio of consumer loans. There is however emerging evidence of a slight slowing of consumer financing. Funding costs look set to increase in the second half of the year as older borrowing facilities mature and are replaced.

Bad debt provisioning has been increased to reflect market conditions. Overall the business going forward remains stable. As in Appliances, work continues to take cost out of the business and we maintain an acceptable cost to income ratio.

Appliances first half result will be significantly down at both an operational and reported level compared to the previous corresponding period. Operational earnings have been impacted by increased costs for raw materials which have eroded margins. Markets are slowing. We are progressively reducing finished inventory levels which has resulted in lower production through our factories and impacted our economies of scale in the short term. Interest costs are also up due to the increased funding requirements during the transitional period of the factory relocations.

As expected, earnings at a reported level will be lower in the first half due to the costs and the provisioning associated with the factory relocations. Planned duplicated overhead costs have been incurred during the transition phase, for the relocation of manufacturing facilities off shore. This duplication of resources is however, imperative to the success of the relocations in order to complete the transfer of knowledge and maintain continuity of supply during start-up. They are in place to mitigate as much of the execution risk of relocation as possible. Included are engineering and maintenance staff as well as a replication of procurement and accounting personnel. These short-term costs will be heavily weighted to the first half and then reduce as the transition phase for Laundry is fully completed.

There remains uncertainty in the future of raw material pricing, interest and exchange rates, as well as the direction of market environments. Competitor pricing pressures continue in all markets, impacting margins. It is too early to gauge the impact our price increases will have on revenue and sales levels.

Based on the foregoing we expect the normalised first half after tax result to be approximately 50% down on the previous corresponding period and after deducting the significant abnormal costs associated with the relocations, a post tax reported loss of approximately \$7-\$10 million.

However due to the expected improvement in the second half, after tax earnings for the full year, both at a normalised and reported level, are forecasted to be at the low end of analysts' current projections.

The process of relocating some of our manufacturing plants continues to be on track. I am confident that the results we have experienced from the first phase of the global manufacturing strategy will ensure the forecasted savings will be fully realised. The lower manufacturing costs are now starting to flow through from the Thailand factory. These actual and forecasted savings are exceeding initial expectations.

The second half of the year will see the full gains from the Thailand plant and preliminary gains from the Mexican plant being realised. The relocation of some cooking products to our Italian factory from December onwards will see that factory's production efficiencies

also improve. Once completed, these measures will have significant positive impact on future bottom line results.

Our new product development pipeline is significant. Engineering and design teams continue to work closely with customers in order to deliver products that bring real features and benefits to the end user. We continue to push the boundaries in both design and functionality.

Before handing back to the Chairman, I would like to thank our suppliers and our customers for the ongoing support they give to us. As the Company expands offshore, we widen the reach we have with both of these parties.

The make up of our staff is an ever evolving one, and as we develop in offshore markets so too does our Company culture. We have a proud heritage and I know we will take this with us as the business develops globally.

I am pleased to say that after again working closely with the Unions in these difficult times, we have settled the annual wage agreement in both Australia and New Zealand. I would like to thank the salaried staff of the Company in agreeing to a deferred salary review for 3 months, and the Senior Executives of the Company who have agreed to a postponement of their annual reviews.

I would also like to thank you our Shareholders for your valued support. As always we strive to deliver value to you by way of dividends and capital growth.

To my fellow Directors, thank you for your wise counsel, guidance and understanding. Your continued support has given the Company the confidence to take on the challenging goals we have set ourselves.

**This address will also be made available on the Company's website [www.fisherpaykel.com](http://www.fisherpaykel.com)**