

## Chief Executive Officer's Report

*Record earnings before interest and tax (EBIT) and net profit after tax (NPAT) assisted by earnings growth in cement, concrete and aggregates, and concrete products.*



**MARTIN BRYDON**  
CHIEF EXECUTIVE OFFICER

A handwritten signature in blue ink, appearing to read 'M. Brydon', with a stylized flourish at the end.

### Performance

It is a pleasure to be able to tell you in my first Annual Report as Chief Executive Officer that Adelaide Brighton has delivered record earnings for shareholders and made important strategic achievements that enhance our ability to grow earnings into the future.

Demand conditions across our businesses were generally favourable in 2014 and these combined with a significant contribution from operational improvement to grow earnings. We saw a recovery in residential demand for our products, particularly in New South Wales and Queensland, and ongoing strength in resource sector demand in Western Australia and the Northern Territory.

Revenue increased 8.9% to a record \$1,337.8 million and NPAT increased 14.3% to \$172.7 million, also a record result. Underlying NPAT of \$166.5 million was 8.5% higher than the underlying figure in 2013.

Reported earnings before interest and tax increased 11.1% to a record \$247.5 million on an EBIT margin of 18.5%. Earnings before tax were aided by net significant items of \$2.3 million. Excluding these items underlying EBIT increased 8.5% to \$245.2 million. Our underlying EBIT margin was stable overall at 18.3% on the expanded revenue base. Return on funds employed increased slightly to 17.5%.

One-off items and the acceleration of income tax payments caused operating cash flow to decline to \$194.0 million in 2014. However, despite these items, cash flow was ahead of expectations in the second half.

Due to strong second half cash flow our net debt increased by less than was expected at the time of the major acquisitions announced in August 2014. Net debt to equity gearing of 31.7% ended the year well within the target range of 25% to 45%.

Cement and clinker sales volume increased 3% supported by continued demand from projects in the resources sector in Western Australia and the Northern Territory, and a residential recovery in New South Wales and Queensland. Activity in the non-residential building sector remained subdued. Cement volume declined slightly in South Australia and Victoria.

Higher volume, lower costs and improved prices led to increased earnings in cement and clinker, concrete and aggregates, and concrete products. The recovery in earnings in concrete products is particularly encouraging given the significant effort that has been put into improving this business in the last few years.

The recent concrete and aggregates acquisitions in South Australia and Queensland contributed to revenue in line with expectations. Excluding these acquisitions, concrete and aggregates volumes were up, led by the stronger residential market.

Lime sales volume declined approximately 7% affected by the downturn in the gold sector and a production suspension by a major customer in the first half, impacting revenue and EBIT, although the business improved in the second half of the year.

HY-TEC MELBOURNE SUPPLIED  
APPROXIMATELY 25,000M<sup>3</sup>  
OF SPECIAL CONCRETE MIX  
FOR 'PRIMA TOWER' - A 72  
LEVEL APARTMENT TOWER IN  
SOUTHBANK, MELBOURNE



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## Corporate restructure

# \$4.0m

2015: \$2.0m further benefits

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Operational improvement remained a key focus of management in 2014 with corporate restructuring, rationalisation of operations, energy efficiency and other initiatives adding \$19.7 million to EBIT.

The contribution from our joint ventures was lower overall with improvement in the Queensland operations offset by a lower contribution from the Victorian business.

### Strategy

Adelaide Brighton continues its successful long term strategy of growing shareholder value through three key areas:

- > Cost reduction and continuous improvement across the Company;
- > Growth in the lime business to supply the resources sector in Western Australia, South Australia and Northern Territory; and
- > Focused and relevant vertical integration into downstream concrete, aggregates and concrete products businesses.

During 2014, the Group delivered on a significant number of initiatives in line with its long term strategy.

### Operational improvement

During the first half, a group wide review of operational, human resources, information technology and administration functions was undertaken. This resulted in restructuring costs of \$5.4 million for the year. Pre-tax benefits from the corporate restructure were \$4.0 million in 2014 and are anticipated to be \$2.0 million in 2015.

In line with the strategy to grow shareholder returns through improving efficiency and leveraging an industry leading import capability, Adelaide Brighton largely ceased the production of clinker at Munster, Western Australia, in December 2014.

The capacity rationalisation delivered EBIT improvements of \$5.0 million in 2014 and a further \$5.0 million is expected in 2015.

Adelaide Brighton has an ongoing focus on the management of its power and fuel costs. Benefits of \$4.9 million were delivered in 2014 through the increased use of alternative fuels, electricity demand management, fuel switching and plant efficiency.

Further benefits of \$5.8 million were delivered through a variety of other measures, including transport efficiencies, raw materials sourcing and a range of procurement initiatives.

### Import strategy underpins competitive supply into key markets

Following the rationalisation of clinker manufacture at Munster, Adelaide Brighton's imports of cementitious products, including clinker, cement and blast furnace slag, increased to more than two million tonnes in 2014, which represents approximately 20% of Australian industry demand.

Since the mid 1990s, the growth of import capacity to replace ageing, less efficient domestic manufacturing has been a key element of Adelaide Brighton's strategy to secure its long term position in the Australian market and grow value for shareholders.

The use of imported materials allows Adelaide Brighton to supply customers with competitively priced product into a range of markets where demand exceeds the Company's manufacturing capacity.

### Efficient lime operations with strong competitive position

Following the completion of major upgrades to both Munster (Western Australia) lime kilns in 2013, improvements in production capacity, efficiency and environmental performance of the kilns have been realised.

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## Energy efficiency programs

# \$4.9m

2015: continued focus

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Efficiency gains partially offset the impact of lower volumes and increased energy costs during 2014. Despite a decline in lime volumes in 2014 following the 2013 closure of some gold mines, the long term prospects for lime demand remain strong.

While the threat of imports remained, the falling Australian dollar increases the cost of imported product.

### Concrete and Aggregates acquisitions in South Australia and Queensland

Adelaide Brighton continues to make progress on its downstream strategic plan. The Group now produces more than 1.5 million cubic metres per annum of premix concrete and more than 6 million tonnes per annum of aggregates. The footprint of this business now reaches from South Australia through Victoria and New South Wales, to south east and northern Queensland.

In 2014, Adelaide Brighton acquired BM Webb Construction Materials in Queensland, and Penrice Quarry & Minerals and Direct Mix/Southern Quarries in South Australia at an overall enterprise value of \$172 million. These acquisitions are consistent with the strategy of focused and relevant vertical integration.

The assets acquired include strategic quarrying operations producing approximately 2 million tonnes per annum of aggregates. The acquired businesses also produce more than 250,000 cubic metres of concrete annually, securing a significant volume of the Company's cement sales in the South Australian market.

Integration of the acquisitions, including the information systems, has been completed on an accelerated time frame delivering synergy benefits in logistics operations, procurement and back office functions. The estimated \$4.4 million synergies per annum are expected to be realised in 2015.

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## Munster rationalisation EBIT benefit

# \$5.0m

2015: \$5.0m additional

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Earnings from the acquisitions were in line with expectations for the period to 31 December 2014.

### Strategic attractions of Sydney aggregates

Adelaide Brighton has a significant investment in aggregates in the Sydney market through its Austen Quarry at Hartley, New South Wales. Aggregates earnings increased in 2014 in New South Wales supported by a recovery in the Sydney construction materials market. The Sydney market is transitioning to aggregate sources supplied from outside the metropolitan area, following the exhaustion of reserves at existing competitor quarries. Due to this structural change it is expected that Sydney aggregate prices will increase above the CPI rate in the short to medium term.

### Land sales releasing capital

Adelaide Brighton has a land portfolio that is expected to release a total of \$130 million in cash in the medium to long term. The Group is actively engaged in preparing these properties for sale to maximise value. The program has delivered approximately \$16 million in revenue since the beginning of 2013, including a sale that contributed \$9 million in cash and \$1 million profit before tax in 2014.

### Outlook

The outlook for Adelaide Brighton remains positive.

Sales volume of cement and clinker in 2015 is expected to be similar to or greater than 2014. Demonstrating the benefits of a vertically integrated business, reduced cement sales from January 2015 to a major customer in South Australia are expected to be offset by:

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## Other initiatives

# \$5.8m

2015: ongoing focus

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- > Sales of other cementitious products to that customer;
- > Increased sales in Western Australia; and
- > Improved demand in Victoria, New South Wales and Queensland.

Lime sales volume in 2015 is anticipated to be similar to, or slightly higher than 2014 and average realised prices are likely to increase. The threat of small scale lime imports in Western Australia and the Northern Territory remains, however the weaker Australian dollar is likely to reduce the competitiveness of imports relative to Adelaide Brighton's low cost operations.

Price increases have already been announced for March and April 2015 in cement, clinker, concrete, aggregates, and concrete products.

Price increases achieved in 2015 are expected to exceed those achieved last year. A number of factors are supportive of higher prices including strengthening demand and capacity utilisation and the weakening Australian dollar, which increases the cost of import substitutes.

Aggregate prices are anticipated to increase significantly above CPI, particularly in Sydney where average delivered costs have increased significantly as the industry moves to supply from further afield as traditional sources have depleted.

First half 2015 imports have been fully hedged, however, the deterioration in the Australian dollar will increase the direct cost of imported materials for Adelaide Brighton. Assuming the Australian dollar remains at around Yen90 and USD0.75, costs are expected to increase by approximately \$7 million in a full year, prior to their mitigation through price increases. Gas related fuel costs in South Australia are now expected to increase by \$2 million pre-tax in 2015.

There are a number of benefits which will flow through to 2015:

- > The unwinding of the carbon tax to benefit circa \$3 million compared to 2014;
- > Potential transport cost savings of \$4 million from lower fuel costs assuming current oil prices and exchange rate;
- > Further Munster rationalisation benefits of \$5 million; and
- > Full year benefits from the 2014 corporate rationalisation of \$2 million.

### Our people

This past year has been a challenging and rewarding one for our Company.

We have performed well and strengthened the foundations for future growth in earnings and rewards for shareholders.

I would like to thank the senior management team and all employees of Adelaide Brighton for their dedication and skill. Our success is built on years of hard work and incremental improvement.

I am particularly grateful for the support I have received from the Board since commencing as Chief Executive Officer in May 2014.

I am proud to be leading this 132 year old Company and its people and believe we have a positive future ahead of us.