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Penrice Soda Holdings Limited
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Penrice Soda Holdings Limited today released a market update that included unaudited financial estimates indicating reported net profit after tax (NPAT) for the year ended June 2009 would be $6.5 million to $7.4 million, with underlying NPAT up more than 28 percent from the previous year to over $8.5 million and underlying EBITDA up more than 21 percent to over $24 million. Given incremental EBITDA from your Way Forward Plan of $5 million, the plan appears to have accounted for all the earnings growth. Can you comment?

MD Guy Roberts
The Way Forward Plan was designed to create the mechanism by which we'd grow earnings in each part of our business. It's unsurprising then that it encapsulated all of the growth in the recent year.

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You expect to continue to deliver growth in the current year ending June 2010, with both your businesses expected to perform strongly. What assumptions regarding demand conditions, plant utilisation levels and cost trends underlie this expectation and can you provide more specific earnings guidance?

MD Guy Roberts
We're not going to give more specific earnings guidance other than to say we expect this year's profit to be ahead of last year's. But I can comment on some of the underlying trends.

In our Chemicals group, which incorporates our soda ash and sodium bicarbonate businesses, we foresee demand growth. Soda ash is a mature, commodity-style chemical and traditionally GDP growth has been a good proxy for its demand profile. While demand for soda ash has benefited in recent times from the growth in the mineral processing sector, that demand has slackened due to the impact of the global financial crisis, which has seen two soda ash customers go into receivership. While this hasn't been material to our earnings, we see demand growth returning to around GDP growth levels for at least the next two to three years until the mineral processing sector takes off again.

In our sodium bicarbonate business we see demand growth of 6 to 8 percent continuing. Our bicarb is premium quality and is used in high end applications such as food and pharmaceuticals, demand for which is being lifted by the westernisation of Asian consumers' food preferences which is underpinning a shift to bakery products from rice based products, and the aging and increasing affluence of the population which is driving an increase in demand for pharmaceuticals and medicines. We're also seeing growth in bicarb demand in specialist applications such as in haemodialysis and in the treatment of industrial waste gases.

In our Quarry & Mineral business, we supply a variety of civil and construction markets, and industrial applications. Our competitive advantage is governed by logistics and the location of our mine in Adelaide's outer northern metropolitan region puts us in a very good position to deliver to the growing number of government funded projects relating to road infrastructure and population growth in Adelaide's north. We're also seeing demand from major defence projects around the port of Adelaide.

Plant utilisation in our soda ash plant has been at 100 percent for over a decade, and the business has preferentially sourced imports to satisfy demand in excess of capacity. In sodium bicarbonate, we've had a succession of five expansions over the last decade, the most recent of which was commissioned in December 2008. We expect to sell out this recent expansion within the next 18 months. And in Quarry & Mineral, at current sales levels we're at close to maximum mine capacity without any restructuring of the operation.

Strategically, productivity is very important and we've got a number of productivity improvement initiatives underway in the Chemicals business, particularly around better plant integrity, preventative maintenance and better statistical process control techniques. Similarly in Quarry & Mineral we have a number of programs designed to manage and improve the productivity of the mining fleet.

In our Chemicals business, we've consistently seen an increase in our cost bar of around 3 percent per annum. That's a function of having most of our strategic raw materials under long-term contract. It's also a function of having access to low cost raw materials – notably salt and limestone – from our own captive sources. In the last year we saw unusually large increases in the price of two key raw materials, coke and ammonia, which are not under long term pricing arrangements.

Prices spiked last year but have since retreated and are expected to remain subdued this year and beyond.

In Quarry & Mineral, we've got a history over the last three years of reducing our unit cost per tonne, largely through the agency of the new mobile mine fleet we started leasing in 2006. With an increase in volumes, we expect a continued reduction in the unit cost per tonne at the Angaston mine.

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You've indicated that investment under the Way Forward Plan was completed in 2009, one year ahead of schedule, with $50 million invested under the plan in 2008 and 2009. Your market update suggests ROE rose to around 16.7 percent in 2009 from 13.7 percent in 2008. What scope is there to further improve returns without significant additional investment?

MD Guy Roberts
We believe there's scope to improve returns without significant additional investment. In Chemicals we expect to see a full year benefit from price increases we put through in the first half of last financial year. A large proportion of our business is under contract and there are some existing contracts where increases are yet to flow through.

We'll also see an uplift in earnings from the sodium bicarbonate expansion: we expect the plant to reach capacity by the start of 2011.

In the Quarry & Mineral business, we're not forecasting significantly increased volumes out of the mine, but we're expecting to be selling out inventory and reducing working capital. We'll also be running the Angaston mine operation on a much reduced overburden extraction rate which will significantly reduce the cash costs of the operation and over the medium term, improve the profitability of the mine as well.

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You've indicated capex will reduce to around $10 million in 2010 from $22 million in 2009. To what extent does this reflect the ongoing level of sustenance capex? What metrics will you consider in any decision on further material growth capex?

MD Guy Roberts
The $10 million level is a good indication of our ongoing sustenance capital. As a guide, we'd target capex equal to the rate of depreciation on the plant, with roughly $8 million allocated to Chemicals and roughly $2 million to the mine. In the Chemicals business, we have a very old soda ash plant that's in need of replacement capital. The sodium bicarbonate plant on the other hand, is very new and requires very little capital. In the Angaston mine, we'd seek to replace fixed equipment only, roughly in line with depreciation.

Beyond that, every growth opportunity would be subject to its own business case, and we stringently uphold a 15 percent return on net assets hurdle. We also look at related metrics such as internal rate of return and net present value. A minimum

15 percent return on net assets will drive the sort of returns our shareholders are after, and would put is in the top quartile of ASX listed companies over time, which is our aim.

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Penrice expects net debt of $88 million as at the end of June 2009, up from $71 million a year earlier. Net debt to net debt plus equity is expected to be 60 percent, unchanged. You expect to begin programmed debt repayments in the June 2011 year. What is the expected trend in debt in the current year and what is your long term gearing target for the business?

CFO Frank Lupoi
The level of debt has basically peaked, so we're projecting a flattening of our debt and in the 2011 financial year we'll commence programmed debt repayments from operating cash flows. The Board would anticipate that we'd get to the lower end of our 50 to 60 percent gearing target range in the medium term. Long term, our target range is under review.

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Penrice has announced the extension of its syndicated loan facility to March 2012. How do the terms of the refinance compare with the previous arrangements and what will be the impact on your debt servicing costs?

CFO Frank Lupoi
Our debt facility has been repriced upward, in line with trends industry has seen over the past 12 months. The majority of our interest rate hedging rolls off in July 2009 so we'll change to a more variable rate exposure, which we expect to result in lower rates than we paid in the June 2009 financial year. After also taking into account our increased average debt levels, we're still expecting an overall slight reduction in debt servicing costs in the current financial year compared with 2009.

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You've indicated that inventory stood at $57 million as at the end of June, up from $38 million a year earlier, but that inventory levels had peaked. What gives you confidence that this will be the case? Will you need to make further additions to the overburden held as inventory as a result of developing the Angaston mine?

MD Guy Roberts
The Chemicals group has had very well managed inventories over the long term. We hold one month's stock in the Chemicals business which is at least equal to best practice in businesses of this type around the world. However, there was a spike in inventory in the second half reflecting the reduction in soda ash demand from our mineral processing customers and a slight softening in demand from glass makers. We'll absorb that increased stock, and rebalance our inventories by reducing imports in the current year.

The majority of the increase in inventory reflected the increase in overburden resulting from the widening of the Angaston mine, which was necessary to get to the ore-body. Remember, the overburden we remove from the mine is classified as inventory because we're selling, and plan to continue selling, aggregates and schist into construction and landfill projects. A reduced overburden extraction rate going forward will return the mine to cash flow break-even this financial year.

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Overburden from the Angaston mine appears to account for $28 million to $29 million of Penrice's $57 million total inventory. How is the inventory valued? How long is it expected to take to sell the overburden inventory down to more appropriate levels and what will be the drivers of sales?

MD Guy Roberts
The overburden inventory is valued conservatively at cost. We have about two to three years' worth of aggregates in stock which we can sell into civil construction and other industrial markets. This makes up about 50 percent of our inventory at the mine. The remainder of the inventory is schist which is a lower grade material that can be used for less demanding applications such as landfill projects. We expect to sell off all of the schist inventory over the next 10 to 15 years, depending on future levels of government-sponsored and large private sector development activity.

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At its upcoming shareholder meeting, Penrice is seeking shareholder approval for an extension of a provision allowing it to issue up to 15 percent of issued share capital in a 12 month period. Why are you seeking this extension? Given the provision relates to placements, won't it advantage new shareholders at the expense of existing shareholders?

MD Guy Roberts
We acknowledge that our debt and gearing levels are high. Raising equity is the easiest way to reduce those levels, and we have that option under review. Issuing 15 percent of issued share capital is only a theoretical option, but we're taking the opportunity of the upcoming general meeting to raise this as an agenda item.

We do not seek to disadvantage any particular group of stakeholders and are very conscious of the interests of both institutional and retail shareholders. In any future capital raising, our preferred method would be to undertake a rights issue.

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Penrice suspended its interim dividend but you've indicated that directors wish to resume dividend payments in line with improved results. What is the expected time line and will you maintain your policy of paying out 60 percent of post-tax earnings?

MD Guy Roberts
Capital preservation and balance sheet strength have to be the Board's priorities at the moment. We've invested heavily in the future of the business and look forward to our shareholders enjoying the benefits of this investment as cash flows and earnings improve.

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What is your long term strategy for the business and how is Penrice currently positioned versus your strategy goals?

MD Guy Roberts
Our overall strategic goal is to invest in, nurture and leverage our existing businesses in such a way that they achieve an annual return of at least 15 percent on net assets. Our sodium bicarbonate and Quarry & Mineral businesses have already exceeded that rate of return on the investment we've made in them to date.

The next 12 to 18 months will be important for our soda ash business, which now enjoys improved plant integrity and hence more reliable output. Successful repricing as contracts roll over would take soda ash over the 15 percent return threshold, enabling us to invest further in small-scale expansions in the future.

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Thank you Guy and Frank.

For further information on Penrice Soda Holdings Limited visit www.penrice.com.au or call Frank Lupoi on (08) 8402 7000

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