

ASX Announcement: 17 February 2010

## CEO & CFO on H1 10 Result & Outlook

Open Briefing interview with CEO Doug Tough and CFO  
Rustom Jilla



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### In this Open Briefing<sup>®</sup>, Ansell CEO Doug Tough and CFO Rustom Jilla discuss

- Stronger than expected first half result
- Sustainability of revenue growth; outlook for costs
- Upgraded EPS guidance

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#### Record of interview:

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Ansell Limited today reported net profit of US\$54.3 million for the first half ended December 2009, flat compared with the previous corresponding period. EBIT was up 7 percent reflecting strong growth in Professional and a recovery in Occupational. How sustainable are these trends and given you expected earnings to be down from the relatively strong previous first half, where did actual conditions vary most markedly from your expectations?

##### CEO Doug Tough

Sales were much better than expected with strong growth in surgical, pockets of strength in Consumer and a broad based Occupational recovery. Other factors were margins that were solid in H1 (due to product mix, FX, and lower input costs) and the restructuring program (which had a lower net cost than expected). Admittedly, sales benefitted from a weaker USD, but sales volumes also exceeded expectations.

There is every reason, at this stage, to believe that the positive sales trends are sustainable. Margins in H2, however, will be impacted by the surge in natural rubber latex (NRL) prices, and increases in other commodities and energy. There will be a lag before selling price increases and manufacturing initiatives offset these increases. In addition, we will see H2 benefits from our restructuring program, the bulk of which has been completed.

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First-half EPS was US\$0.403, up 1 percent and you've upgraded your EPS guidance range for the full year ending June 2010 to US\$0.69 to US\$0.74 from the top end of the range of US\$0.56 to US\$0.62. This implies EPS of US\$0.29 to US\$0.34 in the second half, or period on period growth of 1 to 31 percent. What are the factors that could push the second half result to the top or bottom of the range?

### CEO Doug Tough

Let me deal with the risks first. If there was to be a double dip recession, our Occupational sales would suffer and this would flow through to the bottom line. You might expect us to include natural rubber latex prices here but we believe that our forecasts adequately cover this ... and any price increases after March will not really impact F'10's results. Upsides could come from a faster improvement in the global economy than expected, and continued tight management of our costs.

### CFO Rustom Jilla

Movements in FX rates also impacted our sales and this will happen again in H2. However, in H2, we do not expect much of an impact on EBIT, either positive or negative, as we have hedged almost three quarters of our local currencies into USD. These hedges are evenly balanced between revenue and cost currencies and unless the USD weakens or strengthens sharply against only one currency – FX should have little effect on our latest EPS guidance.

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The Occupational business booked EBIT of US\$32.8 million, down 6 percent half on half, on sales of US\$253.8 million, which were down 3 percent. This was a strong rebound from US\$18.8 million and US\$215.7 million respectively in the second half of 2009. Where has recovery been strongest and to what extent does it reflect real demand as opposed to restocking?

### CEO Doug Tough

Our Occupational business performance has been very gratifying. Being the world's premier synthetic Occupational glove provider has enabled Ansell to rebound quickly from the GFC and we believe that we have picked up market share during this period. We know some distributors have been restocking (though not to pre GFC levels) and we are also seeing end users consuming more as the global economy expands. The extent of our sales recovery as F'10 H1 progressed, is illustrated by the fact that the sequential previous half (F'09 H2) had a sales decline of 25 percent vs. the comparable period. Our running rate exiting H1 gives us confidence that Occupational sales growth will continue and perhaps accelerate.

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The Professional business booked EBIT of US\$26.0 million, up 59 percent from the previous corresponding period, on revenue of US\$175.1 million, up 4 percent. EBIT margin improved to 14.8 percent, up from 9.7 percent reflecting lower input costs and a more favourable product mix, including your exit from unprofitable exam glove business in the US and Europe. How much further can the exam glove segment be reduced without hurting the Ansell brand among healthcare providers? Can Professional margins be maintained at these levels?

### CEO Doug Tough

In relation to examination gloves, our approach is simple. We will continue to supply quality exams, but only where we receive a reasonable margin. We also produce only about 25 percent of the exam gloves we sell, which gives us supply flexibility. However, we also would not give up exam business if that caused us to lose significant surgical volumes or if we thought our overall brand would suffer. Exams are part of our toolbox. Some customers demand quotes for both surgical and exam gloves. Others accept our position that we cannot supply exams at a loss. Fortunately there are also customers who are willing to pay for

Ansell's exams to have the confidence of knowing that all their medical glove needs are being met by a market leader. That is the value of our brand.

#### **CFO Rustom Jilla**

Professional margins are very unlikely to stay at H1's levels in H2. The cost/kg of NRL consumed in H2 will probably be up 40 percent on H1. This large an increase cannot be offset simply by further improvements in our surgical vs. exams mix. And we (and others), don't seem to be able to increase selling price quickly enough to offset rapid cost increases which is why we continue to focus on manufacturing efficiencies and technology upgrades.

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Latex prices have increased sharply in recent months. To what extent are they yet to impact the Professional cost base? How has the cost base of the Professional business changed since the last peak in latex prices and what is its current ability to pass cost rises on to customers?

#### **CFO Rustom Jilla**

Significantly higher NRL prices began flowing through the P&L only towards the end of H1. We are passing NRL cost increases through to customers in our Occupational and Consumer businesses but we are not able to do this as swiftly in Professional. This is because we have longer term contracts with hospitals and purchasing organisations where we can walk away ... but we can't modify pricing easily. Ansell's position is, however, comparable to others.

Approximately 44 percent of our H1 sales came from NRL based products vs. 48 percent in F06. Please do also remember that Ansell has had to deal with sharp upticks in latex prices before, and helped by our portfolio of businesses and strong market positions – has nevertheless grown profits through these periods. Beyond raising prices where feasible, we are undertaking other actions to improve our latex usage efficiency.

#### **[openbriefing.com](http://openbriefing.com)**

In the Consumer business you booked EBIT of US\$10.5 million, down 29 percent on sales of US\$104.4 million, up 3 percent. Factors in the earnings dip included reduced sales through government tenders which were US\$6.4 million, down from US\$11.8 million and distributor changes. Without significant tender wins in the second half, can Consumer match last year's earnings of US\$21.2 million in the current year?

#### **CEO Doug Tough**

Ansell has had great success with our SKYN polyisoprene condom, which is being rolled out in many countries and with products like "Zero" here in Australia. However, we have had patchy performances in a few other geographies. We also had to make significant distributor changes in a key country ... at a short term cost, but with the expectation of longer term benefits. Significant tender volumes have slipped from H1 into H2 due to delays in orders some of which were since received. Finally we have incurred \$2.2 million of restructuring in H1 in Consumer and there will be more in H2. But the short answer is that achieving last year's EBIT in Consumer will be challenging.

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Ansell's SG&A expenses were US\$132.9 million in the first half, up 4 percent from the previous corresponding period. To what extent can SG&A costs be held at this level without damaging your ability to grow sales?

**CFO Rustom Jilla**

Firstly – H1 SG&A includes over US\$6 million of restructuring costs. Take them out and we are down half on half, despite FX and performance incentives. The weaker USD helped sales but meant that our expenses in Euro's, AUD etc, translated into a higher SG&A number. Finally, in F'09, there were no short term incentive payments across most areas. This year, we are doing better than budget and the results include higher provisions for performance incentives.

When the GFC hit us, we spent several months working out how to make a structural reduction in our cost base – without reducing our capability to grow. Hence the 7 percent reduction in global SG&A positions in F'10. However, we have continued to invest in the business. Project Fusion will transform Ansell via the introduction of a new ERP system and processes. Once we are finished, this should give us even greater ability to leverage our infrastructure and grow sales without growing overheads proportionately.

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Ansell has flagged an ongoing EPS benefit of more than US\$0.10 from FY 11 from its recent restructuring initiatives. In which specific areas do you expect to realise these benefits?

**CFO Rustom Jilla**

Slightly more than half of our restructuring net benefits commitment will come from manufacturing, where we commenced taking necessary actions in F'09 itself. Both manufacturing and SG&A savings come from all three businesses.

We expect to complete our planned restructuring this year at a lower net negative EBIT impact than envisaged, equating roughly to an expected US\$0.01 of EPS in F'10. The F'11 contribution flagged previously was derived by comparing projected full year benefits in that year with net costs in F'10. Given that the F'10 impact from restructuring is expected to be about US\$0.01 per share better than originally anticipated, it is now expected that the year-on-year incremental EPS benefit in F'11 will be slightly lower (@ ~US\$0.09).

**CEO Doug Tough**

The work the team has done in this area has been first class, comprehensive and thoughtful, and their fast reaction time has put the Company in a great position to recover from the GFC quickly.

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Ansell generated free cash flow of US\$67.2 million in the first half, up from US\$42.7 million in the previous corresponding period, and had net debt of US\$82.9 million at the end of December, down from US\$180.5 million a year earlier. Net debt to net debt plus equity was 13.2 percent, down from 27.5 percent. Given the strong cash flow and a relatively "lazy" balance sheet, are you considering a more aggressive capital management program?

### CFO Rustom Jilla

For years, we have followed a “balanced capital management program” that includes dividends and share buy-backs to return surplus funds to our owners. In the first seven months of F’10, we have bought back around 5.1m shares at a cost of approximately A\$51 million.

In H2, we expect significantly higher capex spending on Project Fusion (our transformational ERP project) and frankly – we just cannot continue to improve working capital each period at the same rate as we have been doing for years. Our existing buy-back approval still has 2.5 million shares unutilised and we can always seek Board approval for an extension. Meanwhile, our strong cash flow generation and very low gearing give us acquisition capacity and spending flexibility.

### CEO Doug Tough

We continue to search for acquisitions but with our strict internal guidelines we have been unable to consummate a deal this year. We have certainly been surprised at the lack of takeover candidates surfacing during the GFC. We expected multiples to fall and opportunities to arise but the reality is that this has not been the case. As always, we are keeping an eye on a number of potential targets and, if there is a transaction that builds shareholder value – I am sure that management and the Board will move appropriately.

### [openbriefing.com](http://openbriefing.com)

Ansell announced an unfranked interim dividend of A\$0.13 per share, up from A\$0.12 last year. What is the outlook for dividends for the full year in light of the upgraded EPS guidance?

### CEO Doug Tough

This is clearly a Board matter, and we never give guidance on dividends. However, as you can see from our history, we look to steadily grow dividends over time and there is no reason to believe this cannot occur this year.

### [openbriefing.com](http://openbriefing.com)

Thank you Doug and Rustom.

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