Company Name: Brambles Limited (BXB)
Event: Baird 2015 Industrial Conference
Date: November 11, 2015

<<Al Root, Analyst, Robert W. Baird & Co>>

All right, good morning, everyone. Welcome to day three of the Industrial Conference again, I'm Al Root, the Industrial Sector Strategist here at Baird. It’s my pleasure to introduce Brambles, global supply chain logistic company; incredibly diverse, a set of businesses operating in 60 countries; serving consumer goods, beverage, general manufacturing in terms of numbers that may boggle your mind; they own or manage 500 million pallets, reusable containers and containers for global supply chain.

With us today are James Hall, from the Investor Relations, organization and presenting is Peter Mackie, President of Pallet Division, Peter?

<<Peter Mackie, Group President, Pallets>>

Great. Thank you very much and thanks everybody for coming this morning. We are one of Australia’s great export in secrets, so I'll try and demystify us a little bit. So I am Peter Mackie, I run a division of Brambles, which is our Pallets Division. We're about 75% of the Group. I've been in the company 14 years overall, I run it in Europe, I run it in Asia-Pacific and I've also run it in the Americas, so I have multiple set of McDonald's stars, which qualifies me to run the company globally.

So as I said, we're a sort big Australian export secret really, so although we’re listed on the Australian stock exchange actually only less than 10% of our revenues actually come from Australia these days. So the majority of our revenue actually comes from Western Europe and also North America. So we sort of have a quite a high exposure to those markets, but actually we’re also in most of the emerging market regions around the world.

So they represent about 10% of our revenue, but they are the fastest growing piece of our portfolio. So when we get described as a business, especially my business I get described as a Pallets business. And actually fundamentally what we’re about, what sets our business apart actually isn’t the equipment at all. So I will talk about the equipment, but the thing that makes the real difference in this business actually is the network that we have in each of the local markets in each of the regions, but then also globally.

So the first part of our network actually is our service center. So this is a map of our business in Europe. And the little dots that you see on the screen there are actually the service centers that we have in Europe. So those are the centers where we will take return equipment we’ll inspect it, we’ll repair it, if it needs it and then it will go back out to customers again.

We also have small service centers like most business we love three letter acronyms here, but basically they're small service centers. They're very, very close to customers in a lot of cases; they're actually on customer locations. And they really only inspect the equipment, that's all they do and it just means that actually if the equipment is suitable to get back to a customer it actually goes straight back to a customer, rather than coming all the way to the service center. So we have some network optimization going on with those small centers.

But the key piece of our network and the key piece that sets us apart in this industry actually is the customer element of this network. So these dots actually don't represent individual customers, they actually represent a cluster of customers around a postcode, right. So they get a feel for how many customers we have in Europe and these are manufacturing customers. So these in the fast moving consumer goods space are some of the biggest manufacturers around, so Nestle, Unilever, Procter & Gamble these sorts of companies are our customers and a fundamental part of our network.

The other part of our network actually is the retailers, all right. So in Europe, the Tescos, the Sainsburys, the [indiscernible] are all key customers of our CHEP pallet business. And globally we're working with all the major retailers including Wal-Mart in the U.S. But this is where this network gets really useful because our customers, our manufacturing customers can ship their goods using our equipment wherever they want, all right.

So because we have this coverage of the retail locations that they all ship to, they could ship wherever they want. And that's what these blue lines represent. So shipments of their goods wherever they want to, whenever they want to sent, all right. The fundamental piece of this network is it's incredibly dense, all right. So the network is incredibly dense, but when we pick our equipment up that density basically means that we can pick it up when it's empty and not adding value for the customer and actually move it a very short distance to a repair center or straight back to another customer that's very close.

So a customer may ship from the U.K. to Spain, but that pallet won't go all the way back to the U.K., that pallet will get given to a customer in the Spain and may well then ship to France, okay. So some of the very thin yellow lines here, you're seeing that we have to sometimes rebalance the pool. But in general the big focus of this network is moving the empty equipment, the shortest distance that you possibly can, all right. But what really sets this business out, the reason we make the returns that we make is that we have this density of network in a majority of markets in which we operate around the world and its very, very hard to build a network this takes decades to build the network like this.

So I said, it's not so much about the product, okay but is the products that actually we've put through these kind of network. So although what I showed you there was our pallets network, actually for our containers businesses and our RPC businesses, we also have very similar networks and in fact sometimes those networks also overlap.

Now the important thing with these products actually is there is a little bit of IP in these products, but it is not the key piece for us. So the IP is around, how do you make them strong enough to do recycle and reuse with this equipment. How do we make them the highest quality that we can, so that customers product remains undamaged, when they ship it and then some of the IP and – how do we make them fold, as flat as possible. So in the reverse logistics, when they're empty, actually the cost of them moving them around is very low. So we move them a short distance and we try and get them as flat as possible in order to keep the logistics costs down of moving them.

But the IP is sort of less important to us, it's less important that these products are unique in the marketplace. Because the reality of what we want actually and the reality of what we do in markets is to get there first and create the standard. Because when you create the standard, it means that conveyors are built around the equipment, racking is built around the equipment and the materials handling devices are also built around the standard, all right.

So unique products is not what we're about, we try and actually either create a standard or grab hold of a standard that exists, because all of the equipment in the supply chain gets built around those standards. And it's a fundamental part of our business. I mean many of you heard about this new phrase called the sharing economy. Well, Brambles has been at this for quite a long period of time. These assets are all about creating the standards, so that they can be shared, so that we can give them to different customers in different locations. There is a little bit more IP, it's fair to say in the containers business and as you will see later some of the product that flows in these containers is very high value. So actually making sure that you get, as much of that product out as you possibly can, before the containers are washed is fairly key. So there is a bit of IP, more IP I think in the containers design. So before I, maybe before I step off the product, so the network is pretty fundamental to our economics, it's pretty fundamental to our customer value case. And actually having good strong robust products with good return economics is also important.

But fundamentally for these pooling shared economy business, it's really about how do we do get the maximum amount of reuse out of this equipment. How we do make sure it turns, as fast as it possibly can. So the other bit for us is really picking the supply chains that this equipment gets used in. So when you look at the supply chains that we serve, these are some of the world's most important supply chains. So we're fundamental in a number of countries to actually the flow of goods in some key supply chains. So our RPC business, so those folding plastic containers that you saw, really predominantly focused on fresh produce. Getting fresh produce from the farm all the way into the retail store in the right condition at a much lower cost than you can shipping it in one way disposable cardboard. And our job in this area is to make those crates turn as fast as possible. But it works in fresh produce, because the fresh produce supply chain is a very, very fast supply chain.

Now the Pallets business that I run actually really spreads across a number of different supply chains. But the fundamental supply chain, we serve actually is the fast moving consumer goods. But you can see why we chose the fast moving consumer goods actually to get this business started because our assets do turn at good speed in those supply chains. And then the containers business actually supplies a broader range of supply chains, all of them have an element of speed to them.

In a number of cases here actually this is where the value of the product in the containers is also quite important, which is why I said the IP in the container that enables you to get more of the product out or enable it to be handled very quickly in an automotive environment is also fairly key to the value that gets delivered to the customer at the end of the day. So we have a great network, we have great products and I think we've chosen the right supply chains in which to operate.

So what does our market position look like? If you look at us around the world, we are by far and away the global leader and we're by far and away the local leader in all of the markets in which we operate, other than two. So we're number two in Malaysia and also in Thailand, but other than that we're the global leader. Our competition around the world is not global; our competition is local and in some of these markets quite fragmented. And in some of these markets actually its - some of the competition on here is actually customer-owned pools. So there they've started acquiring their own assets and eventually we look to try and convert them across.

But the other key message from this Slide is the white space, okay. So this is one way packaging or exchange type packaging solutions. This is a chart for pallets, but the other businesses are very similar to this. There's still a lot of white space for conversion and as you see fuel prices go up and in our case timber costs go up and the management of sustainable timber sources become more of a challenge, this white space really does open up more and more to pooling, all right. So we have a great market position, but we still also have quite a lot of white space to grow this business. And it's a similar chart for those of you who have been joining us later in the day for the other two business units as well.

Now the consequence of that growth opportunity in front of us, there is a lot of opportunity to deploy capital into the business and as you will see the split is fairly well shared across the three businesses, based on their size. And then I think what you should also notice from this chart that we're in, our financial year is July to June. So we're just starting a year of quite significant investment in growth. It kind of started in FY '15, but there's lots of opportunity to deploy capital into this business. So what's in it for our investors, but we have a great market leading position. We actually deliver a really strong value case to the customers that we serve and actually just because of that network that we have in the countries in which we operate, we managed to get a share – a fair share of that value. So that gives us really good quality returns in a business that still has plenty of opportunity to grow around the world.

And the important point I think from the previous chart is that, there is a lots of white space in the markets that we're in. But actually there's lots of opportunity for us to enter into new markets. So in this financial year, we've entered into Russia, Peru and into a number of countries in the southern cone of Africa, in addition to the 60 that we're in today. So geographic expansion is a key additional white space to the one we talked about there.

So where are we heading, our objectives really for FY '19, this was the last time we spoke about our five-year plan externally is sales growth in the region is 6% to 8% and actually getting to a ROCI in FY '19 of about 20%. And I'll share with you to some degree how this looks different across the portfolios. So this is my business, so if you consider the curved line there is creating value over and above our cost of capital, so really generating economic value. In each of the five regions that I run around the world, we actually have strong value creating businesses and all of them with opportunity to grow. You'll see what I said before, there is a heavy exposure to Western Europe and the U.S here, but the fastest growing bubbles on this chart are actually those in the emerging markets.

On the RPC business, the Chart needs probably just a little bit of explanation in the – this is an area where we've made some acquisitions, so there is some goodwill in the accounting here, which clearly we need to earn-out. But as we look at this business and where to place the capital and how to grow it, it's really worth looking at the light of bubbles here.

So the two things in the RPC business is if excluding goodwill, the incremental returns that we get out of the European RPC business, the AMZ and the South Africa RPC business and the Latin America businesses are all very strong. In the U.S business, there is a huge amount of growth in front of us at the U.S business. So these businesses in our view still sub-scale. So we're still building a stronger network here. So the intention is to get that above the value curve here. Some elements of profit improvement, but really focused on getting that business to something of scale.

The Containers business actually has been built a lot from other than in the automotive space; this is being built a lot from acquisition around a small container business that we've previously been running. And there are three in that space, that actually are very strongly returning businesses and especially from an incremental return perspective. But there are two businesses here that are work-in-progress. So the Lean business here and the Aerospace business here, we're working very hard to get them one, to scale and two, above the value creation line. But relative to the RPC business what I talked about before, these businesses require significant effort to get them above the line. But we're on the case with those businesses.

So our FY '15 performance, so for the last five years as a group, we've guided to the market on the top line and also on the profit line. And every year of those five years, we've delivered what we said we were going to deliver including in FY '15. Now as we look at our business, so I think there is one important thing to note here, which is we earn our revenue, its multi-local business. We earn our revenue and our costs are actually in pretty much in the same currencies. There's one or two exceptions, but pretty much it's in the same currency.

So when you look at us, you really do need to look at us on a constant currency basis. And in the last financial year, top line we grew by 8% and actually the bottom line here we grew by 10%, so good leverage to the bottom line. Actually mainly through operational efficiencies and some synergies with the businesses that we acquired over that period of time. So the ROCI here went down slightly, but that - well it was because of acquisitions, actually excluding acquisitions the ROCI improved slightly, so up by one-third. Cash flow here is really a story about the start of some growth investments that we made in FY '15 and then we did make a slight increase in the dividend as part of our progressive dividend policy.

So if we move on to the guidance that we give going forward. So I've mentioned it before, we're really looking for that single high digit growth rates and getting to a ROCI FY '19 of around 20%. And our expectations for FY '16 actually to be in the range both top line and bottom line of 6% to 8%. So we adjust at the end of our first quarter going into the second quarter and we're at the top end of that. So we still have three quarters to go and in the world’s economies there's lots of challenges out there, but we've actually started well to this financial year.

So what do you get, so I mean, this is my final slide and then I'll open up for any questions you might have here. What do you get with Brambles? So across all three business units, you get a business with strong market positions around the world. And the reason we have those strong market positions is because we have a compelling value proposition for our customers. We're first to market in a lot of new countries around the world, that's where a lot of this comes from. And we build a network in all of those countries enables us to get a fair share of the value and its very sustainable value proposition. What you get with us is still room to grow, so still opportunity to deploy more capital into this business. And what you actually get with us is in track record of saying if we're going to do something, we do it and that's what you get with Brambles.

Okay, so thanks for listening to me for all that time, I don't know if we've got short moments now for any questions you might have.

Q&A

<Q – Al Root>: Yeah, thank you that was great. We have few minutes for questions, you can feel free to use the iPad, of course we're session two at rwbaird.com. And maybe I'll take the first one from the iPad. When you talk about customer in-source logistics or pallet operations versus a pooling arrangement, what sort of savings or what's the value proposition, when you go ahead and you try and convert the Pallet business?

<A – Peter Mackie>: Yeah, the value proposition there is very simple, so if you imagine for somebody who is - we have some of these in South Africa, so you'll have noticed on the AIME one. You may have beverage companies, who actually are shipping to a number of places and historically they have the vehicles coming back empty. So they'll abort the pallets, they'll be shipping downstream and the vehicles are coming back anyway, so they put the pallets, the empty pallets back on the vehicle and they come back. However the world of supply chain is changing quite dramatically and it has been some time now. So people are always looking for a vehicle that may deliver somewhere, it could do more useful work on the return leg back than bringing empty pallets back. So there is much more pressure on those companies now to say the real cost of bringing a pallet, all the way back from where it was delivered back to the source actually is uneconomic. And joining a pool where you share an asset, you leave it, where your products are left and then you don’t worry about it anymore, those economic shifts. So for those customers, as their supply

chains get more complex and there is better opportunities for those empty reverse legs and moving empty pallets is never a good equation, so that's the key piece.

And then the other piece and this is one fundamental of pooling, whether it's in automotive or actually in fresh produce. Some of these businesses are very seasonal; they have various different peaks and troughs. So if you invest in your own equipment, actually you do have periods, where you actually need to buy for the peak and you end up with a lot of equipment sat around for the rest of the season. So actually joining a pool, actually enables you take some of that seasonality out of the mix. And you will always have this equipment available when you want to.

<Q – Al Root>: Yeah, following up on that is – and is there a sweet spot either in the business cycle up or down, where converting some of that customer CapEx to OpEx is easier or harder?

<A – Peter Mackie>: Yeah, there is a – the CapEx to OpEx one is always an interesting one. The fundamental and we're sort of in this phase at the moment. The main shift is around that white space that I talked about. So as you see construction going up, the price of lumber goes up, all right. So the cost of lumber into pallets then also goes up. So it just makes those less efficient models. So those models that are only shipping one way or aren't very efficient exchanges. As those sort of input costs go up, fuel and labor and timber actually our model is fundamentally more efficient and people begin to see cost escalating in that space. So that's probably the big driver of when we see conversions take place. So those economies although we've – people leave there whole time, so in fast moving consumer goods, it's relatively stable. But actually as economies pick up, you do begin to see this pressure on that white space that sort of intensifies the shift.

<Q – Al Root>: Okay. Any questions from the audience? Go ahead.

<Q>: [Question Inaudible]

<A – Peter Mackie>: Yeah, I know, so it's somewhere in the range of 10% depending on it, but it depends very much on how inefficient they are. So if you imagine – if you're a P&G or a Unilever you have highly automated facilities, you need a very high quality pallet. If you're in a world where they were previously, which is you're shipping your goods on a high quality pallet, but the pallets that you're getting back in return are not the ones that you ship down, all right. So what you get back is you get the average quality of the market. So you put very good quality into the market and you've got average quality back in return. Now they can't use a large number of those pallets that they've had back previously. So they have to buy new ones in order to be able to put through their automated system. So for somebody with a high degree of automation, shipping very long distances, so single factory regional shipping the cost savings can be significant, so they can be 30% to 40%, but on average it's generally in the range of 10% to 20%.

<Q>: [Question Inaudible]

<A – Peter Mackie>: No, for the retailers, I mean the way we, generally when we enter a market we will generally start talking to the retailers first. Because what happens in a pallet system that's not working is people try and put the lowest quality they can get away with because they're struggling to get what they want back in return. And it's the retailers that bear the brunt of that poor quality. So as markets modernize, more high bay racking goes up and the need for quality becomes really, really important. So the retailers have a lot to gain from moving to a high quality standard system, where the quality is good and consistent. So yeah, the retailers is generally the place we start in a market because those are the customers that are actually feeling the pain the most.

<<Al Root, Analyst, Robert W. Baird & Co>>

All right, you know what there is a lot of interest on the iPad and then I think we'll cut if there and suggest the break out downstairs. Please join me in thanking Peter and James for excellent presentation.

<<Peter Mackie, Group President, Pallets>>

Great. Thank you.