Level 21
25 Bligh Street
Sydney NSW 2000

Colorpak Ltd (CKL.ASX)

RESULTS REVIEW – A solid first year

Friday 19 August 2005
Containers & Packaging

Rating:	BUY
(previous):	BUY

Michael Henshaw
mike.henshaw@fostock.com.au
+612 9993 8166

Colorpak's maiden set of full-year accounts as a listed company delivered a strong performance with revenues 10.5% above the prospectus forecast and normalised NPAT growth of 9.0% pcp. The group announced a number of significant new customers and said that due to continuing strong demand it expected to enjoy a good year in 2006.

The FY'05 result

Revenues of $58.5m were up 19.2% pcp (FY'04: $49.1m) or 12.1% excluding the contibution from Castle Graphics. EBITDA grew 8.7% to $11.2m (FY'04: $10.3m) with margins contracting (19% vs 21%) as a result of a higher staff expense and a slip in the gross margins due to new customers coming from outside the group's core high-margin niche in healthcare. Normalised NPAT of $5.4m was 2.8% ahead of the prospectus guidance and +9.0% pcp. The 1.5c second half dividend lifted the FY payout to 2.5c.

Upgrade to FY'06 revenue, downgrade to profit

We have upgraded our forecasts for revenue by 4.5% and we are now expecting 18.8% revenue growth (FY'06: $69.6m). Excluding Castle Graphics this equates to organic growth of 14.0%. Gross margin compression and one off relocation costs, means the strong topline growth translates into just 6.4% profit growth and our FY'06 NPAT forecast falls 6.0% to $5.8m, from $6.2m. Our NPAT forecast for FY'07 is unchanged.

Cashflow & Debt

Operating cashflow was strong at $7.9m or 145% of normalised NPAT. The cash cost of the Castle Graphics acquisition ($2.6m) and capex of $3.8m meant that debt was reduced by just $0.7m to $27.5m equivalent to net gearing of 39%.

Valuation & Recommendation

We have rolled-forward our DCF valuation (and price target) which moves from 87c to 88c. Despite our downgrade for 2006 profitability we re-iterate our BUY recommendation as we see the current year a necessary investment to secure a step change in the group's development. We welcome the management's decision to grasp the opportunity. With a strong track record for strategic planning and integrating acquisitions investors should continue to back them.

Year to June ($m)	2004a	2005a	2006e	2007e	2008e
Revenue	49.1	58.5	69.6	75.3	81.0
% change	n/a	19.2%	18.8%	8.2%	7.5%
EBITDA	10.3	11.2	12.6	14.7	15.8
EBITDA margin	20.9%	19.2%	18.1%	19.6%	19.5%
NPAT (reported)	2.6	3.1	5.8	6.8	7.8
NPAT (normalised)	5.0	5.4	5.8	6.8	7.8
EPS (diluted) (cents)	6.4	6.9	7.2	8.5	9.7
% change	n/a	7.1%	4.6%	18.1%	14.4%
Dividend (cents)	-	2.5	2.7	3.2	3.7
PER (x)	9.7	9.0	8.6	7.3	6.4
EV/EBITDA (x)	7.6	6.9	6.4	5.3	4.7
Yield (%)	n/a	4.0%	4.4%	5.2%	6.0%

Numbers exclude abnormal items and goodwill

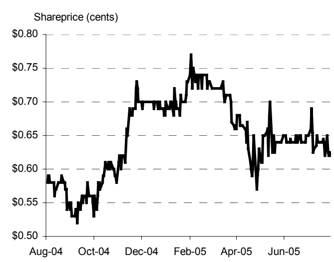
Source: Company, Foster Stockbroking

Share price:	$0.62
Price target:	$0.88
(previous price target)	$0.87
NPV per share	$0.88
Risk:	Med
Shares on issue (m):	80.5
Shares (diluted) (m):	80.5
Free float:	67%
Average daily volume:	85,745
Market cap (m):	$49.9
Enterprise value (m):	$77.4
Net Debt (m):	-$27.5
Gearing (ND/ND+Equity):	40%
Shareholders equity (m):	$41.9
Book value per share:	$0.47

Forecast:	2006
Free cash flow (m):	-$0.74
Return on average equity:	13%
Net interest cover (x):	5.2

Forecast:	2007
Free cash flow (m):	$5.38
Return on average equity:	14%
Net interest cover (x):	5.3

Shareprice (cents):



www.fostock.com.au

THE RESULT

The results were with inline our expectations for revenue, EBITDA, NPAT and EPS. The group's maiden set of full year results marked a strong performance with revenues 10.5% ahead of prospectus forecasts and NPAT 10.7% of 2004.

Figure 1: Result vs Foster Expectations

Year to 30 June $m	2005e	2005a	Difference
Revenues	**58.04**	**58.54**	0.9%
% change	18.2%	19.2%	
Gross profit	34.88	34.25	-1.8%
% margin	60.1%	58.5%	
Staff	-17.08	-17.87	4.6%
Occupancy costs	-1.79	-1.78	-0.4%
Other	-4.99	-3.49	-30.0%
EBITDA	**11.26**	**11.22**	-0.4%
% margin	19.4%	19.2%	
Depreciation & Amortisation	-1.80	-1.66	-7.8%
EBIT	7.12	7.207	
Net Interest	-1.92	-1.87	-2.3%
Pretax profit	5.21	5.34	
Tax	-1.95	-2.26	15.7%
Reported NPAT	3.26	3.08	-5.5%
NPAT (normalised)	**5.60**	**5.44**	-2.9%
% margin	9.6%	9.3%	
Reported EPS	4.28	3.93	
EPS (normalised)	**6.96**	**6.87**	-1.2%
Dividend	2.50	2.50	0.0%
Payment for PPE	-1.57	-3.76	139.5%
Operating cashflow	6.22	7.88	26.6%
FCF	4.65	4.12	-11.5%

Source: Company; Foster Stockbroking Pty Ltd

Revenue

As foreshadowed by strong first half (1H05: $27.9m, 14.5%pcp) the group beat the prospectus forecast of $52.7m by 10.5%. The Castle Graphics business, acquired in December last year, contributed $3.5m, excluding this, organic growth was 12%.

Customers

Typically the folding-carton industry grows in line with GDP. Colorpak has therefore maintained its record of market share gains. Most notably the company said that it had won an account for Clairol (Proctor & Gamble), thereby securing the continuance of its contract with Wella (also P&G). This was won from Wadepack, as was the sizable Riverwood contract, which the company hopes to grow considerably over the next three years. A contract with PB Foods was won from Amcor (~$1m pa) and Telstra has awarded Colorpak a ~$1m pa contract to produce phone-card holders. Only one contract (Philip Morris) was lost during the period (~$0.6m) but the company believes that this will be made-up by offshore work from the US giant.

Margins

We were disappointed by the second half gross margin (56.7% vs 60.0% expected) as we believed that our forecasts had captured the compression from the acquired Castle Graphic business, where margins are just half those of Colorpak.

The shortfall would appear to be due to our underestimation of the impact of new contracts where the initial tooling expense is absorbed the margin in the early phase. Additionally, an increasing quantity of incremental sales is outside the group's higher-margin pharma/health niche. The proportion of sales from other sectors grew to 43% from 39% in the first half. We anticipate some margin recovery in 2006 to due moving die-cutting in-house and deflation in cartonboard prices.

Operating costs

Operating expenses were in line with expectations, but we had underestimated staff costs, specifically a $0.34m management bonus paid for overachievement of the prospectus guidance. Despite our expectation of gross margin erosion, due to ongoing expansion outside healthcare (where the group already command a near 50% market share), we believe that over the long-term the group can maintain EBITDA margins through economies of scale and additional efficiency gains.

EPS

EPS (normalised) of 6.87c were inline with our expectation, as was the 1.5c dividend, which took the full year payout to 2.5c.

Capex & Debt

Capex was ahead of expectations, but this was brought forward expenditure earmarked for 2006. Debt was unchanged on the first half at $27.5m equivalent to gearing of 39.3%. With operating cashflow a robust $7.9m for the year and interest cover of 5x this looks onerous, but not threatening.

Outlook

"2005/06 year had commenced well despite a soft economy…Demand is expected to remain strong for the balance of 2005/06 and we therefore believe we should have anther good year."

Escrow

The company announced that 25.5m shares came out of escrow. These are the Commins family shares and Alex Commins (CEO) has said many times that none of the family members are sellers. Should a member of the family wish to sell there is a legally binding agreement that the rest of the family have pre-emptive rights.

FORECASTS AND EXPECTATIONS

Colorpak has reiterated on several occasions that it expected to win a number of contracts following Carter Holt Harvey's acquisition of Wadepack. Our discussions with unlisted peers Hannapak and Anzpac corroborate this contention. New customer wins revealed in the broker presentation indicate that despite our expectation of 14.6% growth in 2006, we have been underestimating the opportunity.

We have therefore upgraded our forecasts for revenue by 4.5% and we are now expecting 18.8% revenue growth. Due to some margin compression and one off relocation costs ($0.4m), this translates into 6.4% NPAT growth. Excluding the relocation expense of ~$0.4m our current year EPS forecast would have been up 9.8% to 7.54c.

Figure 2: Change in forecasts

Year to June	NEW		OLD		CHANGE	
$m	**2006e**	**2007e**	**2006e**	**2007e**	**2006e**	**2007e**
Revenues	69.56	75.28	66.54	73.63	4.5%	2.2%
% change	18.8%	8.2%	14.6%	10.7%		
Gross profit	40.52	43.41	39.56	43.26	2.4%	0.4%
% margin	58.2%	57.7%	59.5%	58.7%		
EBITDA	12.60	14.74	13.14	14.45	-4.2%	2.0%
% margin	18.1%	19.6%	19.8%	19.6%		
Depreciation	-2.30	-2.65	-2.20	-2.37	4.5%	11.6%
NPAT	5.79	6.85	6.15	6.83	-6.0%	0.2%
% margin	8.3%	9.1%	9.3%	9.3%		
EPS	7.19	8.51	7.65	8.49	-6.0%	0.2%
EPS (ex. relocation)	7.54	8.51	8.01	8.49	-5.9%	0.2%

Source: Foster Stockbroking Pty Ltd

Capital expenditure is expected to be $8.5m in the year ahead. We estimated that this will not be covered by operating cashflow (FY'06: $7.8m) and expect the group to increase debt by $3.5m to $31.5m.

In view of the group's revenue opportunity the decision to undertake a substantial expansion in capacity (+30%) and take gearing to 40% is a calculated risk - comparisons with PMP are inevitable.

We believe however that Colorpak's history of successful expansion has been predicated on the management's decision to stay ahead of the investment cycle; a focus on the highest level of service and efficiency; and willingness to grasp opportunities. This requires investment, and inevitably means that for a long-term outperformance short-term gains will sometimes need to be sacrificed.

We have lowered our expectations EPS for 2006 by 6% despite the upgrade to our revenue forecasts. For 2007 we are anticipating a marginal outperformance of our earlier expectations.

Our DCF valuation has been rolled forward a year and now stands at $0.88. At this price the shares would be trading on a prospective PER of 12.2x for 2006 and 10.4x for 2007. We consider this a reasonable multiple for a company that we expect to deliver 14% CAGR in EPS over the next three years, with an additional 3.6% return provided by the yield.
We reiterate our BUY

FORECASTS

Profit & Loss

Year to 30 Jun	**2004a**	**2005a**	**2006**	**2007**	**2008**
$m	Pro-forma				
Revenues	49.12	58.54	69.56	75.28	80.96
% change	0.0%	19.2%	18.8%	8.2%	7.5%
Gross profit	30.17	34.25	40.52	43.41	46.22
% margin	61.4%	58.5%	58.2%	57.7%	57.1%
Staff	-12.71	-17.87	-20.40	-20.87	-31.10
Occupancy costs	-1.54	-1.78	-2.32	-2.42	-2.82
Other	-5.67	-3.49	-5.20	-5.38	-5.57
EBITDA	10.25	11.22	12.60	14.73	15.81
% margin	20.9%	19.2%	18.1%	19.6%	19.5%
Depreciation	-1.50	-1.66	-2.30	-2.65	-2.53
EBITA	9.12	9.57	10.30	12.08	13.28
Goodwill	-2.34	-2.36	-	-	-
EBIT	6.78	7.21	10.30	12.08	13.28
Net Interest	-2.13	-1.87	-2.00	-2.28	-2.06
Pretax profit	4.65	5.34	8.30	9.80	11.22
Tax	-2.00	-2.26	-2.51	-2.96	-3.39
Reported NPAT	2.65	3.08	5.79	6.84	7.83
NPAT (normalised)	4.99	5.44	5.79	6.84	7.83
Reported EPS	3.41	3.93	7.19	8.50	9.73
EPS (normalised)	6.42	6.87	7.19	8.50	9.73
% change	-	7.1%	4.6%	18.2%	14.5%
Dividend	-	2.50	2.73	3.23	3.70
EV/EBITDA	7.62	6.90	6.42	5.30	4.72
PER (normalised*) (x)	9.66	9.02	8.62	7.30	6.37
Yield	n/a	4.0%	4.4%	5.2%	6.0%

*before significant items and amortisation of goodwill

Source: Company; Foster Stockbroking Pty Ltd

Balance Sheet

Year to 30 Jun ($m)	2004a	2005a	2006	2007	2008
Current Assets					
Cash Assets	0.0	0.0	0.6	0.9	0.3
Receivables	9.5	10.8	12.4	13.5	14.4
Other	3.9	6.3	7.0	7.6	8.0
Total Current Assets	13.3	17.1	20.0	21.9	22.8
Non Current Assets					
PPE	15.2	19.6	25.8	26.1	26.7
Deferred tax	0.5	0.9	0.9	0.9	0.9
Intangibles	45.6	43.6	43.5	43.5	43.5
Other	0.0	0.1	1.6	1.8	1.9
Total Non Current Assets	61.4	64.2	71.8	72.3	73.0
TOTAL ASSETS	74.7	81.3	91.8	94.2	95.8
Current Liabilities					
Interest bearing liabilities	4.1	3.9	3.9	3.9	3.9
Payables	4.6	5.9	7.2	7.5	7.8
Other	0.0	0.0	0.0	0.0	0.0
Provisions (dividends and tax)	2.9	4.8	5.4	5.8	6.2
Total Current Liabilities	11.5	13.6	16.5	17.1	17.9
Non Current Liabilities					
Interest bearing liabilities	24.1	23.6	27.6	25.1	21.1
Provisions	0.7	0.9	0.9	0.9	0.9
Other	0.0	0.6	0.6	0.6	0.6
Total Non Current Liabilities	24.8	25.1	29.1	26.6	22.6
TOTAL LIABILITIES	36.4	38.7	45.6	43.7	40.5
NET ASSETS	38.3	42.6	46.2	50.5	55.3
EQUITY					
Contributed equity	36.9	38.9	38.9	38.9	38.9
Accumulated profits (losses)	1.5	3.8	7.4	11.6	16.5
Total Equity	38.3	42.6	46.2	50.5	55.3
LEVERAGE					
Gearing (ND/ND+Equity)	42.4%	39.2%	40.1%	35.8%	30.9%
Interest Cover (EBITA/Net interest) x	4.3	5.1	5.2	5.3	6.4

Source: Company; Foster Stockbroking Pty Ltd

Cashflow

Year to 30 Jun	2004a	2005a	2006	2007	2008
$m	Pro-forma				
Cashflow from Operations					
EBITDA		11.1	12.6	14.7	15.8
Net Interest		-1.9	-2.0	-2.3	-2.1
Tax Paid		-1.5	-3.0	-2.7	-3.1
Changes in working capital		0.1	0.2	-1.4	-1.1
Other		0.0	0.0	0.0	0.0
Net cash (used in) from operations		7.9	7.8	8.4	9.5
Cashflow from Investing					
Payment for PPE		-3.8	-8.5	-3.0	-3.1
Proceeds from sale of PPE		0.0	0.0	0.0	0.0
Purchase of a business (net of cash)		-2.6	-0.2	-0.2	-0.2
Net cash from investing		-6.3	-8.7	-3.2	-3.4
Cashflow from Financing					
Repayment of borrowing		-3.2	0.0	-2.5	-4.0
Proceeds of borrowing (inc overdraft)		3.3	4.0	0.0	0.0
Equity issue		0.0	0.0	0.0	0.0
Dividends Paid		-0.8	-2.4	-2.4	-2.7
Other		0.0	0.0	0.0	0.0
Net cash (used in) from Financing		-0.7	1.6	-4.9	-6.7
Net change in cash held	-2.2	0.8	0.6	0.3	-0.6
Cash at beginning of period	0.0	-0.8	0.0	0.6	0.9
Cash at end of period	-0.8	0.0	0.6	0.9	0.3

Source: Company; Foster Stockbroking Pty Ltd

Dupont Analysis

Year to 30 Jun ($m)	2004a	2005a	2006	2007	2008
NPAT margin	10.2%	9.3%	8.3%	9.1%	9.7%
Asset utilisation	65.8%	72.0%	75.8%	79.9%	84.5%
Return on assets	6.7%	6.7%	6.3%	7.3%	8.2%
Financial leverage	194.9%	190.7%	198.6%	186.7%	173.1%
Return on equity	13.0%	12.8%	12.5%	13.6%	14.2%

Source: Company; Foster Stockbroking Pty Ltd

FOSTER STOCKBROKING CONTACTS

DEALERS

Stuart Foster	+61 (0)2 9993 8131	stuart.foster@fostock.com.au
Kevin Massey	+61 (0)2 9993 8130	kevin.massey@fostock.com.au
Trenton Brown	+61 (0)2 9993 8161	trenton.brown@fostock.com.au
Kevin Curran	+61 (0)2 9993 8167	kevin.curran@fostock.com.au

ANALYSTS

Mark Fichera	+61 (0)2 9993 8162	mark.fichera@fostock.com.au
Michael Henshaw	+61 (0)2 9993 8166	michael.henshaw@fostock.com.au
Jocelyn Laurence	+61 (0)2 9993 8152	jocelyn.laurence@fostock.com.au
Jun Bei Liu	+61 (0)2 9993 8135	junbei.liu@fostock.com.au
Brenda Lennon	+61 (0)2 9993 8142	brenda.lennon@fostock.com.au

FOSTER STOCKBROKING Pty Limited A.B.N 15 088 747 148 FSR Licence No. 223687
Level 21, 25 Bligh Street, SYDNEY, NSW 2000 Australia
Tel: +612 9221 8711 Dealing: +612 9221 8700 Fax: +612 9221 1031 Email: www.research@fostock.com.au
PARTICIPANT OF ASX GROUP

Foster Stockbroking recommendation ratings: Buy = return >10%, Hold = return between -10% and 10%; Sell = return <-10%, Spec Buy = return > 20% for stock with very high risk. All other ratings are for stocks with low-to-high risk. Returns quoted are annual.
Important Notice: