# Chief Executive Officer's Report

## The two years since the merger have been a challenging but pivotal period for Brambles. We have taken tough measures to address fundamental issues in segments of the business and we are putting in place comprehensive plans to rectify them.

Much of this work is centred on ensuring that CHEP, which remains a unique business with attractive growth prospects, is better placed to achieve that growth in a sustainable way. In the past year, management's focus has been on instituting changes needed to improve the profitability of CHEP Europe and continuing to progress the performance improvement program in CHEP USA.

A priority in Cleanaway has been to ensure its operations in Germany are prepared for the impact of the re-tendering of contracts in the national packaging recycling scheme, which will come into effect in early 2004. Its UK operations are very well positioned to take advantage of the market's movement towards waste recycling.

Recall continued to grow strongly and Brambles Industrial Services also performed well, having built a solid foundation for future progress.

A summary of our profit performance and other key financial indicators can be found on page 4.

Despite the operational issues identified that impacted on profitability this year, Brambles' businesses maintained strong revenue growth, with revenue in continuing businesses increasing 3% to A$7.9 billion. This demonstrates the strength of our service offerings and the leading market positions of each of our businesses.

The adoption last year of Brambles Value Added (BVA) – measuring our performance as profit after deducting the cost of capital – has sharpened the focus of the management team globally on both the profitability of our businesses and the efficient use of capital.

Our strong focus on BVA and capital discipline in each of our business units has led to significant cash flow improvement for the group. Operating cash flow after capital expenditure improved by A$283 million during the year. Capital expenditure was reduced by 19% to A$1,244 million, without jeopardising long term growth potential.

Divestments during the year further streamlined our asset portfolio and included Brambles Shipping and Heavy Contracting and other non-core businesses such as the Building Repair and Maintenance Business of Cleanaway. Meineke, a specialist automotive service franchise in the Americas, was sold in August 2003.

## CHEP

During the late 1990s, an over-emphasis on revenue growth led CHEP to a disproportionate level of investment in new pallets and to an insufficient focus on collections and repairs, as services were extended to distributors outside CHEP's network and to greater numbers of smaller distributors. This led to lower asset productivity, reduced profit margins and a very high level of cash outflow.

To address these issues, major restructuring programs have now been put in place, both in the USA and in Europe.

CHEP is implementing changes to its service offering and pricing structure, which more accurately reflect the costs of serving specific flows of pallets and the needs of customers engaged in various activities. While reflecting the higher cost incurred in serving non-participating and smaller distributors, the pricing of CHEP's services will continue to provide economic and value-added service advantages to our customers compared to other alternatives.

The USA restructuring program – which was initiated in early 2002 – is beginning to show results.

The flow of pallets outside our participating distribution network in the USA has declined from 5.1% of total pallet movements last year to 4.1%. Importantly, some of this improvement relates to the conversion of a number of those distributors to become part of CHEP's distribution network. At the same time, the prompt recovery of pallets from non-participating distributors has improved from 56% to nearly 78%. As previously announced, specific pricing for the non-participating distribution channel in the USA has been introduced successfully.

A revamp of CHEP's USA service centre network is resulting in a reduction of unit transport costs. A new pallet return policy, whereby major retailers return pallets to CHEP directly by taking advantage of this new service centre network, is also being implemented successfully, with resulting cost savings.

While the ongoing improvement program in CHEP USA will lead to better performance, its performance this year was impacted by an increase in pallet repair costs, caused by the need to achieve, and maintain, the pallet quality standards we set for ourselves, as well as higher damage rates of pallets recovered from non-participating distributors and Total Pallet Management customers.

The new service centre network in the USA is now complete. In the transition from the old to the new network, there had been a build-up of pallet stock awaiting processing. A key task ahead is to reduce this excess stock to create further efficiency.

Nevertheless, the performance improvement program will give CHEP USA a lower operating cost base, a service offering and pricing structure that are more appropriate to serve its various customers, and tighter asset management.

In other parts of CHEP Americas, Canada, Mexico and Brazil performed strongly, improving their market positions and profit.

While CHEP Europe remains a profitable business, the decline in operating profits in CHEP Europe compared to 2001/02 impacted on this year's overall result for Brambles.

The restructuring program in Europe has two key elements: it comprises measures to improve operational efficiency and measures that focus on asset productivity. These measures are being put in place progressively and implementation is on track.

As already announced, the work to place CHEP Europe on a sustainable footing will incur a total investment of A$238 million over 30 months. The measures to improve operational efficiency will incur an exceptional item of A$112 million and the cost of the program related to improving asset productivity is expected to be A$126 million, to be shown as a significant item as incurred.

In the year under review, total significant items of A$151 million, before related tax benefit, related primarily to the investment in the CHEP Europe restructuring program.

A new pan-European structure has been in place since October 2002, ensuring we look at our business in Europe as a whole, not simply as an alliance of country-based operations.

The initiative to streamline the organisation and reduce indirect cost has started. With our workforce across Europe, we are discussing the changes that will make our operations more efficient.

A detailed review of our European service centre network is being undertaken to ensure that it is both located and configured appropriately, and we are beginning to more accurately streamline our service offering and pricing structure to reflect customer activity and the costs associated with such activity. In the long term, this will enable our customers to use CHEP's services in the most cost-effective way.

From the late 1990s, the total size of the European pallet pool had grown at a much faster rate than the growth in revenue. As a consequence, we were unable to achieve the optimal level of return from the assets we had invested in Europe. To reverse this trend, the restructuring includes a program to collect and condition the excess pallets, as well as redistribute the pallets within CHEP's new pan-European network to better meet customer demands. A great deal of work has been undertaken on this element of the program since it was announced. There has been a one-off relocation of 2.4 million pallets across CHEP Europe's service centre network to ensure pallets are better placed to meet customer demand. As a result of the intensified program of physical audits, 1.1 million pallets have been added back to customers' holdings, with associated revenue gains. Customer shortfalls led to compensations being charged for a further one million pallets. In addition, provisions have been made in relation to four million pallets that have been written-off as a result of this process.

These measures are important not only for CHEP, but for its customers, as a more efficient pallet pool will deliver benefits across the supply chain. To achieve this, we are working with our distributor customers to develop a better asset management system.

Much work has been done in CHEP Europe to quantify the issues, and to develop the most appropriate – and enduring – solutions. While there is considerably more to be done over the remaining 20 months of this restructuring program, progress is on track and we are committed to improving service quality, reducing cost and improving the return on capital invested in this part of our business.

Elsewhere, CHEP's operations in our markets of Asia-Pacific and Africa had a good year, with revenue up 13% and an improvement in operating profits.

The implementation of a standard IT platform with SAP – initially in the USA and, more recently, in Europe – has been completed. A major business process change of this scale is rarely achieved without issues and the SAP rollout in CHEP Europe did cause some process disruptions, particularly in the area of invoicing. Continuous improvement is being made and, by the end of the year, debtor days outstanding for CHEP had reduced by seven days year on year, with an even greater rate of improvement in Europe. This important systems investment provides great potential for process standardisation and improvement, and additional projects are currently underway to pursue these opportunities.

Despite the challenges in some regions, CHEP remains an attractive business proposition, with a globally recognised brand franchise and a significant competitive advantage in each of its regions.

Clearly, improved asset productivity will be the driver of performance in CHEP, while offering our customers tangible benefits including quality, technology, reduced cost, innovative products and convenience.

## Cleanaway

Despite difficult conditions in some markets, our waste management and recycling division continues to perform steadily and generate a strong cash flow.

Cleanaway remains one of the best performing waste management businesses in Europe, partly due to its strategy to limit its exposure to landfill operations in the UK. This strategy served Cleanaway UK well in 2003 as it was not affected to the same degree as its competitors by the new, and more restrictive, Landfill Directive.

In the UK, Cleanaway's strategy to build a profitable municipal waste business culminated in a number of important municipal contract wins during the year. In 2002/03 Cleanaway made excellent progress in the municipal market sector, increasing its order book by £188 million and growing market share. The total value of the UK municipal order book now stands at around £750 million.

Cleanaway also competes effectively in the UK Commercial and Industrial segment, with a focus on building local density and market share, as well as developing relationships with large companies through its Total Waste Management business.

The Rainham Materials Recycling Facility, which was opened last year, has reached operating targets ahead of schedule and is a superb example of the infrastructure required in the UK to meet the country's sustainable waste targets and global environmental responsibilities.

Our German operations were able to maintain profit at similar levels to last year despite the weak German economy and the impact of the introduction, in January 2003, of a compulsory deposit scheme for drinks containers, which had the effect of removing volume from the national recycling system (the Duales System Deutschland, known as the DSD).

DSD – a privately operated, non-profit organisation responsible under the German Packaging Ordinance for the recycling of sales packaging – is in the process of re-tendering its contracts with the waste management companies. In 2003 the DSD program accounted for 20% of Cleanaway's revenue in Germany – or 7% of total Cleanaway revenue. The outcome of the re-tendering is expected to be known in late 2003 and the new contracts will take effect from January 2004. We have factored in some inevitable price reductions arising from such a comprehensive re-tendering. Plans are in hand to consolidate facilities and reduce costs to mitigate some of the negative profit impact.

Cleanaway Australia also continued to be successful in the area of municipal contracts, winning 15 tenders during the year, in addition to securing extensions of three contracts. The business has also focused on a number of environmental initiatives, including an innovative 'bio-insert' bin for green waste, which is exclusive to Cleanaway and now being used as part of a municipal contract in South Australia.

Cleanaway Asia, already well established in Taiwan, has directed its main development focus on mainland China. After the start up of the first landfill gas-to-energy plant in Nanjing last year, work on a new plant is well advanced in Xian. Our recovered paper trading business in China has doubled over the last year.

Despite current pressures in some areas of its operations, Cleanaway's strength in the collection and recycling sections of the waste management value chain means that this business remains well placed for future success.

## Recall

Our information management division completed another very successful year, increasing revenue by 10% and comparable operating profits (as defined on page 81) by 17%.

Recall's organic growth rate was strong and was supported by growth from the 18 acquisitions undertaken during the year, notably those in the USA, UK and Sweden.

Recall continues to expand to achieve targeted levels of coverage in selected regions and economies of scale. In this context, its acquisition strategy is based on two key objectives: extending its business 'footprint' in key strategic or new markets and adding important storage capacity, particularly for its Document Management Services division. Recall maintains a highly disciplined approach to acquisitions, seeking a strong strategic fit at an acceptable price.

New geographic markets entered during the year included a move into Sweden and Finland.

Our continued expansion into the growing market for Secure Destruction Services was also augmented by acquisition. In this segment, Recall is the market leader in the United States, where it was boosted by new, national contracts, and future growth will be aided by the heightened business and legislative focus on secure destruction of data, arising from both privacy and commercial concerns.

North America remains the most important market for Recall and there are opportunities to strengthen the business in Europe, where acquisitions fuelled 43% revenue growth for the year.

The Asia-Pacific and Latin American businesses continued to perform soundly. While revenue growth in Australia and New Zealand slowed relative to some other markets, profit growth of 35% was achieved. Asia delivered modest growth in an under-developed market.

Recall is now well positioned with operations right across the information management spectrum, providing opportunities to leverage its service menu with customers globally.

## Brambles Industrial Services

The strong performance in Australia, which comprises about half of this division, was the cornerstone of a robust performance for Brambles Industrial Services for the year under review.

The successful restructuring of the Australian business has been the culmination of the program commenced three years ago to refocus this division on selected industries in which we serve key customers, offering a powerful combination of outsourcing benefits to our customers and earnings potential for Brambles.

Highlights in Australia included a strong year from the new pulverised coal injection plant at BHP Steel's works at Port Kembla, New South Wales. A feature of the year was the successful renewal of a number of major contracts, in addition to further new contracts being won.

The Australian result was offset partly by weaker performance in the Northern Hemisphere, where the business is focused solely on the steel industry. Reported profit was lower than in the previous year due to reduced volumes from Corus at Port Talbot in the UK and the write-off of assets following a customer bankruptcy.

Despite the recent uncertainties surrounding the UK steel services activities, contracts in this business are generally characterised by both their stability and duration. In addition, Corus' restructuring plans indicate the competitiveness and promising future of our key site at Port Talbot, where Corus' UK activities will be consolidated and capacity increased.

Overall, Brambles Industrial Services continued to be a strong generator of cash.

## Regional Businesses

The result for Brambles' Regional Businesses was impacted by a poorer trading performance by Interlake, arising from a softer US economy and reduced demand. Interlake's cost structure is being reduced and its manufacturing plant in California, USA was closed during the year.

## Quality improvement programs

In each of our divisions, we have the opportunity to ensure we deliver service quality in a consistent manner and we are applying standard productivity and quality initiatives across our businesses.

Each of CHEP, Recall and Cleanaway now has universal quality improvement programs to transfer best practice globally to develop robust business models to underpin future growth. Brambles Industrial Services is currently implementing such a program in Australia. These programs are focused on achieving measurable improvements in two specific areas – service quality and internal productivity – and each program engages our employees directly in this process.

In CHEP, every pallet and container must travel through our customer network in a predictable, error-free fashion – from delivery through to invoicing. We call this program the Perfect Trip. Recall's statistically-based service improvement program, the Perfect Order, is a global initiative to both deliver and measure quality service, providing an important competitive advantage to attract and retain business. Cleanaway is developing its Clean Run program for implementation globally and application locally. Brambles Industrial Services is progressively implementing its Big Picture program, which seeks to standardise policies and procedures, leading to consistencies in approach for the benefit of customers and employees.

## People

I would like to pay tribute to the significant effort and commitment by Brambles' 30,000 employees around the world in driving the growth and, where necessary, implementing vital changes in our businesses.

We are continuing to work hard together to build a stronger Brambles to create value for shareholders.

Today, we do this under a common, accepted framework for our business dealings. The Brambles Code of Conduct was formalised and rolled out in October 2002 across the group globally, and has recently been updated and strengthened. The Code, reflecting the principles embodied in our shared values (see page 2), embodies the view that we are responsible to our shareholders who provide us with the capital to do business, and to our customers, our colleagues and the communities in which we operate.

The Code of Conduct spells out what is expected of everyone at Brambles in honouring those responsibilities in the way we go about our work. It makes clear our common obligations in fostering and protecting our businesses, their prosperity and their reputation.

## Corporate social responsibility

During the year, Brambles also strengthened its commitment to corporate social responsibility (CSR), adopting a CSR policy which has been communicated to our employees as part of the Code of Conduct.

The mere existence of a policy does not fulfil our CSR responsibilities; rather, it is testimony to our sharpened focus on these issues. Brambles embraces the principles of CSR and, on pages 29–37 of this report, we provide details of our performance in these matters, including in the key risk areas of environment and health and safety.

## Strategic focus

In summary, our strategy is to maximise organic growth in CHEP, to continue to pursue organic growth and selected acquisition in Recall and Cleanaway, and to ensure the continuing robustness of Brambles Industrial Services and the Regional Businesses.

A comprehensive restructuring program is being put in place in CHEP and progress is on track. Throughout Brambles, our management structure and capability have been strengthened. Quality programs, involving a large number of our employees, are being introduced across our businesses to measure and improve customer service – strengthening our relationships with, and the quality of our service offerings to, our customers. Importantly, the cash generation capacity of Brambles has been greatly enhanced to support sustainable growth.

For the year ahead, management's priority is to:

- Successfully implement the CHEP restructuring to return this business to profitable and sustainable growth,
- Continue to manage Cleanaway to weather the challenging conditions in its sector,
- Continue to grow Recall through organic investment and by selective acquisitions that can add value,
- Maintain progress in Brambles Industrial Services, and
- Improve the effective application of capital and improve cash flow generation.

I am confident that the work undertaken during 2003 will support the successful pursuit of those goals.

**CK Chow**
Chief Executive Officer