CALSIL'S CORPORATE FINANCE POLICY

By G. Schaffer, Perth

(This address was delivered by Mr. George Schaffer, Chairman & Managing Director of Calsil Limited, at a luncheon meeting of the Society in Sydney on 2 April, 1974. The Figures and Comparative Statistics were prepared by Prof. Philip Brown, University of Western Australia.)

This is the second time I have had the honour to address you. The first time I addressed one of your Monthly evening Meetings held on the 17th of March, 1971. The theme your then President asked me to speak on was "Changes In the Brick Industry". The reason for giving me this theme was obvious. My company, Calsil Limited, came onto the Sydney Market with a bit of a "bang" and some people feared we could even endanger the existence of the clay brick industry.

Today, however, I intend to discuss our Corporate Finance Policy. May I start by saying firstly a few words about:

a) Our Product - the Calsil brick,
b) our technology, and
c) our enthusiastic executives, who are responsible for the day-to-day running of our operations.

a) Our Product

As mentioned in my first Paper, the calcium silicate brick is neither new to Australia, nor to other parts of the world. Despite its critics, the brick is eminently suited to Australian conditions, both from the point of view of the availability of raw materials and the product itself. The natural white colour of our bricks enhances their acceptance in this, our sunny country, where bricks are used without an external render. End users appreciate our bricks. It is a brick in its own right.

The product has been accepted throughout the world and our company - formed 19 years ago - has gone on from strength to strength, so much so that today we operate in Blacktown, N.S.W., the largest calcium silicate brick plant in the world. This, for the benefit of some of your members who may be influenced by the "die hards" in a conservative industry. They must accept that the building industry, like any industry, is subject to change. Our 19 years "track record" proves this.

The removal of raw materials used in the manufacture of the sand-lime brick enhances the environment. In lieu of digging deep holes in a fertile land, it levels useless sand-dunes, dredges sand which blocks the free flow of rivers and utilises lime-stone, a material which is plentiful throughout Australia. Fuel consumption is only a fraction of that used by the clay brick industry, thus reducing air pollution.

You will agree with me that such progress could not be achieved on a very competitive market with an unexciting product. You all know that apart from Queensland, bricks are now readily available throughout the Commonwealth.

b) Our Technology

Being an up-to-date product, the Calsil brick (may I call your attention that I am now talking of the calcium silicate brick produced

Figure 1 - Earnings per Share

by my company, Calsil Ltd.) is manufactured by most up-to-date machinery Three of our latest factories have fully automatic, electronically-controlled machinery. I understand the first similar factory to ours - in Finland - has only now (2 years after we installed our first) been supplied.

Our plants are designed to our conditions - a scarce labour supply. For production in a two press factory, we need only three men: 1 on the material preparation, 1 operating the two presses and 1 operating the curing - steaming plant. Obviously we then need a manager, maintenance staff and despatch - loading crew. But to emphasize, let me repeat that production of the bricks is performed by only three men.

c) Our Enthusiastic Executives

To introduce a new product to a market which has become conservative, by virtue of its long history and tradition, to operate new machinery for which every operator, maintenance man, etc., must be trained, one has to rely on enthusiastic executives. Calsil is lucky. For our executives, their work is a challenge. They are never satisfied with the achieved results, they accept that one cannot "stay put", that they must advance or give up! Many of them have been selected from our staff members and advanced with the company.

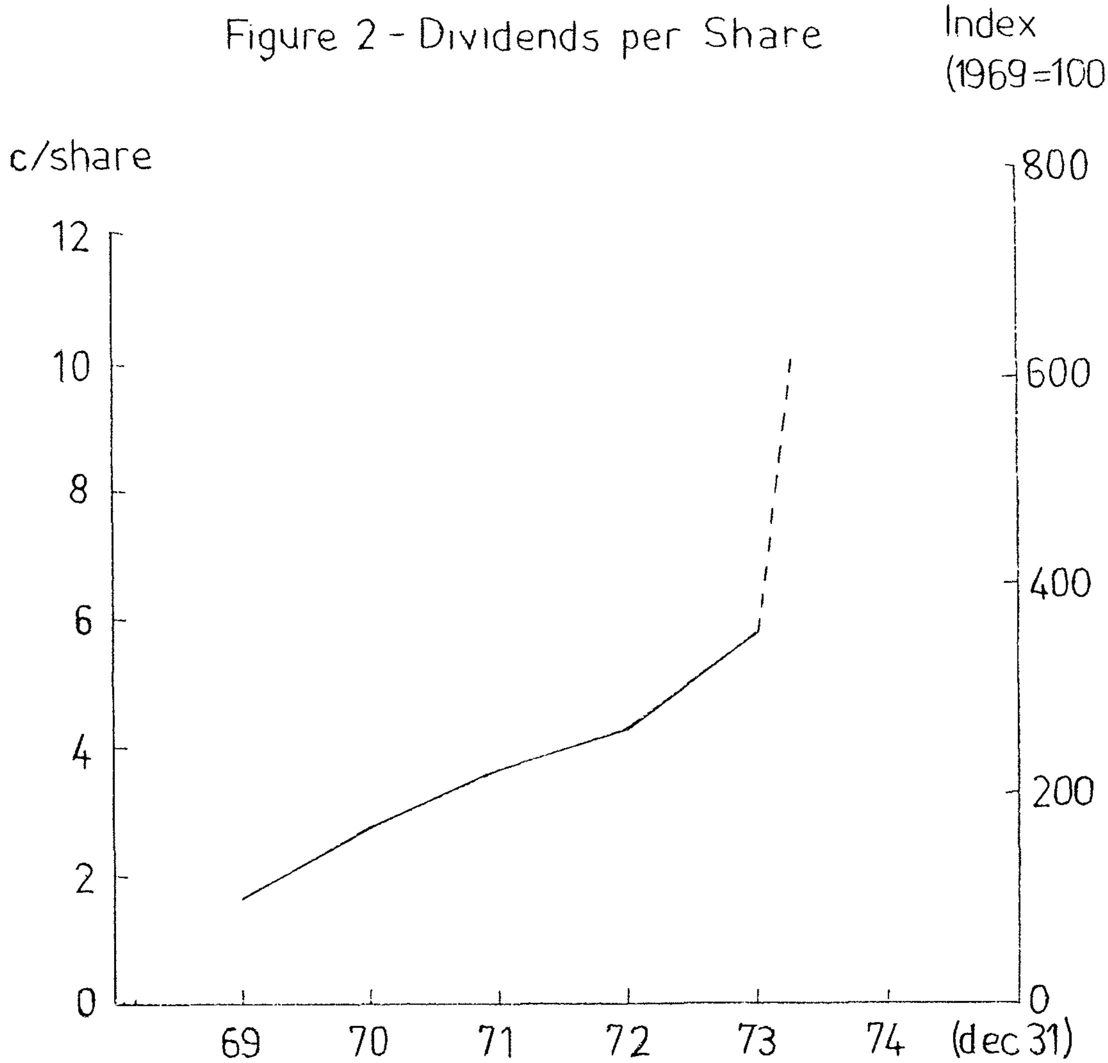
Relying on such enthusiastic executives we have been able - in a relatively short time - to revitalise languishing companies that we have acquired, namely: Colortone Bricks, Great Southern and Albany Brickworks, Besser (W.A.) and Hollostone (W.A.).

Board's Corporate Philosophy Towards Shareholders

To understand Calsil's Corporate Finance Policy one must be aware of its Board's Corporate Philosophy towards its shareholders. It is based on the belief that the shareholder expects to receive maximum possible benefits from his investment. We believe THAT THE SHAREHOLDER MAY WANT TO ENJOY HIS INVESTMENT RATHER THAN LEAVE IT FOR POSTERITY.

We also believe as we manufacture an excellent product, that we should endeavour to develop and enlarge our company to supply the available market, subject to a balance being struck in our rate of growth.

The result of our corporate philosophy can be seen from the exhibited



graphs. They show that over the 4 years to 31st of December, 1973, Calsil's

* Tangible assets have grown from $2,681,000 to $11,547,000 - equal to a compound growth rate per year of 44%

* Shareholders' equity from $1,282,000 to $6,000,000 - equal to a compound growth rate per year of 47%

For the same period,

* Earning per share has grown from 6.29c to 18.97c i.e. at a compound rate p.a. of 32%

* Dividend pay-out from 1.63c to 5.76c, an annual growth rate of 37%

This compares with an anticipated dividend pay-out of 10c this year.

Calsil's paid up capital is $3,292,005 divided into 6,584,011 shares of 50c each, of which only

* 37% or 2,443,500 shares have been subscribed in cash, and
* 63% or 4,140,511 shares issued to the shareholders as bonus shares from tax-free reserves.

The first bonus issue made in 1969 was six years after the public float of the company, and a further five bonus issues have been made in the ensuing four financial years.

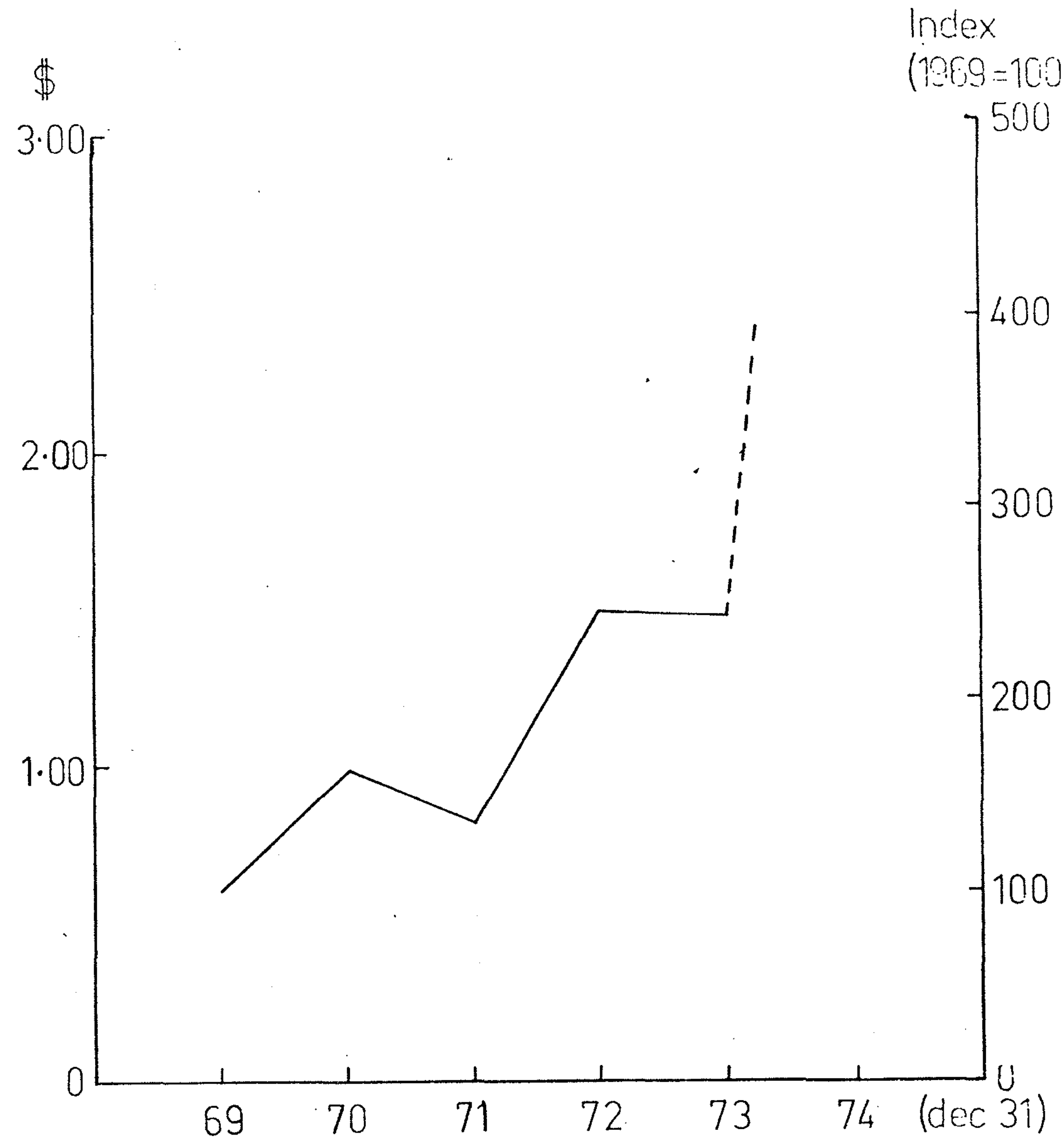
To illustrate what this means in practice, may I enlarge on the Calsil share portfolio of one of our shareholders. He took up an allocation of shares when the company was floated in December, 1963, costing him $640. He purchased on the market additional shares four months later for $200; he took up the two cash issues in May, 1968 and on February, 1969, costing $700. Accordingly, he invested $1,540. The market value of his protfolio at present is in excess of $18,500 and he is entitled - at present rate of dividend pay-outs - to $774 p.a., equal to more than 50% on his invested capital.

Calsil's Corporate Finance Policy

The fore-runner of Calsil Ltd. was Calsil Pty. Ltd., formed in early 1955, which started manufacturing towards the end of November the same year. Hence we are now in our 19th year. In December, 1963, Calsil became public. As the listing requirements were that we must have not less than 200 shareholders and £100,000 paid-up capital, we decided to raise only the difference between our then paid-up capital of £71,577 and the £100,000 and also appealed to our existing shareholders not to apply for shares. The sole purpose of the float was to gain access to the public investor when funds for our planned expansion were needed. The shares were therefore offered to the public at the book-value of six shillings. We have since made only two cash issues to the shareholders - in 1968 and 1969 - both at a small premium.

In our accounts we adopted what we believe to be a realistic policy to appropriate profits in the year they occur. This explains our practice to credit the investment allowances to the benefit of the profit and loss account of the year when it was claimed. In turn, the holding charges for funds raised for expansion are written-off.

Figure 3 - Investment Performance



From the outset, we endeavoured to balance equity financing and borrowing, but at the same time, to limit our calls on the ordinary shareholders. A high operating cash flow, coupled with an earnings retention rate in excess of 50%, plus sufficient cash placements at market values, have enabled us to maintain our equity/debt ratio and still cope with financing rapid expansion.

Calsil has employed cash placements to provide equity funds. We have tried as much as we can to compensate our long-term shareholders for their reduced equity by making numerous bonus issues.

COMPARATIVE FINANCIAL STATISTICS

	EPS c/share	DPS c/share	Investment Performance	Market Capitalisation
			$	$m
Dec 31 1969	6.29	1.63	.61	2.640
1970	10.33	2.76	.98	5.873
1971	8.74	3.64	.82	5.106
1972	10.93	4.27	1.49	9.837
1973	18.97	5.76	1.48	9.746
Mar 31 1974	*	10.00	2.40	15.802

Notes:

EPS: EPS adjusted for bonus and rights issues; calculated from published financial reports; amount is per share outstanding as at March 31, 1974

DPS: actual dividend entitlement, adjusted for bonus and rights issues; amount is per share outstanding as at March 31, 1974; 1974 figure is a forecast based upon recent reports to the stock exchanges

Investment Performance: amount which, if invested on the indicated date, would have accumulated to $2.40 (the value of a Calsil share) by March 31 1974, assuming reinvestment of dividends, and bonus and the theoretical value of rights issues.

Market Capitalisation: number of ordinary shares on issue multiplied by the price per share.

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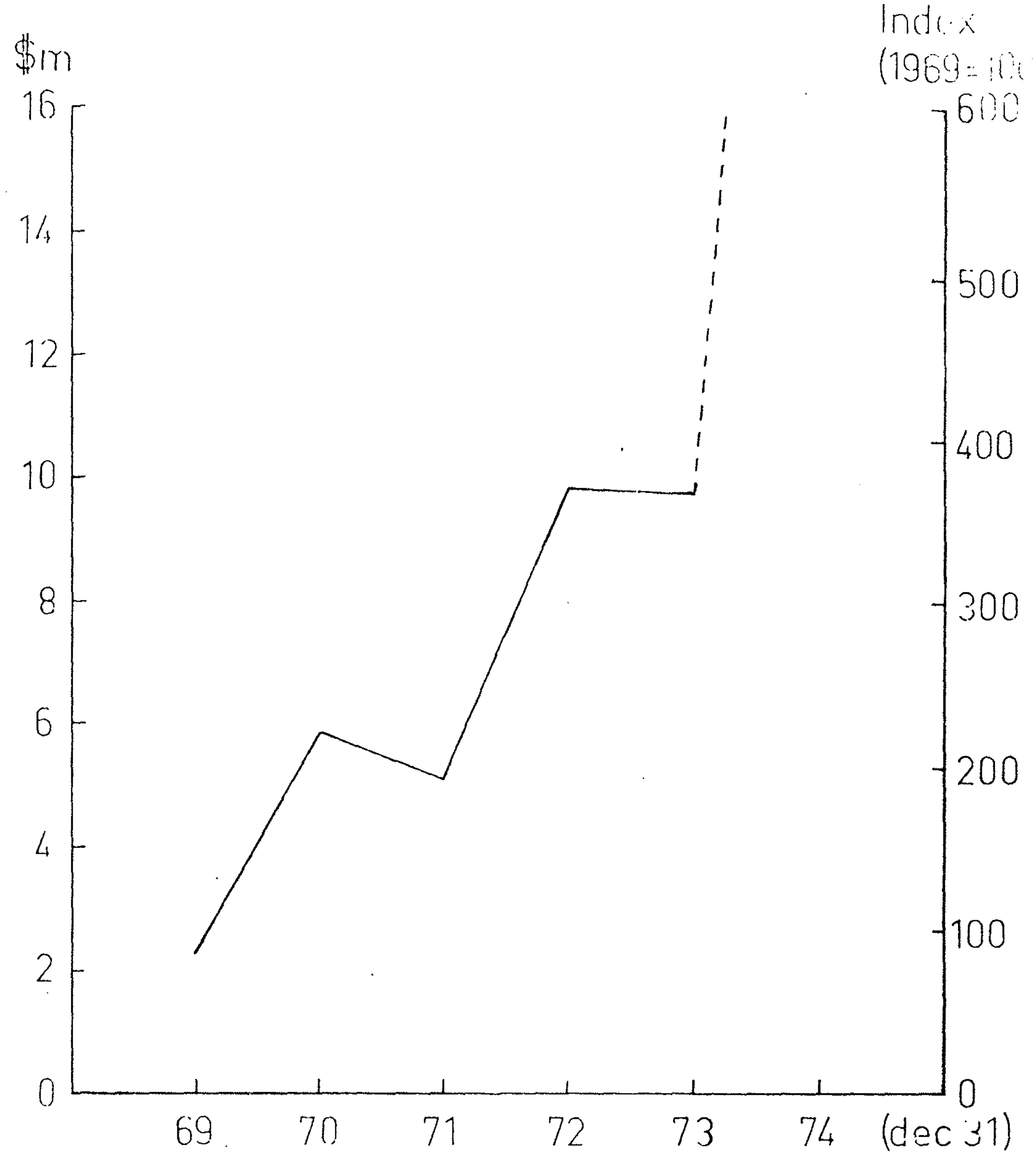
Bonus issues are also our way of expressing confidence in Calsil's future, since we have made bonus issues only after being satisfied we could service the increased capital at at least the same rate of dividend as previously.

In 1971, the company entered into a Trust Deed to facilitate the issue of debenture stock. The Trust Deed simplified the giving of security by the company and has been of assistance in achieving the appropriate debt/equity financing. Under the Deed, Calsil has issued fixed term debentures and given demand security debenture stock to our bankers to cover our accommodation.

In 1973 Calsil made a Convertible Note Issue to shareholders which necessitated the creation of a Notes Trust Deed. I am of the opinion that convertible notes have a place in the financing of our company as the company will ultimately receive a share premium that it would not normally be able to ask of its shareholders, whilst at the same

Figure 4 - Market Capitalisation



time, the shareholders receive a security offering an attractive rate of interest with the opportunity of converting their notes into shares, should this ultimately be to their benefit.

The recently announced Debenture Issue of $2,000,000 will result in secured borrowing being 25% and total liabilities 55% respectively of the total tangible assets. It should be borne in mind that ultimately $1,375,000 of convertible unsecured borrowings, being 18% of our total indebtness, may transfer above the line into shareholders' funds.

Future

I assume that you would like to hear from me of our future plans. There is at present a market for over 2,000 million bricks p.a. in Australia. Hence, ample room for expansion. We believe the pre-fabrication of walls is imminent. In our opinion, future demands will be for pre-fabricated brick panels. We are gearing-up for it.

Summary

Calsil has used all the forms of finance available to companies in this day and age, and we now have the company in a position to quickly arrange the right finance for the right set of circumstances.

Calsil is a manufacturing company. My Board subscribes to the school of thought that the value of a share, or better still, the strength of a company, lies in its earning potential, while the asset backing is of somewhat lesser importance.

If Calsil Ltd. is more successful than average, it is because we produce an exciting product with a modern technology. It is perhaps worthy of note that the Board refrained from being enticed into any mineral or property development projects during the respective booms.

The critics of our corporate finance policy are saying that we can't continue with the constant bonus issues! While inflation continues, however mild it may be, and as long as our company continues to grow, we see no reason to change our policy.

Remember Ladies and Gentlemen that Calsil's corporate finance policy is very strongly orientated towards the shareholder. We are endeavouring to give him the maximum benefits, similar to that he would attempt to get if he were to run his own enterprise. Note, three out of our five board members are foundation directors, each has a large part of his capital invested in Calsil.

We all accept the creeping inflation - which at present has considerably quickened - and isn't it therefore our duty to protect our shareholders by constantly revaluing THEIR HOLDINGS AND UPGRADING THEIR RETURNS?

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