

# REVIEW 2010

## Summary

For the year ended 30 September 2010 HGL reports an increase in underlying profit to \$6.8 million (2009: \$5.0 million) and an increase in reported profit to \$13.4 million (2009: \$8.0 million). Our balance sheet is strong and with net cash of \$2.0 million (2009: net debt \$13.4 million) we are well placed to fund further growth.

The 2010 financial year has been one of achievement. The change of strategy has been implemented and is yielding pleasing results. With the sale of all listed shares the transformation to being a supplier of market leading branded products for specialist markets has been completed.

## Business approach

HGL continues to source market leading branded products for specialist markets. The fragmented nature of the specialist markets and the strength of the brands enables us to retain more pricing power than if we were selling to large dominant customers. Mass market consumer brands are unlikely to be distributed as the gross margins tend to be lower, the marketing expenditure higher and the market dominance of several customers too great.

We sell into specialist markets and maintain close focus through having discrete business units for each market. Through adopting a decentralised model we are able to have a better understanding of the products and future trends within each market. Each business unit focuses on a specialist market and strives for higher levels of customer and supplier satisfaction. HGL's approach facilitates rapid response to changes in tastes and demand together with speedy adoption of new products and technologies. The markets, brands and business units are described on pages 6 to 10.

HGL builds the value of brands for the long term benefit of customers, suppliers, employees and shareholders. The value of a brand is increased by growing sales; in brief this is achieved by investing in the training of our staff and in properly targeted advertising and marketing support. We aim to excel at representing our brands and to be the first choice distributor in our markets.

The strategy for continued growth includes gaining new product agencies in existing and adjacent markets. The purchase of additional business units in new markets will also occur when the brands and the people meet our rigorous criteria. Most importantly we continue to improve internal processes to generate additional sales and a lower cost.

## SUMMARY OF RESULTS

	2010	2009
	\$millions	\$millions
Underlying profit	6.8	5.0
Other	6.6	3.0
Reported profit	13.4	8.0

	cents	cents
	per share	per share
Underlying profit	13.3	10.0
Other	13.0	6.0
Reported profit	26.3	16.0

Gearing*	0%	14%
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\* Net debt : net debt plus equity

## DIVIDENDS

	cents	cents
	per share	per share
Interim	6.0	3.0
Final	5.0	5.0
Total	11.0	8.0

first choice distributor in our markets

market leading branded products for specialist markets

focus sharpened by business units for each market

## SUMMARY OF TRADING RESULTS

	2010	2009
	\$millions	\$millions
Sales	170.1	164.7
Cost of goods sold	(93.5)	(95.1)
Gross margin	76.6	69.6
Expenses	(61.5)	(58.5)
Business EBIT	15.1	11.1
Gross margin %	45.0	42.3

## Financial summary

The financial performance for the year ended 30 September 2010 is summarised as follows:

- Underlying profit after tax increased by 36% to \$6.8 million (2009: \$5.0 million) being 13.3 cents per share (2009: 10.0 cents per share).
- The profit on items excluded from underlying profit was \$6.6 million (2009: \$3.0 million). This profit largely arose on the sale of listed shares. All listed shares have been sold.
- Fully franked dividends per share of 11.0 cents (2009: 8.0 cents).
- Sales increased by 3% to \$170.1 million (2009: \$164.7 million).
- Underlying business earnings before interest and tax (EBIT) increased by 36% to \$15.1 million (2009: \$11.1 million).
- At the end of September 2010 capital employed was \$74.7 million (2009: \$71.9 million). The EBIT to capital employed ratio was 20.2% (2009: 15.4%) and has returned to a level above our internal hurdle rate of 20%.
- Dividend income from listed shares declined to \$0.2 million (2009: \$0.9 million) due to the sale of the listed shares during the year.
- Net interest expense declined to \$0.7 million (2009: \$2.0 million) as debt has fallen.
- The operational cash flow combined with \$13.1 million from the sale of listed shares has resulted in net cash of \$2.0 million at 30 September 2010 (2009: net debt \$13.4 million).
- After tax underlying return on equity of 9.7%.

## Trading summary

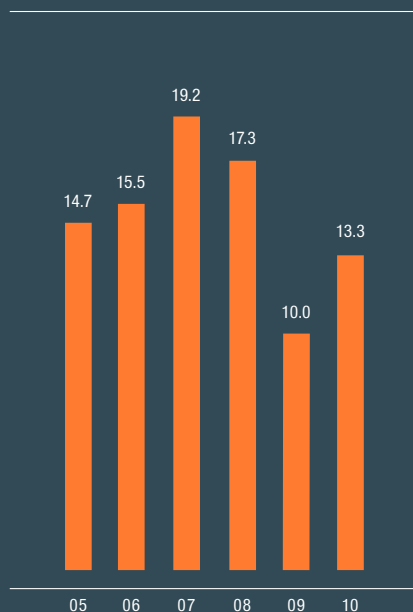
The trading results are summarised in the table on the left. The year can be divided into three distinct periods:

- In the three months to 31 December 2009 the economy benefitted from the government's stimulus measures. Sales and profits were very strong in this quarter.
- In the six months ended 30 June 2010 customer sentiment was patchy and unreliable. Monthly sales and consequently profits were lower than in the first quarter.
- As the last quarter of the financial year progressed customer sentiment improved and with it sales and profitability.

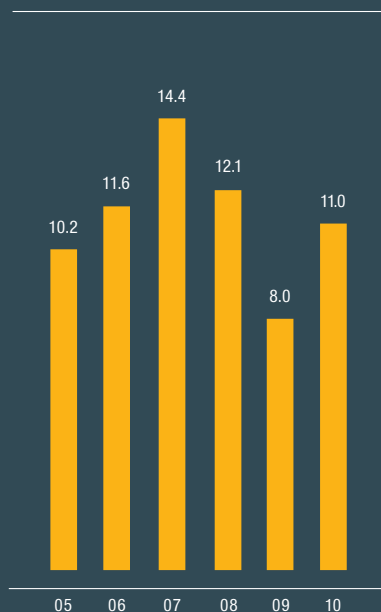
Compared to the prior year sales increased in most of our markets. The exceptions were large format printing, where we ceased selling a product range with a gross margin of only 15% and annual sales of \$4 million, and in collector model cars where severe production delays in the second half of the year reduced sales of new models by \$3 million compared to 2009.

As the majority of our products are purchased in US dollars a strengthening US\$ exchange rate will, all other things being equal, reduce our costs. The US\$ exchange rate strengthened over the year with an average of 90 cents during 2010 (2009: 74 cents). As our competitors have received the same benefit market forces tend to result in the lower product costs being passed onto consumers and retained by suppliers. Likewise when the US\$ exchange rate weakens market forces tend to allow price increases to customers and price reductions to be negotiated with suppliers.

**UNDERLYING EARNINGS  
PER SHARE - CENTS**



**DIVIDENDS  
PER SHARE - CENTS**



**SUMMARY OF UNDERLYING PROFIT**

	2010 \$millions	2009 \$millions
Business EBIT	15.1	11.1
Dividend income	0.2	0.9
Net interest expense	(0.7)	(2.0)
Underlying profit before tax	14.6	10.0
Taxation	(4.3)	(2.5)
Minorities	(3.5)	(2.5)
Underlying profit after tax	6.8	5.0

The gross margin increased to 45.0% (2009: 42.3%). This improvement was created by a combination of a shift to higher margin products and retaining part of the benefit of lower product costs.

Expenses were well controlled; 65% of expenses are associated with employees. In the second half of the year the number of employees increased by 40 to 480 to support new product agencies obtained during 2010 and for growth opportunities planned for 2011.

Two key financial performance measures are the EBIT to sales ratio and the EBIT to capital employed ratio. The EBIT to sales ratio measures how much of each sales dollar is flowing through to profit and the EBIT to capital employed ratio ensures prudent growth and working capital management. The EBIT to sales ratio increased to 8.9% from 6.7%, an aim for 2011 is for this ratio to improve further. The EBIT to capital employed ratio increased to 20.2% (2009: 15.4%) returning above our internal target rate of 20%.

Six of the business units are owned in conjunction with management and minority interest increased to \$3.5 million (2009: \$2.5 million) as the profits increased. HGL now typically owns 100% of the larger business units and this is envisaged to be the more likely future direction.



is pursuing organic growth and growth by acquisition. If you know of a brand or a business that may be of interest to HGL please contact **Michael Mahoney** or **Andrew Whittles** on (02) 9221 7155 or michaelmahoney@hgl.com.au or andrewwhittles@hgl.com.au

A selection of the brands we represent are on the pages 6 to 10 and our acquisition criteria are summarised below.

#### ACQUISITION CRITERIA

##### › Pre-tax profit of \$2.0 million to \$5.0 million

HGL is seeking established businesses with a track record of profitability. Businesses with less than \$2.0 million of pre tax profit are of interest where the business can be integrated into one of our existing operations. HGL targets a long term return on capital employed of 20%.

##### › Business type

Importers and distributors of branded products for specialist markets, these may include a small element of light manufacturing.

##### › Fees

HGL will pay an appropriate fee where a successful transaction occurs.

#### Foreign exchange management

HGL sells products where most of the medium and long term exchange fluctuations can be borne by our customers and suppliers. To provide sufficient time for operational adjustments to occur a combination of foreign currency bank accounts and foreign exchange contracts are utilised.

#### Profits excluded from underlying profit

The disposal of the remaining listed shares generated a profit after tax of \$6.6 million and cash of \$13.1 million. Last year the listed shares generated a profit after tax of \$3.0 million. There are no listed shares remaining.

#### People and the environment

Our success can be attributed to our highly skilled and motivated employees who have an extensive knowledge of our customers, suppliers and markets. The board thanks each of the employees for their efforts during the year.

Although operating in low risk environments there is a high level of awareness concerning occupational health and safety, there is no complacency. An overriding theme is "safety first".

In October 2010 Mr Kevin Eley retired as Chief Executive Officer after very ably managing the company for over 25 years. We are indebted to Kevin for handing over the company well placed to strengthen its earnings and growth. Kevin will continue as a non executive director. Mr Michael Mahoney, the Chief Operating Officer and a primary driver of the current business strategy, is the new Chief Executive. Michael has also accepted an invitation to be a director. Michael's thorough knowledge of HGL will assist in the implementation of the business strategy.

HGL is part of a community and although the operations have limited environmental impact, the consequences of business decisions on the environment are considered. More sustainable products with a smaller environmental footprint satisfying the demands of their customers continue to be introduced.

#### Funding and capital management

The group has net cash of \$2.0 million. The central bank facility which is available to fund both working capital and acquisitions is \$10 million (2009: \$24 million) with a maturity date in December 2012. At 30 September 2010 none of this facility was utilised. As the debt of the group has fallen we have reduced the size of the bank facility. Management continue to meet the bankers several times a year, so if an increase in the facility is necessary, the groundwork has already been performed.

The present capital management policy is to employ the net cash together with prudent borrowings into additional agencies and new business units when they are identified.

## Balance sheet

The balance sheet remains strong with net cash of \$2.0 million. The principal change compared to last year is a \$14 million reduction in financial assets due to the sale of the remaining listed shares with the cash being used to repay debt. Debtors increased due to higher sales in September 2010 and inventories fell. Last year's annual report commented on the increase in inventory at Biante and it is pleasing that part of the overall inventory decline was the result of collector model cars in Biante reducing by 40%.

## Dividends

The policy of the Board remains to pay out between 70% and 80% of underlying profits as dividends. The final dividend for 2010, payable on 16 December 2010, will be 5.0 cents (2009: 5.0 cents) per share fully franked bringing the total dividend for the year to 11.0 cents (2009: 8.0 cents) per share fully franked. The dividend represents a payout ratio slightly in excess of 80% (2009: 80%) of underlying profit.

## Outlook

The current demand for our products and our internal improvements lead to optimism about the year ahead. It is still too early to predict with any accuracy the profit for the 2011 financial year. At the Annual General Meeting in February 2011 the first quarter's trading will be reviewed.

With no debt and a sound strategy the HGL Board is confident about the long term future of the company.

24 November 2010



**Peter Miller**  
Chairman



**Michael Mahoney**  
Director and Chief Executive

## FINANCIAL GOALS

Our financial goals for 2010 were:

- increase gross margin dollars;
- control expenses;
- increase business EBIT;
- control working capital;
- maintain conservative borrowings; and
- increase the dividend.

These goals were achieved and remain the same in 2011.

# Large Format Printing

Sales \$60m



**Anitech** - distributes large format printing solutions to the sign, advertising, point of sale, architects, engineers and construction markets as well as associated consumables and services. Provides third party maintenance and service support for a wide variety of computer based equipment. The business is based in Sydney and has branches in all major Australian cities. Mr Chris Wagstaff is the Chief Executive. The management team own 50% of the business.

[www.anitech.com.au](http://www.anitech.com.au)



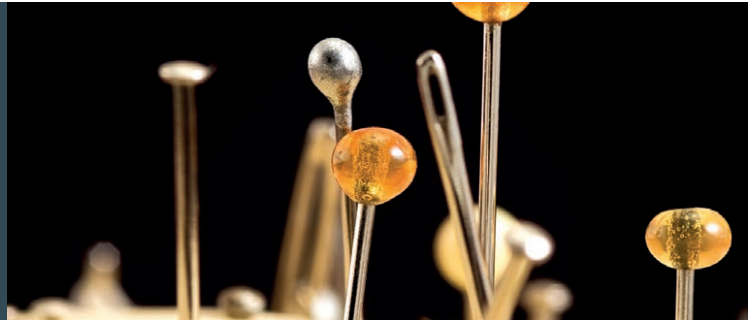
**Aarque Group** - an independent supplier of large format and small format copying and printing solutions, consumables and service. The head office is in Auckland with offices throughout New Zealand. Mr Peter Bult is the Chief Executive. The management team own 50% of the business.

[www.aarque.co.nz](http://www.aarque.co.nz)    [www.frontline.co.nz](http://www.frontline.co.nz)



# Home Sewing and Craft

Sales \$20m



## LEUTENEGGER

ESTABLISHED 1891

**Leutenegger** - supplies quality imported fabric and haberdashery brands as well as designing its own Beutron and Make it collections. Exclusive agencies include DMC, Prym, Zweigart and Robert Kaufman. Leutenegger continues to be the pace setter in the home sewing market. The business is based in Sydney. Mr Chris Roche is the Chief Executive.

[www.leutenegger.com.au](http://www.leutenegger.com.au)



**XLN Fabrics** - imports and distributes quality home sewing fabrics. Exclusive agencies include Marcus Brothers, Benartex, Westminster and Free Spirit. The business is based in Sydney. The Chief Executive is Mr Vince Parry. The management team own 50% of the business.

[www.xln.com.au](http://www.xln.com.au)

ADORNit<sup>®</sup>  
just sew



Benartex  
Fabric for quilters. By quilters.

BEUTRON

Blue Hill  
FABRICS

country threads



Free Spirit

Henry Glass & Co.

[make it]<sup>®</sup>

makower

MARCUS  
FABRICS

one·duck·two



Riley Blake  
DESIGNS

ROBERTKAUFMAN  
FABRICS

ROWAN



Shannon Fabrics, Inc.  
Making The World A Softer Place

S.T.U.D.I.O. fabrics

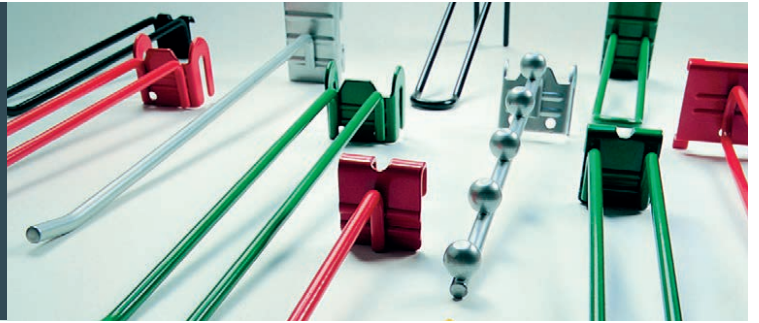
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WESTMINSTER  
FIBERS  
Lifestyle Fabrics

# Point of Sale

Sales \$28m



## SPOSgroup

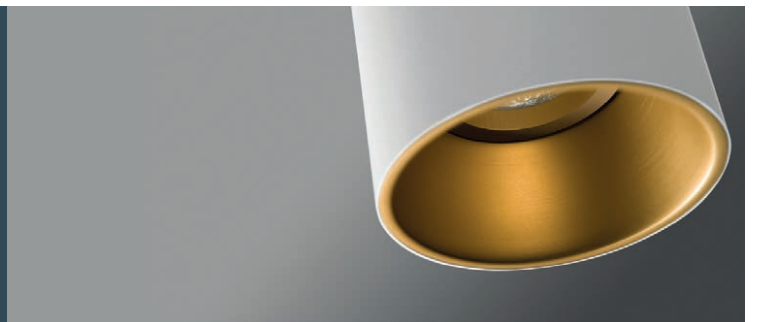
**SPOS** - a leading provider of marketing and retail solutions in Australia and New Zealand, creating and supplying effective point-of-sale materials designed to enhance the overall appearance of the products in-store and ultimately stimulate sales. SPOS includes 3 divisions: SPOS Retail, icandy Creative and Propel Interactive. The head office is located in Sydney with offices in Norwest, Melbourne and New Zealand. The Chief Executive is Mr David Evans.

[www.spos.com.au](http://www.spos.com.au)   [www.icandycreative.com.au](http://www.icandycreative.com.au)  
[www.propelinteractive.com.au](http://www.propelinteractive.com.au)



# Top End Lighting

Sales \$18m



**JSB Lighting** - supplier of architectural specialist lighting equipment for the commercial market its world class brands include Modular, LTS, ACDC and Brick In The Wall. Also supplies lighting control solutions from Lutron and Sensor Switch. The business is based in Sydney with sales offices in Melbourne and Adelaide. The Chief Executive is Mr Dudley Hewitt.

[www.jsblighting.com.au](http://www.jsblighting.com.au)   [www.jsbcontrols.com.au](http://www.jsbcontrols.com.au)



# Eye Testing Instruments

Sales \$12m



**BOC** - imports and distributes ophthalmic equipment to retail optometrists, ophthalmologists and laboratories. Agencies include Nidek, Optovue and Righton. BOC continues to expand based on excellent customer service and increased penetration of the ophthalmology market. The business is based in Sydney. Mr Tony Cosentino is the Chief Executive. The management team own 50% of the business.

[www.bocinstruments.com.au](http://www.bocinstruments.com.au)

MAGNON



optovue

Reichert®

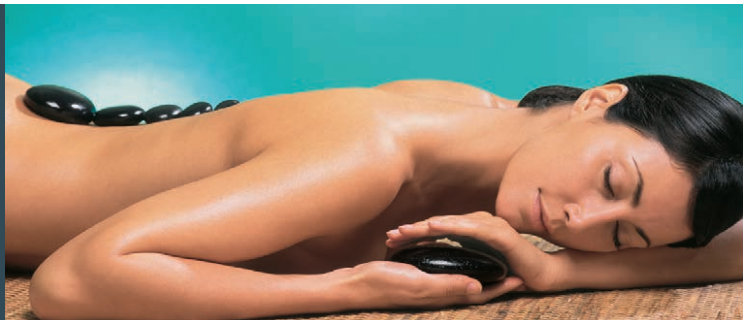
Righton

WelchAllyn®

Advancing Frontline Care™

# Beauty

Sales \$11m



**BLC.**  
COSMETICS

**BLC Cosmetics** - is the exclusive distributor of leading beauty and skin care brands in Australia and the South Pacific. Thalgo the company's heritage skincare brand remains the key product line in salons, day spas as well as spas at leading hotels and resorts with the Terrake brand found at only the most luxurious properties. Essie continues its growth in the Australian marketplace and adds Myer to the growing distribution channel of retail stores, salons and nail bars. The boost in popularity of natural and organic skincare has resulted in Grown gaining market share in pharmacy and department store channels. In 2010, whilst reviewing opportunities to capture niche segments of the skincare market VitaMan was added to the portfolio to address the specific needs of men's skin care. The business is based in Sydney with offices in Melbourne and Brisbane. Mr Gavin Caganoff is the Chief Executive. The management team own 40% of the business.

[www.thalgo.com.au](http://www.thalgo.com.au)

essie

GEHWOL®

ORGANIC BEAUTY  
**GROWN**®  
BOTANICAL ALCHEMY

THALGO  
LA BEAUTE MARINE

TERRAKÉ

VITAMANN

# Collector Model Cars

Sales \$10m



## BIANTE™ MODEL CARS

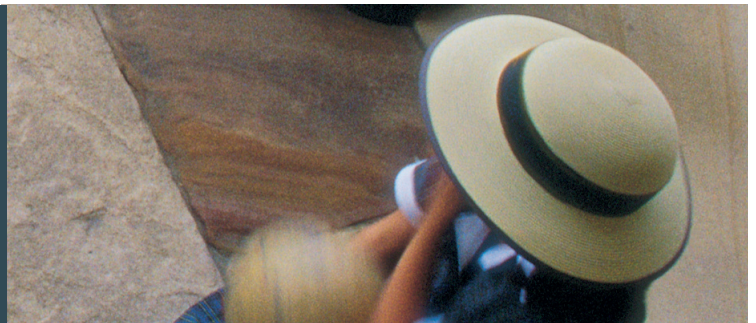
**Biante** - Australia's leading distributor of diecast collector model cars. The cars are scale replicas designed in Australia and made in world class factories. The Biante brand continues to be heavily promoted and this year it continued the V8 arena with prominent exposure at both Bathurst and Homebush. The design centre is located in Perth with sales offices in Sydney and Perth. The Chief Executive is Mr Chris Roche.

[www.biante.com.au](http://www.biante.com.au)



# Specialist Headwear and Uniforms

Sales \$10m



Est. 1835

**Mountcastle** - imports, distributes and manufactures specialist headwear and uniforms. It is the market leader in supplying contract headwear to organisations such as the police, defence forces and schools. The business is based in Brisbane. The Chief Executive is Mr James Baldwin. The management team own 50% of the business.

[www.mountcastle.com.au](http://www.mountcastle.com.au)



## BALANCE SHEET

AS AT 30 SEPTEMBER 2010

	CONSOLIDATED	
	2010	2009
	\$'000	\$'000
<b>Current Assets</b>		
Cash and cash equivalents	8,432	8,126
Trade and other receivables	31,589	29,651
Inventories	33,322	33,368
Current tax assets	-	1,121
<b>Total Current Assets</b>	<b>73,343</b>	<b>72,266</b>
<b>Non-current Assets</b>		
Investments accounted for using the equity method	1,749	2,235
Other financial assets	2,011	15,924
Property, plant and equipment	11,842	10,530
Intangibles	27,394	27,489
Deferred tax assets	3,716	2,371
<b>Total Non-current Assets</b>	<b>46,712</b>	<b>58,549</b>
<b>Total Assets</b>	<b>120,055</b>	<b>130,815</b>
<b>Current Liabilities</b>		
Trade and other payables	20,697	21,245
Borrowings	3,117	2,477
Current tax liabilities	2,951	-
Provisions	3,905	3,865
<b>Total Current Liabilities</b>	<b>30,670</b>	<b>27,587</b>
<b>Non-current Liabilities</b>		
Borrowings	3,296	19,016
Deferred tax liabilities	-	673
Provisions	1,453	987
<b>Total Non-current Liabilities</b>	<b>4,749</b>	<b>20,676</b>
<b>Total Liabilities</b>	<b>35,419</b>	<b>48,263</b>
<b>Net Assets</b>	<b>84,636</b>	<b>82,552</b>
<b>Equity</b>		
Issued capital	34,479	33,678
Reserves	1,943	9,235
Retained earnings	33,307	25,474
<b>HGL Limited Equity Interest</b>	<b>69,729</b>	<b>68,387</b>
<b>Non Controlling Interest</b>	<b>14,907</b>	<b>14,165</b>
<b>Total Equity</b>	<b>84,636</b>	<b>82,552</b>



HGL Limited ASX CODE > HNG

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## PROFIT AND LOSS STATEMENT

FINANCIAL YEAR ENDED 30 SEPTEMBER 2010

	CONSOLIDATED	
	2010 \$'000	2009 \$'000
Sales revenue	170,067	164,653
Cost of sales	(93,497)	(95,089)
Gross profit	76,570	69,564
Other revenue	10,887	7,594
Share of associates' profit	484	397
Sales, marketing and advertising expenses	(25,055)	(22,837)
Freight and distribution expenses	(7,116)	(6,765)
Administration expenses	(25,373)	(24,800)
Occupancy expenses	(4,614)	(4,351)
Impairment of available for sale assets	-	(1,665)
Fair value of interest rate swap	-	(651)
Finance costs	(1,229)	(2,502)
<b>Profit before income tax expense</b>	<b>24,554</b>	<b>13,984</b>
Income tax expense	(7,211)	(3,515)
<b>Profit for the period</b>	<b>17,343</b>	<b>10,469</b>
Attributable to:		
Equity holders of the parent	13,416	7,972
Non controlling interest	3,927	2,497
	<b>17,343</b>	<b>10,469</b>
	CENTS	CENTS
Basic earnings per share	26.3	16.0
Diluted earnings per share	26.3	16.0

### Reconciliation of underlying profit before interest, tax and non controlling interest to net profit after tax:

	CONSOLIDATED 2010			CONSOLIDATED 2009		
	UNDERLYING PROFIT \$'000	OTHER \$'000	CONSOLIDATED \$'000	UNDERLYING PROFIT \$'000	OTHER \$'000	CONSOLIDATED \$'000
Underlying profit before interest, tax and non controlling interest	15,365	-	15,365	11,945	-	11,945
Realised profit on sale of listed securities	-	9,373	9,373	-	6,039	6,039
Write off lease incentive	-	(239)	(239)	-	-	-
Acquisition discount	-	761	761	-	-	-
Disposal of controlled entity	-	-	-	-	(316)	(316)
Movement in equity liability	-	-	-	-	584	584
Revaluation of available for sale assets	-	-	-	-	(1,665)	(1,665)
Interest income	523	-	523	550	-	550
Interest expense	(1,229)	-	(1,229)	(2,502)	(651)	(3,153)
Net profit before tax	14,659	9,895	24,554	9,993	3,991	13,984
Income tax expense	(4,306)	(2,905)	(7,211)	(2,493)	(1,022)	(3,515)
Profit after tax	10,353	6,990	17,343	7,500	2,969	10,469
Non controlling interest	(3,586)	(341)	(3,927)	(2,497)	-	(2,497)
Profit after tax and non controlling interest	6,767	6,649	13,416	5,003	2,969	7,972

Revenue is predominately derived, in Australia, from supplying branded products into niche markets. Approximately, 9% of revenue is derived from providing maintenance and repair services. Revenue from no single customer is greater than 10% of the Group's revenues. There were no intersegment sales during the year (2009: \$nil).