Fletcher Building sees no Australia housing rebound for two years

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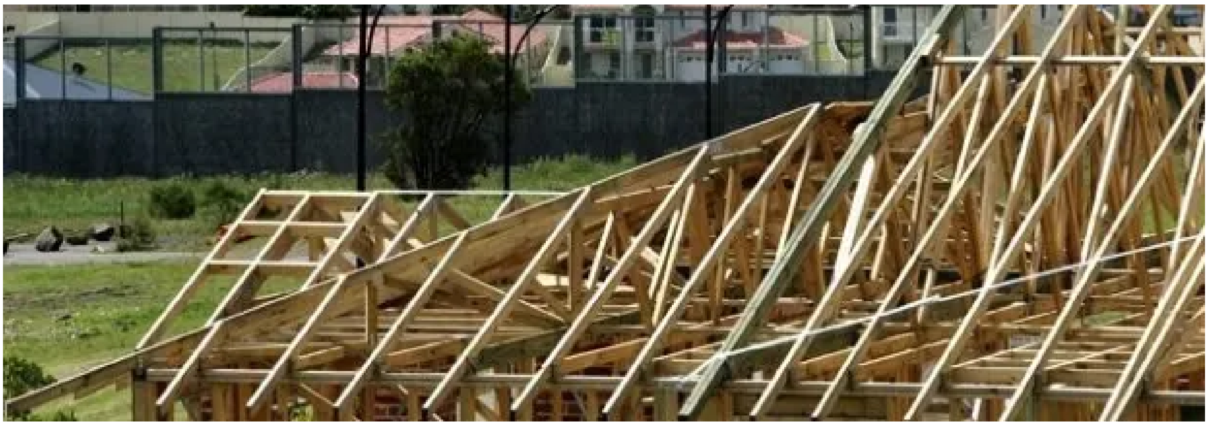
KEY POINTS

- Fletcher Building CEO Ross Taylor says the Australian residential construction market won't begin to show an improvement until 2020-21.
- He says interest rates are already so low that more cuts by the RBA aren't likely to deliver much in the way of fresh momentum.
- The Australian building products arm, which makes revenues of $3 billion, needed an "intervention" after years of poor performance.

Fletcher Building chief executive Ross Taylor says the Australian housing construction market won't begin to recover until 2020-21, and more cuts in interest rates are unlikely to drive a quicker rebound.

Fletcher's Australian building products operations generate about $3 billion in annual revenue, but he labelled their performance as "disappointing" in a soft market as he stepped up plans to rip $100 million in costs from the local unit.

Fletcher's Australian operations include Tradelink plumbing and bathroom supplies, Iplex pipes, Rocla concrete, Stramit steel products, Tasman Sinkware and Fletcher insulation.



Fletcher Building Ltd generates about $3 billion in annual revenues from its Australian building products business. **Photo: Rob Homer**

Fletcher expected Australian residential approvals to drop to between 150,000 amd 160,000 in 2019-20, from 190,000 in the year ending June 30. Approvals would then experience a marginal improvement to 170,000 in fiscal 2021 before a rebound to 200,000 in the year ending June 2022.

"That feels about right," Mr Taylor said on Wednesday. Talks with builders and other market players suggested similar views but the bottom hadn't been reached yet in a market still contracting.
Rival building products group CSR was more circumspect, with soon-to-depart managing director Rob Sindel saying on Wednesday it was too difficult to predict the timing of any upturn in housing construction.

He told the CSR annual meeting that volumes in the building products business in April and May hadn't shown any pick-up compared with the March quarter. But cuts in interest rates, better credit availability as banks revamped lending criteria and the fact that policy on negative gearing and capital gains tax remained the same after the federal election meant there was more optimism that demand would eventually rise.

Mr Taylor was much more direct and said interest rates were already so low, the impact of any further cuts by the Reserve Bank of Australia wouldn't deliver a sharper improvement.

"It can't hurt, but I'm not sure it's a major driver," Mr Taylor said.

"Interest rates are pretty low as it is."

Mr Taylor did however say that the May 18 election victory by Prime Minister Scott Morrison had contributed to some improvement in sentiment in the industry.

"Post election, the sentiment is certainly better out there."

Fletcher, which has just finalised the sale of its Formica laminates business to Dutch industrial group Broadview for NZ$1.185 billion ($1.13 billion), also announced a NZ$300 million share buyback on Wednesday.

Mr Taylor said Fletcher's New Zealand commercial construction arm, which lost its way 18 months ago after serious cost blowouts on some big NZ projects triggered NZ$1 billion in writedowns, would now begin bidding again on commercial building projects as industry margins improved.

But he said poor business discipline in the Australian building products division and weaker market conditions meant the Australian unit would deliver a poor result for 2018-19 of earnings before interest and tax of just NZ$55 million. It would deliver a weak 2 per cent EBIT margin.

Mr Taylor said the group's Laminex and Stramit units were heavily skewed to the residential housing market and had felt the brunt of the tougher conditions. All of the Australian building products businesses were now under one management structure, and about 60 per cent through a cost-cutting program to pull out $100 million in costs by 2020-21.

"There were no sacred cows in approaching it this way," Mr Taylor said.

Self-Help

The Australian business was expected to achieve "modest" profit growth in 2019-2020 despite the weaker overall market as the internal improvements gathered speed.

"We can deal with the self-help issue," Mr Taylor said.

He is targeting 7 per cent EBIT margins in the Australian business in the medium-term.

"It really is upside rather than downside in where we're going."

Fletcher is dual-listed on the New Zealand and Australian stock exchanges.

The heavy restructuring of the Australian operations had been prompted by a realisation than an "intervention" was needed after years of underperformance.

"We just can't keep doing the same things over here," Mr Taylor said.

Australian residential housing starts hit 230,000 in 2017-18 and Fletcher projects they are likely to return to that level again in 2022-23.

Fletcher shares on the ASX have risen by about 12 per cent since mid-March, but are still only half the value they reached in late 2016 of $9.80.

The company was forced into a $710 million-plus capital raising in late April, 2018 to bolster its balance sheet after it hit strife with the big commercial building writedowns in New Zealand.

Mr Taylor said on Wednesday the circumstances were very different for Fletcher when it raised capital last year, and conducting a share buyback just 14 months after, was recognition that the company was headed in the right direction now.

"The company was in a very different place," he said. The retail price for the entitlement issue in April last year was set at $4.51.

Fletcher revealed three separate cost blowouts in March, July and October of 2017, which sapped investor confidence in the company.

The cost blowouts claimed the scalp of chairman Sir Ralph Norris. Sir Ralph, a former Commonwealth Bank of Australia chief executive from 2005 to 2011, stepped down as chairman last year.

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