# UNEDITED TRANSCRIPTION

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**Start of Transcript**

Operator: Welcome to the Billabong conference call. Joining us is Derek O'Neill, Chief Executive Officer, Craig White, Chief Financial Officer, and Paul Naude, General Manager of North America. We will commence with a short introduction from Derek O'Neill, and then open the call to a question and answer session. Please note that we will be seeking to restrict the call to a maximum time of 60 minutes.

Derek O'Neill: Okay, thanks very much. Good afternoon all, and welcome to the call. Firstly I'll just kick off with a bit of an apology for reporting to the market so late in the day, but we've only really just reached our final agreement, and with things happening all over the world, this was really the only time we could do this. Really, if it's any consolation for any of you, I'm currently over in our office in France, so it's been a bit of an all-nighter for me, but that's okay. We've also got Craig White in our Australian office and Paul Naude in our US office where it's about midnight for Paul as well.

So I'll just look first, just a little bit of housekeeping. We're going to restrict the commentary on this call to today's announcement. So we will not be providing any trading updates, and I'd appreciate if you could restrict your questions to today's announcement. I know that quite a few of you will be keen to get further detail on the strategy, and even beyond this call, but I'm conscious that today is just the start of a process that's likely to run for a couple of months.

With this in mind, and given that we can't talk about our current financial performance, we are looking at the prospect of holding an analyst day in the week -- sometime in the weeks after we report our full-year profit results on 20 August, so definitely we will be getting back to you once we determine the best timing for that analyst day which will be held in Australia.

So moving across to today's announcement. So I trust you may have had a chance to take a quick look at the announcement and the supporting presentation. Together, they provide some of the key transaction details, the strategic overview of our plans, a little colour on the West 49 business and an outline of the key timelines of the deal. There's just a couple of key points worth referencing for anyone yet to view the material.

We already have the unanimous support of the West 49 board, and the support of some key major shareholders, who together represent approximately 55% of the shares on issue. Under the agreed plan of arrangement, we required two-thirds support from voting shareholders to effect the deal, so we are already well on our way to meeting this threshold. In terms of funding, we can proceed under our existing debt facilities, so it is not conditional on financing. Assuming we gain financial support from West 49 shareholders, we expect that the transaction will be EPS accretive in FY2011, and we foresee significant synergies flowing through the business by FY2012 as we work to optimise the vertical brandings.

For us really the way we're looking at it is it's really an opportunity to increase the availability of our brand in a key board sports market. We obviously want to get as close to the consumer wherever we can. Our current mix of product in West 49, the group that's about 15%, and we'll be looking to increase that over time. As mentioned, it's EPS accretive from 2011, which is always a positive. West 49 has always been a key account of ours, and has sat as high as number two by size in the North American business, so it's definitely a key account. It really has an authentic feel compared to some of the other mall-based operators in our sector. They haven't [chased] hard after the home brand story, and therefore haven't suffered maybe some dilution of the customer, and the offer's always been pretty solid, and we were looking for ways to work better with them over a long period of time. Certainly as well, they do operate five Billabong licenced stores in Canada, so we're a significant customer of theirs.

Just to give you a bit of an idea on some of the banners because there is some banners other than just West 49. West 49 itself has 81 doors. West 49 has a real authentic, almost a skate feel, that they touch into surfing and snowboarding as well. They deal with the majority of the brands that are in our sector, and as I said, we've been one of their largest suppliers for a long period of time. The other banners in the group is the Off The Wall chain, which has been primarily more of a girl's offer, but they will be introducing some men's products, 100% branded men's product in the latter part of 2010. They deal with brands like [unclear] Element already, but also across into brands like Roxy, Matix, Hurley, Bench, other brands in the sector, slightly older demographic than the West 49 chain. They have a chain called Amnesia, which is around 18 or 19 doors, and Amnesia's stores are all in malls in Quebec - a little bit of a version - similar to Beachworks that we have operating in Southern California, but probably a little more skate orientated. Probably targeting a slightly younger, 16-type area, but Amnesia is a good addition.

They also have a slightly different one for us, a banner called D-Tox. It's a little more music inspired, very involved with local music scene, lots of licensed products from bands, Pink Floyd, Metallica, maybe a bit of Rolling Stones stuff as well. A lot of more logo-driven product t-shirts, but also deal with brands like Element, Hurley is in there as well, Vans, Converse, and they have a fair concentration of private D-Tox products. Slightly older demographic, probably 18 to 25, a little more like that.

So look, we've provided lots of information, I won't go through the presentation page by page. I know that some of you may not have had a chance to read it all in the short period of time since the release, but I think what I'll do considering our timing, we'll just throw it open to questions.

Operator: We will now begin the question and answer session. Your first question comes from the line of Phil Kimber from Goldman Sachs. Please ask your question.

Phil Kimber: (Goldman Sachs, Analyst) Derek, I was just wondering if you could give a bit of background -- you said it was a number two account in North America, maybe in Canada I assume therefore it's the largest account. Who is the next largest and some commentary on the average store size, whether they're leased, malls, that sort of information.

Derek O'Neill: Look, Phil, mostly the accounts we deal -- well, apart from West 49, all the accounts we deal with up there are private, I wouldn't necessarily split out who was number two in Canada. Just let me give you a bit of an idea. In total in Canada, we probably work with getting upwards towards around 1000 doors in total in Canada. Obviously, West 49, 138, that's a fair chunk of that. It's easily the largest account for us up there, but you know, there's probably close to 600 accounts across the country. It's a strong territory for us. Sales, we haven't split them out before and I don't intend to now, but sales in Canada have been in excess of 10% of North American sales, so it's well into the tens of millions.

We see that -- this is an account that already exists. We think that -- we're not expecting a lot of cannibalisation, we're not expecting a lot of dilution. The fact is that West 49 are already operating in that marketplace, and I think that like when we've bought retailers in other areas, we would like to think that we can co-exist quite well, and keep prices in general at a premium where we can, and try and showcase our products, but we will be leaving them multi-branded.

Primarily, West 49 is a mall-based operator. There are other smaller mall-based operators, with 20, 25 doors in a couple of cases, but mostly close to 600 accounts, we've got 1000 doors around the country, you can see it's a pretty fragmented market.

Phil Kimber: (Goldman Sachs, Analyst) Can I ask then one more on the execution. Retail is going to pretty well get close to 30% of revenue with this acquisition of group revenue. Can you talk a bit about how you manage it globally and then by region, and maybe the speed of information flow, given retail's such a day to day business, yet your heritage is wholesale, how you're managing that transition as you go more into retail?

Derek O'Neill: I think that there's probably a bit of a thought process externally outside of our company that -- you know, we probably should have a global head of retail. I don't think there's even a global head of retail at McDonald's, even if you look at -- McDonald's is probably the closest -- McDonald's or Starbucks is probably the closest global retailer, and ultimately, there's variations in McDonald's even between countries. I think that's really the way we approach retail as well. We're happy to say that -- Sam Baio we've been working with for a long time. Sam's got a lot of strengths, particularly in merchandising, he's a really good retailer.

We think that this will help strengthen our total North American retail team, but it will still operate under its own steam, effectively. It still has to perform. We'll look to integrate some parts of the back end over time, if that's what should happen, but ultimately Sam will report directly into Paul and his team in the North American business, the same as Quiet Flight or Beachworks or Honolua do, just slightly larger in this situation.

Phil Kimber: (Goldman Sachs, Analyst) Okay, that was all, thanks.

Operator: Thank you. Your next question comes from the line of Shaun Cousins from JPMorgan. Please ask your question.

Shaun Cousins: (JPMorgan, Analyst) Hey guys. Just a question in regards to the multiple that you're paying. You've spoken a fair bit about EBITDA, but am I right to say that you guys are paying like a 37 times fiscal 12 multiple, is that right? We haven't had a long time to look at it, but is that right?

Craig White: No, Shaun it's Craig. That's not correct. You're saying fiscal 12, can you just help me understand how you'll be calculating that multiple?

Shaun Cousins: (JPMorgan, Analyst) Yes, the year ended 12 January, I'm looking at Bloomberg that I think says you guys are doing - the company's doing $0.042 per share.

Craig White: Look, I don't obviously have that data in front of me, but the multiple we're paying on the forward FY11 analysts' consensus base is 10.4 times.

Shaun Cousins: (JPMorgan, Analyst) Yes, that's EBIT or EBITDA, what's your P/E multiple that you're paying?

Craig White: It would -- look it certainly is higher than that. I think what I would say is in terms of the overall multiple that we're paying, there's probably just a couple of things just to think about here. One is, you're talking a multiple [for the] existing business [which] obviously excludes any synergies that we will realise, and we expect that those synergies over time will be significant. I think the other you need to bear in mind is that this is a business that historically has traded a lot more strongly. If you look back, say for example the year just prior really to the GFC, the business did EBITDA of just over $13 million compared with around $7 million in the 2010 year.

So when you take a combination of synergies and historical trading performance, the -- it's a little misleading just to look at the, if you like, the analysts' consensus number in isolation. I don't obviously have those Bloomberg numbers that you're looking at so it's difficult for me to comment.

Shaun Cousins: (JPMorgan, Analyst) Yes, I guess just in terms of looking after your own shareholders it looks as though you're paying a fairly full premium for a business here at a much higher multiple, even on an EBITDA basis, relative to what you guys are trading at now.

Craig White: Obviously we've done our homework where, done a lot of financial modelling ourselves, and the synergies that we believe we can realise through this business over time are not insignificant as we seek to grow the vertical links of Billabong's family of brands, and they're a very strong driver of profitability for us going forward.

Shaun Cousins: (JPMorgan, Analyst) Where do you think Billabong will get as a percentage of the sales from the current 15% base now? How you guys are thinking about it?

Craig White: Yes, look, obviously -- and Derek, maybe you'd want to comment as well, but I think it's obviously going to vary by chain. Some of the store banners have lower percents of Billabong brand share, others are higher. But if you look at some of our other stores, the multi-brand stores that we have around the world, the percentage of Billabong family brand share can vary from the mid-40s up to the mid-60s, and that's -- really depends on which job you figure and which banner, but look, I don't think I'm going to be too specific in terms of what that number looks like for West 49 for us going forward.

Derek did you want to comment there?

Derek O'Neill: Shaun, I'll probably be a little more specific than Craig. I think that over a couple of years, 45%, somewhere around there probably wouldn't be a far-off balance. We wouldn't try to go too much higher than that. Obviously there's potentially some opportunity for some further Billabong stores, and that's something that we look at over time. Ultimately, I think that some of the banners as Craig said would support a slightly higher percentage. West 49 may support a slightly higher percentage, but don't expect it to become just a complete store with our own brands.

Craig White: And Shaun, just to comment on your previous point around multiples and so on, at the end of the day, our model, the deal is EPS accretive year one, it exceeds our pre-tax cost of capital in FY12. I think from our perspective, and we're probably being -- try to be reasonably conservative, I think those are pretty strong numbers.

Shaun Cousins: (JPMorgan, Analyst) I guess you just gear up your balance sheet sort of how you can get EPS accretion. Just in terms of Quiet Flight, you've highlighted in the presentation you've made retail acquisitions in the past, can you talk about where you've taken the Billabong brand as a percentage of sales, and how you've gone at delivering cost savings in that business? Because I guess that's our most -- the closest example in terms of what you've done with the retail business.

Derek O'Neill: Look I think that if you take a look at it, Quiet Flight is only one example, we've had Honolua, we've had Amazon in New Zealand, we've got Beachculture in Australia, Two Seasons in the UK, and others. Quiet Flight's a completely different one because it's more of a beach, surf orientated business. I don't think that you could compare really Quiet Flight and West 49, they're in two completely different markets and it'd be hard to compare.

Saying that though, there's no question that we've tried to find a balance of getting further exposure for our brands in Quiet Flight. If any of you have been in those stores, I think that you would see that we've been able to achieve that without throwing the balance and the feel of the stores off, or without making them feel like they're too overbaked in their brands. And that has led to contributions at the bottom line level, albeit that Florida at various times over the last 12 months has had some challenges in particular in the -- you know, probably back to school a year ago, period. I think we're reasonably content with the performance that we've had at Quiet Flight, but there's not a lot of similarities.

Shaun Cousins: (JPMorgan, Analyst) Okay, and the threat of Zumiez, because they've announced they're entering Canada, and there's a bit more skate in this business?

Derek O'Neill: Well, they have announced that they're planning to come into Canada, and we work well with Zumiez. I think we'll continue to work well with Zumiez, and Zumiez will no doubt come in and open some stores there. But I think that we'll compete as we'll have to do, I don't think that Zumiez's recent announcement changes anything for us.

Shaun Cousins: (JPMorgan, Analyst) Thanks very much.

Derek O'Neill: Actually it probably highlights that potentially there's still some opportunity in the Canadian market.

Shaun Cousins: (JPMorgan, Analyst) Great, thanks guys.

Operator: Thank you. Your next question comes from the line of Craig Woolford from Citigroup. Please ask your question.

Craig Woolford: (Citigroup, Analyst) Hi Derek. Can I just start off with a question around the margins within West 49, even if I look back to '08, it looks like it's been a very low margin business at an EBITDA level. Can you just comment as to some reasons why it's had such low profit margin?

Derek O'Neill: I think if you go back a couple more years, they were running EBITDA margins around 6% or 7%, which frankly for a mall-based retailer hasn't been too bad. They're standalone margins, obviously, I did say that they haven't gone too aggressively down the home brand path, but I think there's, like everybody, the last couple of years of the GFC has probably whacked those around a lot. They've had a return to positive margins moving into this year, and in their last reported results, and certainly some of the discussions that we've had with Sam, we think he's got a pretty good plan to increase those margins over time.

Now, at a group level, the benefit of a hopefully rising margin retailer with the additional horsepower of wholesale margins behind it, we think that joined together, this operation can be quite profitable moving forward. So we think that Sam's got a bit of a plan, and we're supporting that, and you should see a steady return to mid to high single digit EBITDA, standalone isolated margins over time, and then with the added benefit of wholesale margins to come on top of that as well.

Craig Woolford: (Citigroup, Analyst) Right. Forgive me if I sound cynical but why would the shareholders of West 49 sell -- I mean on a sales multiple, it's 0.5 times sales, surely they would feel that they can then improve margins themselves before selling out to Billabong?

Derek O'Neill: I think you'd have to ask the shareholders that frankly, I'm not going to comment too much on the way they'll think. We think that it's a pretty compelling offer for them, and -- but I'm not going to really pre-empt which way they would decide. I think that the support of the major shareholders is a key part of this, and ultimately I think that's probably as far as I'll go there. As I said, I don't want to pre-empt which way they'll eventually think.

Craig Woolford: (Citigroup, Analyst) Sure, that's understood. With regards to the businesses they run, can you give a sense of the store sizes? Are they what we typically expect in the US market, or any distinctions there?

Derek O'Neill: Yes, pretty much. General sort of 150, 300, 350 square metre. There's not too much different than your sort of average speciality board sport store than you would see in the US.

Craig Woolford: (Citigroup, Analyst) And to get an EPS accretive outcome in FY11, is that a function of very low cost of debt, or that you expect better EBITDA than the broker consensus that was put in the presentation?

Craig White: Yes, I think Craig, I'll answer that. I think clearly the synergies that we see in this acquisition will be realised over time but you will see those synergies flow through in the first year, so I think that's a significant driver of it. Again, I think we've tried to be balanced in setting what level of synergies we'll achieve, and that's probably the simple driver.

Derek O'Neill: Can I just state over the top of that, just for understanding, you don't want to come in and just change everything overnight. That's the last thing that we want to do. And also there's orders and even production of some of their own products that are in the pipeline, and therefore you just don't want to upset that balance. It's not like we're going to be cancelling any orders or cancelling supplies or anything like that. We want to run this operation as a going concern and look to see where we can add value for both West 49 and for our larger group as well. We can't get either of them out of whack, it's not going to be a case of just forcing products down, because we may then alienate the end customer.

So it has to be a staged modification over time, and that's where the synergistic value starts to really get in ... in the latter part of '011 but definitely starts to kick in a lot more in '012.

Craig Woolford: (Citigroup, Analyst) Okay, but maybe to clarify this EPS accretion in year one, are you incorporating the benefits of the wholesale in margin that would be achieved from the time of acquisition or completion?

Craig White: Yes, I think we are, but I think what Derek's saying, Craig, is that those synergies, you know, there's not a lot [unclear]. There's a lot of order in the system and so on, and as Derek says, you've got to carefully manage the brand mix and the stores. Part of it also is some of the costs we'll save in terms of West 49 will de-list. There's lots of costs associated with being listed. That will go towards that EPS positive result in year one.

Craig Woolford: (Citigroup, Analyst) Cool. Just lastly from the big picture around managing retail, I appreciate the nuances of the different countries means that you do need to act local in managing the retail chain, but how does Billabong at a corporate level keep a handle on inventory management or any major unforseen events that could be quite damaging to profitability if you keep it local and decentralised?

Derek O'Neill: Look, I think we've done a reasonable job at it so far. The inventory comes from, in the main, certainly for the smaller retail chains, the inventory comes from our main holdings, effectively. In the US, we don't necessarily produce too much specific product for our own retail. So it comes from the general line. I think there's -- this gives us the opportunity to start probably looking at it a little different over time, in the sense of should we start adapting and changing, and potentially doing some products specifically more and more for retail. And I think that that's something that could potentially happen over time, I'm not calling that out as a definite, but it's something that’s occupying part of our discussion.

Craig Woolford: (Citigroup, Analyst) Thanks guys.

Operator: Thank you. Your next question comes from the line of Andrew McLennan from CBA. Please ask your question.

Andrew McLennan: (CBA, Analyst) Hi everyone. Just a quick one. I just wanted to clarify the -- at the close of trade in Toronto, the market cap was C$35 million and 53.8 million shares on issue. I'm just wondering, where there any other shares out there, or options, management options et cetera that needed to be taken into account?

Craig White: Yes, Andrew, there are some pref shares. Those pref shares are convertible basically at C$1, so the assumption is they will convert. So that would be counting the majority of the uplift in number of shares. There's a small number of options as well.

Andrew McLennan: (CBA, Analyst) So if we're comparing to the C$0.55 price of the shares we're trading at at the last close, what kind of premium are we talking about, after adjusting for all of the preference shares?

Craig White: I think the way you need to think about this, Andrew, we can talk about that, because it is a substantial premium to the last closing price. You're talking about a company who has a share register that's incredibly tightly held. It's very, very illiquid. And the fact that effectively we have lock-up agreements with such a high proportion of those shareholders, 56% of shareholders committing to the transaction, illustrates to an extent that illiquidity. When you look at average volumes, basically you're talking around, look, over recent days or recent times, about 30,000 shares, and previous to that even lower still.

So it's not -- you know, really, I think a fairer way to look at this is more on a multiple basis of earnings, and then you've got to look at the earnings of the standalone business versus the earnings of the business in our hands. But to look at this as a premium to the last traded price is frankly almost irrelevant.

Andrew McLennan: (CBA, Analyst) Okay. So if we assume that your pre-tax WACC sort of in the vicinity of 12.5% or so, that would imply an EBITDA of around about the C$14 million mark. Is that in the order of what you're anticipating for FY12?

Craig White: Andrew, I'm not going to specifically on the numbers that we've got in our model, that's forward-looking stuff and I don't think it's appropriate to go into the model in that level of detail. I think one thing to remember is that we've announced this transaction, but this is not a completed transaction, it's a public company. And this is basically one stage of the journey.

Andrew McLennan: (CBA, Analyst) Okay, so on that basis, it would be an EBITDA multiple in the vicinity of 7.5 to 8, which compares to Billabong's multiple of 6.7 roughly in FY12. Just wondering whether you anticipate that once all the synergies have played through, that you would actually have it at a -- have acquired this at a lower multiple than that, than the 6.7?

Craig White: That 6.7, is that an analysts' consensus number?

Andrew McLennan: (CBA, Analyst) Yes it is.

Craig White: I would expect that, yes, I think it would be a fair statement to say that we would expect the multiple that we would have acquired the business on would be a lower multiple than Billabong.

Andrew McLennan: (CBA, Analyst) Okay, just to clarify, you mentioned 15% of your sales -- sorry, of the West 49 sales are Billabong. Just excluding the Billabong branded stores, what's that percentage?

Derek O'Neill: I'll take that one. It would drop down into the low teens, but in the West 49 stores, it would probably be up in the high teens, you've got a couple there that we don't do a lot of business in at the moment, particularly D-Tox. We'll look to rebalance a bit of that over time, but that gives you a bit of an idea on -- it's not like we're 30% or 40% or 50% of any one banner.

Andrew McLennan: (CBA, Analyst) Would you take the view that something like D-Tox would be non-core? Would you look to manage yourselves out of any of these brands?

Derek O'Neill: I don't think at this stage we'd be prepared to sort of really make any comment there. Frankly, I think we just need to get in and have a look at the business a little bit more, and understand it a little bit more. I think that -- successful retail can be successful regardless of how much of our product that we have in there, so I think we'll look at it over time. The feel of the store feels pretty good, and ultimately if they perform over time, you know, I don't think we'd look to change too much at all, but I think we'd want to close and get in and begin to take the look at it.

Andrew McLennan: (CBA, Analyst) Okay, thanks very much.

Operator: Thank you. Your next question comes from the line of Richard Barwick from Hunter Green. Please ask your question.

Richard Barwick: (Hunter Green, Analyst) Hi all. How long has this acquisition been in the pipeline?

Derek O'Neill: We worked very closely with West 49. Probably maybe about a year, a year and half ago, West 49 were beginning to talk to us for a lot more specific product that they wanted make for the Canadian market, and I think that at a management level, we started to probably become a little more interested in -- you know, we had a couple of wins with some product that was working well through there. We just started to look at talking to them in a lot of different ways about how we could work closer together.

I don't think it's an understatement to say that there are a lot of retailers around the world, particularly over these last couple of years, that would like to see different ways of working together. And some of that can be us making specific product for them, or doing specific marketing that's more focused around their local customer base, or in this situation, potentially joining together and expanding the opportunities.

So I would say that whilst not specific around an acquisition, we've been really discussing for probably well over 12, closer to 18 months, in ways of just how we can improve our business together. Because we've always had a lot of respect for West 49, and the stores and the authenticity that they've been able to take. Once you're in malls it's definitely -- it's a little more mainstream than a one door speciality customer, but they've done a great job in a sense of not losing that sort of authenticity, and hats off to Sam for that.

Richard Barwick: (Hunter Green, Analyst) Right, I'm just thinking if you go back far enough ago, when you did the capital raising thing, I think you caught a few people by surprise at that time. I'm just wondering if that raising was done to put you in a position for this type of acquisition?

Derek O'Neill: Not specifically, no. I mean, there was a lot of other things that we were dealing with at that time, and we were -- when I say we were beginning to work closely with West 49, really from a -- way more from a product point of view.

Richard Barwick: (Hunter Green, Analyst) Right. I guess the other thing to think about here is -- I mean, the recent acquisitions have all been a very Aussie and US- centric, and I guess I, when I think about your retail expansion - the company owned retail - was then thinking more Asia, South America and Europe, some of the um -- more -- less developed markets, if you like. So how do you marry these acquisitions up with [unclear] talked about in the past is moving, or pushing further into those areas that are less developed?

Derek O'Neill: The difference is in the word acquisition. The fact is that we're still continuing to open stores in Asia. We're still very [fluid] down in Brazil, and we have some fantastic retail down there. We actually have just won a significant Brazilian retail award down in Brazil for our Billabong stores, and they are continuing to happen. But we don't do a ASX announcement for every store we open in Malaysia or something, so it probably just seems that what's coming on your radar screen a little more lately is a couple of these retail acquisitions, and therefore it's probably highlighting it a little bit more.

We've continuously looked at retail as a way to try to attract the new customer where there are no existing retailers, but more and more likely, as you've seen, we've got some retailers that want to talk in a lot of different ways in terms of partnering up. And that can be a factor of credit environment, or some of the trading some of them have seen over the last two or three years, it just leads to various conversations.

I do take your point on the acquisitions side, particularly this one in the number of doors, it's bigger than anything we've done before, so it does create a bit of that impression. But we're still actively searching for ways to get our product in front of the consumer where there are no retailers in South America and Asia in particular.

Richard Barwick: (Hunter Green, Analyst) Yes. I just noticed these guys have got a bit more of a focus within -- or some sort of role within BMX and motocross as well. Has this sort of opened the door for Billabong to then move down that path as well to those categories?

Derek O'Neill: I don't think that as a Billabong brand that we'd be looking to go really down into those parts. I think that you've got to remember in Canada, particularly when you go inland, the kids are skating, they're wakeboarding, they're kite surfing, they're snowboarding, but they're probably also BMX and motocross as well. It's sort of part of the lifestyle, and some of the brands that we have like Nixon, Von Zipper, do cross into some of those sort of territories. I don't think that we necessarily want to go specifically into those categories with any of the existing brands, nor are we really looking at those markets for any specific brand that may come into that group.

Richard Barwick: (Hunter Green, Analyst) That's where my question is stemming more from, Derek, if you'd be tempted down by some specific brands.

Derek O'Neill: No, it's not our focus, no.

Richard Barwick: (Hunter Green, Analyst) Not your focus, okay. Okay, that's all the questions I have, thank you.

Operator: Thank you. Your next question comes from the line of Nick Berry from Nomura Securities. Please ask your question.

Nick Berry: (Nomura Securities, Analyst) G'day Derek. Just following on from the questions relating to margin. To what extent can the profitability of this business via the synergies that you expect to pull out approach that of your existing Americas business? And what is the scope for top line growth in terms of incremental doors?

Derek O'Neill: The last quarter results, our EBITDA margins in retail were running around 14%. I think that we've had them up higher in the past. Some of those are a little bit boosted by some of the better performing stores in Australasia, but I would -- I think it's a fair statement to say that US retail margins have been improving for a while, and therefore we'd like to think that -- Sam is a pretty good operator, it's an experienced team here, and I'd like to think that this chain should deliver retail margins as high as -- over time, as almost anything else would be [unclear] in our retail space in the US.

I'm not sure if that quite gives you the answer you want, but we'd be looking at, over time, all our retail margins begin to pick up. We think that we're getting better at retail - we're not perfect at it by any means - but the retail margin in the first half expanded, whereas our wholesale margins actually contracted slightly. So we do -- I think it's a fair statement to say I think we're getting a little better at it, and we'll look to improve the margin in this operation over time as well.

Nick Berry: (Nomura Securities, Analyst) And how much growth do you think you can get coming through the business in terms of the top line? Can you just give us a feel for what the markets are growing at, and what you think you might be able with West 49?

Derek O'Neill: Well the first store opened in 1995, and there's now 138. The other banners have generally come in from acquisition, but West 49 had strong growth in itself. I don't think I want to try and put two many of the existing customers offside by being targeting how many doors. I think that Sam and his team have definitely indicated that there's still quite considerable growth available in the Canadian market. I think that as I already indicated, Zumiez obviously see that as well.

We just never really hang out to numbers. I might have a go at it when we do our analysts' day, but I think that for the moment, let's try and get closed first.

Nick Berry: (Nomura Securities, Analyst) Yes, no problem. Final one from me, in terms of optimising the vertical brand next, where do you see the biggest opportunities there? Are there any particular categories in terms of growth that you want to change the focus to targeting?

Derek O'Neill: Some of our brands are probably a little underdone. I think that Nixon's really got a lot of opportunity up there in the Canadian market, [unclear] is a strong brand already in North America, and -- but every time in any retail space where we'd put in a lot of time, we'd see immediate results. There's -- it's not out of the question that this could help us probably bring a brand like Tigerlily along quite a bit over time, there's -- you'd be hard pressed to really pull one out. Element and Sector 9 do quite a bit of business up there already, I think it's a little more skate than surf, being based where it is, but we'd look to try and maximise it.

I think that we also recognise that we have an ability to produce product, so while we talk that house brands should never get too big a percentage, the fact is that we could probably do a pretty reasonable job on house brands. I think as well that it's also worth noting that if we end up closing this acquisition, that we'll be a pretty large customer for some of our competitors, and ultimately there may be some benefit in more of a global approach to some of the suppliers that supply West 49, and also Quiet Flight and Two Seasons and Amazon, et cetera. So there's quite a few different areas that I think that we can extract some benefit.

Nick Berry: (Nomura Securities, Analyst) Okay, thanks Derek.

Operator: Thank you. Your next question comes from the line of Grant Saligari from Credit Suisse. Please ask your question.

Grant Saligari: (Credit Suisse, Analyst) Yes, hi. I just wanted to check on your claim first of all on EPS accretion, Derek and Craig, because if I heard correctly to the earlier answer, you're including currently generated wholesale profits in that analysis. Is that correct, or did I misinterpret that?

Craig White: No, so what we'd be saying is incremental to what we have today Grant, the deal is EPS accretive.

Grant Saligari: (Credit Suisse, Analyst) That's surprising, because the business at the moment generates, or incurs, some C$5.5 million of amortisation. If I take that of a C$9 million or C$10 million EBITDA line, keeping in mind the business has ever only generated C$12 million, that was back in '07, it's just hard to see where that EPS accretion comes from. Or again, have I misinterpreted some of the facts there?

Craig White: No, I think that as I said, if you take the business that we're acquiring, you build in some synergies, not a lot in year one, you factor in some cost savings, basically that incremental piece is EPS accretive in 2011 on our numbers.

Grant Saligari: (Credit Suisse, Analyst) Okay, understood. A second question really is on the intent here, because it just strikes me that you might be creating somewhat of a dilemma for yourselves, because to get some material growth out of this business, presumably you'll to open some doors. But this business currently would account for some 15% of the total doors that you distribute to in Canada, so you sort of inevitably head down a track of increasingly competing with your own customers, I must assume that makes them a little bit nervous. Is that dilemma present in your own thinking at all? Or how do you resolve that?

Derek O'Neill: Yes, Grant, it does, but I'll just sort of clarify again. I made the comment earlier that this retailer currently exists. The fact is that if we own it, or someone else owns it, it exists. So the existing customer, you know, unless they opened this door 25 years ago, they've been effectively trading within that market with West 49 for quite a period of time. Ultimately, as I said, we will endeavour to keep premium pricing where possible. We've being co-existing in a number of markets around the world like Japan, New Zealand and others, the UK, with retail that stretches into areas where there are other retailers as well. And I think we've managed to try to find a fair balance.

It's never 100%, there's no question that not all retailers that we deal with are that appreciative of it. But we try to work very hard if they get affected by one of our doors, then we might try and help them out in some way, particularly drive their marketing, or whatever. You have to remember that in this environment, ultimately -- for some retailers - and this is not for West 49, this is just in general - I've talked at length in the past that over the last couple of years that some retailers, instead of buying product that's going to sell out of their store, they buy product that's probably more based on whatever deal they're getting.

Sometimes an account may have had a very effective space for us over a long period of time, suddenly that changes rapidly when we're not prepared to offer huge terms. I think that the retail landscape is changing, and ultimately, the market and the industry will kind of change with it. But I think that, as I said, we'll work hard to try to mitigate any impact of us owning this store that was there last week and will be there next week, we'll work hard at mitigating any real impact that is felt by the rest of the account base where ever we can, and we've done that in many countries so far. It's not an aggressive let's try and eat everything up, it's a let's try and see if we can maximise the consumer that shops in malls in Canada, where we see an opportunity.

Craig White: Yes, Grant, just to add to that, and I think your questions sort of presupposes that the market is fully saturated with stores. We think there's probably a number of opportunities out there where there's opportunities to expand the store banners into space where there is no suitable retailer. So it's not as though we're cannibalising either our existing wholesale sales or competing with a retailer. There are those incremental opportunities.

Grant Saligari: (Credit Suisse, Analyst) I appreciate what you're saying, it just strikes me that you're becoming extremely vertical, and companies that go that route tend to have difficulty balancing some of those competing objectives, but I appreciate what you're saying. That's it from me in questions, thanks.

Operator: Thank you. Your next question comes from the line of Tom Kierath from Morgan Stanley. Please ask your question.

Tom Kierath: (Morgan Stanley, Analyst) Hi guys, could you give me a bit of a sense of the synergies that you're expecting, and I guess compared with the underlying growth that you're expecting for the business? And also a bit of clarity on the debt cost that you're assuming in that calculation?

Derek O'Neill: Tom, I think we're not going to go into details around synergies, as I said this is an announced transaction, it's not a complete transaction. I think the only thing we'd say is it's EPS accretive year one, and it does exceed the group's pre-tax cost of capital in FY12. So -- and as increased synergies start to flow through, so really I can't say anymore than that. And sorry what was your second question?

Tom Kierath: (Morgan Stanley, Analyst) Just the debt costs?

Derek O'Neill: Look, the debt costs, again we don't publicly disclose what sort of margins we've paid, but we would expect to fund in Canadian dollars through our multicurrency facility, and so we'd be basically using Canadian dollar base rate, and adding to that is the margin now, I'll let you assess what sort of margin you think we would pay as investment grade credit.

Tom Kierath: (Morgan Stanley, Analyst) And should we expect any more acquisitions? I think you were pretty much fully penetrated in North America at the moment, I'm just a bit surprised by it. Should we expect anymore?

Derek O'Neill: I think that we've always remained opportunistic. We've done -- if you look through the investor presentation over the years, we've certainly been looking to add business on. This is no doubt a large one, but it's just sometimes amazing who's on the other end of the phone sometimes. So I think that we'll remain opportunistic, I think we're pretty focused on this one right now. We'll look to close, work hard with it, look to make [unclear] opportunities. Don't read that we're opportunistic into too much, but you can't hear the same error, I mean, as I said, sometimes the phone rings, and you go wow.

Tom Kierath: (Morgan Stanley, Analyst) But so these guys --

Craig White: The other thing I'd say Tom, just to clarify, I think we've made some statements about the -- I don't think we've never said never do any more acquisitions, but we've talked more in the context of brand acquisitions, the brand portfolio is increasingly complete. That's not to say that we wouldn't -- you know, if there were suitable opportunities that came along, that we wouldn't seek to add to it, but really we've been talking about it in the context of brand portfolio rather than retail.

Tom Kierath: (Morgan Stanley, Analyst) And just to confirm, so these guys approached you, it wasn't the other way around?

Derek O'Neill: I think it's fair to say that the initial discussion evolved from us doing specific product for them and seeing a few wins, and seeing how we could maximise that, and so it evolved into us finding out if they were ever interested in potentially selling the company and joining up with us.

Tom Kierath: (Morgan Stanley, Analyst) Okay thanks.

Operator: Thank you. Your next question comes from the line of Greg Dring from Macquarie. Please ask your question.

Greg Dring: (Macquarie, Analyst) Yes, Derek, just a question. You talk about partnerships, but in reality, these guys have sold their business to you and become employees?

Derek O'Neill: Now look I think that's --

Greg Dring: (Macquarie, Analyst) So you're taking all the risks?

Derek O'Neill: Sorry I didn't hear the second part, Greg?

Greg Dring: (Macquarie, Analyst) So you're taking all the risks?

Derek O'Neill: Yes, I think that's probably a fair way of looking at it. Ultimately we are buying their business, but we're not going in to steamroll the whole thing and try and strip the guts out of it and run it in a different way, so I still see it as a partnership effectively.

Greg Dring: (Macquarie, Analyst) I guess our perception of your business has been that great brands don't need to control their distribution, but you've got a distribution strategy here that can only get bigger?

Derek O'Neill: That's why I think there's probably time for us to have an analysts' day in September, and we can explain a little more about probably where we're going.

Greg Dring: (Macquarie, Analyst) Yes, but you can just see the vertical plan here starting to take shape, which sort of begs the question, are you guys losing confidence in the independent core board sports retailer in any country you care to name to continue to grow or even sustain sales of your brand?

Derek O'Neill: Well my answer to those both is no, the fact is that I don't see this as a vertical strategy moving forward, because even if it gets closer to 30% of revenue, there's still 70% out there with wholesale, and so it's still a lion's share of our business. Two is that we look at these sort of things in terms of five, 10, 15, 20, 25 years, so I mean I look it in this way, that frankly our ability to continue to get product in front of the consumer over the next 20 to 25 years is assured in the Canadian market, and therefore -- you know, I look at it in that sort of sense.  Frankly if the wholesale marketplace -- you know, I think everyone would agree that a lot of operators over the last couple of years in a restricted credit environment is particular for small businesses.  This is no West 49 comment, but in particular for small businesses, some of them find it tough.

And so we're looking to take a look at a lot of different markets, and see where the markets are likely evolve to.  I think it's a fair statement to say that some wholesalers that are currently in business, that currently own their stores, someone else may own those over the next five years, I think that there will be a bit of a shift and there will be a consolidation.  We'll be part of some of that consolidation, but I suspect that other people in the industry will also be part of that consolidation in the direct to consumer business for any brand, whether you look at sportswear companies or others, it's becoming a part of their business.  It's just a reality of where business is today.

But I don't think it's a -- we are encouraging wherever we can, a wholesale customer base.

Greg Dring: (Macquarie, Analyst) Okay, thanks Derek.

Operator: Thank you.  Your last question comes from the line of [Alex Scarlet from Colonial First Team].  Please ask your question.

Alex Gallard: (Colonial First Team, Analyst) Hi Craig, just wondering if you could give me a bit of colour about the balance sheet.  You've bought the business for C$100 million, and looking at the balance sheet from last year, there's basically C$100 million of assets. Could you just give me more colour about inventory, and maybe the goodwill you're paying for the business, what you think?

Derek O'Neill: Look, I think if you look at the -- we made a comment in the presentation, Alex, that this is a business that does just over C$200 million of revenue.  We think we are probably looking at a lot of the same current earnings which largely reflect a business operates with the majority on a retail margin only, but effectively the price represents a replacement cost for stores. So notwithstanding the fact that the premium of the last traded price looks high, and the multiple based on the analysts' consensus, which obviously excludes the synergies, we think that the actual tangible asset value of the business we're acquiring is high relative to what we're paying.

Alex Gallard: (Colonial First Team, Analyst) And just one more quick question, how long are Sam and the management team are actually locked in?

Derek O'Neill: Well they've basically signed a lot of arrangements with us under this plan of arrangement. The board has -- the West 49 board has certain fiduciary rights, but effectively if this deal progresses, then they'll have committed to lock up.

Alex Gallard: (Colonial First Team, Analyst) Okay, thank you.

Derek O'Neill: Thank you. Alright, that's an hour up, hopefully we've covered most of your questions. As I said, we do intend to have an analysts' day sometime in September, most likely in Sydney, though if we get enough votes for Burleigh Heads, we're more than happy to do it up there. And I look forward to talking with you all in much more detail at that analysts' day and also at various other times once full year results are released.

**End of Transcript**