

ASX ANNOUNCEMENT: 15 November 2010**MD & CFO on FY10 Results**

Open Briefing with CEO James Fazzino
and CFO Frank Micallef

Incitec Pivot Limited

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In this Open Briefing®, James & Frank discuss

- Main drivers of the results
- Moranbah provision write-back schedule
- Outlook for debt & gearing

Open Briefing interview:**openbriefing.com**

Incitec Pivot Limited today reported net profit, excluding individually material items, of A\$442.8 million for the year ended September 2010, up 27 percent from A\$347.8 million in the previous year. EBIT was A\$648.3 million, up 13 percent. Second half EBIT was up 38 percent year-on-year, versus a 15 percent year-on-year drop in the first half. How did trading conditions change across the year and how indicative is the second half performance of the outlook for the current year ending September 2011?

CEO James Fazzino

Our business has a significant earnings skew to the second half: in our traditional Fertiliser business due to the positive impact of the winter crop on second half sales in Australia; and also in Explosives, driven by the slow-down in construction in the North American winter months.

This year, the skew was exacerbated by the cyclical de-stocking in the quarry and coal industries in the US that impacted our Americas Explosives business in the first half. We are now of the view that these markets bottomed early in 2010, with a recovery in demand – particularly in coal – in the second half.

In the Fertiliser business, global prices for di-ammonium phosphate (DAP) also reached their cyclical bottom in the first half of our 2010 financial year after reaching a cyclical peak in the first quarter of 2009. Prices recovered in the second half, which of course had a significant impact on our results.

Domestic demand for fertiliser was also unusually skewed to the second half of 2010, with dry conditions in the first half restricting pre-plant sales for the winter crop, and a break in drought conditions on the east coast of Australia from June which drove record top-dress sales of urea in the last quarter of our financial year.

The strength of our Fertiliser business – and in particular the extra flexibility that the establishment of our trading business Quantum has brought to the group – was highlighted by our ability to meet the volatile demand in Australia during the year. In June, through Quantum, we diverted cargoes of urea slated for sale to Asia into eastern Australia to supply farmers here.

The combination of these demand patterns in our Explosives and Fertiliser businesses drove a 35/65 percent skew in first half/second half profit compared with a more normal 40/60 percent.

We've started 2011 with strong global fertiliser prices, an improved outlook for the Australian farm sector now the drought has broken, and what appears to be a recovery in volumes, albeit slow, in our Americas Explosives business. On the negative side, the higher Australian dollar and continued strong competition in our Australian domestic fertiliser market will provide headwinds for Group earnings.

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EBIT in the Explosives business was A\$340.7 million, up 12 percent and EBIT margin increased to 22 percent from 17 percent. How sustainable are margins at this level?

CEO James Fazzino

The margin improvement is sustainable and should continue over the next few years, with the caveat that there is no double-dip recession in the US economy.

The increase in the non-cash write-back of the Moranbah provision accounted for some of that improvement. Excluding the write-back, underlying margin would have improved from 13 percent to 16 percent. This reflected a reduction in the cost of supplying Moranbah foundation customers, but more importantly, the gains we've made in efficiency through our Velocity program which has delivered cumulative benefits to the business of US\$140 million to date.

We expect margin improvement in the future will be driven by a number of factors. First, there is upside in the Americas Explosives business as volumes recover from financial crisis levels, particularly in the quarry and construction segment. The completion of the Velocity program in 2011 will also assist.

Second, the start-up of our Moranbah ammonium nitrate (AN) plant in Queensland will drive a step change in margins in the Asia Pacific Explosives business as we move from being an importer of AN to being a manufacturer. Manufacturing margins of course reflect the returns required to support the capital intensity of manufacturing AN in Australia.

Finally, in the longer term, the adoption of "lean principles", starting in 2012, will drive continuous improvement in business efficiency which will support ongoing increases in EBIT margins.

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EBIT from the Americas Explosives business was down 17 percent to A\$163.2 million, reflecting the negative translation impact of the stronger Australian dollar. In US dollars, EBIT was up 2 percent, with US\$54.8 million in benefits from the Velocity business efficiency

program offsetting reduced volumes and lower nitrogen prices. Given US\$32.4 million of the Velocity benefits were delivered in the second half amid some signs of volume recovery, to what extent will further significant Velocity benefits depend on continuing volume recovery?

CEO James Fazzino

We plan to complete the remaining projects embodied in the Velocity program in 2011. This means we'll exit the year with all of the approximately 500 projects completed that in total will deliver US\$204 million in cumulative benefits.

We're targeting incremental benefits of US\$34 million in 2011 and US\$30 million in 2012 subject to underlying volumes in the Americas Explosives business recovering. In particular, recovery in the coal segment would allow all the uptime improvements at our AN plants to be fully realised, while recovery in quarry and construction would allow the improvements at our initiating systems plants to be fully realised.

With the downturn in the US economy in the last couple of years, much of the benefit of the Velocity program has been offset by underlying softness in our key markets – in particular quarry and construction. However, we are very well placed for the future as we have a far more efficient business today.

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You have signalled an end to the Velocity business efficiency program and a move towards "lean principles" across the business in the future. How will this be implemented and what are the implications for earnings?

CEO James Fazzino

Business improvement is a core competency of the IPL Group, and has been since we implemented the Tardis efficiency program after the merger with Incitec, followed by the Velocity program after the acquisition of Dyno Nobel.

The success of our business efficiency programs has been built around our project office, led by Christine Trotter, which provides dedicated project management resources outside the operating businesses. While the efficiency programs rely on input from our employees in the businesses, the work is largely driven by the project office.

The move toward lean principles is the logical approach to driving sustained improvements through business efficiency. Our aim is to build a continuous improvement culture in the IPL Group consistent with one of our core values of "Challenging and Improving the Status Quo".

The roll-out of lean principles will be coordinated centrally by the project office but will empower people in the business to own and more frequently engage in business improvement activity. We want all of our employees, whether they are in the back office, manufacturing, blasting on a bench or in front-line sales, to constantly examine how waste and inefficiency can be eliminated.

In our initiating systems business, where lean principles have been applied for a number of years, we've seen how powerful and sustainable this approach can be. I'm excited about the potential for this approach to substantially improve business efficiency across the Group over time.

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The Asia Pacific Explosives segment booked EBIT of A\$176.0 million, up 60 percent, largely reflecting a A\$23.5 million increase in the Moranbah provision release to A\$85.4 million and a reduction in the cost of supplying Moranbah customers of A\$19.2 million to A\$24.0 million. How will the Moranbah provision release impact earnings in the period ahead of beneficial production in the March 2012 quarter and thereafter?

CFO Frank Micallef

In 2008, prior to our acquisition of Dyno Nobel, the construction of the Moranbah AN plant had been put on hold indefinitely due to the project no longer meeting Dyno Nobel's internal investment criteria.

To underpin the construction of the Moranbah project, the previous Dyno Nobel management had signed contracts with five foundation customers. The contracts had a fixed price and volume commitments starting in the 2008 year and extending until 2019.

At the time of our acquisition of Dyno Nobel, the projected cost of supplying imported AN to fulfil the contracts had increased to a level significantly above the contracted sales price. As a result, every tonne sold to the Moranbah foundation customers was incurring a loss and was expected to continue to do so for the remaining life of the contracts. That expectation was based on market data including forward AN prices, and the fact that at the time of the acquisition, IPL had not made a decision on whether the Moranbah project would recommence. IPL management made this decision some time after the acquisition, based on a detailed study of the engineering feasibility and a full financial and funding analysis.

The Australian Accounting Standards (AAS) required us to recognise a liability reflecting the estimated losses on the tonnes to be supplied under the foundation contracts over the period 2008 to 2019, discounted to net present value. At the time of the acquisition this gave rise to the recognition of an unfavourable contract liability of \$534 million and a deferred tax asset of \$160 million, which in effect increased the amount of goodwill recognised by IPL.

AAS require the liability to be unwound as IPL fulfils its obligations under the Moranbah foundation customer contracts. Over the period of the contracts IPL will recognise the full liability as a reduction in cost of sales in its income statements in line with the original estimates of the AN supply to the foundation customers.

Unlike other provisions that get remeasured at each reporting date for changes in underlying market assumptions, unfavourable contract liabilities do not get remeasured and the amount written back to each period's income statement does not vary from the original schedule.

Subsequent to our acquisition of Dyno Nobel, the expected cost to serve the Moranbah foundation customer contracts has changed significantly, with the price of third party sourced AN falling substantially, significantly decreasing the loss on each tonne sold, and some foundation customers agreeing to a reduction in the tonnes of AN required to be supplied under their contracts.

These factors have resulted in IPL incurring actual losses that are significantly lower than estimated at the time of acquisition. That is, while the yearly write-back of the liability

continues per the original loss estimates, the actual loss incurred has been significantly lower since 2009. We've disclosed the impact of this in the Group's profit releases.

In addition, the completion of the Moranbah AN plant, which is expected in the March quarter of 2012, should enable us to supply the contracts at a profit, rather than at a loss. However, the accounting standards do not allow us to vary the rate at which the liability is unwound.

The following schedule shows the impact of the liability on our financial statements, historically and until the completion of the contracts:

Financial Year	Provision Unwind \$m	Actual Cost Incurred \$m	EBIT Impact	Discount Unwind (Interest Exp) \$m	PBT Impact	Tax effect \$m	NPAT Impact \$m	Net Provision Unwind \$m
2008	9.0	(9.0)	(0.0)	-	(0.0)	-	(0.0)	9.0
2009	61.6	(43.2)	18.4	(1.8)	16.6	(5.0)	11.6	59.8
2010	85.4	(24.0)	61.4	(9.7)	51.7	(15.5)	36.2	75.7
2011	83.9	TBD	TBD	(16.0)	TBD	TBD	TBD	67.9
2012	81.1	TBD	TBD	(21.1)	TBD	TBD	TBD	60.0
2013	66.1	-	66.1	(21.4)	44.7	(13.4)	31.3	44.7
2014	68.8	-	68.8	(26.3)	42.5	(12.8)	29.8	42.5
2015	73.6	-	73.6	(32.1)	41.5	(12.5)	29.1	41.5
2016	80.5	-	80.5	(39.0)	41.5	(12.4)	29.0	41.5
2017	89.2	-	89.2	(47.2)	42.0	(12.6)	29.4	42.0
2018	100.2	-	100.2	(57.1)	43.1	(12.9)	30.2	43.1
2019	16.1	-	16.1	(9.8)	6.3	(1.9)	4.4	6.3
Total Liability recognised	815.5			(281.6)				534.0

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You've indicated that the Moranbah project is about 55 percent complete, and that 90 percent of the 330,000 tpa AN output is contracted. The level of committed off-take is unchanged from six months ago. What is behind the stalling in off-take commitments? Can you achieve your return targets for the project if some capacity needs to be sold on spot markets?

CEO James Fazzino

The Bowen Basin is a world class, world scale, high quality, low cost coal deposit that is supplying a significant portion of the metallurgical coal required to sustain the industrialisation and urbanisation of Asian economies, particularly China. As coal mining in the Bowen Basin grows, additional AN is required.

Moranbah is well positioned to supply AN to customers in the Bowen Basin by virtue of its low cost, gas-backed position and its proximity to the mines. Given this, I don't think we'll have a problem selling out the plant in its footprint before beneficial operation in the March quarter of 2012.

Moranbah will result in a step change in the earnings of the Asia Pacific Explosives business and have a significant impact on Group results from 2012. I'm very confident that the incremental earnings the project will generate will meet our investment criteria.

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The Fertilisers business booked EBIT of A\$334.4 million for the year, up 11 percent, partly reflecting a 21 percent increase in EBIT from the Southern Cross International (SCI) manufacturing business to A\$222.6 million on a higher global DAP price, which offset the adverse impact of the stronger Australian dollar. Trading volumes were boosted by Quantum

Fertilisers, which started up in December 2009. What are the growth opportunities for SCI and Quantum, and are current DAP prices sustainable?

CEO James Fazzino

We don't forecast DAP prices. What I can say, though, is that global DAP demand and supply appears to be well balanced at the moment, and that current DAP prices are being supported by strong soft commodity prices.

The successful first year of the Quantum joint venture shows that we have a great opportunity to grow our business by trading third party sourced fertiliser, for both the Australian and international markets. I'm very pleased with Quantum's performance, not only in terms of the earnings it has generated, but also the value it has added through better sourcing of manufacturing inputs and finished product for both the Fertiliser and Explosives businesses.

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The Incitec Pivot Fertilisers (IPF) distribution business booked EBIT of A\$112.4 million, up 20 percent, largely due to higher volumes, particularly in the second half, offset by lower Australian dollar urea prices. To what extent have volumes recovered to "normal" levels after years of drought? How might volumes be impacted by the recently released Murray Darling Authority plan?

CEO James Fazzino

Our fertiliser sales volumes on the east coast of Australia increased to 1.7 million tonnes in 2010 from 1.4 million tonnes in 2009. Those improved volumes indicate a partial recovery in the east coast agriculture markets. I believe that higher soft commodity prices and better rainfall and water availability could support a further increase in agricultural activity in Australia and, therefore, higher fertiliser volumes.

There's no doubt that the long standing drought in much of eastern Australia has broken, and this has helped the outlook for most farmers in 2010 and should further improve the outlook for 2011.

While long term water allocations in the Murray Darling is an issue that's yet to be resolved, the water situation across most of eastern Australia is much improved after very good rainfalls in recent months, and this should assist increased planting of irrigated crops in 2011.

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Incitec Pivot recently announced a 20-year off-take agreement with Perdaman Chemicals and Fertilisers for about 2 million tonnes per annum of granular urea fertiliser from Perdaman's proposed Collie plant in Western Australia. Are you planning to enter fertiliser distribution in Western Australia? What's the rationale behind entering this agreement?

CEO James Fazzino

The Perdaman off-take agreement is about growing our trading business and we have no plans to extend our IPF fertiliser distribution business into Western Australia.

The agreement will give us a fantastic platform to further grow and leverage our trading business. The product will be available for sale in Oceania, India, Pakistan, Asia and the

Americas. In 2009 these target markets accounted for 16 million tonnes out of the total global trade of urea of 35 million tonnes.

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Net operating cash flow for 2010 was A\$528.9 million, up from A\$337.4 million in the previous year. However, second half cash flow was flat compared with the previous corresponding period, largely reflecting a weaker reduction in trade working capital. How do you reconcile this with the generally stronger operating performance in the second half?

CFO Frank Micallef

This is another anomaly that arose in the Fertiliser business in 2009, certainly a year of challenges in the business. We had high inventory levels in the business at the end of the first half of 2009, after a very slow second quarter of sales. Subsequently, in the second half of 2009 we did a good job of selling down that inventory, resulting in a bigger than normal positive turnaround of cash flows, with about A\$290 million of cash inflow relating to fertiliser inventory reduction in the second half.

In contrast, the inventory we held in Fertilisers at 31 March 2010 was much lower after a strong first half of sales and, subsequently, the reduction of fertiliser inventories in the second half was only about A\$80 million.

Although trade working capital was higher in 2010 on an absolute dollar basis, on a relative basis it was better managed, as you can see by the reduction in our average trade working capital to sales ratio to 12.9 percent in 2010 from 16.9 percent in 2009.

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Net debt was A\$1,097 million as at 30 September 2010, down from A\$1,464 million a year earlier. Net debt to EBITDA was 1.39 times, down from 1.97 times and realised interest costs dropped to 4.7 percent from 5.7 percent. What is your level of comfort with these metrics in light of your planned investment in Moranbah? Has debt peaked and are interest costs sustainable at this level?

CFO Frank Micallef

We expect that, given the traditional build of trade working capital across our businesses in the first half of the financial year, together with the ongoing spend on Moranbah construction, net debt to EBITDA will peak around March 2011. We expect the peak to be inside our target debt level of 2.5 times net debt to EBITDA and for debt to level out until Moranbah is complete. Once Moranbah is complete, we should quickly return to lower debt levels as outflows of cash to fund construction will be replaced by significant cash inflows from AN sales.

The outstanding debt result we delivered in 2010 was driven by improved cash flows and by the impact of the higher Australian dollar on our US dollar debt, which helped to offset the negative impact of the higher Australian dollar on our earnings. This illustrates the inherent sense in our US dollar funding strategy.

Of course, next year absolute interest costs will increase, reflecting increased debt. In addition, in 2010 we were able to take advantage of very low short term floating interest rate levels in the US by swapping some long term fixed interest commitments to a short term

floating exposure, which helped reduce the effective interest rate. It's unclear whether interest rate markets will present the same opportunity in 2011.

However, given our US dollar debt exposure, I expect our average interest rate will remain relatively low in the foreseeable future.

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Incitec Pivot announced an unfranked final dividend of 6 cents per share, bringing the full year payment to 7.8 cents, up from 4.4 cents, 48 percent franked, last year. This represents a pay-out ratio of 29 percent of NPAT excluding individually material items, at the mid point of your payout policy range of 20 to 40 percent. What factors might lead to a lift in the payout ratio? Given the dividend is unfranked, have you considered other ways of returning cash to shareholders?

CFO Frank Micallef

The Board's dividend policy is to pay out 20 to 40 percent of net profit after tax before individually material items, subject to franking availability and financing needs.

There will be an opportunity for the Board to look at moving up higher in our dividend payout range once Moranbah is completed and the outflow of cash for construction is replaced by cash earnings from the plant. However, when considering increasing the payout ratio in the future, we'll also need to consider the alternative of using some of the increased cash generated in the business to fund growth opportunities that meet our financial investment criteria.

The completion of Moranbah should also assist our franking position, as it will result in additional Australian earnings which will increase our tax payable in Australia.

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Thank you James and Frank.

For more information on Incitec Pivot, visit incitecpivot.com.au or call Lyn Shalless, General Manager Investor Relations, on +61 3 8695 4511 or +61 412 289 472

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