

Research Update

Colorpak

Tracking in line with expectations

Sector: Materials
Analyst: Nick Maclean

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MELBOURNE

Level 29
35 Collins Street
Melbourne Vic 3000
Tel: (03) 9242 4000
Fax: (03) 9242 4040

SYDNEY

Level 35
60 Margaret Street
Sydney NSW 2000
Tel: (02) 9247 8666
Fax: (02) 9247 9366

PERTH

Level 30
44 St. George's Tee
Perth WA 6000
Tel: (08) 9268 4888
Fax: (08) 9268 4884

ADELAIDE

Level 14
90 King William St
Adelaide SA 5000
Tel: (08) 8407 5700
Fax: (03) 8407 5717

GERALDTON

38 Marine Terrace
Geraldton
WA 6530
Tel: (08) 9964 3800
Fax: (08) 9964 5811

MOUNT WAVERLEY

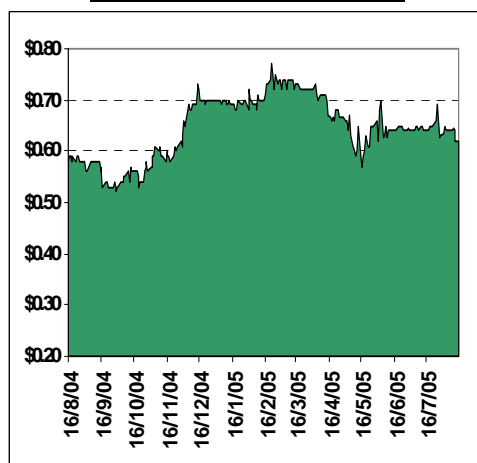
284 Stephenson Rd
Mount Waverley
Victoria 3149
Tel: (03) 9831 5000
Fax: (08) 9809 5746

MAROOCHYDORE

Level 3
Bryant House
26 Duporth Ave
Maroochydore
Queensland 4558
Tel: (07) 5409 6100
Fax: (07) 5409 6199

ASX Code:	CKL
Price:	\$0.65
Valuation:	\$0.69
Recommendation	Accumulate (From Hold)
Risk Rating:	High
Market Capitalisation:	\$52.3m

12-Month Share Price Chart



Year 30 June	04A	05A	06E	07E
Revenue (\$m)	49.6	58.6	67.6	70.6
Net Profit (\$m)	2.6	3.1	5.7	6.1
EPS* (c)	6.4	6.9	7.1	7.6
EPS growth (%)	n.a.	8.0	2.4	7.4
P/E Ratio (x)	10.8	9.4	9.2	8.6
EBIT	6.7	7.3	10.7	10.8
EV/EBIT	11.7	11.0	7.8	7.8
EBITDA Margin	21.5	19.5	19.3	19.1
NPAT Margin**	10.1	9.4	9.0	8.7
Dividend (c)	0.0	2.5	2.75	3.25
Yield (%)	n.a.	3.8	4.2	5.0
Franking (%)	n.a.	100	100	100
Current Ratio (x)	1.16	1.26	1.69	1.77
Net Debt / Equity (%)	73.6	64.5	64.1	57.2
EBITA/Int. Exp. (x)	4.8	5.2	5.0	5.1
ROE (%)	6.7	7.3	12.3	11.6

* Pre-goodwill amortisation

** Pre-amortisation & non-recurring items

Recommendation: Accumulate

Key Points

- CKL reported FY 05 NPAT of \$3.1m (slightly ahead of our \$3.0m forecast) with revenues totalling \$58.6m (versus our forecast of \$56.7m). Corresponding pre-goodwill amortisation EPS equated to \$0.069 (forecast \$0.068).
- Operating cash flows remained solid at \$7.9m while free cash flow totalled \$4.1m. The correlating capital expenditure (capex) of \$3.8m related to the purchase of new equipment as well as general maintenance capex.
- These solid earnings and cash flows enabled the company to declare a 2H 05 DPS of \$0.015 which brings the FY 05 total to \$0.025c (65% payout ratio).
- While earnings and revenues were up, EBITDA margins fell from 21.5% to 19.5%. This was primarily a result of earnings from the lower margin Castle Graphics business, the company pursuing and securing new clients and management incentive payments.
- Despite the increase in capex, CKL's healthy operating cash flows enabled an \$0.7m reduction in total borrowings to \$27.5m. Net debt to equity now stands at 65% (down from 74%) while interest cover is up from 4.8x to a comfortable 5.2x.
- Although the debt repayment is pleasing, we expect total debt to increase in FY 06 to \$31.5m as the company continues its capex program. As a result, we have forecast interest cover to fall, albeit to levels which we believe are still comfortable given the stability of the company's operating cash flows.
- CKL's FY 05 results further demonstrate the company's consistency in terms of its steady earnings growth and stable operating cash flows.
- While our bottom line FY 06E EPS target has decreased to \$0.071 (previously \$0.074) this is a result of a non-recurring \$0.4m relocation charge.
- We have continued to value CKL using both Discounted Cash Flow (DCF) and earnings capitalisation approaches. Applying these techniques derives a per share valuation of \$0.69 which is in line with our previous valuation.
- With the share price currently trading at a 10.4% (including dividends) discount to this valuation we have upgraded our recommendation from HOLD to ACCUMULATE.



FY 05 FEATURES

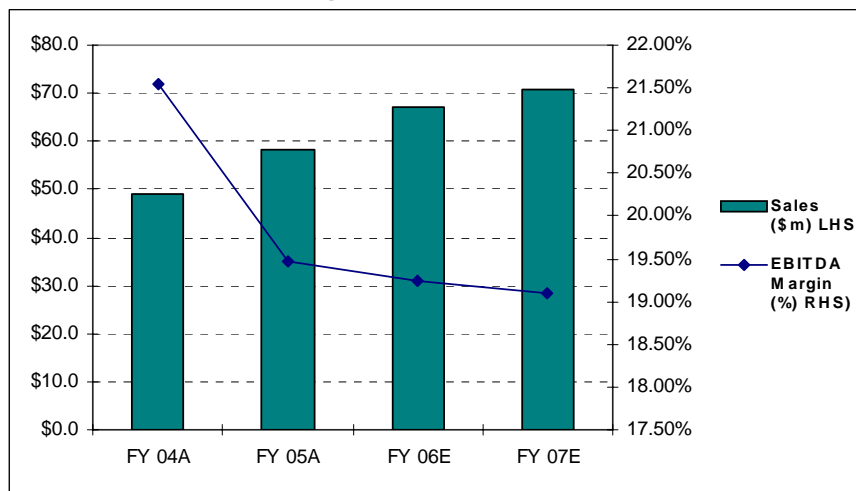
CKL's FY 05 results exceeded prospectus forecasts and highlighted a sound operational performance. Revenues were up 18% to \$58.6m while EBITDA increased 7% to \$11.3m. When excluding the sales contribution from the recently acquired Castle Graphics, CKL exceeded its prospectus revenue target by \$2.1m.

	FY 04A	FY 05A	Change
Revenues (\$m)	49.6	58.6	18%
EBITDA (\$m)	10.6	11.3	7%
EBITDA Margin (%)	21.5	19.5	-9%
NPAT (\$m)	2.6	3.1	19%
NPAT Margin (%)	5.2	5.3	2%
NPAT (\$m) pre-goodwill amortisation	4.9	5.5	12%

Unsurprisingly, FY 05 EBITDA margins fell to 19.5% with the 2H 05 EBITDA margin of 18.9% down on the 20.1% earned in 1H 05. The margin squeeze was a result of the company winning new clients - securing new customers is more expensive than maintaining existing clients, the addition of Castle Graphics lower margin offering and management incentive payments.

The margin contraction was not unexpected with the company clearly highlighting its aggressive attack on new customers and the subsequent initial hit on profitability this can cause. Furthermore, Castle Graphics has been highlighted as a lower margin business than CKL's traditional activities. Despite the decline in EBITDA margin, CKL's NPAT margin improved from 5.2% to 5.3%, aided by lower borrowing costs which fell from \$2.2m to \$1.9m.

EBITDA margin versus Revenue Growth



Return on Equity (ROE) and Return on Assets (ROA) were subdued at 7.3% and 9.0% respectively. However, we note we have forecast ROE to improve to a far more satisfactory 12.3% in FY 06 as goodwill amortisation is removed.

The \$3.8m FY 05 capex meant free cash flow totalled \$4.1m (\$0.051 per share). This capex was focussed on new equipment, maintenance capex, the die shop fit out and general maintenance expenditure.

Margin Contraction

Returns

FY 05 Capital Expenditure



Debt

CKL's consistent operating cash flows enabled an \$0.8m reduction in total borrowings despite the \$3.8m capex and continued dividend payments. While the consistency of the company's operating cash flows supports its gearing, we would like to see debt reduction continue in FY 07 in order to increase EBITA/interest cover from the FY 05 level of 5.2x. This is purely to provide a margin of safety in the face of any economic downturn while also giving the company greater flexibility should any suitable takeover targets appear.

OUTLOOK

Further potential upside from Carter Holt Harvey's Acquisition of Wadepack

CKL reiterated its positive outlook statements made at the time of its 1H 05 results. In addition, we remain bullish as to the upside offered by Carter Holt Harvey's acquisition of Wadepack through CKL leveraging off its customer focussed image and product quality to win over new clients. This is supported by CKL's fifth consecutive year rated number one by reputation in the BIS Shrapnel customer satisfaction survey of folding carton suppliers.

Improved efficiencies

We are targeting improved penetration of the NSW carton market as CKL further integrates its Castle Graphics acquisition. We also expect both the company's new equipment and the relocation to the Regents Park plant to improve efficiencies. This plant is expected to be operational by April 2006.

Forecast Capex

We believe the company will continue with its capex program designed to further upgrade and improve its fleet of equipment. As such, we have forecast FY 06 capex to increase from \$4.7m to \$8.5m. The bulk of this expenditure relates to two new six colour twin coater presses. While this lowers forecast free cash flow, it is designed to keep CKL at the technological forefront of the industry while facilitating its ongoing growth. Assuming no further acquisitions, we expect CKL's capex to return to levels approaching \$2m per annum from FY 07.

Forecast financing

In light of CKL's ongoing capital expenditure requirements, we have forecast FY 06E net debt/equity of 64% with corresponding EBIT/interest expense cover of 5.0x. This assumes no further acquisitions. In light of the company's stable operating cash flows and solid client base, we are comfortable with this level of gearing. In addition, with CKL's forecast profitability and low payout ratio we estimate it to be in a positive Net Tangible Asset (NTA) position by FY 06.

Braeside expansion

CKL is planning to utilise additional storage space at its Braeside plant – new land is to be developed adjacent to its current factory. This land will be rented from the Commins family. The expansion is expected to improve logistics and in turn, customer service.

Earnings Outlook

On the back of another pleasing profit result and with the company positioning itself to meet continued demand, we have forecast FY 06 revenues to rise 15% to \$67.6m (up from our original forecast of \$64.7m). However, we have assumed an ongoing reduction in CKL's EBITDA margin to 19.3% equating to EBITDA of \$12.9m.

	FY 06E	FY 07E
Sales Revenues (\$m)	67.3	70.6
EBITDA	12.9	13.5
EBITDA Margin	19.3	19.1

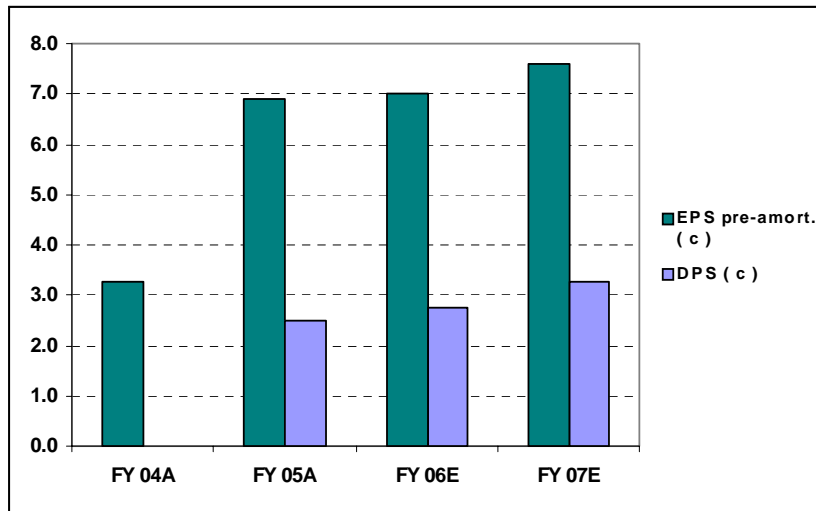


We have also allowed for a \$0.4m charge to NPAT resulting from the relocation to the company's Regents Park NSW site. As a result NPAT (pre-amortisation) is expected to show modest growth of 4.1% to \$5.7m. This equates to corresponding EPS of \$0.071 versus original estimates of \$0.074.

DPS

In light of the company's earnings and cash flow outlook, we have forecast FY 06E DPS of \$0.0275. In addition, we have forecast FY 07E DPS of \$0.0325. However, we believe there could be upside to this FY 07E DPS target through an increase in the company's payout ratio. In particular, with earnings continuing to grow and capex expected to reduce, we expect there to be room for such a capital management initiative.

EPS & DPS Growth



CONCLUSION

CKL's FY 05 profit result has illustrated another successful period for the group via both organic and acquisitive growth. Furthermore, the company has established a solid base to continue to expand future earnings and cash flows. In particular, we believe the Carter Holt Harvey/Wadepack acquisition, continued expansion within its target markets, better penetration of the NSW carton market and potential future acquisitions offer CKL solid prospects in FY 06.

We have continued to value CKL based on both DCF and earnings capitalisation methodologies. Applying a Weighted Average Cost of Capital (WACC) of 11.8%, organic growth of 4% from FY 07 and a terminal growth rate of 2% derives a per share valuation of \$0.69. This would place the company on a FY 06 p/e ratio of 9.7x and corresponding fully franked dividend yield of 4.0%. While we believe this represents fair value we note that further upside to this valuation could arise from any earnings accretive, strategically beneficial acquisition.

With the share price currently trading at a 10.4% (including dividends) discount to our \$0.69 per share valuation, we have upgraded our recommendation from HOLD to ACCUMULATE.



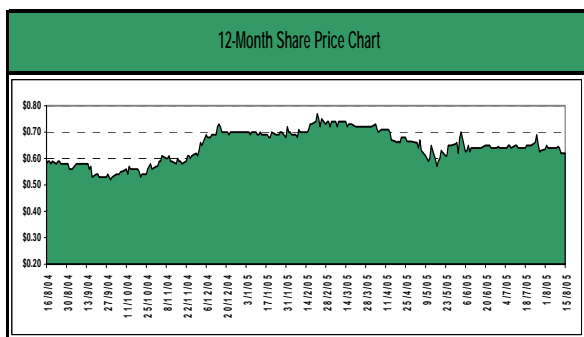
NUMBERS

Summary	2004A	2005A	2006E	2007E
EPS* (c)	6.4	6.9	7.1	7.6
EPS Growth (%)	n.a	8.0%	2.4%	7.4%
P/E Ratio (x)	10.2	9.4	9.2	8.6
CFPS (c)	5.7	9.8	8.7	8.8
Price/CFPS (x)	11.4	6.6	7.4	7.4
DPS (c)	0.0	2.5	2.8	3.3
Dividend Yield (%)	n.a	3.8%	4.2%	5.0%
Franking (%)	n.a	100%	100%	100%
Payout Ratio	n.a	65%	37%	43%

Key Performance Indicators	2004A	2005A	2006E	2007E
Revenue Growth (%)	n.a	18.2%	15.3%	4.5%
EBITDA Growth (%)	n.a	7.2%	14.1%	4.2%
EBIT Growth (%)	n.a	8.6%	47.4%	0.9%
NPBT Growth (%)	n.a	18.0%	61.0%	1.1%
NPAT (pre-amort., incl. non-recurr. Items) Growth (%)	n.a	10.2%	4.2%	7.4%

Key Value Indicators	2004A	2005A	2006E	2007E
EBITDA Margin (%)	21.5%	19.5%	19.3%	19.1%
EBIT Margin (%)	13.7%	12.5%	16.0%	15.3%
NPAT (pre-nonrecurring items & amortisation) Margin (%)	10.1%	9.4%	9.0%	8.7%
EV/EBITDA (x)	7.4	7.0	6.5	6.1
EV/EBIT (x)	11.7	11.0	7.8	7.6

Balance Sheet Analysis	2004A	2005A	2006E	2007E
NTA Per Share (c)	(10.10)	(2.49)	6.65	10.19
Price/Book	1.70	1.52	1.32	1.25
Net Debt (\$m)	(28.2)	(27.5)	(31.5)	(29.7)
Net Debt / Equity (%)	73.6%	64.5%	64.1%	57.2%
Debt/(Net Debt + Equity) (%)	42.4%	39.2%	39.1%	36.4%
Interest Cover (x)	4.8	5.2	5.0	5.1
ROE (%)	6.7%	7.3%	12.3%	11.6%
ROA (%)	9.0%	9.0%	12.0%	11.9%



*EPS calculated pre-goodwill amortisation

Profit & Loss Statement (\$M)	2004A	2005A	2006E	2007E
Revenue	49.6	58.6	67.6	70.6
EBITDA	10.6	11.3	12.9	13.5
Depn/Amort.	(3.9)	(4.1)	(2.2)	(2.7)
Total EBIT	6.7	7.3	10.7	10.8
Net Interest Expense	(2.2)	(1.9)	(2.1)	(2.1)
Pre-Tax Profit	4.5	5.4	8.6	8.7
Tax	(2.0)	(2.3)	(2.6)	(2.6)
NPAT (pre-non-recurring items)	2.6	3.1	6.0	6.1
Non-recurring Items	0.0	0.0	(0.4)	0.0
NPAT pre-amortisation (incl. non-recurring items)	5.0	5.5	5.7	6.1

Balance Sheet (\$M)	2004A	2005A	2006E	2007E
Cash	0.0	0.0	0.0	0.0
Receivables	9.5	10.8	12.4	14.9
Inventories	3.4	5.2	5.9	6.2
PPE	15.2	19.6	25.8	25.2
Intangibles	45.6	43.8	43.8	43.8
Other Assets	1.0	2.0	1.1	1.1
Total Assets	74.7	81.3	89.1	91.3
Creditors	4.6	5.9	7.4	8.5
Borrowings	28.2	27.5	31.5	29.7
Other Liabilities	3.6	5.3	1.1	1.1
Total Liabilities	36.4	38.7	40.0	39.3
Total Shareholders Equity	38.3	42.6	49.1	52.0

Cashflow Statement (\$M)	2004A	2005A	2006E	2007E
NPAT	1.5	3.1	5.7	6.1
Depreciation + Amortisation	1.9	4.0	2.2	2.7
(Increase)/Decrease in Working Capital	(0.8)	(0.6)	(0.9)	(1.7)
Increase/(decrease) in other	1.8	1.4	0.0	0.0
Net Operating Cash Flow	4.4	7.9	7.0	7.1
Capital Expenditure	(0.3)	(3.8)	(8.5)	(2.0)
Equity (Acquisitions)/disposals	(2.6)	(2.6)	0.0	0.0
Other Disposals	0.1	0.0	0.0	0.0
Other	(0.9)	0.0	0.0	0.0
Net Investing Cash Flows	(3.6)	(6.3)	(8.5)	(2.0)
Cash Dividends	0.0	(0.8)	(2.2)	(2.6)
Equity Issues/(buybacks)	1.3	0.0	0.0	0.0
Repayments	(2.9)	(3.2)	0.0	(2.4)
Drawdown	0.0	2.5	4.8	0.0
Other	0.0	0.0	(0.8)	0.0
Net Financing Cashflow	(1.6)	(1.5)	1.8	(5.0)
Net Cash Flow	(0.8)	0.0	0.4	0.1
Cash at Beginning of Period	0.0	(0.8)	(0.8)	(0.4)
Cash at End of Period	(0.8)	(0.8)	(0.4)	(0.4)

Source: Tolhurst Noall Ltd



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We have divided our recommendations into five main categories:

Strong Buy: Expected Total Return in excess of 25% over a 1 year period relative to All Ordinaries Accumulation Index

Buy: Expected Total Return between 15% and 25% over a 1 year period relative to All Ordinaries Accumulation Index

Accumulate: Expected Total Return between 5% - 15% over a 1-year period relative to All Ordinaries Accumulation Index

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Medium: Company typically has moderate price volatility and earnings variability, external liquidity and a medium size market capitalisation.

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