

Research Update

Colorpak

"Adding some color"

Sector: Materials
Analyst: Nick Maclean

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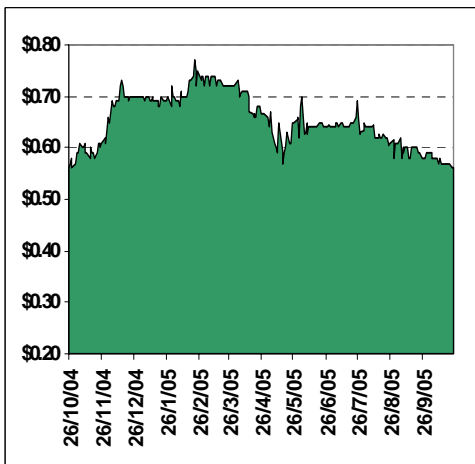
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ASX Code:	CKL
Price:	\$0.55
Valuation:	\$0.69
Recommendation	Buy
Risk Rating:	High
Market Capitalisation:	\$45m

12-Month Share Price Chart



Year 30 June	04A	05A	06E	07E
Revenue (\$m)	49.6	58.6	67.6	71.3
Net Profit (\$m)	2.6	3.1	5.7	6.2
EPS* (c)	6.4	6.9	7.1	7.7
EPS growth (%)	n.a.	8.0	2.4	8.9
P/E Ratio (x)	8.6	8.0	7.8	7.1
EBIT	6.7	7.3	10.7	11.0
EV/EBITDA	6.7	6.3	5.8	5.4
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	2.70	3.3
Yield (%)	n.a.	4.5	4.9	5.9
Franking (%)	n.a.	100	100	100
Net Debt / Equity (%)	73.2	64.5	63.2	56.4
EBITA/Int. Exp. (x)	4.8	5.2	5.0	5.1
ROE (%)	6.7	7.3	11.5	11.5

* Pre-goodwill amortisation

** Pre-amortisation & non-recurring items

Recommendation: Buy

Key Points

- CKL continues to trade in line with our FY 06 forecasts as it expands and diversifies its operational capabilities. In line with this growth the company has commissioned its forme making facility, die cutting machine and 6 colour printing press at its Braeside plant with the two machines performing at their expected capacity.
- The expansion will continue into FY 06 with CKL set to install another 6-colour printing press. It also expects to open its new finished goods warehouse in Braeside this calendar year.
- CKL should be integrated into its new Regents Park facility by May 2006. The delay (initial expectation of April 2006) does not effect our revenue forecasts or our relocation costs which we have charged to FY 06.
- With diversification into new markets and the cost of acquiring new accounts, CKL's margins have experienced some compression - in line with our forecasts. We expect this to remain a feature as the company gradually expands into new segments in addition to the pharmaceutical and healthcare sector (57% of total turnover).
- While we expect modest EPS* growth of 2% in FY 06, this is affected by non-recurring relocation charges. FY 07E NPAT is forecast to increase by a more respectable 9%.
- In relation to recent share price weakness, we have addressed and offered a counter argument to the issues we see as of potential concern to the market. Namely, flat FY 06E earnings growth, high FY 06E capital expenditure, the possibility that potential rising interest rates will significantly increase net interest expense, delays with the Regent's Park relocation and the possibility of a macro economic slowdown.
- We believe fears surrounding these issues are over done. Furthermore, although the company does have a modest organic NPAT growth profile, this is adequately reflected in the current share price.
- While we have moderately increased our FY 07E earnings we have retained our \$0.69 per share valuation. With the share price now trading at a discount to this valuation and on attractive forecast multiples we have upgraded our recommendation from Accumulate to Buy.



INVESTMENT FEATURES

Trading in line with expectations

Set against the backdrop of a large expansionary drive and pending site relocation, CKL continues to trade in line with our FY 06 forecasts. In particular, the company notes its new die cutting machine and 6 colour printing press are operating at expected capacity while its move to Regents Park remains on track. We expect another 6-colour printing press to become operational as the company settles into Regents Park.

Earnings Multiples

With forecast FY 06 NPAT growth (ex-goodwill amortisation) of 4%, CKL is currently trading on a FY 06E p/e of 7.8x. On a normalised basis (excluding goodwill amortisation and the relocation charge) EPS growth is 9%.

FY 06 DPS

Although operating cash flows are expected to remain strong, we have moderately downgraded our FY 06 DPS forecast from \$0.0275 to \$0.027 per share. While this may prove conservative, we have done so to account for the increased FY 06E capex given the company's focus on managing its debt profile. This generates a fully franked FY 06E yield of 4.9%.

Increased FY 07 estimates

In light of strong trading conditions, we have moderately increased our FY 07E sales growth assumptions leading to an increase in total revenue from \$70.6m to \$71.3m. This has flowed down to a mild 2% increase in our target NPAT from \$6.1m to \$6.2m while corresponding EPS increases from \$0.076 to \$0.077. We have retained our FY 07E DPS target despite increasing forecast capital expenditure from \$2m to \$2.7m – in line with depreciation.

	FY 07E Original	FY 07E Revised	% Change
Revenue (\$m)	70.6	71.3	1%
NPAT (\$m)	6.1	6.2	2%
EPS (c)	7.6	7.7	2%
DPS (c)	3.3	3.3	0%
Capex (\$m)	2.0	2.7	35%

Potential issue overhanging share price

With the company continuing to deliver on its operational objectives we address the issues as to why, irrespective of recent weakness in stock market conditions, the share price has been languishing.

In particular, we believe issues weighing on the minds of investors include the company's flat FY 06E earnings growth, high FY 06E capital expenditure, the possibility that any increase in interest rates will drive up net interest expense, delays with the Regent's Park relocation and the possibility of a macro economic slowdown.

1. Flat FY 06E earnings growth

Much of the subdued FY 06E earnings outlook is the result of a non-recurring \$0.4m charge relating to the relocation to the company's new Regents Park site. When this abnormal item is removed, FY 06E EPS growth totals a far more respectable 9%.

2. High FY 06E capital expenditure

CKL is accelerating its capital expenditure program in FY 06 in an attempt to capitalise on positive market conditions and the acquisition of Wadepack by Carter Holt Harvey. While FY 06E capex levels look daunting, we have forecast this to slow in FY 07 (forecast \$2.7m) as the company beds down its organic growth.



3. Threat of a rising interest rate environment on borrowing costs

CKL has a high level of total borrowings (\$27.5m at FY 05) which we have forecast to increase to \$31.3m in FY 06. At FY 05 it had \$20.6m or 75% of this total debt fixed for between 1 – 5 years. We estimate this to roll over at various stages with the bulk weighted toward FY 07. Of the remaining debt, \$3.0m is fixed until FY 06 with only \$3.8m floating.

	Floating	Fixed 1 yr. or Less	Fixed 1-5 yrs.
FY 05 Int. Bearing Liab. (\$m)	3.8	3.0	20.6

Therefore, even in the unlikely event that we were to see a 25bp or even 50bp rise in interest rates at next month’s Reserve Bank meeting, our FY 06E net interest expense would barely change, nor would our FY 07 targets.

4. Regent’s Park relocation

CKL is expecting to relocate to its new Regent’s Park site in May this financial year – note our \$0.4m relocation charge. So what will happen if they don’t move in until FY 07? In short, our revenue and normalised earnings assumptions will not change as our revenue growth is not dependant on the move. The effect on our bottom line estimates is that the relocation charge will simply be rolled forward to FY 07. So no change to our valuation!

5. Macroeconomic slowdown

CKL sources 57% of its revenues from the healthcare and pharmaceutical markets which is less exposed to economic fluctuations than discretionary areas of the economy. While its earnings may weaken in the event of an economic recession, we note the majority of CKL’s products are manufactured for non-discretionary items such as detergent and pharmaceuticals. We also refer to CKL’s track record of 15% annual compound growth over the last ten years.

VALUATION & RECOMMENDATION

CKL is a well managed business with strong cash generating abilities. While FY 06 will incur a relocation charge and heavy capital expenditure, at current prices the market is not factoring in the upside benefit from this “consolidation” year.

Despite the marginal increase in our FY 07 estimates, with the increase in capex and decrease in FY 06E DPS we have not amended our \$0.69 per share valuation – arrived at via a Discounted Cash Flow (DCF) analysis which we cross reference with various earnings capitalisation techniques.

Our DCF approach continues to use:

- WACC of 12.3%
- Revenue growth of 3% post FY 07
- Consistent EBITDA margins of 19% post FY 07
- Terminal growth rate of 2%

At this valuation CKL would trade on a FY 06E P/E of 9.8x, EV/EBITDA of 6.7x and carry a fully franked yield of 3.9%. We believe this represents fair value for the company.

In light of recent share price weakness relative to our valuation we have upgraded our recommendation from Accumulate to **Buy**.



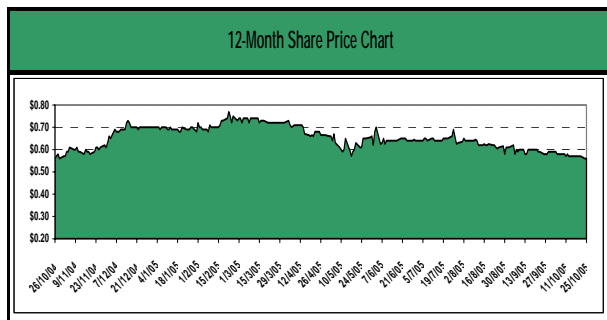
NUMBERS

Summary	2004A	2005A	2006E	2007E
EPS* (c)	6.4	6.9	7.1	7.7
EPS Growth (%)	n.a	8.0%	2.4%	8.9%
P/E Ratio (x)	8.6	8.0	7.8	7.1
CFPS (c)	5.7	9.8	8.7	9.4
Price/CFPS (x)	9.6	5.6	6.3	5.8
DPS (c)	0.0	2.5	2.7	3.3
Dividend Yield (%)	n.a	4.5%	4.9%	5.9%
Franking (%)	n.a	100%	100%	100%
Payout Ratio	n.a	65%	36%	42%

Key Performance Indicators	2004A	2005A	2006E	2007E
Revenue Growth (%)	n.a	18.2%	15.3%	5.4%
EBITDA Growth (%)	n.a	7.2%	14.1%	5.2%
EBIT Growth (%)	n.a	8.6%	47.4%	2.1%
NPBT Growth (%)	n.a	18.0%	61.0%	2.6%
NPAT (pre-amort., incl. non-recurr. items) Growth (%)	n.a	10.2%	4.2%	8.9%

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%	15.4%
NPAT (pre-nonrecurring items & amortisation) Margin (%)	10.1%	9.4%	9.0%	8.7%
EV/EBITDA (x)	6.7	6.3	5.8	5.4
EV/EBIT (x)	10.5	9.9	7.0	6.7

Balance Sheet Analysis	2004A	2005A	2006E	2007E
NTA Per Share (c)	(10.10)	(2.49)	6.99	10.72
Price/Book (x)	1.43	1.29	1.11	1.05
Net Debt (\$m)	(28.2)	(27.5)	(31.2)	(29.6)
Net Debt / Equity (%)	73.2%	64.5%	63.2%	56.4%
Debt/(Net Debt + Equity) (%)	42.3%	39.2%	38.7%	36.1%
Interest Cover (x)	4.8	5.2	5.0	5.1
ROE (%)	6.7%	7.3%	11.5%	11.5%
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	71.3
EBITDA	10.6	11.3	12.9	13.6
Depn/Amort.	(3.9)	(4.1)	(2.2)	(2.7)
Total EBIT	6.7	7.3	10.7	11.0
Net Interest Expense	(2.2)	(1.9)	(2.1)	(2.1)
Pre-Tax Profit	4.5	5.4	8.6	8.9
Tax	(2.0)	(2.3)	(2.6)	(2.7)
NPAT (pre-non-recurring items)	2.6	3.1	6.0	6.2
Non-recurring Items	0.0	0.0	(0.4)	0.0
NPAT pre-amortisation (incl. non-recurring items)	5.0	5.5	5.7	6.2

Balance Sheet (\$M)	2004A	2005A	2006E	2007E
Cash	0.0	0.0	0.1	0.0
Receivables	9.5	10.8	12.4	14.6
Inventories	3.4	5.2	5.9	6.3
PPE	15.2	19.6	25.8	25.9
Intangibles	45.6	43.8	43.8	43.8
Other Assets	1.2	2.0	1.1	1.1
Total Assets	74.9	81.3	89.2	91.8
Creditors	4.6	5.9	7.4	8.7
Borrowings	28.2	27.5	31.3	29.6
Other Liabilities	3.6	5.3	1.1	1.1
Total Liabilities	36.4	38.7	39.8	39.4
Total Shareholders Equity	38.5	42.6	49.4	52.4

Cashflow Statement (\$M)	2004A	2005A	2006E	2007E
NPAT	1.5	3.1	5.7	6.2
Depreciation + Amortisation	1.9	4.0	2.2	2.7
(Increase)/Decrease in Working Capital	(0.8)	(0.6)	(0.9)	(1.3)
Increase/(decrease) in other	1.8	1.4	0.0	0.0
Net Operating Cash Flow	4.4	7.9	7.0	7.6
Capital Expenditure	(0.3)	(3.8)	(8.5)	(2.7)
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)	(2.7)
Cash Dividends	0.0	(0.8)	(2.3)	(2.7)
Equity Issues/(buybacks)	1.3	0.0	0.0	0.0
Net Debt	(2.9)	(0.7)	4.6	(2.3)
Other	0.0	0.0	0.0	0.0
Net Financing Cashflow	(1.6)	(1.5)	2.3	(5.0)
Net Cash Flow	(0.8)	0.0	0.9	(0.0)
Cash at Beginning of Period	0.0	(0.8)	(0.8)	0.1
Cash at End of Period	(0.8)	(0.8)	0.1	0.0

Source: Tolhurst Noall Ltd



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Expected total Return is measured as (capital gain (or loss) + dividend)/purchase price

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

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

Sell: Expected Total Return less than -5% over a 1 year period relative to All Ordinaries Accumulation Index

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Risk is a subjective assessment of overall risk within a company including price volatility and earnings variability, external liquidity, and size.

We divide our risk into three categories:

High: Company typically has high price volatility and earnings variability, low external liquidity and has a small market capitalisation.

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

Low: Company typically has low price volatility and earnings variability, high external liquidity and is a large size market capitalisation.

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