

ANNOUNCEMENT

6 NOVEMBER 2002

ANNUAL GENERAL MEETING

CEO'S REPORT

REMARKS OF FREDERICK G. HILMER, AO

When I addressed this meeting in past years, I concentrated on the business—our revenues, costs, how we are performing, and what we are doing to improve.

This year, as we weather some of the worst advertising conditions in over two decades, I would like to do something a little different.

I want to talk to you about the basis of our business: the products we produce and sell. As shareholders, when you invest in Fairfax you are investing in our people, mastheads and brands, printing plants and other assets. You need to know first and foremost that we are managing the business carefully, gaining at least our fair share of revenues and keeping costs well under control.

But the success of all of this depends on us continually publishing outstanding newspapers, magazines, and web sites that attract and sustain growing reader loyalty, and that are more attractive to advertisers than those offered by our competitors. I have great confidence in the future of this company, even when viewed from the depths of an advertising recession, because our products do meet these tests, and will do so even more effectively in the future, given the improvements already in place as well as those under way.

I am also confident because of the continuing outstanding efforts of our staff, whose dedication to our publications and values underpins all we have achieved. I thank them for their efforts throughout the year.

Many think of newspapers as a mature industry—and it is. But the papers can—and do—grow as they are refreshed, relaunched, reformatted, and improved with ever more compelling, quality journalism, colour, magazines, supplements, and inserts.

I will begin by talking about Fairfax products in general—which are the foundation of our company—and conclude by outlining our priorities for the next few years.

Fairfax Products

There are four distinct publishing groups across the company: our metropolitan mastheads, including *The Age*, *The Sydney Morning Herald* and *The Sun-Herald*; Fairfax Business Media, including *The Australian Financial Review*, *BRW* and other business and financial publications; our regional and community newspapers anchored by the *Newcastle* and *Central Coast Herald*s, *The Illawarra Mercury*, and the *Warrnambool Standard*; and our f2 News and Classifieds sites. All the publications of these four groups share certain core characteristics:

1. Our products rest on strong editorial content, reflecting clear and strongly held values. In our corporate values statement, we have committed ourselves to “serving our communities through high quality, independent journalism.” We strive to be respected for the quality of our journalism, which is predicated on “truth, accuracy, integrity, fairness and balance.”

Adhering to these values may cause those whose activities we cover and some readers discomfort from time to time as we put forward facts or views that challenge theirs. However, it is important to understand that we are in the business of being respected for the quality and integrity of what we do, not of being liked by those we cover. If we are doing our job of reporting without fear or favour there is inevitably some healthy tension between our papers and public officials, or corporate executives, or foreign governments.

This is not a professional mandate only at the metropolitan level with our broadsheets, or at the national level with the *AFR*. It is every bit as important when we cover the corruption of a sports franchise and a local council, or when

we start a new paper in a growing community, as we have with *The Central Coast Herald* in NSW.

Our journalism is consistently recognised in the industry and worldwide. In this year's Walkley Awards, Fairfax journalists have more nominations than any other newspaper group. The *SMH-Age* correspondent in New York, Paul McGeough, this year received a distinguished award from Johns Hopkins University for international reporting. Here in Melbourne, *The Age* has won 40 awards for editorial excellence in the past year. It is this commitment to excellence that makes our publications the best in each of their markets.

2. Our publications are targeted at specific communities and audiences. We are not a "mass market" company seeking to be all things to all people. We deliberately seek out leadership qualities in our readership. While we do not always sell the most papers in a market—even though the SMH and the weekday editions of *The Age* have had impressive circulation gains over the past 2 years—we do sell the most papers to the target market we are seeking to serve.

The Sydney Morning Herald, *The Sun-Herald* and *The Age* all have clear leadership positions with the most attractive and demanding audiences in their respective markets, defined in the industry as key AB readers. The *SMH's* AB readership has increased by nearly 5 percent this year, and *The Age* leads in AB readers across all days of the week. Our regional and community newspapers are capitalising on the strong growth of medium-sized cities and their surrounding communities. In the 2002 financial year, their revenue was up 5.7 percent, and EBITDA grew 15.4 percent.

The *Financial Review* has the pre-eminent position in financial journalism in Australia. Our internet sites also appeal to audiences of high quality, with f2 a market leader in site users with higher incomes and full time employment.

From this position of audience strength, we are able to build and sustain high value classified markets based on trust in our publications. Earlier this year, we restructured management responsibilities to provide a clearer focus on the key advertising categories of employment, real estate and automotive, and to provide a concerted strategy in our metropolitan newspapers on display advertising. We are already seeing the success of these efforts, such as with Domain Prestige for high-end real estate properties.

3. We value good design and production. The Weekend *SMH* is a package that is the best in the industry, and *The Sydney Morning Herald* and Fairfax Printers Chullora have won the prestigious IFRA International Newspaper Quality Club award for print quality, the first Australian newspaper and printing plant to be so recognised. With *The Sun-Herald*, we introduced tabloid inserts with a wrap of the Metropolitan cultural section. *Good Weekend* is the most successful inserted magazine in the country. *The Age* had a successful make-over this year in advance of the printing innovations that will be made possible by Tullamarine.

Our objectives have not always been met. We have exhausted our colour capacity. Production bottlenecks sometimes mean late print runs. Production deadlines mean that late breaking news, and particularly late sports scores, may not make early editions of the Saturday papers in Melbourne.

These are some of the reasons why we decided to invest \$220 million in a new printing plant at Tullamarine for *The Age*, the *AFR*, and a further range of value-added publications, and \$90 million to upgrade our plant at Chullora. This investment will provide Fairfax with the best printing capacity in the country, the benefits of which will begin to be realised during this financial year.

4. We embrace technology and the new channels to market throughout our operations, from photography to publishing systems and printing, to improve the quality of our products and how we work. Our strategy with the internet is a good example. We have squarely refocussed our online businesses on the News and Classifieds franchises to complement our print activities while the internet businesses grow in their own right. Our masthead websites are the leading news sites in Australia, with combined traffic volumes for smh.com.au, theage.com.au, and afr.com that are far higher than every other news site, including those offered by the ABC, Ninemsn, and News Limited. This growing traffic benefits the classified sites that complement our print advertising franchises in employment (MyCareer.com.au), real estate (Domain.com.au) and automotive (Drive.com.au). The result is that f2 revenue is increasing in a tough market, while costs are decreasing sharply. f2 is on track for the loss at the EBIT line to be under \$10 million in the 2003 financial year, and moving towards breakeven thereafter.

We have introduced charging for bundled print and online advertising listings through our call centres. We are also expanding our electronic ad placement

capabilities via AdOnline, our internet-based ad placement service, which will lower costs and improve client service.

By being a significant player in both print and online, with a strong position in both media, we have a most attractive complementary offer. Our ability to offer a combined print/internet package is an extremely cost effective way for our motoring, real estate and employment clients to maximise the reach of their advertisements.

Our Priorities

To keep our product focus in this difficult advertising environment, we have four priorities:

1. We are managing carefully through this current cycle. Over the past year, we contained our costs by improving our business operations and tightly controlling discretionary expenditures. The restructure to focus on revenues will enable us generate growth in advertising revenues. We will keep improving our processes and operations, finding cost savings and improving productivity. Any organisation can do less with less. Our challenge, and one we have been meeting, is to continually improve the way we work so that we can do more with less, recognising the leadership position of our mastheads in their markets.

I also want to take this opportunity to respond to a question I am asked often: is this a cyclical downturn, or a structural shift?

The current downturn is, in our view, cyclical and not structural.

The decline in some advertising markets in the current cycle is almost entirely due to declines in some sectors of the economy. Other sectors have been strong. If there was a structural shift in the way companies advertised, it would be reflected across all advertising sectors. This is not the case.

Specifically, while there has been a downturn in employment and some parts of display, we have had sustained upturns in two key advertising categories: real estate and automotive. In the 2000 boom, it was employment and parts of display that were up, with real estate and motoring stagnant. Each category has its own cycles and dynamics, rather than there being an across-the-board reallocation of advertising spend.

The downturns in employment advertising and display are a further consequence of the cyclical downturn in several key sectors: telecoms, IT, financial services, and travel. Both employment and other advertising from these sectors is down sharply, but is expected to increase as the sectors recover.

2. We are putting improvements into place to strengthen the earning power of the core business. These include the reorganisation of key advertising categories referred to earlier as well as the investments in Tullamarine and Chullora.

With respect to Tullamarine, I am pleased to report that the plant is proceeding well towards full production. We have successfully printed our first commercial product this week. The Agenda preprint and The Green Guide will be printed fully at Tullamarine this month. *The Sunday Age* and some weekday editions of *The Age* and *The Australian Financial Review* will be printed in December, with the *Saturday Age* making the transition in January 2003. All remaining preprints and editions will transition to Tullamarine over the following 6 weeks. Tullamarine gives *The Age* the capacity to transform the paper, making it even more attractive to readers and advertisers.

3. We will continue to manage the balance sheet effectively. We regularly assess capital management options. However, these options need to be weighed against our strategy for Fairfax as well as expected free cash flows and stability of the Company's long term credit rating.
4. We are prepared to move on growth options. Where we can expand our print footprint, we will – as we have with the initiation of daily publication in New Zealand of the *AFR*, and the launch of *The Central Coast Herald*. We regularly review acquisition opportunities in the industry, with a threshold requirement that they add to shareholder value. With respect to media deregulation, as the Chairman has observed, it is clear that the elimination of artificial constraints on our growth will give us options for future directions—options that will create opportunities for Fairfax.

Conclusion

Fairfax is a strong business at a difficult point in the economic cycle. As the Chairman stated, while we cannot predict results with any certainty, advertising revenues are up marginally year-on-year, with the trend improving over the last month. Hence we expect EBIT growth in the first half of approximately 15% compared with the corresponding period

last year. At the same time, we are continuing to strengthen our competitive position, and we face the future with confidence.

I would like to conclude with a few words of thanks to our Chairman. Brian's almost 5 years as Chairman saw the company navigate significant challenges. He helped us to rebuild our businesses and infrastructure. Brian brought strong and consistent leadership to the board. He provided invaluable counsel to me, particularly given his deep understanding of our industry. We wish him well in the next phase of his distinguished career.

Thank you.

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Contact:
Bruce Wolpe, Corporate Affairs (02) 9282 3640