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iiNet Limited
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Record of interview:

corporatefile.com.au
iiNet Limited yesterday announced completion of the acquisition of internet service provider (ISP), Westnet, for $81 million. What is your strategic rationale for acquiring Westnet?

MD Michael Malone
This is a value enhancing deal for iiNet shareholders. The two businesses are a great fit. Westnet has a significant subscriber base that has grown nationally to be the sixth largest ISP in Australia with 138,000 DSL broadband and 39,000 dial-up subscribers. It has a quality and loyal subscriber base with below average churn rates. Its strong national reseller channel and industry leading customer service levels are distinct competitive advantages. Westnet has a strong regional presence which comprises 60 percent of its subscriber base. The business is well established, having been operating since 1994, and has a credible and competent management team.

iiNet's strengths lie in our ability to leverage off our own infrastructure which is largely a fixed cost network. We have great, innovative products, including ADSL2+, Naked DSL, VoIP and advanced business products.

A combined group can capitalise on the strengths of both businesses. Benefits will flow from being able to sell iiNet's products through the Westnet reseller channel. Obvious synergies exist via the combination of customer bases off iiNet's network. Westnet has consistently set the benchmark for service in the ISP industry, and we look forward to learning how we can improve our service even further.

The combination of these two businesses reinforces iiNet as Australia's third largest ISP and gives us a dominant market share in Perth at around 35 percent. This scale positions us as a serious competitor to the nation's biggest telecommunications companies.

corporatefile.com.au
You are paying $81 million in cash for Westnet. How did you arrive at that price? What earnings and revenue multiples are you paying?

MD Michael Malone
The business was valued using discounted cash flows. This was based on current subscriber numbers and anticipated run rates and churn rates. The EBITDA multiple, before synergies, is 6.8 times with a revenue multiple of 0.6 times.

The deal is accretive to earnings both before and after synergies with the EBITDA multiple dropping to 4.3 times after synergies.

corporatefile.com.au
What are the expected synergies from this acquisition?

MD Michael Malone
We are expecting synergies in year one of $2.5 million. Substantial synergies will flow from scale benefits of iiNet infrastructure and improved costs from Telstra Wholesale. There will be reduced transmission costs through the use of iiNet's infrastructure as well as significant savings via our agreements with Pipe Networks.

corporatefile.com.au
You have funded the purchase by a placement of 25.6 million shares raising $41 million and $40 million in debt and cash. On consolidation of Westnet, what will your expanded balance sheet look like?

MD Michael Malone
iiNet is debt free and strongly cashflow positive. So we saw an opportunity here to use our balance sheet instead of issuing more equity. This still puts us at a very conservative 17 percent gearing ratio with substantial interest cover.

corporatefile.com.au
During the December half, you increased your on-net customers by 11.5 percent to 152,000 and increased gross profit margin by 12 percent to $28 per month per subscriber. What has been the trend in these metrics in the current half year?

MD Michael Malone
Closing on-net subscriber numbers as at 30th April were 166,000 representing a 9.5 percent increase from the end of December. We are on track to at least match the 11.5 percent increase from the first half.

Our gross profit margin for the nine months to 30th March 2008, is marginally up from the 6 months to December 2007, as we are continuing to drive the profitability of our on-net subscribers, including Naked.

corporatefile.com.au
Higher interest rates are negatively affecting consumer spending. Has this squeeze affected your customers' telco' service spend?

MD Michael Malone
Internet access is no longer considered discretionary spending. Customers these days consider the internet a necessity rather than a "nice to have". For $10 a week it provides cheap entertainment. We like to compare it with beer; during a recession, beer sales stay up, but people are more likely to drink at home.

corporatefile.com.au
You mentioned in your FY08 interim presentation that you are opening a new office in Cape Town. What is the rationale for that move and how is it progressing?

MD Michael Malone
The call centre in Cape Town will deliver an additional 150 seats and implementation is going very well. iiNet is a big believer in the 'Follow the Sun' methodology. Including South Africa, we'll have call centres across four time zones, putting us in a better place to offer Customer Service staff comfortable working hours, and in turn, a high level of service to our customers. Additionally, it will provide our staff with great opportunities for travel and relocation. It will also help to alleviate some of the challenges resulting from the constrained labour market in Australia, particularly in Perth.

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In February, you reported normalised net profit growth of 55 percent for the first half of FY08 to $7.6 million compared with the first half of FY07. You also provided guidance for second half earnings to exceed the first half's underlying EBITDA of $23.0 million and NPAT of $7.6 million? Are you still comfortable with this guidance? What were the drivers of this growth?

MD Michael Malone
Yes, we remain on track to deliver our guidance in the second half of FY08. Our growth continues to come across the board from top line growth of our Naked DSL and other products and the continued improvements in our cost base.

You can see that we also have some exciting times ahead for FY09 with increased scale that will allow us to drive further growth from our brand and infrastructure advantages.

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Thank you Michael.

For more information about iiNet Limited visit www.iinet.net.au or contact Michael Malone or David Buckingham on 08 9214 2207.

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