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iiNet Limited's net profit for the first half of FY08 of \$7.6 million, excluding a one-off \$2.0 million profit, represented growth of 55 percent on the normalised net profit for the first half of FY07 on revenue growth of 3 percent. EBITDA was ahead of guidance at \$25.0 million and an increase of 21 percent on the second half of FY07 and 35 percent on the previous corresponding period's normalised EBITDA. What were your key financial achievements in the half year to 31 December?

**MD Michael Malone**

We continue to build on the strength of owning our own network and again delivered half on half profit growth. iiNet has invested over \$50 million in ADSL2+ infrastructure and we've now entered into long term supply agreements which make our cost of sales predominantly fixed. Hence, as our on-net subscriber numbers increase so too does our margin per subscriber.

During the December half, we increased our on-net customers by 11.5 percent to 152,000. At the same time, we increased our gross profit margin by 12 percent to \$28 per month per subscriber. As a result our gross profit margin rose to 45 percent compared with 35.0 percent in the previous corresponding period and our EBITDA margin rose to 21 percent compared with 16 percent in the first half of FY07.

We've made further improvements in other key metrics of the business, including growing our revenue per customer. Free cash flow from operations rose to \$23 million which enabled us to convert net debt of \$7.7 million into a cash surplus of \$9.5 million and increase our interim dividend per share to 3.0 cents from 1.0 cents a year ago.

We are pleased with what we've achieved to date. However, we're continually looking for ways to structurally change our cost base to maintain our competitive cost advantage. In December, we negotiated short term agreements which have reduced our international bandwidth expense. The full benefit of this change will be realised in the second half of the year.

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The agreement with Pipe Networks in January gives you international bandwidth capacity on Pipe's undersea cable from Sydney to Guam which is expected to be completed by late 2009. What is your strategy in making this long term commitment? What will be the benefits?

**MD Michael Malone**

Over the last 2 years we've been executing our 'Protect the Core' strategy with the objective of giving our business certainty over input costs. Following our investment in the ADSL2+ network, the ACCC finalising Line Sharing Service charges in July 2007 and the rollout of dark fibre, the last plank of the strategy was to lock in long term certainty of meeting our international bandwidth requirements.

The 15 year supply agreement with Pipe ensures certainty over our bandwidth requirements and pricing. The agreement also provides us with flexibility to increase the capacity supplied to meet our requirements.

Currently, our annualised international bandwidth cost is around \$17 million. With the current usage trends and the growth in our broadband customer base we expect this expense to increase. As a foundation customer on the Guam cable which will join existing cable systems to provide connectivity to Asia, the United States and Europe, we will enjoy benefits which we believe will maintain our competitive advantage.

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You have over 500,000 active accounts at 31 December of which 150,000 were on-net. What is your strategy for meeting the challenge of growing subscriber numbers and revenues in 2008? What new products are in the pipeline?

**MD Michael Malone**

We maintained our marketing push, spending \$3.5 million in the December 2007 half year on promoting new products. During the first quarter, the marketing investment was primarily focussed on continuing the strategy to build the brand.

In November, we were the first telco to introduce a full scale Naked DSL product to the Australian market. Naked DSL allows customers to receive broadband without renting a fixed line. This product has been very positively received by our customers and the industry critics having won the Australian PC User Magazine "Product of the Year" award.

At the start of February 2008, we commenced our Naked DSL advertising campaign in Sydney and Perth which is having terrific results in driving our organic growth strategy. To date we've exceeded our expectations with over 8000 customers joining iiNet and switching off their phone. We expect Naked DSL will drive subscriber growth through 2008.

In addition, we have recently negotiated a deal to stream the English Premier League online to our customers. This is the first step in our content strategy which will see other exciting content released over the coming 12 months.

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Operating cash flow in the latest half year was \$32 million and your balance sheet has surplus cash. How will you use this financial strength?

**MD Michael Malone**

Our stronger balance sheet provides us with the ability to grow our business through acquisition.

Aside from building our existing businesses, iiNet's growth strategy is to participate in industry consolidation. We are seeing the momentum building with Soul and TPG announcing their intentions to merge and we know there are other opportunities where iiNet can participate and we are currently assessing these..

At our AGM in November, we said we would re-commence our acquisition strategy. A primary criterion for us in assessing acquisitions is the location of the customer base. This is because we have rolled our ADSL2+ network into 301 metro exchanges. By bringing acquired customers who are on the Telstra wholesale network onto our network we can substantially increase the contribution from these customers and give them a better product. As we complete these transactions, additional capacity will need to be built into the network. This is a significant consideration for us when we are making our investment decision.

In January, we completed the acquisition of Perth Internet Service Provider Up 'n' Away which had 1,800 broadband customers and 900 dial customers whom we've since successfully integrated.

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Are you now ready to consider larger acquisitions?

**MD Michael Malone**

We are seeing rationalisation at both the small and large ends of the ISP spectrum and we're constantly being presented with opportunities. We can see both the opportunity and the strategic value of acquiring a large ISP, as long as it meets our strict acquisition criteria.

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You had some significant and well publicised problems in the June 2006 half. Do you feel those are well past now?

**MD Michael Malone**

The key drivers that led to the problems in FY06 were the dramatic pricing changes we received from Telstra Wholesale and our immature back office processes. Both of these issues have been addressed. Firstly, through investment in our ADSL2+ network and the 'Protect the Core' strategy which has driven our earnings growth over the last 18 months. Secondly, there have been major process improvements in the back office function which mean we have first class scalable and robust reporting systems.

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You said in November that in FY08 you expect to comfortably exceed the FY07 NPAT normalised for one-off items of \$11.9 million. What updated guidance can you provide for FY08?

**MD Michael Malone**

We are looking at a very strong full financial year for 2008, with half on half growth for the 6 months to 30 June 2008.

The NPAT for the first half of \$9.6 million included a \$2 million benefit from our successful challenge of certain stamp duty charges on acquisitions. Underlying NPAT was \$7.6 million. With the benefit of a full six months of the international bandwidth savings and a further increase in our on-net subscriber base, we expect the second half earnings will exceed the first half's underlying EBITDA of \$23.0m and NPAT of \$7.6m.

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Thank you Michael

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For more information about iiNet Limited visit [www.iinet.net.au](http://www.iinet.net.au) or contact Michael Malone or David Buckingham on 08 9214 2207.

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