



CPI GROUP LTD

Chairman's Report – 2006 Annual Report.

Net profit after tax of \$3.95 million for the fiscal year to 30 June 2006 was clearly inadequate, and included \$3.265 million profit from the sale of the Braeside property. Trading margins fell once again, an experience shared by nearly all of the major Australian paper merchants, highlighting the persistent and increasing difficulties of the Australian paper market.

Continued production surpluses at many paper manufacturers overseas has resulted in stock frequently being sold, some would say dumped, into the Australian market at low prices that often undercut many standard lines imported under normal trading relationships. In addition there are low barriers of entry to new merchants who, with the support of an offshore manufacturer wishing to penetrate the Australian market, are able to set up low cost operations providing selected services only.

Effectively that is the challenge for Australian paper merchants: get smaller and carry fewer lines, or get bigger to obtain economies of scale and lower unit overhead costs. Industry rationalisation is a necessary requirement for the latter and CPI is well positioned to play a part in that when the opportunity arises, to attain a commercial return on funds invested.

CPI's machinery division performed adequately during the year, but also suffered price competition that at times was extreme. On a number of occasions CPI experienced prospective sales based on quality and performance being undercut by prices from a competitor that were below cost.

The various challenges outlined above have caused the company to continue to search for still further efficiencies and cost reductions, with considerable success, and to maintain the highest standard of service and product. As an example, independent and customer testing of CPI's inks has shown these to be amongst the best quality available, and to be at the forefront also on a value for price basis.

One significant recent matter is the conclusion of the hearing in the Federal Court of Australia of the commercial dispute between CPI and a supplier. This matter is outlined in Note 31 of the notes to the attached financial statements. It is anticipated that the Court will deliver its judgment in the period prior to 31 December 2006. The directors are of the opinion that a provision is not required in respect of this matter. However, if the Court decides in favour of the supplier, the amount payable by CPI will have a material effect upon the financial results for the 2007 fiscal year.

Looking forward, there is much work to be done, but similarly much has already been achieved. The company has rationalised its activities, cash flow has been improved, and management is strongly focused on the bottom line.

CPI staff have performed very credibly under challenging conditions, and the morale and determination to complete the turnaround to satisfactory profitability - despite the adverse circumstances - is striking. Credit is due particularly to the management team led by Bernard Cassell.

I want to thank also CPI's non executive directors, who have participated actively, and given unstintingly of their time, experience and expertise. On the 26th of May 2006, Mr Graeme Cureton resigned because of heavy work commitments, and the board elected Mr Jason Ters of GPG in his place. Mr Cureton has agreed to act as an alternate to Mr Ters.

Gerry van Wyngen
Chairman

28 September 2006.