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Skilled Group Limited
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SKILLED Group Limited (ASX: SKE) announced on Friday that it completed the equity placement of 53.93 million ordinary shares and had accepted $80.9 million rather than the planned $70 million. What was the rationale for accepting the increase in the share placement amount and how will the funds be allocated?

MD & CEO Greg Hargrave
We're pleased with this outcome. Demand for the placement was strong from many major Australian institutions such that we could have raised over twice the original $70 million we were seeking if we had wanted to. Given the strength of the demand, the Board decided it was worthwhile to take a little more than we had planned. We also welcome Thorney Investments as a major shareholder in our business.

This raising and the SPP that we are also progressing will be used to retire debt and de-risk our balance sheet, thus positioning us for any economic upturn.

In addition, most of the vendors of our Offshore Marine Services (OMS) Australia business decided to take some of their September 2009 earn-out payment in scrip rather than cash. Not only is this a sign of strong support for the company but it has preserved an additional $4.8 million of cash.

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As a result of the placement, Thorney Investments has an 8 percent stake in SKILLED. Are they seeking board representation?

MD & CEO Greg Hargrave
We're pleased to have a quality shareholder such as Thorney on our register. They know and understand our business and they are not seeking board representation.

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You recently reported net debt of $258.7 million down from $299.1 million six months earlier. What is the outlook for debt at the end of the current year and what level of debt is appropriate for the business in the current environment?

CFO Terry Janes

The $80.9 million placement, target $10 million SPP and the cash withheld by using scrip for the part payment of the OMS earn-out, will be used to reduce debt. By the end of the year, we expect to have debt down to below $200 million through the equity raising together with effective working capital management. This will give us a gearing ratio in the high 30 percents which we feel is an appropriate level given the current environment.

We've also taken the opportunity in recent weeks to extend our debt facilities for three years to August 2012 and will reduce the size of the committed facility from the current $350 million to $250 million by the end of FY10.

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Given you'll improve your balance sheet, what role will acquisitions play over the next 12 months?

MD & CEO Greg Hargrave

Our primary focus will be on our existing business operations and ensuring we extract the most value we can from them. We believe the current environment requires a conservative balance sheet position and also believe there's opportunity for substantial growth within our existing business.

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You have not provided EBITDA guidance for the current year ending June 2010. Can you explain the rationale behind this decision?

MD & CEO Greg Hargrave

The issue we face is how to give practical guidance when there is still uncertainty around the size and timing of an economic recovery. While we believe the worst is over it is not clear what the trajectory of recovery will look like. We expect our performance to be above what we delivered in the second half of FY09. I would also note that as a business we have high leverage to any economic improvement. No matter what slowdown we look at over the last 20 years we have emerged with rapid growth rather than a slow incremental build-up. We see no reason not to expect the same pattern this time around.

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Underlying NPAT was $34.1 million and underlying EBITDA was $88.7 million down 19.4 percent and 5.7 percent respectively compared with the previous year. Underlying NPAT for the second half was $6.9 million compared with $27.2 million in the first half. What were the main changes in trading conditions between the two halves and how indicative is the second half of current conditions?

MD & CEO Greg Hargrave
In the first half, we saw a continuation of strong organic growth in revenues and a rising EBITDA margin as the strategy we had in place around pricing management and back office productivity flowed through. This allowed us to deliver record profits and we were on track for a great year. However, with the global financial crisis, demand fell away abruptly from about November onwards. While we began reducing our cost base back in November the speed of the fall in revenues meant we were playing catchup on the cost side and we therefore had a profit squeeze. The situation has now stabilised and we're delivering EBITDA run rates above that of the second half of last financial year.

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What is SKILLED's competitive position in the current environment and to what extent are you seeing pricing pressure from your competitors?

MD & CEO Greg Hargrave
We remain the #1 player in the industry. While overall market demand has fallen we have had very little customer churn and in many cases have been able to increase our market share within individual customers as they have sought to consolidate supply.

Over the last 6 months we've seen varying pricing strategies among our competitors. Many have chosen to compete hard. The net effect on us has been pretty limited overall. In most cases we've been able to demonstrate our differentiated service and safety performance and have therefore been able to limit any price reductions.

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You've responded to the slow down in the economy by reducing costs by more than $44 million. What scope is there to reduce costs further if business conditions continue to deteriorate?

MD & CEO Greg Hargrave
While we believe the worst is now behind us we have prepared detailed plans for addressing any further market weakness. Our cost base remains highly flexible and therefore we're able to manage circumstances that other businesses would find very difficult. But as I mentioned before, we do not expect the market to weaken further.

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You've restructured SKILLED's operations from two divisions into three divisions – Staffing Services, Engineering and Marine Services and Business Services. What was the strategic rationale for this change?

MD & CEO Greg Hargrave
There are a few reasons why we have restructured the business. Firstly, it will allow us to drive further productivity improvements and enhance joint selling opportunities along similar lines of business. It will also assist in sharing best practice among related businesses. Finally, it will enable us to streamline management decision making.

The restructure reflects different customer needs and organisational capabilities required for success in the markets that we operate in. This restructure will deliver about $4 million in cost savings and that's included in the $44 million cost savings we've talked about previously.

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Workforce and Maintenance Services EBITDA after corporate costs was $42.6 million down 23.5 percent compared with the previous year. Revenue from this business is predominantly from blue-collar hire and maintenance services to clients in the industrial and mining and resources sectors. To what extent has the slowdown in the mining and resources sectors impacted the earnings contribution of this business?

MD & CEO Greg Hargrave
The slowdown in the mining and resources sectors has had some impact on our earnings contribution in Workforce and Maintenance Services especially with second tier miners. Besides this, general manufacturing, automotive and infrastructure and utility sectors also had an impact on the earnings contribution. As a result we reduced cost in this area by reducing staff numbers and closing 13 offices.

Our business has benefited from our broad industry exposure with sectors such as FMCG and the top tier miners providing a level of stability. We've seen this segment stabilise in the last few months and are seeing growth emerging on a client specific basis.

The closure of BHP Billiton's Ravensthorpe operation and general reduction in capital and maintenance expenditure across the economy meant that the significant success of ATIVO early in the year could not be maintained. Activity in this sector remains subdued although ATIVO has had recent successes with wins in the mining, infrastructure and utilities spaces.

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EBITDA after corporate costs for Other Businesses was $43.4 million up 13 percent on the previous year. What factors contributed to the increase in earnings for Other Businesses in FY09?

MD & CEO Greg Hargrave
Offshore Marine Services (OMS), SWAN and Excelior performed well through the year. Origin Healthcare, Mosaic and PeopleCo have been impacted by the downturn.

OMS had strong growth in FY09 and whilst we expect this growth to moderate in FY10 in Australia, we expect good performance here and internationally going forward. SWAN with its large exposure to the oil and gas sector in West Australia looks to be able to sustain this into FY10. We expect Excelior to continue to perform well with some good wins in recent months and a strong pipeline of well developed opportunities.

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Cash flow from operations was $121.7 million in FY09. Cash flow in the second half was $71 million up from $50.7 million in the first half, reflecting a reduction in working capital, which offset the contraction in EBITDA. What scope is there to further reduce working capital? What are your expectations for cash flow in FY10?

CFO Terry Janes
We continually try to improve working capital management but the scope for further major improvements is limited given we anticipate stronger revenues. In fact we hope that we have to increase working capital as it would show that we were returning to a growth environment. Cash flow for this year is unlikely to be as strong as last year.

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You've announced a fully franked final dividend of 1.5 cents per share bringing the full year dividend to 10.5 cents per share. What is the outlook for dividends in the current year?

MD & CEO Greg Hargrave
We're still focused on cash preservation and balance sheet management. In the current environment, we anticipate paying between 30 percent and 50 percent of NPAT in dividends. Once business conditions return to a more normal basis we expect to return the dividend back towards its historical levels.

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Thank you Greg and Terry.

For more information about SKILLED, visit www.skilledgroup.com.au or call Craig Renner, Chief Strategy Officer on 03 8646 6406.

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