SKELLERUP

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Skellerup maintains dividend as strong cash flow offsets slower earnings

Key Points for the six months ended 31 December 2012

- Operating cash flow was strong at $14.6 million, up $5.4 million on the prior corresponding period (pcp). Net debt reduced by $4.7 million to $4.5 million on the pcp.
- Interim dividend maintained at three cents per share.
- Net profit after tax (NPAT) of $9.5 million, down from $11.5 million in the pcp.
- Agri Division earnings were relatively stable. Industrial Division earnings were down with reduced demand for pumps and technical rubber products as customers delayed both technical testing and purchasing decisions.
- The slow start to the year has lead management to reduce its full year NPAT forecast to $20 million from $22 million - $24 million.

Skellerup made a slower than expected start to the 2013 financial year as the turbulent environment in key markets led to an overall drop in sales.

Chief Executive Officer David Mair said: “Our earnings performance for the six months to 31 December was a timely reminder of the challenges of operating in overseas markets and how the decision-making process of our customers influences earnings. Whilst the Agri Division benefits from more predictable demand patterns of a key consumables market where replacement decisions can’t be put off for too long; the same can’t be said for the Industrial Division where product demand tends to be a lot more discretionary.”

“A good example of this was our record full-year earnings performance last year when we experienced a late flurry of orders in the second half of that financial year. This was in part fuelled by strong activity in the North American oil and natural gas exploration market driving demand for pumps through until March 2012. From that date, demand reduced as activity in the exploration sector slowed and replacement decisions were put on hold. We saw a similar trend with our industrial rubber products where demand has, for the meantime, slowed down in our key markets of Australia, Europe and the USA.”

“Of course, there will always be challenges, but the real benefits and opportunities of dealing in global markets are clear. Competition forces us to get it right by focusing on the needs and demands of our customers and ensuring that our production capability and product mix matches those needs. Our strategy of ensuring that our existing operations are meeting their potential and continuing to invest in developing new sales channels and opportunities remains intact. Though we will always be captive to changing market forces, the impact of these changes can be mitigated by being close to our customers. This enables us to quickly align production to actual demand. We have continued to make improvements with inventory management and reduced delivery lead times.”

Financial Summary			
$000 (Unaudited)	**Half year ended 31 December 2012**	Half year ended 31 December 2011	Percentage Change
Revenue	**94,992**	102,971	(8%)
Earnings before interest and taxation	**13,814**	17,673	(22%)
Net profit after taxation	**9,489**	11,517	(18%)
Earnings cents per share	***4.92***	*5.97*	*(18%)*
Dividend cents per share	***3.00***	*3.00*	*0%*
Net debt	**4,538**	9,211	51%
Cash from operations	**14,627**	9,185	59%

Industrial
This past six months has been the most difficult trading period since the six months ended 31 December 2009 when the full impact of the Global Financial Crisis was felt. Indications are that there will be some improvement in trading conditions in the second half.

Although sales of industrial vacuum pumps have reduced, the underlying drivers for gas exploration are positive. With the recent increase in the natural gas price to above US$3/MMBtu (Henry Hub), indications are for a lift in demand in the second half as the northern hemisphere moves out of winter. Skellerup used this relatively slow period to successfully move its manufacturing/ warehouse operation within Lincoln, Nebraska to take advantage of the expected upturn in business.

Sales of technical rubber products were adversely affected by lower demand from the European gas market and lower construction activity in Australia. To counter this we have expanded our product range in Europe and established a sales and distribution facility in North Carolina to service the USA market and early indications are that this project is going to benefit from the upturn in the USA economy.

The economic contraction in the Australian, USA and European markets has also impacted on our Deks business which designs and sells roofing and plumbing products. Deks has successfully overcome this weakness in these traditional markets by smart innovation in its product range and successfully growing in the developing markets of Latin America and Asia.

Sales of the Flexiflo ore chute lining system were ahead of expectations during the first half; however demand has since slowed due to a collapse in iron ore prices. We are progressing our plans to expand the market for this unique product into other geographical markets for iron ore and also establishing a test site for brown coal.

We have successfully relocated Skellerup's closed cell foam manufacturing facility to Vietnam during the past six months. Inevitably we have incurred one-off costs that will not be repeated in the second half. The reduced cost of manufacturing and improved quality now being achieved should secure new opportunities for growth.

Agri
The Agri Division performance was relatively stable but was impacted by two key factors. Firstly drought conditions in the USA limited supplies of corn stock feed which drove the price to record levels, putting pressure on dairy farm expenditure. This in turn impacted demand for liner and tubing consumable products. Secondly, Fonterra forecast a lower pay-out which resulted in subdued spending on dairy consumable products in the NZ market as farmers deferred replacing their dairy liners and tubing. Ultimately farmers need to replace these consumables to ensure they maintain their milk quality to optimise their returns. In addition with Fonterra recently having announced an

increase in the forecast milk pay-out we have seen recent stronger demand for dairy liners and expect this to continue for the second half.

Sales of Ambic branded product range, which is used to maintain hygiene throughout the dairy milking process, have been solid as the dairy industry pushes for higher standards of milk quality to meet more stringent compliance standards. Similarly, Stevens Filterite business also recorded improvements with increased demand for filter products in the dairy milking process.

Skellerup's footwear range including the new Red Band work boot was well received in the market during the first half. Indications are that some traction for our footwear range is now beginning to be achieved in the American market as well as UK and Europe.

Dividend
The Directors have declared an interim dividend of three cents per share, fully imputed, which will be paid on Thursday 28 March 2013 to shareholders on the register at 5pm on 15 March 2013. The Dividend Reinvestment Plan will not be operative for this dividend payment.

Outlook
Chairman Sir Selwyn Cushing said: "The 2013 financial year is shaping up to be a tougher year for the company than the previous one. Reflecting that, we have wound back our earnings expectations for the full year with NPAT now expected to be $20 million. Our customers have been impacted by unpredictable weather patterns and a slowdown in activity, but as we have seen in the past, orders can quickly turn and we must be ready for this. Skellerup is a good company with diligent and committed management. I am confident in its ability to outperform the market in the foreseeable future. The signs of recovery are starting to show."

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