TRANSCRIPTION

Company: **DGL Group Limited**

Date: **27 February 2024**

Time: **11:00AM AEDT**

[START OF TRANSCRIPT]

Simon Henry: Thank you very much, [Krista]. Good morning and thank you for joining DGL's First Half Year 2024 Results Webinar. I'm Simon Henry, Founder and CEO of the Company and I'm joined by Rob Perkins, our CFO and Alex Wing, our COO. Alex joined DGL in February last year.

I'm delighted to present our results for the first half, which is a solid performance notwithstanding pressures on earnings, which we'll discuss. I am pleased to note the second half has started strongly, but more on that later on.

I'll move past the disclaimer slide, being slide 2 and we'll move on to slide 3. The graphic on slide 3 shows that we have built a significant business at DGL and we will continue on growing the business in coming years. We service a wide range of essential industries in Australia and New Zealand, delivering specialised chemical services that are critical in keeping our society operating, growing and staying healthy. We are proud of the diverse business that we are building and the important place it has in our economy and supporting how people work and live.

Turning to slide 4. Total sales and underlying EBITDA in the first half were broadly consistent on the prior year. We experienced a good level of demand across our broad service offering, although several areas pulled out earnings below what we wanted to achieve. Our crop protection products were lower than expected. The austere warnings in August and September of last year of a pending drought across much of Australia had an impact on the farming community.

There were also delays in orders due to overstocking by customers in prior periods, due to COVID and supply chain issues. We believe this impact will normalise in the current half year. It turned out that weather forecasts weren't accurate, as subsequent rains have proven. Fortunately, we are seeing a strong recovery in the second half, both in crop protection and pest control and our order books are full.

We also saw a reduction in volumes through our recycling plants with increased competition, which resulted in lower profit. We have been proactive to address this, leveraging our established transport network to get in front of customers to secure the important materials that we need. We have seen an increase in collections as a result, which is a positive improvement on volumes so far in this half.

orient capital

Some key products, including auto chemicals, saw price pressure in some commercial segments, although the diversity of our customer network is helping to alleviate these pressures by diversifying sales. Despite these sectors, we are pleased to report an improvement in our EBITDA margin to 14%, even with considerable inflationary pressures on wage costs.

Our net profit after tax is down on last year, due to higher finance costs and depreciation as we invest in growing our network and asset base. We are also investing in systems to improve the overall profitability of the entire Group. This is investment for growth, which includes transport capacity for our liquid waste treatment facility in New South Wales which will come onstream during July this year.

We are expecting the implementation costs of our new ERP system which will drive efficiencies across the Group. We have also invested in over 40,000 square metres of additional warehousing and manufacturing space to support ongoing organic growth. We will see benefits from this investment in coming periods.

Turning to slide 5, our underlying cash flow of $28 million in the half represents cash flow conversion of 93%, still healthy and back to normalised levels. We have invested $13 million in three add-on acquisitions, which I'll discuss in more detail later, and $21 million in property, plant and equipment to support ongoing organic growth.

Our net debt remains at conservative levels, below 2x underlying EBITDA and we're delivering safe and reliable operating performance and we delivered a safe and reliable operating performance through the period.

Turning to slide 6, this slide shows a snapshot of our extensive network of facilities across Australia and New Zealand. This delivers DGL's compelling competitive advantage in delivering essential services to our customers. Several of the largest chemical companies globally are using DGL's assets and services for their complex chemical formulation and material handling requirements.

As we further broaden our service offering and delivery network, we become the obvious choice. We are also improving our route planning for our logistics fleet to deliver more efficient services to our customers and save DGL costs.

Now turning to our profit and loss on slide 7. While Group sales were stable, gross profit increased 23% to $97 million due to the normalisation of some raw material pricing and focused management. In addition to the weather-related impacts in the first half, industrial action at Australian ports held back our overall performance. There are positive indications in the current half that these disruptions are normalising.

I'll now hand the slide pack over to our COO, Alex Wing, who will take you through the next slide.

orient capital

Alex Wing: Thank you, Simon. H1 saw a positive period of growth in manufacturing revenue for our non-crop protection industries, with key price reviews across our existing work put through and these will take effect in H2.

Internal procurement practices have been adopted across the Group as well. This sourcing will continue in H2, with these prices expected to remain low compared to FY23. Bulk purchasing and management of the supply chain is providing both internal and external benefit as the entire Group grows. Our manufacturing businesses in general are seeing a strong rally in H2.

Currently, we are experiencing a busy period of tendering for existing and new business across our manufacturing, transport and warehousing divisions, with sizeable contracts expected to be won beginning in FY25, with a clear growth focus in front of mind for our commercial staff. These require continued integration of the businesses, improving efficiencies between our operations and across our segments. DGL has seen a clear advantage in the multiservice offering to our customers. Reducing supply chain links and streamlining services are a focus for DGL as we continue our innovative offering.

Our water treatment services remain in strong demand, with increased capabilities and scale due to H1 improvements. The operational efficiencies have reduced the requirement for capital investment in this space as our sales volume has increased. Focusing on unit cost production and bringing complementary services in-house across the Group and particularly in our environmental services, is proving beneficial so far in H2. Back to you for slide 9, Simon.

Simon Henry: Thank you very much, Alex. Slide 9, our balance sheet remains strong. We have seen an increase in inventories due to acquisitions and the residual impacts of recent supply chain issues. We are actively managing our inventory position to improve our working capital efficiency. As noted, our net debt remains conservative.

Turning to slide 10, operating cash flow of $19 million was lower due to the timing impact of some non-recurring activity levels in the prior period. Underlying operating cash flow was strong at $28 million, with 93% cash conversion. The investing cash flow follows our ongoing investment for further growth.

Turning to slide 11, DGL has achieved triple ISO certification for its manufacturing business. This is a key step in standardising quality and safety and processes across our sites. Health and safety remains a clear focus for DGL and we have dedicated staff to compliance, quality and safety systems across the Group. These staff facilitate site compliance, quality control and assurance and timely monitoring and reporting of health and safety metrics for the business.

Standardised policies across the entire Group will go live in March through a centralised document hub. We are also moving to online training to deliver - to make it easier for specific training to take place across the Group and to keep up with regulatory and certification requirements to ensure that all staff are suitably trained.

Turning to slide 12, we are pleased with our performance in the half, even if it isn't fully reflected in the bottom line. We continue to integrate our operations and to drive cross-sell between parts of our Group, we will see more cross-sell benefits coming through. We will benefit from customers wanting to rationalise their supply chains, DGL's diverse service capabilities make us the obvious choice.

We have continued to invest in plant and in fleet and in capacity to support ongoing growth. We're also getting better at driving economies of scale with centralised procurement and trading across the Group and the rationalisation of underutilised assets and the consolidation of warehousing and manufacturing operations.

The three acquisitions made in the half have added product capabilities with powder blending in Queensland and Bondlast construction products in New Zealand. We have also added transport and chemical storage capacity to the Group, with the acquisition of Kinnear Transport in Perth.

Turning to slide 13, our strategy remains very clear. We are focused on providing specialist chemical products and services to essential industries throughout Australia and New Zealand. We have invested, both before the IPO in 2021 and since, to create a complete solution from procurement to manufacturing, to storage and transport, to recycling and the disposal of chemicals.

We will continue our focus on investing for growth and you will see a marked shift from M&A growth to organic growth. We have created a network of assets that will let us drive strong organic growth and reduce the levels of M&A. We will still acquire capabilities as opportunities arise, but we will be increasingly selective. Our focus will be on further integration to maximise value, costs and operational disciplines and drive organic growth.

Turning to slide 14, in terms of our current trading the outlook is positive. We feel we are working through the last stages of the supply and demand disruption of the last two years. We are seeing stronger volumes in January and February in crop protection products and environmental services, including our liquid waste and our lead asset recycling operations. We are focused on costs and productivity and working through the tight labour market that continues in Australia and New Zealand.

Historically, our second half is somewhat stronger than the first and we expect this to be the case this year. We are very positive about the outlook and we see stronger revenue and profit performance in the current half. We expect full year net profit to be below last year's due to higher financing costs and the level of investment that we are making in people and assets to support ongoing organic growth. We will see the benefits of these investments in future periods.

Now we'll turn to slide 15. We are building a comprehensive network of essential chemical and industrial services that are increasingly critical to the economies of Australia and New Zealand. We are profitable and we continue to invest for growth and to add to our already considerable capabilities. You will see a positive shift to capture more internally generated organic growth and we are positive and very excited about our future.

Now I'm going to hand over to Andrew Draffin, our Company Secretary, for questions.

Andrew Draffin: Thank you, Simon. We've received a few questions so far, I'll read off the first one. Can you please explain the acquisition strategy? Is it to build scale, to drive enhanced financial performance in the future?

Simon Henry: When we look at a company we're going to buy, we assess its strategic value across the greater Group. What customers will it bring into the network? What licences will it come with? The calibre of the people in the company and the geographical coverage and also its share capacity, or what will it add into our existing capacity? It's very much of a holistic view of the benefits of acquiring a subject company.

Andrew Draffin: Thank you.

Simon Henry: The next question, Andrew?

Andrew Draffin: Second question, can you please talk through the revenue EBITDA performance for the chemical manufacturing division specifically by channel, agriculture [inaudible] sector?

Simon Henry: The first half, crop protection products was challenged in Australia due to the widespread media coverage of a pending drought, so we did have considerably lower orders. Though with the good rains that we've seen our order books are now full and our plants are working flat-out to cope with the demand. The other mainstream we work in is auto chemicals, AdBlue and other materials. That channel remains strong and our manufactured chemicals for mining and water treatment both remain strong.

Andrew Draffin: The next question, in light of the increased interest payments, are you planning to accelerate paying back some of the debt?

Simon Henry: No, not at this time. We're completely comfortable with where our debt sits. That said, as I've mentioned, we are doing this U-turn to go back into the business and instead of acquiring companies at the rate that we have bought them since listing, the focus is going to be on organic growth which in many ways uses much less debt.

Andrew Draffin: The next question, can you talk about the progress that's been made in tolling agreements with offshore manufacturers?

Simon Henry: Only we've got some commercial sensitivity around those. That said, we are pleased to have now become accredited tollers. If I use BASF as one good example, the world's biggest chemical company, Halliburton's is another. DGL now has the internal controls and disciplines and is able to demonstrate to these international chemical companies that we are suitably qualified to handle their Australia and New Zealand tolling requirements. In many ways it's a demonstration of DGL coming of age.

Andrew Draffin: Are you able to - can you talk about the outlook for organic growth by division?

Simon Henry: Yes, that's an interesting question, Andrew. I predict that we're going to see some current competitors in the chemical logistics in Australia exiting the market. I talked about the significant expansion that we have carried out in the first half of some 40,000 square metres of space and hardstand and we are going to look to mop up business that's abandoned, you might say, by competitors, so strong growth there.

There's been very strong growth in the first half in our warehousing and logistics operation and we are seeing strong growth and as Alex our COO mentioned, a large number of tenders and other potential business flowing our way in the second half.

Andrew Draffin: You've largely answered the next question in that answer, but is the outlook for the strong second half based on organic growth or additional M&A?

Simon Henry: Not M&A, it'll be on extracting organic growth out of our existing assets, making full use of the 40,000 square metres and increased fleet that we invested in in the first half. But more importantly, you've got favourable growing conditions now over some of the primary agricultural regions in Australia, which is driving our crop protection products segment well. Really, any growth or that growth that we're expecting that we're experiencing now will be organic.

Andrew Draffin: Is it possible to get a rough breakdown of where the $21 million in CapEx has gone in the first half?

Simon Henry: Our CFO, Rob, is on the call. Rob, so you have that number handy?

Rob Perkins: Yes, Simon. I'll just refer people to the half year review report. There is a breakdown of those additions, but broadly speaking there was about just over $5 million in London buildings, about $3 million in plant and equipment, about $8.5 million in transport fleet additions. Then about $3.7 million capital work in progress on projects like the liquid waste treatment plant that Simon referred to in the presentation.

Simon Henry: Thank you, Rob.

Andrew Draffin: Just a follow-up, what is the outlook for CapEx in the second half?

Simon Henry: I'll answer it, Rob. We don't have any capital intensive projects that need funding in the second half, so we have got ample funding internally to fund anything that comes along that we think's worth investing in.

Andrew Draffin: Thank you. Given the share price, particularly this morning, will a share buyback be reconsidered?

Simon Henry: Not at this time. We are completely committed to driving organic growth in this half and reinvesting earnings to grow the network of assets, our customer base and our capabilities in capacity.

Andrew Draffin: Thank you. In slide 15 it mentions Australia, New Zealand and beyond when describing the business. Can you talk about the beyond a little further?

Simon Henry: Yes, we've got various businesses or commercial events taking place in North America. We don't own anything in America, we don't have any people on the ground, we're managing to do it well from Australia. We formulate chemicals in Australia and export them into Asia, so we do have an increasing global reach. But we have no plans to invest capital outside Australia and New Zealand, but just simple use our capabilities that we've already established to extend our commercial reach.

Andrew Draffin: Thank you and the last question I've got here is what do you say to shareholders, given the share price this morning, that are investing in the Company and the ongoing year-on-year growth? Is more M&A activity planned? I think you've answered that. Or is the focus now on organic growth?

Simon Henry: I can rest assure the party that submitted the question that management and the staff of DGL are utterly committed to running this Company well, ensuring its ongoing profitability and extracting organic growth from its existing assets.

Andrew Draffin: Thank you, that is all the questions that have been posted. I'll hand back to you, Simon, to close it out.

Simon Henry: Thank you very much and thanks to all those listening to the call. We look forward to talking with you again at the full year. I have a series of broker and analyst calls that I need to go to now, but thank you very much. Thank you to Krista for hosting it.

[END OF TRANSCRIPT]