

October 12th 2024

Skellerup Limited (SKL)



The company will hold its Annual Shareholders Meeting at **2.30pm Thursday 24 October 2024**.

The location is the **South Stand at Eden Park, Reimers Avenue, Auckland**.

You can also join the meeting [at this link](#).

Company Overview

The company is a designer, manufacturer and distributor of polymer and elastomer products and vacuum systems to customers in dairy rubberware, water and related infrastructure, roofing, plumbing, automotive, mining and a range of other industrial applications.

It has two divisions – Industrial and Agri – employing nearly 800 people. It has over 3,900 customers in 80 countries worldwide. Over 80% of its revenue is generated from international markets with manufacturing and distribution facilities and partners in New Zealand, Australia, China, Vietnam, UK, Italy, and USA.

Of note, the company is the second-largest manufacturer of dairy rubberware in the world.

After serving as Managing Director and CEO for 14 years, David Mair resigned as CEO in March 2024 but will continue to serve on the Board as a non-executive Director. The former CFO, Graham Leaming, was appointed CEO.

Current Strategy

Skellerup is a global leader in the design, manufacture and distribution of precision engineered products. It works closely with customers to define and solve their problems through a deep understanding of material properties, tool design, and manufacturing processes.

The company provides innovative solutions for customers in a wide range of critical and high-performance applications including dairy, potable and wastewater, roofing, plumbing sport, and leisure, electrical, health and medical, automotive, and mining.

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Key

The following sections calculate an objective rating against criteria contained within NZSA policies.

Colour	Meaning
G	Strong adherence to NZSA policies
A	Part adherence or a lack of disclosure as to adherence with NZSA policies
R	A clear gap in expectations compared with NZSA policies
n/a	Not applicable for the company

Governance

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Directors Fees	G	Excellent disclosure.
Director share ownership	G	See below.
CEO Remuneration	A	See below.
Director Independence	G	A majority of Directors are independent.
Board Composition	G	See below.
Director Tenure	G	See below.
ASM Format	G	Hybrid meeting.
Independent Advice for the Board and Risk Management	G	See below.

Director Share Ownership: In line with NZSA policy, the company notes that “*Directors are not required to own shares in the Company although ‘ve of the six Directors currently are shareholders of Skellerup.*”

CEO Remuneration: The company provides a simple overview of remuneration governance, strategy, principles and policies within the Annual Report. We note the focus on pay equity – the company is one of the few that reports on the gender pay gap and CEO/worker ratio within its organisation.

Incentives: The new CEO is paid a base salary and a short-term incentive (STI), both in cash, and a long-term incentive (LTI) by way of share options.

NZSA encourages fulsome disclosure in relation to any incentive payments made to the CEO, including disclosure of measures (or measure ‘groups’), weightings, targets, and the level of achievement versus target for each component associated with any awards. This methodology is supported by the new [NZX Remuneration Reporting Template](#), which the company has followed in developing its disclosures.

For both STI and LTI, there is no disclosure as to the ‘target’ *award* level in relation to base remuneration. The design of the scheme does not support a target remuneration mix.

The methodology for the STI is set out on page 60 of the Annual Report. As the STI scheme is a profit share scheme, based on achievement of EBIT (with a high-water mark), NZSA notes there is no cap on the maximum amount able to be earned.

Graham Leaming, in his previous role as CFO, was granted 800,000 options on 1 November 2022, at an exercise price of \$5.17 per share. The exercise price was the weighted average share price on the twenty-day trading period preceding issuance. The options are exercisable in the period beginning on 1 September 2024 and ending on 1 November 2024. The current share price is \$4.65.

LTI share options have been issued every two years, with an exercise price relating to a formula calculated at the time of issue. Note:

- the LTI options are exercisable only between a narrow window two years after issue. As we commented last year, this offers some potential for the CEO to ‘game’ or influence the share price to maximise option value during the trading period.

- The number of options granted does not appear to be related to the CEO's base salary.
- NZSA also considers the vesting period of 2 years to not be reflective of 'long-term' performance. We note the announcement made by the company on [October 4th](#) a change to a three year vesting term for options issued this year – a change supported by NZSA.

The nature of the STI calculation means there is no theoretical 'cap' on STI, albeit a high hurdle rate applies. This means that NZSA's preferred weighting towards LTI (to align with the long-term interest of shareholders) cannot be calculated.

Golden parachutes: We note the Annual Report states *"Skellerup does not make discretionary sign-on, retention or departure payments to incoming or existing employees (including non-executive Directors)."*

Board Composition: The company does not participate in the IoD's Future Director programme designed to develop and mentor the next generation of Directors. NZSA expect NZX50 companies to participate as part of a responsibility to develop and mentor the next generation of Directors.

Skellerup provides thorough disclosure of the skill sets associated with individual Directors and their relationship to the overall 'collective' skills required to govern the company. This is also highlighted on their website. The nature of the company's Board indicates a commitment to thought, experiential and social diversity, with relevant experience for Skellerup.

The Chair has commented in the Annual Report around the former Managing Director and CEO continuing to serve on the Board. NZSA assesses each situation like this on its merits: Mair's retention on the Board may create undue influence in the new CEO (Graham Leaming) charting any revision to strategy. On the other hand, his institutional knowledge is likely to offer support to the new CEO in the short-term.

Given SKL's track record, we are supportive of Mair's retention on the Board at this stage. However, given his length of service and the risk associated with the transfer of his institutional knowledge, we do not necessarily expect a significant future tenure.

Director Tenure: NZSA looks for evidence of ongoing succession or 'staggered' appointment dates that reduce the risks associated with effective knowledge transfer in the event of succession. We also prefer a term maximum of 9-12 years, unless there are exceptional circumstances that may apply.

The former Managing Director/ CEO, David Mair, was appointed to the Board in 2006 and as CEO in 2011. The other appointments range from 2015 to 2022. As discussed above, the company recognises Mair as a non-independent director, given his former role.

Independent Advice for the Board & Risk Management: NZSA looks for evidence, through disclosures, that a Board has access to appropriate internal and external expertise to support board assurance activities. We also look for evidence that Boards are across their risk management responsibilities.

We note that the statement in the Board Charter that *"A committee or individual director may, with the prior approval of the Chair of the Board, engage professional advisers at the Company's expense"*

to advise or assist them in carrying out their responsibilities.” It is unclear, however, as to the extent to which internal assurance staff have unfettered access to the Board. Discussions have indicated that the company does not have any internal assurance staff, operating a ‘co-sourced’ model for internal audit that reports to the Board. The Board also undertakes a significant programme of site visits.

The Annual Report offers good disclosure as to its financial, non-financial, business, operations, and climate change risks and how these are governed and managed.

Audit

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Audit independence	G	Good disclosure.
Audit rotation	A	See below.

Audit Rotation: The company ensures the Lead Audit Partner is rotated at 5 years as required by the NZX Listing Rules. We note the lead audit partner was appointed in 2023, but the appointment date of the audit firm (EY) is not disclosed.

Environmental Sustainability

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment
Approach	G
Sustainability Governance	G
Strategy and Impacts	G
Risk and Opportunity	G
Metrics and Targets	A
Assurance	R

Overall approach: Skellerup have provided some sustainability commentary in their disclosures since 2017, although there was still plenty to do ahead of the New Zealand Climate Standards becoming mandatory in 2024. Skellerup has made significant progress during FY24, achieving NZSA policy criteria in almost all areas.

NZSA policies encourage issuers to take a “broad approach” to environmental risks; this may result in disclosures that offer more insight into relevant environmental risks for the business beyond climate change. The company appears to have taken this broad approach, albeit much of the sustainability focus has (appropriately) been on climate-related disclosure compliance during FY24.

We note that the company has adopted most of the possible adoption provisions related to the CRD regime. NZSA considers this an appropriate step in the company building its capability to meet full disclosure.

Sustainability Governance: Skellerup says that “*The Board recognises a skills matrix can assist with identifying and assessing existing Directors’ skills and competencies*”. They provide a list of Director Core Competencies which shows the numbers of Directors that possess each of the 13 Core Competencies, one of which includes ESG. They also dedicate human resources to sustainability issues by way of the Sustainability Committee.

Strategy and Impact: Skellerup acknowledges that climate change is already having an impact on the markets in which the Group operates. While they report that the Group has not experienced any material impacts from climate change during FY24 they do note the increased pressure from customers and suppliers for greater transparency of their ESG initiatives and performance. They also conducted climate scenario analysis to map out potential climate-related impacts on the Group.

Risk and Opportunity: As signalled in their 2023 Annual Report, Skellerup have improved the disclosure of their climate-related risks and opportunities to standard required by the New Zealand Climate Standards. They identify numerous climate-related risks with detailed descriptions of each and associated mitigation measures. They also identify multiple climate-related opportunities.

Metrics and Targets: Skellerup have been measuring their Scope 1 & 2 GHG Emissions since FY2020 and provide comparative data from FY22, which shows a consistent reduction. They also began limited reporting of their Scope 3 emissions from FY24 which they intend to expand to all operating subsidiaries from FY25. They are yet to set science-based long-term emissions-reduction targets.

Assurance: Skellerup disclose that their GHG emission inventory has not been subject to any external assurance for FY24, but will be in FY25. When Skellerup begins this process next year, NZSA encourages the company to include the wider scope of all environmental statements or claims made in its Sustainability Report.

Ethical and Social

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Whistleblowing	G	Good disclosure.
Political donations	G	“ <i>Under Skellerup’s Code of Ethics, contributions to political parties are expressly prohibited.</i> ”

Financial & Performance

Policy Theme	Assessment	Notes
Capital Management	G	
Takeover or Scheme	n/a	

Skellerup's share price rose from \$4.75 to \$4.78 (as of 19th September 2024) over the last 12 months – a 1% increase. This compares unfavourably with the NZX50 which rose by 11% in the same period. The capitalisation of SKL is \$931m, placing it 37th out of 124 companies on the NZX by size and makes it a large company.

Metric	2021	2022	2023	2024	Change
Revenue	\$280m	\$317m	\$334m	\$331m	-1%
Gross Profit Margin	41%	40%	42%	43%	4%
NPAT	\$40.2m	\$47.8m	\$50.9m	\$46.9m	-8%
EPS ¹	\$0.206	\$0.245	\$0.26	\$0.239	-8%
PE Ratio	29	23	17	20	
Capitalisation	\$1.2b	\$1.1b	\$874m	\$931m	7%
Inventory Turnover	3.24	3.18	2.69	2.56	-5%
Current Ratio	2.56	2.66	3.47	3.36	-3%
Debt Equity	0.45	0.59	0.52	0.46	-12%
Operating CF	\$58.8m	\$43.3m	\$54.1m	\$70.8m	31%
NTA Per Share ¹	\$0.71	\$0.75	\$0.81	\$0.83	3%
Dividend Per Share ¹	\$0.17	\$0.205	\$0.22	\$0.24	9%

¹ per share figures based off actual shares at balance date (not weighted average)

In what was undoubtedly a tough environment, SKL performed well. Their NPAT figure was also affected by a one-off law change affecting the tax expense adversely.

Revenues were down 1% to \$331m, however Cost of Sales were down 4% meaning the profit margin increased to 43%, and EBIT increased to \$72.7m.

After adjusting for a one off, adverse tax expense related to removal of tax depreciation on buildings of \$3.1m, NPAT was down 8% to \$46.9m which provided EPS of \$0.239 and enabled SKL to pay an increased dividend of \$0.24. Excluding the taxation impact, NPAT would have remained broadly consistent with the prior year.

Dividends are only partially imputed to 14% and we note that EPS is lower than dividends. The company could look at more tax efficient, alternate means of distributing excess cash.

The PE ratio increased slightly to 20. There are signs that the NZ and global downturn is at its nadir, and falling interest rates will also provide relief.

The company has traded well, but inventory turnover was down further to 2.56, and Inventory levels fell slightly. SKL remains in a sound financial position with an ever-decreasing debt-equity ratio of 0.46 and paid off \$10.3m of long-term debt during the year.

SKL trade at a generous 474% premium to their NTA of \$0.83. This is partly a reflection of their exceptional longer-term performance and also their relatively large holding of intangible assets on the balance sheet.

In conjunction with their full year results, the company [provided](#) the market with a presentation.

The company as is their wont has not provided forward guidance for FY25.

The company register is extremely widely held and the largest shareholder is Forsyth Barr Custodians Limited.

Resolutions

1. To re-elect Alan Issac as an Independent Director.

Alan Isaac Alan was appointed to the Board in August 2016. Alan has considerable experience governing and leading businesses and sporting organisations. He is currently Chair of the New Zealand Community Trust. He is also a director of NZX listed Oceania Healthcare Limited and Scales Corporation Limited. He was Chair of KPMG NZ for 10 years until 2006, is a past Chair of Cricket NZ, past President of the International Cricket Council, and the New Zealand Institute of Directors. Alan's contribution to sport and business was acknowledged with his appointment as a Companion of the New Zealand Order of Merit (CNZM) in 2013.

We will vote undirected proxies **IN FAVOUR** of this resolution.

2. To re-elect John Strowger as an Independent Director.

John Strowger was appointed to the Board in March 2015 and as Chair in October 2022. He retired as a partner of Chapman Tripp on 30 November 2022. John specialised in corporate, contract and securities law, mergers & acquisitions as well as heading the firm's China desk. He was named NZ Deal Maker of the Year at the 2015, 2017 and 2019 Australasian Law Awards. John is a Director of NZX listed Sanford Limited and sits on the boards of, and advisory committees to, a number of private sector businesses.

We will vote undirected proxies **IN FAVOUR** of this resolution.

3. To increase the Director Fee Pool by \$200,000 (31%) from \$650,000 to \$850,000.

The current Fee Pool was approved by shareholders at the 2021 ASM. With David Mair now a non-executive Director the Fee Pool needs to be increased to provide for his fee. At the current fees, the total paid would be \$750,000 leaving headroom of \$100,000. This would provide for the appointment of additional Director if deemed appropriate.

The Board has commissioned PwC to prepare an independent Report and a link to this is included in the Notice of Meeting. The Report includes comparator company data and concludes the current Chair's fee is at 100% of the median and Directors fees are at 106% of the median.

NZSA's own assessment shows that the proposal is towards the top end of our calculated range.

We will vote undirected proxies **IN FAVOUR** of this resolution.

4. That the Board is authorised to fix the auditor's remuneration for the coming year.

This is an administrative resolution.

We will vote undirected proxies **IN FAVOUR** of this resolution.

Proxies

You can vote online or appoint a proxy at <https://www.investorvote.com.au/>

Instructions are on the Proxy/voting paper sent to you.

Voting and proxy appointments close **2.30pm Tuesday 22 October 2024.**

Please note you can appoint the Association as your proxy. We will have a representative attending the meeting.

The Team at NZSA