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Company Insight
the intelligent market update

Swick Mining Services Limited

Date of Lodgement: 30/7/12

Title: "Company Insight – 4Q 2012 Update"

Highlights of Interview

- **Mobilisation is complete for the two major contracts awarded in 3Q 2012**
- **The Company currently has 62 rigs in work compared with 52 rigs at the end of 3Q 2012**
- **Discusses why Swick's exposure to the underground drilling market has major strategic advantages over exposures to surface drilling, where demand has been softening**
- **Explains the reasons why the Company is significantly more resilient in 2012 compared with 2008 - due to lower gearing, better strategic business focus and better commodity exposures.**

Record of interview:

We interview Kent Swick, the Managing Director of Swick Mining Services Limited (ASX: SWK, market capitalisation A$66 million) about the Company's operations during 4Q FY2012.

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How would you describe the operational and demand conditions experienced by Swick during 4Q 2012?

Managing Director, Kent Swick
Following our 3Q 2012 tender successes with Gold Fields St Ives and Argyle Diamond Mine, mobilising to these sites and commissioning these contracts has been our main focus. It has been a busy time throughout the business in all departments as they have had to work to build and commission rigs, crew these rigs and establish two large sites. For these contracts, a total of 9 underground diamond rigs have been mobilised in the last three months – so we now have a full complement of rigs at both St Ives at Kambalda, and at Argyle. We'll see the benefit of these arrangements throughout FY 2013 and beyond, as these are long-term contracts.

4Q 2012 was a little bit quieter in tendering terms, but that was more because of timing. Renewals are going well – and we've found we can avoid going to tender in most cases as generally we have great working relationships and can normally agree on rates without having to go through the full tender process. We're in a bit of a renewal period between now and the end of the year but from our understanding of our client base, our revenue is looking very secure. Generally, clients are focusing on efficiency – and we're on the same page as them. We've been developing additional efficiencies – and have significantly increased metres-per-man-hour this year – which means even though our input costs may increase, the increased efficiency through productivity means our margins are maintained. Clients have been agreeing to reasonable rate rises but nothing that would constitute large increases.

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When will the further six (6) underground drilling rig builds be deployed under the contracts the Company won in 3Q 2012? Also, what did the rig expansion cost, and how was it be funded?

Kent Swick
The six builds were completed late in Q4 2012 and the last two were mobilised to St Ives in early July.

As we indicated, the total cost of the Swick rig builds will be around $6 million total capex for the rigs and their ancillary equipment. This has all been internally funded by cashflow since the Company's EBITDA and operational cashflow is strong. We will also have the ability to self-fund incremental expansion – and in that regard - future builds are likely to be cheaper because the first-builds carry the R&D costs.

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What are the Company's current rig utilisation levels?

Kent Swick
Overall rig utilisation is currently 83% - up from 81% at the end of June 2012.

In the surface RC market, where we target brownfields business, we have 5 of our 7 rigs booked out for the FY 2013 drilling season – there are 4 currently working and another is in the process of being mobilised – so that's good in the current circumstances. At 30 June, the underground diamond division in Australia had 43 out of 47 rigs utilised but was still mobilising a couple of rigs at the June month-end, so that's now 46 being utilised out of the available 50 rigs. North America probably lets it down a bit, with 5 out of 11 rigs working, but the tendering season doesn't come up until the second-half of calendar 2012. Finally, we have all of our 4 underground longhole rigs and 3 out of 3 underground longhole client rigs working.

In summary, we have added 10 rigs in work since the end of March, making a total of 62 rigs in work and a current fleet utilisation rate of 83%.

	At 31 March		**At 30 June 2012**		**Currently**	
	Utilised	Available	Utilised	Available	Utilised	Available
North America	3	11	5	11	5	11
Aust UG diamond	39	45	43	47	46	50
Surface RC	4	7	4	7	4	7
UG longhole	3	4	3	4	4	4
UG long client	3	3	3	3	3	3
	52	70*	58	72	62	75*
Utilisation		74%		81%		83%

* please note that 1 of the 6 additional rigs was completed before 31 March 2012

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What are the current plans for additional builds, and what are your observations on how Swick's rig building processes have developed?

Kent Swick
Since our underground diamond rigs are approaching capacity, our Board has given approval for a second tranche of new builds. We now have another six underground diamond rigs under construction in the workshop, and a fleet retrofit program underway to increase the capacity of the older established fleet. The targeted rig development position is therefore as follows:

Rigs currently available	75
2nd tranche	6 new Swick rigs
Total rigs available after 2nd tranche	81

This new build program comprises new Swick builds where the vast majority of components including the carrier are built in-house. Traditionally our rigs consisted of a hybrid between an Atlas Copco single boom mining jumbo and Boart Longyear drilling components. The Swick builds allow our fleet to maintain its standardisation and removes the reliance on third parties - which allows us to be very reactive to operational needs throughout our contracts.

This new approach allows us a lot of flexibility with our scheduling – we can ramp-up and ramp-down our rig-build program without having to forward order components, chassis and so on. There are also net benefits in terms of capital costs – we expect around a 20-25% reduction in the long-term capital costs of our rigs, which will help our return on capital, but the main improvements are in rig design. The Swick internally-built rigs have a capacity to operate either through hydraulic or electronic controls – and with electronic controls come the potential ability to automate the rigs. We're working with our R&D team and one of our key suppliers – to allow semi-automation of our rigs to the point where we can reduce the numbers of men required to operate our rigs from 2 to 1 – thus generating a significant benefit that can be shared between us and our clients.

We're investing in this technology with the goal of doubling metres-per-man-hour over 5 years, and over the past financial year we've achieved improvements of 20-25%. This is a tremendous achievement to date, and shows the investments and innovations are paying off. In financial terms, we believe the features we're incorporating into all our rigs will ensure profitable paybacks for Swick, and strong rig utilisation for some time to come.

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Is there any evidence of softness in the Australian surface drilling market flowing into the underground drilling market?

Kent Swick
No – not at all. Obviously we're in close and regular contact with our clients, so we understand their needs in advance and cater for them – and there's no indication of paring back in long-term arrangements. We're not seeing this effect at all at the moment.

There are a lot of differences between underground drilling and surface drilling markets, where we've deliberately lowered our strategic exposure.

The surface diamond drilling market is fragmented and much more competitive than other areas of the drilling market. As a result, in times of economic downturn, smaller and less sophisticated drilling contractors than Swick, with lower overheads and operating costs, reduce their charge-out rates and thus become more attractive to clients.

By contrast, underground rigs are an essential part of an underground mine's development and operational activity. Miners need to understand in detail where the ore body is and tune their mining activities towards it. They need to understand an ore body's grade, metallurgical composition, and its position in space so they can mine accurately. They want to know where the envelope is so they minimise dilution. It is very costly to develop underground and they want to minimise their development metres and maximise their tonnes of output. So diamond drilling has a very important function in underground mines – and if people want to keep mining – and they've usually got a huge invested stake – underground diamond drilling will continue. They are not really undertaking traditional exploration drilling - they know the ore body is there at this stage – this is grade control, reserve definition and a bit of exploration on the side to see how far the ore goes and whether there may be additional lenses.

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Overall, how would you assess Swick's position as a business in 2012, compared with 2008, for what - some say - could be challenging times in the resources business?

Kent Swick
There are major differences - we're significantly better-structured in 2012.

Back in 2008 Swick had a balance sheet geared to growth, and had large exposures to surface drilling and nickel. When the rapid expansion came to an end for everyone, our cashflows were significantly affected, in particular by ongoing asset finance commitments of around $1.8 million a month of principal and interest.

So we really targeted our business to focus on our core strengths – underground diamond, underground longhole and surface RC drilling – and sold the surface diamond division to pay down debt and fix the balance sheet.

Now we are completely different. We then had 65% underground revenue, today it's 88%. We are now effectively an underground diamond drilling business where we can provide the best-practice or market-leading services we've developed. Underground is a much better place to be for a quality service provider. Underground miners rely on the information supplied by their underground drilling, and because safety and productivity in brownfields sites are very important, these issues can't be compromised in the same ways as for surface exploration. Strategically, the Company's business revenue is now much more secure - but I should add that underground drilling doesn't just have great defensive qualities - it has also proved to be an excellent growth area for the Company.

Our net debt position will shortly be zero, we've moved our debt from an asset finance basis to a corporate facility and our regional spread is much broader. Our commodity spread is completely different as well – only 2% of group revenue is exposed to nickel versus 24% in 2008. Gold and copper –which have proven to be the more resilient non-ferrous metals – comprised about 83% of our revenue in 2012 compared with 58% in 2008.

So – and perhaps the market doesn't understand our position –we've worked diligently to get our commodity and regional spreads right, and to rectify our business focus and balance sheet settings. The Company is in a significantly better strategic position in 2012 compared with 2008.

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Thank you, Kent.