

Smiles Inclusive Ltd [Smile's] Belated 31December 2019 Report

Smiles has finally been able to produce a half yearly report to 31/12/2019. It remains suspended from trading on the ASX and may be reinstated after it produces full financial year 2020 audited financials to the satisfaction of ASX listing requirements. It is apparent that it's auditors were not prepared to sign off on the half year reports on it remaining a going concern until they were given the comfort of a substantial capital raising being underwritten and indications that Smiles has negotiated a settlement with National Australia Bank involving a partial forgiveness of debt of \$6million out of total debt of \$19million.

Even so the audit sign off was subject to a significant disclaimer. Smiles has undertaken to repay the remainder of its debt to National Australia Bank, partially with the net proceeds of its capital raising of \$8million minus underwriting fee and expenses of the raising. It is apparent that its directors have found another source of borrowings albeit further details need to be confirmed.

The half year report to 31December 2019 revealed a net loss of \$10.9 million and as at 31 December 2019 Smiles had a net deficiency of \$7.2million which was a parlous state of affairs for a small company. Investors originally subscribed \$1.00 per share at IPO whereas this current capital raising is at 2.5 cents per share and follows on from other heavily discounted capital raisings; particularly the 1 for 1 underwritten share issue of 16 October 2019 which raised approximately \$3.3Million.at an issue price of 5cents per share.

Earlier this year founder and initial CEO Mike Timoney sold the shares granted to him and held beneficially in his superannuation fund at 1.1 cents per share in a transaction notified to the ASX. Although Smiles shares had last traded at 3.5 cents prior to being suspended this transaction suggested that it's value was much less.

The half yearly report to 31 December 2019 indicates an increase in revenue over the previous corresponding period but it must be noted that the half yearly accounts included the revenue from the Gatton and Laidley practices which were sold during December 2019 to 1300 Smiles Ltd and also includes revenue from practices closed down as well as Miranda and Yarram practices sold more recently.

It is not stated what impact on revenue that the loss of those income streams had. It is to be hoped that the full year 2019 accounts provide shareholders and possible investors in the coming capital raising an accurate picture of the underlying continuing revenue indicating the past revenue produced by the practices still owned and operated so that investors can get an accurate picture of the likely continuing revenue.

It is noted that ASIC initiated action on 24 September 2020 requiring Smiles to lodge its 31 December 2019 accounts by 3 November 2019. It must be assumed that ASIC is closely monitoring Smiles Inclusive Limited situation.

Further Losses

The full years financials to 30 June 2020 are yet to be completed and must be regarded as urgent given the underwriting of a capital raising. Investors will not be appropriately informed without a full year report. This report is likely to reveal substantial full year losses offset by Jobkeeper payments.

Smiles is a small company, the operations of which, has seen a massive destruction of shareholders capital. It has barely kept afloat through a series of capital raisings at vastly lower prices to that which initial investors subscribed in its IPO.

Close reading of Smiles half yearly report reveals it to be extremely sparing of information.

The report indicates that in the period, July to October 2020, 13 new practitioners joined the group but nowhere has it said how many practitioners have left the group between its IPO and present! It states that it now has 126

dentists, oral health therapists and dentists but doesn't give the numerical breakdown of the three categories, of which dentists are the most significant, nor does it say what the numbers were at the time of its IPO. Nor does it tell us how many of each category are full time staff or how many are part time staff.

We could be forgiven for viewing the numbers provided as an attempt to present a picture that is more attractive than might be indicated if a more complete table of the employed/contracted clinical staff were provided on a fulltime equivalent basis and compared with the numbers at the time of Smiles IPO.

Staff Survey

According to the report 60 percent of dentists and other staff completed a survey showing that they felt that "the new leadership is a positive change for the business and had created a culture of teamwork and cooperation." This begs the question that; If only 60 percent completed this survey does it mean that 40 percent chose not to participate?

And did all of the 60 percent endorse this published conclusion or only a majority of those choosing to complete the survey? And were the questions in the survey designed to lead toward a particular answer? We are given too few facts to form an accurate judgement.

Practice Sales Closures and Consolidations.

There have been several practice sales including the sale of two practices to 1300 Smiles Ltd in December 2019 for a gross amount of \$2million, the more recent sale of a couple of practices in Victoria and several practice closures plus the cessation of a number of premises leases suggesting a consolidation of practices to fewer locations. It is not clear from the report exactly how many locations Smiles is currently providing dental treatment from. This needs to be explicitly set out.

Smiles half yearly report states that;

"The Group also entered into a JVP buyout for Clayfield and Glen Waverly practices, which forms part of the company's multi-faceted strategy". It is unclear whether Smiles was a seller to the Joint Venture partners in those practices or a buyer of their equity?

For shareholders and new investors to be adequately informed as to the future outlook for Smiles business a great deal more information needs to be provided both in its forthcoming 2020 financial year annual report and in the forthcoming offer document. The limited information provided to date is simply inadequate and therefore may advantage some potential investors over others starting with the underwriters to the imminent capital raising.

It is also essential that before considering this new offer shareholders and investors are provided with a reliable statement as to when the ASX will permit trading in its shares to recommence.

Shares Issued and to be Issued.

According to the company's ASX web site it currently has 159.23 million shares on issue compared to approximately 66million shares immediately after its IPO. This new capital raising of \$8million from issue of shares at 2.5 cents per share will result in a further 320million shares being issued **bringing total shares on issue to 479.23million!** The original shares after IPO will have been massively diluted in continuing efforts to keep this company afloat. Those original shareholders who took up the 1 for 1 offer at 5 cents per share a year ago have seen those share heavily diluted as well. Rather than being a reliable business Smiles Inclusive Ltd is somewhat akin to those speculative mining companies which repeatedly use up shareholders capital in the search for illusive mineral wealth and repeatedly return to capital markets for more capital.

Status of Legal Actions

It is noted that;

"The Group is also party to a number of ongoing and threatened legal matters which may result in further liabilities arising, the outcome and quantum of which is unknown at this date."

Information about legal actions is inevitably limited and speculative because the actions can change. While there has been speculation as to the possibility of a class action by those who subscribed to the initial public offer it is impossible to determine whether the risk of a class action by initial investors who subscribed \$1.00 per share has passed until a great deal more time has elapsed.

The company has dismally failed to meet its forecasts as outlined in its IPO offer. It may be expected that it's directors past and present, those advisers who urged investors to subscribe for stock, the investigating accountant who indicated financial performance in the IPO document and professional indemnity insurers will still be nervous. Capital raising and partial debt forgiveness by NAB may lessen their risk but it is too early to be certain that the danger has passed. Or that a threat by a different group of class action lawyers will not emerge.

Best wishes to all dentists

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