Conference call transcript

7 March 2019

INTERIM RESULTS PRESENTATION TO INVESTORS AND MEDIA

Ed Jardim

Good afternoon ladies and gentlemen. Welcome to the Murray & Roberts interim results. Just before I hand over to Henry to kick us off just a quick note on safety. In the unlikely event of an emergency, please move out of this door to my left, and left again towards where the bathrooms. There's an emergency evacuation door on the left. Break the glass to release the door, make your way down the stairs to the ground floor, out and around the building and to the public parking space across from the building. That's the emergency assembly point.

You have another way to evacuate off this floor. It is once again out these doors to my left towards the lift lobby. There are a set of stairs on either side of the lifts. Please make your way down those stairs to the ground floor, out the main entrance where you came in this morning and across the road to the public parking space. That is the assembly point. And our security staff and our HSC reps will assist with the evacuation. Thank you. Henry, over to you.

Henry Laas

Good afternoon all, and welcome to this results presentation. Also welcome to the people on the webcast. And I must say I really appreciate the fact that you've taken the time to be here today. It is so convenient with the technology to view this presentation in your office. And it takes time to travel all the way to our offices and to get back to your office again, so we really appreciate the fact that you've taken the time to be here in person. I think it's important to start this presentation with a statement again that Murray & Roberts as a group has transformed to be a multinational engineering and construction company. It is different to what we've been in the past. The business is made up of three separate business platforms, and this provides some portfolio diversification.

Another aspect which is important to remember is although we have core markets in the business that we are focussing on in the natural resources space, there are also complementary markets that are of equal importance and we focus on these markets as well because collectively they mitigate against the cyclicality that you find in markets. So we have been through this transformation. We have positioned the company as a player in the natural resources space. And this strategy is starting to unfold.

As I said three business platforms. The main markets we are focussing on is Oil & Gas, Underground Mining, and Power & Water. But the complementary markets are also very important, and you will understand that context when we unpack a little bit more, especially in the Oil & Gas platform and the gap that we have with oil & gas projects coming to an end and the new ones not having started yet. The complementary markets have got a specific role to play in that context.

March 2017 was the date when Murray & Roberts moved its listing on the JSE from the heavy construction subsector to the diversified industrial subsector. To us that was the time when we broke away from our past and started this journey on this new strategic future. We believe that we have a clearly defined growth plan for the group. Our business model is clearly defined and we need to diversify our business model. And the fact that we are more and more diversifying into the international market is very important to us. So the growth plans we believe are clearly defined.

Our balance sheet we believe is robust. We have been through a number of years of relatively mediocre performance and we still maintained a very strong balance sheet during this period. It is important for a company such as Murray & Roberts to have a strong balance sheet because we are still pursuing our growth aspirations and we need to be in a position to fund acquisitions as and when these opportunities do present themselves. I will say a few more words about that shortly. And then finally as far as the order book is concerned we believe that we've got a quality order book and the order book is growing. And we are very optimistic that in the second half of this year there will be further substantial growth in our order book.

We have in the beginning of the second half of this financial year just after the reporting period concluded two acquisitions. They are relatively small but they are both of strategic importance to the group. We have been trying for several years to position ourselves in the American market in the Oil & Gas platform. And we have identified a few targets. We have gone through a process but we have never been able to close any of these acquisitions. And I think the biggest problem that we've encountered is that there was a realisation by the prospective sellers at the time that this market was presenting opportunity, and the longer the negotiations continued the higher the expectation became of the selling price. So we were never able to close an acquisition.

As you all know, acquisitions are important, but if you don't take the right price even a good company can turn out to be a bad deal. And what we decided to do is to pursue another target a lot smaller than we had in mind. But we closed the deal and we acquired a company for $5.2 million. It is based in Houston. It is an engineering, procurement and construction company capable to undertake work on an EPC basis up to about $500 million. That acquisition has been concluded. As I said it was at the beginning of the second half of this year. And Peter is already busy with his team to integrate that business. And the ultimate objective is to consolidate our US interests under the Clough USA brand. So we are very pleased with that acquisition which is strategically very important.

Then as far as the Power & Water business is concerned, we have mentioned previously that as we do not see great opportunity in the traditional market of building new power stations in South Africa we had to expand our service offering into other segments of the power market, more specifically opportunities in the maintenance space – and there is not much traction or movement yet – but also as far as transmission lines are concerned. There is a huge shortage or demand for new transmission lines in South Africa and also in Sub-Saharan Africa. We have acquired a small company called Optipower. It is not a big acquisition. It is R37 million. But we are now positioned to take on projects in the transmission space. And Eskom currently has got 300km of 400kv overhead power lines out on tender, and we are tendering on that work, and we are confident that in the second half we will start with execution on some of these tenders that we're currently bidding. But Sub-Saharan Africa as I said is also important. The transmission opportunities in that market are significant. So these two acquisitions, one in Oil & Gas and one in Power & Water, are important for us that we have closed those out in the beginning of the second half of this financial year.

I guess most of you are also here today to ask and to find out more about the ATON attempt of acquiring control of Murray & Roberts. I just want to comment on that very briefly. The ATON mandatory offer is still open. It's in the market. It is subject to various suspensive conditions. ATON is in the process of working through the regulatory approval process. And that process is progressing, but it hasn't reached finality yet. The merger approval was granted in Zambia. It was conditional approval. And unconditional approval was granted in Namibia. The two important jurisdictions where approval is required is Canada and South Africa. And the authorities in both these countries are still working through the application. So no finality yet as far as Canada is concerned, and no finality yet as far as South Africa is concerned. And as I said those are the two important areas where approval is required. If you ask me whether the approvals will be obtained before the long stop date, which is the 31st March, my view is that it is extremely unlikely. It is extremely unlikely that the approvals will be in place before then.

Now, what does that mean? First of all, this long stop date of the 31st March is a date that ATON may elect to extend. It is not a date that is cast in stone. They may elect to extend the long stop date to a later date. How the process will work is if ATON achieves all the approvals what they have to do is they have to make an announcement at the time that the offer becomes unconditional. If all the suspensive conditions have been met they have to make an announcement to announce that the transaction is unconditional. There will be ten business days post that announcement for our shareholders to decide whether they want to accept the ATON offer or not. In the event that ATON does not extend the long stop date and the approvals are obtained before that time then the offer will terminate and it will be the end of that process. So we are approaching the 31st March, and depending on where the approval processes are, ATON may elect to extend the long stop date or they may decide not to do so. So we don't know. It is really a decision which ATON has to take as the offeror.

From the valuation point of view ATON made the initial offer at R15 a share, and that offer was later on increased to R17 per share. The independent board considered the offer and they undertook their own valuation and conclude that a fair price range for control was between R20 and R22 a share. Over the past couple of months the independent board has again through that valuation process and refreshed that valuation taking into consideration current market circumstances and came to the conclusion that the R20 to R22 remains valid as a fair price range for control.

So if the time arrives – and if it does – that ATON declares the transaction unconditional our shareholders will have to decide whether they're going to accept the offer. Currently the share is trading at between R14 and R15 per share. The offer is at R17 per share, and we believe that the true value is between R20 and R22. Our shareholders must then decide whether they would like to accept the offer or not. If you ask me, as I said I think it's unlikely for it to become unconditional before the 31st March. But I think we are reaching the end of this process. It cannot carry on indefinitely. But I would doubt that the 31st March would be achieved for the transaction to become unconditional.

Back to the results. Revenue was slightly down on last year, around R10 billion. Attributable income shows an improvement on last year from R110 million to about R190 million. And diluted continuing HEPS is on par with what we have in the first six months of the previous year. But in a nutshell, what we experienced in the first six months of this year was really an exceptional performance by the Underground Mining Platform. The Oil & Gas platform and Power & Water have disappointed. And there are reasons for that, and we will work through it. Really the highlight of the first six months results was reported by the Underground Mining platform and the growth that we've experienced in that business.

The order book is R32 billion. The order book is starting to grow. And you will see later on in the presentation there is quite significant value in near orders. And as you know by now, near orders find their way into the order book, so we would expect by the end of June to report a further substantial growth in the order book. And the cash position of the company is still robust and strong.

Just maybe a closer look at the Oil & Gas platform. Peter is here as the CEO of that business. Maybe after the presentation if there are questions Peter would answer those with me. The important point to make is that the LNG capex recovery we think will certainly happen within the next two years. This market has been the main market which contributed to earnings in this platform over the past five or even more years. And as you know, we've been through a period with lower investment in this sector and project delays. And what we're currently experiencing is there is pressure on the revenue in the Oil & Gas platform.

We are getting to a point where we are closing out the larger projects that we've been working on like the Ichthys project. All of that is coming to an end. It will be finally concluded and completed in the second half of the financial year. We are ramping down, but the ramp-up on the new projects has not yet started. You will recall that we have earlier this year made an announcement where Clough, or the joint venture which Clough is a part of as a 35% participant in that joint venture, has been identified as the preferred bidder for the Snowy Hydro Project in Australia, which is a multi-billion dollar project. And our share of the work is in the order of R14 billion, and if all goes well the agreement should be signed early in April, early next month.

Should that happen it will be a significant boost to the order book and it will also be very significant to enhance the revenue stream into the Oil & Gas platform whilst we are still struggling to get out of the blocks as far as new capex in the LNG space is concerned. In late January, early February this after, after the six-month period, we have secured a $130 million project with BHP Billiton which will also find its way into the order book when we report at the end of the full financial year.

Then as I mentioned earlier on the acquisition in the USA is important in LNG. Most of the activity currently is in that market, and to have a presence in that market and capability to execute projects on an EPC basis is important for us. So the focus I would think as far as LNG is concerned is moving a little bit away from Australia and more into the international space, specifically what we've done in the US now. But also I think we can agree that the projects in Mozambique are very close to the point of execution. There are also two sizeable LNG projects in Papua New Guinea which Peter is targeting. And we believe that we are very well positioned to participate in those projects through past relationships that we have with the clients.

The Underground Mining business we can say without any doubt that this is the world's leading underground mining contractor. The business acquisition that we've achieved after several years of really hard work… And there was debate whether Murray & Roberts Cementation is the number one underground mining contractor or whether it is Redpath which belongs to the ATON group. But I can really say with confidence that Murray & Roberts Cementation is the number one underground mining contractor. We've done very well in the first half of the year. Our order book has grown strongly and we believe that there is still several years of an upcycle that we will be able to benefit from.

So this is something that we are very excited about. If we talk about this business being a global business, I think that is supported by the fact that we've got a lot of project work in Australia, in Indonesia, in Mongolia, in the US, in Canada, in South Africa and in Zambia. It really is a global business. And the work that we do, eight vertical shafts under construction as we speak, 81 decline shafts, eight contract mining projects, and contract mining is production mining where we essentially operate and mine the ore on behalf of the client. And what we are trying to achieve is a position where at least 50% of our earnings in that platform must come from contract mining projects because the benefit of that is you have continuity of work throughout the commodity cycle. Projects get a peak in the upcycle and get a trough in the down cycle. But in the contract mining you have some protection against the cyclicality.

And then our global reach, the fact that we've got this reputation of safe and successful project delivery in the mining space, has really started to develop into something of real significance. There are currently banks that are providing finance to clients to fund their developments and it is conditional upon Murray & Roberts Cementation implementing their projects. There is more than one example of that where the funding of a project was approved on condition that the Cementation business implemented it. So for us this is something that we are very pleased about. And as I said a business that will continue to make a significant contribution to Murray & Roberts' earnings for several years to come.

The Power & Water business unfortunately there is a lack of meaningful replacement work for Medupi and Kusile. We have completed our work at Medupi and Kusile will continue until sometime in FY2020. And there is just no meaningful work to replace Medupi and Kusile. The baseline power programme in South Africa has been delayed. There is no near-term major opportunity to replace Kusile and Medupi. So we are targeting the broader power market which includes other segments such as maintenance, which includes segments such as transmission. And I've spoken about the Optipower acquisition of R37 million.

I really believe this unbundling of Eskom into three separate units, being generation, transmission and distribution, will create opportunity for ourselves. We have been trying for a long time to break into the Eskom maintenance market and we haven't been able to do so. We responded to a request for proposal in November of last year. There hasn't been any adjudication yet, but we are confident that we will get a sizeable portion of that work. And then as I said through the acquisition of Optipower we have positioned ourselves to participate in the transmission network providing work in that space.

Just to give you a feel if we say there is no meaningful replacement work for Medupi and Kusile, late last year there were two sizeable projects in the market. We secured both of them. The combined value is R600 million. Now, that's not the profit. That's the revenue on these projects. But it gives you a feel for the size of projects that are available to companies such as Murray & Roberts and our Power & Water business to pursue. The investment also in the local waste water treatment infrastructure we think is problematic in South Africa. We know the lack of investment in water infrastructure and the future problems that will come from that. But unfortunately for some or other reason the investment is limited in this space and it is fragmented. We are continuing to hold on to our water business and our capability that we have in that space, and we really believe it's a matter of time before investment will start to flow and we will be able to participate in the water business in a more meaningful way.

The order book, I've already spoken about the mining order book. It is R26 billion. That is a strong order book. Oil & Gas it is low, as it Power & Water. But you will see two slides on it. There is significant opportunity in near orders and all those opportunities will be recorded as order before the end of this financial year. This gives you a feeling of the geography and time distribution. So the order book currently is about 40% SADC, 60% in the international space. When Snowy Hydro comes in it will completely change that balance to 20/80. From a time distribution point of view R13 billion of this order book of R32 billion is scheduled for execution and for delivery in FY2020, our next financial year.

Just to clarify a few definitions if we talk about our order book and our pipeline. The orders at R32 billion are not part of the pipeline. That has already been secured. The pipeline talks to opportunities which have not already been secured and do not form part of the order book. We start with the first category, which is near orders. For an opportunity to be classified as a near order it means that we have to be informed by the client that we've been successful on the project, but we are still in the process of closing out the commercial terms, crossing the t's and dotting the i's in the contract. Oil & Gas there is R14.2 billion, and as I said earlier on we are targeting early April to have all the agreements signed for that R14 billion to move into the order book.

In category one there is R33.2 billion in Oil & Gas. Category one is tenders that have been submitted and tenders that we are currently working on. This project for BHP Billiton that I've mentioned of $130 million or R1.3 billion, that opportunity just after December moved from a category one transaction directly into the order book. So it does not always happen that an opportunity moves from category one into a near order, and from a near order into the order book. Many a time tenders that you've submitted and conditions under which you have tendered are accepted by the client, so there is not much of a negotiation left before you can bring it into the order book. It moves straight from category one into the order book.

In Underground Mining there is R8 billion. R4 billion of that relates to Venetia, and that R4 billion you must not expect to see all to come to orders before the end of Juned because what we have here is a scenario that the work has been awarded to us, but this is a salami slice process. We work through a certain scope of work; then the additional portion of work is released. So that R4 billion will find its way into the order book over time. And then there is a near order of R3 billion for chrome mine. It is a contract mining opportunity. And we heard this morning that we may be two or three weeks away from finalising that agreement. So the pipeline we believe is strong.

And if you consider revenue in the first half of this year was R10 billion, let's just assume for purposes of estimation that revenue in the second half is going to be R10 billion again, it would mean that R32 billion order book will reduce to R22 billion because R10 billion of that would be executed in the second half of the year. And for us to stand still and to maintain the order book at R32 billion we would have to secure R10 billion of new work before the end of June. but if you look at the near orders and the way we see the market presenting itself in Underground Mining we are hopeful that we will see a significant growth in that order book by year-end, notwithstanding the fact that we will burn R10 billion in the second half of the year. Maybe we will be approaching something like R40 billion by June this year. The order book for us is starting to grow, and that is significant because with a business such as Murray & Roberts you need an order book, you need a backlog, you need to have work to generate revenue and be able to generate the profit.

And then on my final slide before I hand over to Daniel to take you through the numbers in more detail, this morning we had a staff presentation and we discussed the results with the staff. And what I said to them was at any time, or at this moment in time, I'm not sure exactly how many projects we have in execution, but certainly it is more than 100. Maybe it's 120. I'm not sure. And for us to be successful on a project from a financial point of view and from a safety point of view you have to have good people on the job and we have to make sure we've got good systems and good processes for project execution. This is quite an organisation and it's quite an achievement I would say to be able to report to you that our lost-time injury frequency rate for the first six months of this year was 0.63. That is expressed per million man-hours. That is in the context of 100 plus projects under execution globally and also taking into consideration the risk conditions under which many of these projects are being built. So that for us is something that is very important.

As you can see on that screen, no fatal injuries occurred in the first half of the year, and that is just great to be able to stand in front of you and to say that. We've got the commitment to make sure that by the end of the financial year that we will be able to maintain the results. Daniel, over to you to talk to the results in a bit more detail.

Daniël Grobler

When I started this morning I said that this is actually the most exciting part of the presentation. So there are going to be no pictures. There are only going to be hard-core financial facts. And anyone who falls asleep now I'm going to struggle to explain that. If you look at the performance of the company as a whole we talked about Underground Mining. EBIT in Underground Mining has gone up as well as the order book. There has been a very steady performance by Underground Mining. We talked about Oil & Gas results. Previously they made R100 million profit. In these six months they made a break-even. I had quite a funny question from the audience this morning on that slide. The Power & Water division made R53 million in the previous six months. These six months they made a profit of R3 million. There are reasons for that.

Investments are slightly down compared to prior year, still a very good investment and still generating the 18.5% returns that we expect, but the prior year number had a once-off figure in. I will explain that to you in a bit more detail. The

Middle East is a green arrow going up, and it is not a mistake. It's a green arrow going up. It is the first time in four years that we made a profit in the Middle East. So good results. Interest has improved. Taxation remains at 38%. I will talk a bit more about that in detail. If you take continuing operations including and excluding Middle East it remains relatively flat. But we have had a significant improvement in our discontinued operations. The discontinued operations in the prior year had a number of elements to that. We managed to contain that loss, and it's a sizeable loss that we managed to contain in the current year. The overall increase in the attributable profit is 61%.

If we unpack that in the income statement, further down in the pack there are a number of slides that give you a lot of detail on the below the line items, what the main movements were. We can see that revenue is down 17% compared to prior year. EBITDA is more or less in line with prior year. If you take EBIT we're slightly up if you take the EBIT including the Middle East. The Middle East in the current year had a profit of R30 million, and that related to a foreign exchange difference on an intercompany loan. If it wasn't for that R30 million foreign exchange gain the Middle East would have made a slight loss, and that is our overhead fees going into the Middle East. If you take the continuing operations and exclude the Middle East from it – and it's very easy to do the sums – Clough's performance is down by R100 million, Power & Water by R50 million, but the Mining platform is up by R100 million. That gives you the R50 million reduction in the earnings.

If you look at net interest and expense, a slightly improvement there. Taxation, we run at a tax rate of 38%. The 38% is quite a high percentage and it's something that we're not going to be able to fix within the next 12 months but there are plans looking at it. What happens is we do operate in areas where there is a high tax rate. We operate across the globe, so when we actually expatriate the profits back into South Africa or whatever country there is withholding tax. That pushes up your tax rate. And the third one is the corporate overhead cost structure sits in South Africa and there is very little revenue to actually put through to reduce your tax rate on that. So if you've got a tax loss sitting on those overheads in South Africa we're not able to raise a deferred tax asset. That alone pushes your tax rate up quite significantly. If we put in three to five years to bring that down to the 25% level I think we would have done well. And again we are looking at various scenarios in terms of doing that.

Discontinued operations, we came in at R29 million loss. The prior year was R114 million. Quite a lot of work has gone into managing assets and liabilities that we retained from both the infrastructure projects as well as the Genrec project. The guys have done well. The team has done well. There are monthly, weekly and sometimes daily meetings to actually manage these liabilities coming our way, but the team have done very well. If you go down to attributable earnings it is up from a low base of R110 million to attributable profit of R186 million. Henry made a comment this morning. He said he saw a Ducati motorcycle for sale. It's R177 million. He has taken the decision that we're not going to buy the Ducati.

Going to the platform analysis, this is where the devil is in the detail. So if you take the Oil & Gas platform, Engineering performed okay. Still a small contribution, but they are ticking well. The order book is there, relatively good margins, relatively good contribution. If you take the Construction platform, that's the platform entering into the new complementary markets you can see growing in that platform. The platform had a loss-making contract which brought the contribution from that platform down. If it wasn't for that project we've got a lot of projects in there that make quite a lot of money and are doing quite well. Global Marine is a business that we've speculated quite hard on. Peter and his team have done quite a lot of work to restructure that business. There are still a number of bids going in. There is maybe a different way to achieve those bids and reduce the overhead structure on that. In the next financial year I think we will see the benefits of that restructuring of the Global Marine department.

Commissioning & Maintenance, you will see the revenue came down from R3.9 billion to R1.6 billion. That is really the reduction of the Ichthys project and the Wheatstone hook-up and commissioning project. You will see the profits came down only marginally. So the way Clough runs their projects and will run their projects is as you go to a project you identify certain risk elements in those projects. As you come to the end of those projects you really try to mitigate those risks and reduce those risks to a minimum. So the risk provisions you have taken against those risks you are able to release at the end of the project. There is still a strong contribution in the current year from the commissioning and maintenance division within Clough.

Corporate overheads you will see in the prior year it went up from R177 million to R255 million. The number of tender activities in Clough has increased immensely over the past year. So the tenders going into the complementary market have increased exponentially. We talked about Snowy Hydro Project. We talked about the [unclear] project that is happening. Yesterday we had a board presentation for a number of projects with the value of A$2 billion that are still being tendered. And you need people to actually tender that, so that is the last place where you want to cut overheads in that division.

This morning I had a question: Why don't we record any operating profit within the platform? That middle stripe means zero. The contribution from the Oil & Gas platform has been zero for this six-month period. Now, there is quite a lot of work that went into maintaining that profit position of zero. It could quite easily slip to something in the negative, so from our point of view it is a disappointing result compared to the prior year, but quite a lot of work has gone in to manage that business and set it up for a good future. We talked about the Snowy project. We talked about the BHP project. So what we expect in this platform is you can see the order book has gone up from R3.8 billion to R3.7 billion. But the challenge for this platform will be over the next six months. The projects that they have are going to generate significant margins to actually mitigate the overheads that the business has to cover. Time will tell. There are a number of projects that are currently being executed. It depends on how quickly those projects get awarded and what the margin is they're going to make on those projects.

We move over to Underground Mining, a very successful story. If we start with the African business. Yes, its revenue increased marginally. They have got an operating profit of R101 million with strong margin. We think that African entity will be able to duplicate those results and there is no reason why they shouldn't be able to do that in the next six months. Australia is sitting at a lower margin of 6%. They had a tough start to the financial year. They had a tough start to the financial year. That has got two elements. One is the raise bore contract where they had some difficult ground conditions. They are through those ground conditions and they're starting to make money again. There is a project there, the Dacian Mt Morgan project, they did development work and the contract moved over to a contract mining type of job. There have been some teething problems moving over, but those problems have now been resolved. In the past two months they've had some good results. What I can say is the R77 million is expected to be significantly more in the second half of the financial year going forward.

The Americas had a very good performance. You can see the operating profit increased from R68 million to R162 million. The order book went up from R3.2 billion to R8.8 billion. Overall the platform has got a R25 billion order book. It is one of the strongest order books we've seen for a long time. The point I would make about the Americas is with the increase in order book, increase in profits and new jobs starting there are certain consequences on the balance sheet. And we will get to those consequences that occur.

In terms of Power & Water the power segment contains not only the Medupi and Kusile contracts but all the historical power projects that we undertook, so those results reflect the combined impact. What you will see is that the revenue came down from R2.3 billion to R1.1 billion, so a significant decrease in the power programme. Medupi has now been largely demobilised, so very little revenue is expected to come from Medupi. Kusile is expected to be demobilised in FY2020, so there is going to be a revenue contribution but at a very reduced rate. Again the R131 million we carried from risk revenues are specific to a number of our power projects. As these projects came to an end we were able to release the provisions that were held, assess them, or maybe reallocate them to different parts of the business.

The water business made a profit of R1 million contribution. To use our usual terminology, water is bubbling on as an entity. The upside for this platform is if and when we get a large Organica project. Some of those projects are up to R1 billion. The second is longer term – within the next 12 months – the country has got an issue with waste water treatment. This platform is well suited to assist in the waste water treatment challenges that the country faces. As and when the country gets its act together to actually open up that market to different players we can start participating in those.

In terms of oil & gas it is a lot of work we do with Sasol. That R79 million includes the loss-making project. And we all know what loss-making projects do. If you've got one loss-making project in a business it takes you about three contracts to actually make up profit for those loss-making contracts. So there is a lot of effort within the Power & Water platform to ensure that they eliminate those loss-making projects that occur on an annual or bi-annual basis that they don't make those mistakes again. E&I is a small business, a small contribution, but it has always been profitable. The jobs are profitable and they continue to contribute.

And then the corporate overhead. There is a real drive by management who realise that the Medupi and Kusile projects are coming to an end. The business going forward is going to look a lot different. So there is a lot of effort going in to try and minimise the overhead costs within that business. You obviously can't cut it down to below the bone. You've got to be able to tender projects. You've got to be able to deliver those projects. And when it's a big project you've got to be able to upscale those projects and make sure you execute them. Again the contribution for that platform is a very flat contribution of R3 billion with a reduced order book.

To get to Bombela and the Middle East, our investments in BCC in the current year made a profit of R114 million. The prior year figure had a once-off amount of R25 million in that. In the prior year we renegotiated the Bombela Operating Company cost base which goes into the BCC model. So we agreed on a lower cost base. That gives you a saving in the overall model. And we took R25 million of that saving within the R139 million. So if you compare apples with apples and strip out the once-off item you've got an investment that is still doing really well.

The Middle East had an intercompany loan where they made a R30 million exchange profit on the loan. And as I said previously that R30 million has been offset by additional legal fees as well as overhead fees. But overall we recorded no further project losses in the Middle East. By the end of the year we should have take-over certificates on all of the contracts, and it is really closing out the commercial issues on these contracts. Probably the biggest one on everyone's lips is the Dubai Airport claim. The Dubai Airport claim's ruling is still expected by the 31st of this month. If we get a good ruling in our favour that can potentially change the results for the company in a good way going forward.

If I get to the balance sheet there are three elements that have an impact on the balance sheet. The first element is IFRS 15. IFRS 15 is a new accounting standard that has been implemented, and companies are forced to implement IFRS 15 as of the 15th July from this year. Now, if you look at the wording of the old standard that applied, IAS 11, that said there has got to be a probable cause for you to recognise revenue. So IFRS further defined probable as more likely than not. If I've got a claim against the client and the claim value is R100 I will sit with the legal advisors and say I've got a strong legal basis, my quantum is right, so I've got a good probability that is more likely than not. Let's assign R60 as uncertified revenue to that claim. That was quite straightforward under the old accounting standard.

If you use the new accounting standard it says 'highly probable'. It says highly probably is defined as significantly more likely than probable. So what that does is it sets a threshold for revenue recognition that the standard compels you to accept. And you've got to measure it [unclear]. So if I've got a claim of R100 previously I took R60 to book. What this now says is, Daniel, you can no longer take R60 to book. You have got to reassess this. It has got to be significantly more likely than probable. So that threshold of taking R60 to book dropped probably to R20 or R30. The difference between the R60 that I took to book and what I've now got to take to book, I've got to take to book as a reduction in my equity. I didn't write the standard. That is how the standard works. And again this is what we are compelled to do and compelled to implement within the business.

At the bottom block we say that the total adjustment against equity was R1.1 billion. But more importantly, in the second point we say that we remain confident that any uncertified revenue that has been reversed, as well as any previous revenue that we recognised but what to reverse under this new IFRS standard, we are still confident that once all uncertainties have been removed that they will come through the income statement. The Dubai element, we have got implement now the 1st July. If something comes through in April this year I've got to book it as revenue again. And we will be very transparent when we come to the market and say this is an impact of an IFRS 15 event. I think that's the biggest most important single thing that impacted the balance sheet.

If we move on from the balance sheet of Murray & Roberts to other elements, firstly in the prior year we acquired an additional 17% in the Bombela Concession Company. We effectively bought that through cash. It is always a bad decision to buy a long-term asset with cash, so we went through quite a painful process to put that investment into a longer-term facility and write that off over a period of time. If you do that it has got two consequences. One is, yes, you get a cash injection because you get paid by the long-term institution. But two, your long-term debt goes up by the same amount that you've received cash. So on a net cash basis there is no improvement, but from the cash point of view your cash balance gets increased.

The second element is our success in the mining industry has probably been the downfall on our balance sheet. It has got two elements. Starting off new contracts we had to bring in additional capex, but capex is an additional burden to the balance sheet. In typical mining capex I buy a machine for R100 million, I price the machine over the three year duration at R100 million and on a monthly basis I recover that from the client as I do the job. So it's not true debt in the sense that it is debt that has got to be serviced through profit. These debts are serviced through revenue collections.

The second impact is because the business grew so rapidly there is an impact on working capital, especially in the Americas. In the Americas it is very difficult to bid a job on a cash neutral basis. In South Africa you can do it. In Clough we can mostly do it. But in the Americas you're going to lose a job if you have done it on a cash neutral basis. But the group as a whole – and you will see it in some of the slides later – had a cash outflow in the six months of the year of R736 million. If I now look at my balance sheet I had R2.4 billion and I've now got R2.2 billion. Not a bad result taking into account I had a R736 million reduction in working capital but I had a R350 million boost when I refinanced BCC. Of the R2.2 billion, R1.6 billion is unrestricted and R0.6 billion is restricted. So we've still got a very large element of our cash that is unrestricted versus restricted cash. We ended up the year as a result of the working capital outflows as well as the additional asset-based finance with still a very strong net cash position of over R1 billion.

The last comment I want to make is our gross gearing improved to 22%. We explained the R736 million debt, but your gross gearing is as a result of your reduction in equity and your increase in debt. 22% is still quite comfortable. It is within our investment margins that we have always communicated to the market. Henry, I've done the easy part.

Henry Laas

Thanks Daniel. Thank you very much. Just for interest, you saw the increase in the Oil & Gas platform overhead cost. That is something that we are monitoring very closely to make sure that we keep overhead cost as low as we can. Why that increase? And Daniel has mentioned the tendering expense that goes into bidding new work. It is almost an exponential increase in our tendering activity in Peter's platform. To give you a feel for what we're talking about here, on Snowy Hydro we started off with a process where a number of companies were invited to tender for the work. And we ended up being one of two companies that were invited to compete finally for this job.

The client agreed to pay for the tender cost for each of these competing bidders and agreed to pay $20 million on tender cost. Now, our joint venture cost exceeded $20 million. That is part of the reason why the cost went in there. That just gives you a feel. If you tender for large projects it is an expensive cost. So the client went to the trouble of paying two bidders $20 million each. And as I said that didn't cover our tender cost. There was an overrun on that $20 million and it was part of the cost that we had to absorb. But you have got to make sure if you secure a project like this one that we're in the process of securing that you've got confidence on your engineering, confidence on your procurement, confidence on your productivity. And you achieve that level of confidence by bringing in a lot of external third=party consultants and engineers that work with you on that bid. So we feel comfortable that we've got a great opportunity in Snowy Hydro. Peter, we are waiting for you to announce that agreement has been signed early in April, please.

I've got one slide that I would like to close out on, and that is the slide under the heading 'Key presentation takeaways'. So you sit in this meeting and get a lot of information and you absorb a lot of information. But when you leave the room what is the message that you leave with? I think first of all we've got growth aspirations as an organisation and we are confident that we will achieve our medium-term growth aspirations. Just before the presentation I had a chat with one of the executives from one of the banks that we deal with. I said as a team we always feel under pressure every year to report growth in earnings, growth in earnings, growth in earnings. And if we are able to achieve that, then all companies can do that. And if you've been in business for 20 or 30 years you will only have mega-billion Rand companies listed on the JSE. But the reality is you work through cycles. You work through up cycles and you work through down cycles, and sometimes earnings are up and sometimes earnings are down. The reason I'm mentioning that is you can't talk about growth aspirations tomorrow. It is medium term, and we remain confident that we can achieve those.

The cash position is strong. We funded those two small acquisitions from our own balance sheet and we are considering other opportunities in that space as well. FY19, the current financial year, what we reported in the first six months I think will be very similar in the second six months of the year where we have Power & Water and Oil & Gas coming in with a negative variance to what we achieved in the previous financial year. And that will be partly offset by a positive variance or increase in contribution from the Underground Mining platform. The Underground Mining platform will continue to make a significant contribution. We expect that for a number of years to come.

The Oil & Gas has achieved success in complementary markets. The oil & gas market itself is showing definite signs of recovery. As I explained earlier on, we are ramping down on a number of projects and we are not yet ramping up on big enough opportunities to replace the work that we are completing now. So there is pressure on the revenue in that business.

Power & Water with Medupi and Kusile coming to an end it will never be the business that it was before. There is just not sufficient scope and opportunity in the South African market for this business. So hopefully it will successful with the unbundling that we expect out of Eskom and the water investment coming back, but I would expect that earnings contribution is probably going to be between R50 million and R100 million per annum where previously it was higher than that. It is just that the market is not there to support a larger business.

We have got substantial new orders, R22.3 billion. As I said, as soon as we get the Snowy Hydro agreement signed that near order will move into orders. And we are still expecting the order book to grow to about R40 billion by the end of June. So finally engineered excellence is not negotiable. Yes, there were two loss-making projects, one in Oil & Gas and one in Power & Water. And that is unforgiveable. You can't have that. But unfortunately it does happen from time to time, and the consequence of that on any business is severe and it is negative. We have absorbed that in the first half of the year, it's in the results and that is done.

So engineered excellence is a concept that applies broadly across everything that we do. It is the way in which we manage our financial position on a project. It is the way in which we manage safety in the business. It is the way in which we manage our people. It is the way in which we engage with you, the investment community. It's the way we do things in Murray & Roberts, engineered excellence. So the standard is a standard of excellence. And we say it is engineered excellence, so it is not just a haphazard outcome. It is an outcome that we plan for, that we engineer and that we then eventually achieve. So all in all I would say personally I'm very pleased with the mining business performance. Some disappointment with Oil & Gas and Power & Water, but all in all a reasonable result for the first six months of the year. Ed, I want to hand over to you now. You are going to manage the Q&A session. I know we have got people on the webcast. I don't know how you want to go about it.

Ed Jardim
Thank you, Henry. Perhaps we will start in the room. Any questions for Henry and Daniel?

Marc Ter Mors
Marc Ter Mors of SBG Securities. Focussing first on mining, a stunning result. More than 40% EBIT up. Southern Africa seemed to be much slower in traction than the Americas and Australasia. Maybe some scope of what the reasons are, and can this accelerate?

Henry Laas
I think the opportunity for us is a function of the investment that mining companies make in certain jurisdictions. Now, we know that specifically in South Africa the mining sector is very strong around platinum. And we haven't seen significant investment in platinum, so maybe that will come back. I hear that some of our local platinum producers are talking about expansion and they announced those plans. So if that materialises then there will be significant opportunity for us. But I think maybe some of the other geographies such as the Americas there's a different commodity mix than what we have here in South Africa. That could also be a reason. It depends on which specific minerals are drawing investment at a specific point in time. But yes, overall it was a stunning performance by the mining business. But as far as the South African business is concerned it has been a little bit slower than the growth we have seen in the Americas.

Marc Ter Mors
And then the arbitration outcome in the Middle East on the airport contract, can you give us an indication of what the potential size of the claims are that went into the arbitration contract?

Henry Laas
Marc, that is unfortunately not detail that we would like to disclose. I don't want to say anything that may jeopardise the way in which this entire process unfolds. Having said that, we believe that the accounting position that we have taken was

fairly conservative. Through this process of IFRS adjustment there was an element of adjustment to that claim value as well, and that has now gone through the books. As Daniel has said, we are confident that we will at least achieve what we have previously accounted for. Hopefully there is going to be a good, positive surprise.

But from a process point of view once the award is made at the end of March it doesn't mean that cash will flow at that moment in time. We need to enforce the ruling through the courts of Dubai, which essentially means that there is a possibility that if we are awarded in our favour to the extent that the defendant is upset by the award through this process of enforcement there may be further challenge. So we hope that we get a favourable award, but not too favourable because if it is too favourable we could be in for another round of legal process. But yes, we are hopeful to get this award by 31st March and we are confident it is going to be good for us. It has been a long haul, more than 10 years.

Marc Ter Mors
A last question relating to Snowy which is obviously potentially very large. From your commentary it sounds like there are two preferred bidders. What is the confidence of Murray & Roberts Clough indeed being the winner of this contract?

Henry Laas
There have been two bidders and they were asked to participate in the tender process. And we won that race. So we ended up as the winner, as the preferred bidder. And we are in the process now of finalising the agreement. So once the final items have been agreed the contract will proceed and we will do the work. It's a five year duration, so $1.5 billion over five years. It is about $300 million per annum if you average it out. And we want Clough to turn $1 billion per annum. So although Snowy Hydro is a sizeable opportunity by itself it's not a business. It's just a large project. We have got expectations from Peter and his team to secure significantly more in complementary markets but also in our core market.

Murray Connellan
It's Murray Connellan from HSBC. Just a quick question for Peter on Snowy please. I just wanted to find out. This is obviously quite a different type of job from what Clough has become accustomed to doing over the past couple of years. I was wondering whether you could maybe take us through what types of changes may need to be made within Clough's technical expertise, whether or not you may need to be outsourcing some of this job from a subcontracting point of view. And I suppose the question is how technically capable you feel Clough is with regards to this job.

Henry Laas
That's an easy question to answer.

Peter Bennett
To be blunt, from a construction standpoint it's not very different to what we've been doing. The ultimate process or the product of the process is different, but it is a large construction project, a civil construction project. From a technical standpoint around the hydro-electric scheme we have our partner who is the world leader in hydro-electric projects. But from a construction standpoint it is a very large underground mining project in many ways, and our sister company, [unclear], is going to be participating with us. There are vertical shafts just like there are in gold mine developments. There are big underground cavern developments like there are in block mining. There are large mechanical equipment installations. There is piping, there is electrical, there is instrumentation, large remote workforce management which is what Clough does on all of its projects. So from a work function and what we actually do not significantly different from the other projects that we have worked on. It is just in a different industry. As Henry pointed out, complementary markets are exactly that. We are not looking to go into areas where we don't have existing expertise and capability, but just different client bases.

Ed Jardim
Thanks Peter. Any other questions? On the phone as well, any other takers for questions?

Daniël Grobler
Ed, maybe one from my side. Is there any uncertainty with regards to IFRS 15? Okay. Good.

Ed Jardim
Thank you very much.

Henry Laas
Ed, is there still time to have a conversation next door? You are all invited. Thank you.

END OF TRANSCRIPT