Conference call transcript

5 March 2020

INTERIM RESULTS INVESTORS AND ANALYSTS PRESENTATION

Ed Jardim

Good afternoon ladies and gentlemen and good afternoon to our stakeholders on the webcast, as well on the call. Welcome to the Murray & Roberts interim results for the six months end of 31 December 2019. Just a quick note on safety before I hand over to our CEO. In the unlikely event of an emergency, you have two evacuations routes off of this floor. The first is out these doors to my left. Left again, to where the bathrooms are there's an emergency evacuation door there. You can depress the glass. That will break and release the door. You make your way down to the ground floor, there is signage that shows the ground floor, out and around the building to the public parking space across from the building where we will do roll call.

Your second evacuation option off this floor is once again out these doors to my left towards the loft lobby. There are a set of stairs on each side of the lift. Please make your way down to the ground floor out the main entrance where you would have come in this morning and across the road towards the public parking space where we'll do roll call. Our HSC executives and security teams will assist with the evacuation and we have no drills planned for today. So, welcome and with that I'd like to hand over to our CEO. Thank you, Henry.

Henry Laas

Thank you, Ed. Good afternoon ladies and gentlemen and welcome. Allow me to make a few introductions. Our Chairman, Dr Suresh Kana. Suresh, would you just stand up please. Then, a few of our executives. Mike Da Costa, that's the CEO of our mining business. Mike, if you could just stand up. Steve Harrison, Power & Water platform CEO, and Peter Bennett, the Oil & Gas platform. Peter came all the way yesterday from Australia. They've changed the timing of the flights from Australia. If you returned from Perth the flights used to be midnight, it's now 14:30 in the afternoon. So, you arrive here 19:00 in the evening, where as previously he only arrived the following morning about 05:00. So, I said to Peter earlier today I'm very glad that he was able to make that flight so he could have watched the last few overs of the cricket yesterday, the ODI between South Africa and Australia. The fact that we have won make it a lots easier for me to speak to Peter. It would have been a lot different if we lost. But welcome. Daniël Grobler will share the presentation with me and you all know Daniël very well.

I would like to start off with the salient features. First of all you will revenue and earnings before interest and tax is up compared to the previous period and that is essentially due to the performance that we recorded in the Underground Mining business whereas Oil & Gas and Power & Water are on par with the last year and in line with our expectation. Attributable profit is down from R186 million to R163 million and that is essentially due to an increase in our interest expense which Daniël will explain in a lot more detail but it relates to the acquisition funding that we've incurred on some of the acquisitions that we've concluded last year as well as the IFRS 16 impact on interest and then there's also additional working capital that we had to finance and there was an interest expense on that. The projects in the Middle East have all been completed now and we've received the takeover certificates and now that that has happened the business was classified as a discontinued operation in the current period and for that reason you will see that revenue, earnings before interest and tax and diluted continuing HEPS on this slide have been illustrated for that adjustment.

The order book was a highlight of the reporting period. It's up to R50.8 billion and you will recall when we did the full year results last year we did indicate to the market that the order book potentially could increase to about R50 billion – R55 billion and you can see it's at R50.8 billion. The significance of this is that only once before in the history of Murray & Roberts was the order book higher than that. It was R60 billion in December 2008. Then, the global financial crisis impacted the business and then very quickly it dropped down to R40 billion in June 2009. I know if you have to adjust it for inflation the numbers would be very different today but still R50.8 billion we believe is a quality order book. The previous high of R60 billion included a lot of projects in the Middle East and you will recall that was a bitter experience for Murray & Roberts as a group, that time that we spent in the Middle East. We don't know about any project in this order book of R50.8 billion that at this stage is at risk from an earnings point of view to potentially not achieve the margins that we've tendered [?] on these projects. That really is a strong order book and to me, as I've said that really is a highlight of the past six months. The net cash position is marginally down to R0.8 billion but when you do the IFRS adjustment the net cash of R0.8 billion changes to a net debt position of R0.1 billion and again, Daniël will give you all the detail.

Lost Time Injury Frequency Rate, it has deteriorated from last reporting period to 1.12 and that is a concern. It's something that we are paying attention to and all effort is going in to bring the safety performance back to where it used to be, around about 0.6 to 0.8 — Lost Time Injury Frequency Rate. We are very grateful, again, that comes to a period without recording any fatal incidents and this has been now for the past, I think, two years that we haven't recorded a fatal incident. In a business that undertakes the type of work that we do in the Underground Mining space, Peter in your space and in your space Steve I think it is a commendable performance. In our organisation we really believe that you can build these projects without injuring people. It is just completely unacceptable, and it will never be acceptable for us to have people losing their lives whilst they're on service. So, we're very pleased with the overall performance for the first six months of the year, more or less in line with our expectation and the order book really was a highlight.

I'm not going to get into too much detail as far as the strategy is concerned. We have covered that off in previous presentations. All I can say is at this stage we don't foresee any change in strategic direction. We are comfortable where we are that the initiatives that we are implementing that those are the right initiatives for the group. We think that the group has now stabilised at this stage at a place where we can grow organically and where we can grow for further acquisition. The strong order book that you see is not going to present us with growth potential in the current financial year. So, you would notice the first half of this year very similar to the first half of the previous year and we do expect that the full financial year results also be more or less in line with what we reported in the previous year. This order book will support growth in FY21.

Now, where will the growth come from? When Daniël goes through segmental analysis you will notice that the mining business really is a platform that is contributing to earnings at this stage. We don't get much contribution from the other two platforms. From a group context the growth will come from the Oil & Gas platform starting to become a meaningful contributor again to group earnings. We do expect that the mining business will continue to maintain earnings at the current levels. About the longer-term outlook we still believe that the natural resources market is the right market for us to be in, but we do undertake work in selected infrastructure markets to balance the cyclicality in natural resources.

I've got a slide on each of the platforms. If we start off with Oil & Gas what you see here is the global footprint and we have now through the acquisition we concluded last year in Houston we've established the meaningful presence in the USA. We don't intend to establish any permanent offices in other geographic regions. It's essentially in Australasia as you can see on the screen and ten also in the Americas and we comfortable that we really positioned in those geographic markets where we can implement the type of projects that we are able to implement. The market focus globally is LNG petrol chemical sectors but in Australia it's got an added element to it where we will continue to focus on those traditional markets where Clough has been very active in more many decades. So, we will do selected infrastructure projects and we will undertake project work in the metals & mineral space. With that being said we've realised that the naming convention of the platforms have to change. The Oil & Gas is no longer an appropriate name for this platform, and we are working in renaming this platform and when we do the full year results after June we will share with you the new name for the Oil & Gas platform.

The market conditions in the USA in the LNG and petrochemical market is presenting us with opportunities. The LNG in Australasia is still limited to opportunity at this moment in time, but the infrastructure market and metal & mineral market is really buoyant. Peter has done a great job when he realised the Oil & Gas was running out of steam at a paid rate to continue focus on your traditional markets and we have secured a substantial order book in that state so well done with that, Peter. From a prospect point of view, as I said quick revenue that will get us growth into financial year 21 and it will also translate into growth for the group as a whole. I've got two bullets on the platform prospects — one talking about transport infrastructure in Australia and the second one talking about the metals & minerals areas – and you will see the significant expenditure in those markets and that where Peter and his team is currently focusing on for that region.

Our business in the USA, Clough USA, we are very pleased with what we have achieved there in a short period of time. The acquisition of the division of Salisbury came with a project that was approaching completion, it had a couple of months to go and we took that project over as part of the acquisition. We had a bit of a hiccup in closing the project out, some loses that we've incurred on that but that is far offset by the profits that we've earned on the Next Wave Project which we've secured shortly after that acquisition. But all-in-all, in time to come North America will be a very big part of this group and it may even be a bigger contributor to earnings than what the Australia region is at this stage.

The Underground Mining platform is well established. Santee is in the South of California just north of the Mexico border and I had a question just before the presentation started about that business, which is Terra Nova Technologies, that's the business that we've acquired in the previous financial year. It operates out of Santee. Again, a very good global footprint. There's no plan to expand that and I think we really have a good presence in all the main mining territories globally. Our focus is in Underground Mining services but that also now includes material logistics which is the services being provided by Terra Nova Technologies conveyer systems, crushers, screens. So, that is a part out of focus.

Market conditions overall we believe that the growth that we've experienced or that we see in the market where our mining clients were increasing their capital expenditure that is no longer happening. So, that has tapered off and that indicates to us that the mining cycles might have reached a plateau. We don't expect significant new greenfields mining opportunities into the foreseeable future and most of the spend will be in brownfields operations. We are performing well in all the geographies, in Australasia, Africa and in the Americas and it really is a very strong business that we have within the group. TNT, we are very pleased with that acquisition. I think it holds great prospects for us an organisation. Currently they're predominantly operating in the Americas and we have no established office in Perth as well for TNT and we will be undertaking or expanding that business into Australia and also into South Africa and into Sub-Saharan Africa.

The Power & Water business is a business which is essentially based in South Africa, Sub-Saharan Africa. It is not the business that has the potential from a market opportunity to operate at the same scale as Underground Mining or the Oil & Gas platform. It always will be a much smaller platform. If you look at the investment that we see in South Africa I think it is an unrealistic expectation if anyone was to expect that this business could potentially compete with an Underground

Mining business or with an Oil & Gas business. It's always going to be a much smaller business. Our focus isn't in the Power & Water space but also complementary markets and for that reason we will also be changing the name of this platform and we will communicate that after the year end results. Power & Water was no longer an appropriate description for this platform and that change will happen.

There's limited investment in power. There's limited investment in water, other than what we see is happening in the city of Cape Town where they have committed to quite an extensive investment program and we were very glad when we secured our first project for waste water treatment in Cape Town, the Athlone Project. Eskom is also presenting an opportunity. You will recall the acquisition was actually last year, but the effective date was the 1st of September, so it wasn't a current period of a company called OptiPower, it's specialist in overland transmission lines, substations and we're very pleased that that business is doing very well. It's been with us now for a quarter, final quarter of the previous six-month period and second quarter and the substantial amount of work out on tender, about R2.5 billion from Eskom. We are tendering this and there are a number of projects currently under adjudication process that we hope to get secured before the end of June.

The LNG market in Mozambique is an opportunity that we've been waiting for a long time and we've all been talking about it for a very long time, but it has now arrived. The projects have started the major EPCs on the projects have been engaging with us. We've received them in our offices not so long ago and we will, I'd say, certainly before the end of December we will have received several packages that we could tender on these projects. It will not bring earnings in the current financial year, it will be too late for that, but we do expect that the work will start towards June 2021, the end of the next financial year. So, that is a nice opportunity for us. We understand that the funding into those projects, a lot of the funding was provided by South African banks and part of the funding agreement is that there should be a certain percentage of spend incurred with South African service providers and that is where we fit into the picture and we believe we've got a compelling service offering that will meet a requirement of those major EPCs. At this stage it's an opportunity that is being pursued through the local South African business but that does not exclude the possible participation of our Oil & Gas platform depending on the type of work packages which is put out to tender. So, we may call on Peter and his team to come in to support us if that is required, if not Steve and his people will execute by themselves.

The order book is up significantly but the growth you will see was predominantly in the Oil & Gas business and that comes from two projects. The Snowy project, we've spoken about that I think at our full year results, but with also the Next Wave Project. And the Next Wave Project is project that we secured in this business that we've acquired in the USA. We're very pleased with the growth that we've seen in the Oil & Gas platform. And as I have said that order book growth will support revenue into financial year 2021 that will make this platform again a meaningful contributor to our group profits. Don't be concerned about the Underground Mining platform that's gone down. The order book has gone down from R35.7 billion to R19.6 billion. The order book is something that comes in lumps and not spread equally every month. We are, I would say in a good position to increase the order book by about R10 billion by June. We would expect that the mining order book which is currently R19.6 potentially could increase by a further 10 billion by June this year, in a few months' time. That would indicate to you that we are very far advanced on negotiating two major contracts and if we conclude those combined value in the order of R10 billion.

Power & Water has got a very low order book. There are no opportunities in South Africa of any scale that can compete with Medupi and Kusile. We have recently secured the project for R890 million. That project is for an international client, but the project has been put on hold because of industrial unrest and community unrest in the area where this project has to be built. Although we have secured the project it's not in the order book and we haven't received a letter of award because of this delay on the implementation. Yes, that is one of the largest opportunities available on the market and if you compare that with the scale of opportunities that we had in mining and in Oil & Gas be it all hundreds of millions and billions of Rands. It is just an indication of the lack of investment in major opportunities that we're currently experiencing in South Africa. Total order book up to R50.8 billion and as I said it really is a good position for us to be in.

This was also an interesting slide. It conveys a few messages. The first is that the order book, if you look at the order book spilt 74% of that is in the international market and 26% is in SADC. This gives a feel for the revenue, how the revenue in the organisation… Where the revenue is earned. Another interesting part of it is if you look at Oil & Gas that R5 billion is secured for the remainder of the 2020 financial year. In other words the six-month period that we're in now that revenue will be earned as we implement the projects. For the current financial year you will see from Daniël's presentation in the first half revenue in that platform is just above R3 billion. So, we do expect that for the full financial year it should approach about R9 billion.

If you look at 2021 that is what we already have as a secured revenue for the next financial year. We are very pleased about that. There are still a number of projects which are under adjudication process and that is not considered in the order book. That's in the pipeline but we already have today secured work equal to the revenue that we will earn in the current financial year. Secured work for the new financial year. Underground Mining, a nice spread. And as I said there's about R10 billion that we expect to secure before the end of June and Power & Water is just a reflection of the lack of opportunity that we have in the local market. Again, the order book at R50.8 billion and then the pipeline — renewed orders, projects that we essentially have secured but the contracts have not been signed yet. What I can say is that this value has subsequent to December moved into the order book, that value has moved into the order book and I'm not sure Mike, from Underground Mining how much of that has moved into the order book.

Category 1, how much? Mike is just saying that in his business R2 billion of the R6.1 billion has already moved into the order book. Just to explain the difference between category 1, category 2 and category 3. The categorisation refers to the maturity of an opportunity. The category 1 would represent projects which we already have tendered or which we are currently busy tendering, so those would be the next wave of projects that will be built. Behind that is category 2, those projects are not at the tender yet. It's in feasibility study stage, budget estimates. So, it's the next wave of projects that will come. Then, category 3 from a [unclear] point of view is further out. There are no tenders, no budget or feasibility work on those opportunities yet but we do track them. When you look at the success rate that we have on our tenders in the various platforms it's varies but overall I would say a reasonable expectation would be of that R70 billion that you see there that at least R30 billion to R35 billion should be secured and should find its way into our order book once the adjudication process has been concluded. Ladies and gentlemen that brings me to the point where I would like to hand over to Daniël and he will talk to you in a bit more detail about the results.

Daniël Grobler

Thank you, Henry. I've asked Ed if I can start the presentation with a lame joke and Ed said definitely not. We have so many serious people from a financial point of view. I've just got to start the presentation and he just gave me the no. he said that in two sentences. What I will start off with is a comparative financial information. I'm going to go into a lot more detail further on in the presentation. Underground Mining had a strong performance when you compare that prior. Oil & Gas were close to breakeven both of the platforms but that's in line with the expectations. The investment in the Bombela Concession Company has done really well and we'll get to the reasons why they've done well. As Henry mentioned, interest decreased significant to the prior year. There are reasons for that. There are some elements that will not repeat in next year and we'll talk to that in detail. Tax is sitting at higher effective tax rate of 28% and I'll get to that part. We've spent quite a lot of effort with Deloitte reviewing the tax rate and seeing how we can get that down. Discontinued operations marginally down compared to prior year and I'll talk you through the readings for that. So, in general attributable profile was down by 12%.

One thing Ed said I can include is the new accounting standard, so these things are always nice to know and nice to understand but when you get to the detailed half then people get lost. So, what I'm going to try and do is explain this in ways I understood and I'm sure if I understood it you'll understand it. In the past we had financial leases and we operational leases. Financial leases when you go and buy a car, your car comes onto your balance sheet and your liability comes on to your balance sheet and you just pay your monthly instalments. Operational leases are a lease like this building. I get an invoice every month, I pay my invoice every month and that's the end of the transaction. What this new accounting standard forces you to do, it says Daniël calculate the rest of your lease payments until the end of your lease period, bring that as a liability onto the balance sheet and then you bring your right to use of the asset onto your balance. So, you've got an asset and liability on your balance sheet which previously you didn't have.

At the bottom sentence of that slide we see that the total assets that we brought onto the balance sheet were R795 million and the total liabilities we brought onto the balance sheet was R886 million and there's a reason why a small difference of R92 million went through the equity. So, what does that mean for the income statement? In the income statement, if you go down the income statement there's a line called earnings before interest and tax depreciation and amortisation. So, previously your operating expense would have been a deduction, it would have been included in that line but the standard number which is your total assets that your brought onto the balance sheet and you depreciate that. So, that was below the EBITDA line. If you take the interest on this liability that you've created, and you include that in your interest line so what will happen is that your EBITDA will be higher compared to prior year and your interest expense will be higher compared to prior year. That was the exciting part of your presentation.

That flows to the income statements. Into the income statements we can see that revenue increase from R9.7 billion to R10.7 billion. EBITDA increase exactly due to these reasons that I've spent 20 minutes explaining. Then, if you look at our EBIT, EBIT R54 million up compared to prior year. We'll unpack that when we get to these segmental slides. Net interest is significantly highly than prior year. I've got a slide following that will unpack that. Taxation remember is high. We've got a tax rate of 38% prior as well as current year. We've done a lot of work with Deloitte trying to lower that. There's no silver bullet but there's a lot of small items we can do to try and get that tax rate down from 38%. We then go down to discontinued operations, 38% compared to 26%. I'll talk to that. Attributable profit down 163% compared to 187% which is a 12% decline. If I go to interest, so in this period we had an interest charge of R91 million. In the prior period we had an interest charge of R9 million. The variance is R82 million, so what does this variance comprise of and which of these elements are expected to occur in the second half of the year but disappear in the next half of the year.

Implementation of IFRS 16 is unfortunately compulsory. You are going to see that in all the quarters going forward so that's going to stick with us for life. The additional 17% we acquired in the Bombela Concession Company was refinanced or was financed in December 2018. So, what that means for prior period July to December '18 there was lower expense and in the second half of that year there would have been an expense. So, I presume the first half of the new financial year there's an expense then it's an incremental R20 million expense when you compared this year compared to prior year.

TNT acquisition funding will incur debt when you buy an asset and the funding you can see is low. We're sitting at 13. In the next six months that will go up probably by another R5 million, but our TNT acquisition funding will be a lot lower going forward in the new financial year. Working capital management is an item I'll talk to on the balance sheet. We were not paid by a number of debtors for a number of reasons and some of those debtors we just work with them through their tough times to try and get them through a difficult situation, but that working capital outflow had to be funded. You will see on the balance that R600 million of that was funded by our cash and then you had to incur overdraft facilities of R600 million to fund the rest. So, those things attract interest, there's no silver bullet that's going to say that from the 1st of January that amount is not going to be there. Working capital management will be included in the second half of the financial year but when you go into the new year the bulk of the working capital items should be sorted out and that line item is not expected to reappear in the next financial year.

If you go into the segmental reporting, plus we've broken down again into four divisions. The first division is engineering and construction. We can see a nice increase in revenue. The water group we can see a… I don't know if the water is nice but a significant increase from R3 billion to R29 billion, but the profit slightly increased from a loss of R17 million to R47 million. Henry mentioned when we acquired the Saulsbury division we took over a project called Next Wave. That project incurred further loses than what we though. Those loses are included in the profit of R47 million. Sadly, had we not had those loses that figure could have been a lot higher and the margin would have been higher but with a project that we acquired in Saulsbury called Next Wave we've got significant profit within the next six months. So, overall that still remains a very good acquisition to us.

Look at Global Marine towards the end of last year they acquired that project in Canada. They had very slow revenue then. You can see the bulk of that project is still sitting in the order book, but we're expected to start building in the next 12 months. Clough in general adopted a business model where they started allocating tender cost per division to those divisions and where it becomes the most blatantly clear is under Global Marine where the operating loss is higher compared to the prior year and that's mainly as a result of the tender costs that were higher compared to prior year.

Commissioning and maintenance is one of those things which we hope would carry on into infinity, unfortunately not but our Ichthys project coming to an end you can see a drop in earning from R1.6 billion to R280 million. We still carry a high level of profit. On each project you build up a contingency reserve and then allocate that against certain risk elements that you identify in your project. Those you go through in terms of closing up these projects, you mitigate these risks. If the risks disappear you can release your contingency. On this specific one we had a provision of $5 million for superannuation which is a form of tax payment in Australia. We were taken to court, but he had an additional $5 million. We won the court action, so we were very successful in releasing the $5 million to come to the income statement and we do that on all of our projects as we go through. We see a reduction in the Clough cooperate and overhead expenses as a result of [unclear] cost savings. They've embarked on a cost saving process and they've allocated them across to the divisions. The pleasing thing is the increase in the order book where it went up from R4.3 billion to R3.4 billion. We believe it's a quality order book. We believe they've got the right people on the job to execute those jobs and that's going to be the challenge going into the new year.

Look at Africa, mining always stays close to my heart. Our friends in Africa had an increase in revenue due to some big projects ramping up. The prior margin at 8% is higher than the current year margin at 6%. Now, the prior year margin was boosted by a project that came to Murray, again with a number of risks on that project which they successfully mitigated. I think they negotiated for a period of three to four months but at the end of that period they had a contingency that they could release that increased the margin for Africa in the prior year.

Australia is a bit of a different story. Australia is a laborious market. They secured contracts and you can see they already increased. Australia had a very difficult contract with the client, and they were able to successfully renegotiate new terms with that client as of the 1st January 2020. So, we'll see going into the new year whether that renegotiation will increase margins. So, we do see a significant increase in the Australian margin in the next six months but for that project it's not going to be an increased margin from the 10% to a profit of 50% it's just a realistic increase in margin.

If you look at the Americas both turnover as well as EBIT increases. That's mainly as a result of the acquisition we got in TNT. Successful acquisition and you can see that both in turnover and operating profits. If you move to the right to the order book, Henry already spoke about the order book. That needs to go up by the end of the year but there's a lot of potential in there, some of the clients are in [unclear] discussing with the clients on multibillion, some boil down to one of two. So, we're confident that that order book will grow going into the new financial year. Look at water, so in the power segment in 2019 it's only the pipe [unclear] you can see it came down from 2018 to 2019 in the very next half. Look at the order book, the order book is sitting at 153 so there's virtually no work left for us on the power program under our conventional contract. What we are willing, and I've said to them outages projects [?] they range from between R20 million and R50 million per project. High margin projects but those come as and when Eskom gets time for us to do some of those maintenance projects. You can see, as I've mentioned in the order book very little work left to do.

Water, last year I had another comment that water keeps dripping along. We're pleased to say that they've secured a contract with Cape Town called Athlone Contract. ICL [?] that contract is R111 million and there's three new water contracts that will come to market in the next three months and we're quite optimistic that hopefully that bubbling of water maybe kind of trickling of a slow river and starting to make a meaningful contribution in the group going forward.

From transmission and distribution is OptiPower and we can see strong performance? They weren't in the bed for the full 12 months. They only came in on the 1st of September but their tender levels on activities have been the highest then they've even been in the industry of OptiPower so we're optimistic about the future of OptiPower and that they can make money going forward. Because we ran out of space on the slide we combined other between resources and industrial, electrical and instrumentation. The two main projects within that are Sappi and Polokwane. What we can say is that those areas operate in a very difficult market. There are so many claims floating about. There are so many unknowns floating about. If you make a slight loss on one of those contracts it's going to have a heavy impact on the margin that you make. We have been shortlisted, as Henry mentioned for an international company. If we win that job that slide will look a lot better but in the meantime they were operating in a tough environment.

Corporate's in line with prior year but the main focus for us and for the Power & Water build is to get that order book up to a level that is respectable and will start contributing to the group. If we can get them to a level of between R109 million and R50 million I think we would have done well, and I think they've got the capacity to do that over a period of time. If we look at Bombela, on the face of it questions are asked. R114 million last year. Guys, you said that that's a reasonable number. That number is now R197 million. So, in the past six months we've successfully renegotiated the settlement agreements with province. There are about eight settlement disputes for the operation period that were concluded in that negotiation. There were a number of clauses which not only posed ambiguity now but also in future, so what we did was we made sure that the wording in that contract is 100% clear going forward and that the risk profile of that contract is understood 100%. So we were able to revalue that contract and that brought another element of profit to the table.

For the firsts time we are including a slide on discontinued operations. The reason we did that was the Middle East in 2018 made a profit of R11 million. That is I think the first profit they have made in ten years. The reason they made the profit was they had a R30 million foreign exchange gain on a loan that they had. And that gain offset some of the legal fees and operational fees. In the current year we had an R11 million loss on the foreign exchange loans, so there was already a R40 million swing. And we had overhead legal fees and other fees which made it difficult for us. So that's why you will see there is a bit of a swing between the total of R48 million versus R26 million. In other we've still got some minor costs coming through between infrastructure and building as well as Genrec. Those items are coming to an end and those costs are expected to become less and less.

This is my second last slide, but probably the easiest one to understand. If we look at property plant and equipment, the top line, in June 2019 it was R2.2 billion. It went up to R2.8 billion. The main reason PPE went up is as a result of the implementation of IFRS 16. You will recall IFRS 16 assets would have gone up by R770 million. So of that R600 million went to PPE leaving elements to other non-current assets and current assets, which are sub-leases within this building and other buildings which we brought on balance sheet. But the main reason for PPE is R600 million. On the asset side we brought additional liabilities of R0.9 billion.

The second big thing that you will see is under current assets. In the prior year it was R7.1 billion. In the current year it is R8.2 billion. So in general your other current assets went up by R1 billion. So that is working capital outflow out the business of R1 billion. So we will call it a perfect storm, but there are reasons why that went up. We are confident that the bulk of those items will be brought back by the end of June. So what were those items? In Power & Water we have three contracts where we do milestone billing. So those milestones we started incurring costs before the end of December. You only get paid in month ten for those costs. By the time you get to receive revenue you have already expensed all these costs. And that was about R220 million. That certificate is due in April and Steve promised his car and his house that that money will be in the bank by the end of June.

In Underground Mining in Africa we had two debtors that weren't paying us. That doesn't concern us. On the one debtor we've got a payment coming through. We've been working with the client very closely to make sure that we are going to get paid. So that payment guarantee ensures that before the end of June we will be paid that money. And then we've got some other debtors in Zambia which we had some issues with which have been resolved. Those monies will be in the bank in the next month. If we go to REC we mentioned that on the Mount Morgan contract that they lost money. They will pay us another A$5 million by the end of April, so that money will come in.

The last one is in Cementation Canada. They were in dispute with one debtor and they were in negotiations with a second debtor. Now that second debtor went owner operator. So there were extensive negotiations as to what they're going to pay us for the equipment, which people they are going to take over. Unfortunately the negotiations started in November and went all the way to February. But the good thing is in February we got paid $15 million and in the next two months we're going to be paid another $5 million. So those are all monies that will come back into the bank to help claw back some of that R1 billion working capital outflow. It is a focus area in the group. There is a lot more focus to ensure that these hiccups don't happen over December or June break. But believe me there are a number of action items that have been put in place to make sure that these things get done by the end of June.

Moving to the debt slide, debt can be viewed in one of two ways. What is the company's total debt? I take that to the credit committee and they say no to everything. Or we actually unpack the debt, and we understand the debt, and then we go to our credit committee and say we understand what the right level of debt is. IFRS 16 is nothing new, and I think the banks will find that everyone will come back and if there is a debt service or any debt facility ratio or any covenants discussions will be held with the bank to remove IFRS 16 from it. It doesn't make sense. Then we have taken the rest of the debt and split it between self-servicing debt and corporate debt.

Self-servicing debt has got two elements to it, and you can see that in the bottom block. If I win a mining project and I buy an LHD for R100, I then put that LHD on the mine and as part of my certificate on the revenue line I say that you need to pay me R10 for my LHD. I take that R10 from my LHD and I give that to Wesbank to service my asset based financing. On top of the R10 in the revenue certificate you earn a profit of 15% to 20%. So you're not utilising the profit on that project to pay that asset. That asset is embedded in the revenue in the contract and it shouldn't be seen as true debt. And it is the same with the Bombela Concession Company. The dividends being generated partly go towards settling the debt and partly towards Murray & Roberts. So we see that as self-servicing debt.

The true debt that we follow is the corporate debt. At the moment the corporate debt is sitting at R1.143 billion. Why is that debt high? We can have a look at the TNT acquisition. That is sitting at R297 million. You can see that within 12 months that has come down by half. And we think a significant part of that will still be paid off within the next 12 months. In terms of overdraft and sundry loans, there are some loans relating to JV [?]. It is very small. But about R750 million of that amount relates to overdraft facilities. These actions that I've taken you through should enable us to bring the overdraft facility down. And then the true figure that we follow is that 21%. That is your gearing ratio for corporate debt. Even with a high overdraft I'm really comfortable. If you take out loans to pay something and that corporate debt rockets up to 30% or 40% that means you've got to generate money and profit within the company to go and service that corporate debt. I get a lot more uncomfortable. So from a debt on the balance sheet point of view where we sit as Murray & Roberts today I'm not too concerned. And that, Henry, I think is my final slide.

Henry Laas
Okay, Peter. Can you tell us what we're looking at there? It's a beautiful part of the country where that dam is and where the project will be built. A national park. A few presentation take-aways. The current financial year as I mentioned is about consolidating these acquisitions into the group, building the order book, which we have demonstrated, and successful project delivery. The order book of R50.8 billion we believe is a robust order book. It is a quality order book. Underground Mining, a strong result with TNT contributing well. We expect this business to continue to do well. Having said that, client expenditure has tapered off. The cycle we believe has reached a plateau, so we don't expect any real growth from the mining platform over the next year or so, unless there is an acquisition. But organically it is going to be hard to grow off that base. But we do expect it to at least maintain that level of earnings into the new year.

The growth will come from Oil & Gas which has now got a solid order book already secured for FY2021, and we are very pleased with that position that we have achieved. The Power & Water business, as you would have noticed from Daniël's slides, is different from a scale point of view. And OptiPower which we required recently we believe is a very interesting business, very profitable, high margins, but from a scale point of view it is not that significantly. The group overall we are happy where we are. The results for the first six months are in line with expectation and I think the order book is giving us confidence into FY2021.

I just want to say a few words about the Middle East. It is now a discontinued operation and every year there is R10 million or R20 million that goes into the Middle East. And some time we need to get to a point where this tap is closed and we can draw a line under the Middle East. We had a very detailed discussion at our board meeting yesterday specifically around the Middle East where all the remaining actions and activities were explored and debated in a lot of detail. We are still of the view that the accounting position adopted by Murray & Roberts on the Middle East in total is fine, but we want to get to a point that we can close the door behind us and throw the key away and never go back. We are targeting June 2021 and hopefully by then we will be able to close the door in the Middle East.

Ian, our Commercial Director, is working with me and with Gary Wells and Daniël – Gary is our executive in the Middle East – to ensure that we achieve that. There are still minefields of risks in the Middle East that we need to mitigate and that we need to navigate around, and we are doing that. And it is a very awkward situation. We are getting to a point where the way in which we understand the rule of law and the way in which it is understood in that part of the world is not always the same. It's a difficult thing for us to do, but the positive message I want to leave you with is we're seeing an end to our presence in the Middle East and we are targeting June 2021 for an exit, and hopefully we can achieve that. Thank you very much. What we would like to do now is give you the opportunity to ask questions, and please feel free to ask questions. Yes, Mark.

Mark Ter Mors
Mark Ter Mors of SBG Securities. A difficult question perhaps. The COVID virus, I'm sure the company would have done scenario analysis and impact studies. Can you comment both short term what supply chain effects could be as well as longer term your view on the impact on commodity cycles?

Henry Laas
Yes. I can't give you a definitive answer because we are still in the process of doing the work and trying to understand what the commercial impact might be. We are looking at it from two angles, first from a health point of view, our people that we employ in various parts of the world. How do we manage that to not expose them to unnecessary exposure to this virus? But then secondly, the work that we do, what the potential impact on that might be and the commercial impact of that. We did say in our press release that should we find that there is a material impact we will come back to the market and we will talk to the market about that. Having said that though, we had a brief meeting before this presentation and currently there are two areas in which we are being impacted.

In South Africa we are building a project for Sappi and we make use of specialist welders out of Thailand. And with travel restrictions it's a bit problematic to maintain that skill on the project. So the impact we need to work out and understand exactly what that's going to be. But we don't think it is much more other than a slowdown in the progress of implementation. That's what the impact is going to be, but it hasn't been quantified yet. The second area, you can imagine Asia and Australasia there may be some concerns because the supply chain to that part of the world for projects essentially all links back to China. We are building a project in Mongolia. It's a mining project. It is a joint venture between a third party, our Oil & Gas platform and our Underground Mining platform. So between Peter and Mike we have a 66% stake in that joint venture. I'm going to ask Peter to be frank. Just tell us what the impact is on this Mongolia project. We haven't quantified the impact yet, but the practical implication on the ground. Just share that with us please.

Peter Bennett
In Mongolia there are probably two mains areas that are impacted. One is from the supply chain side. There is a lot of unsupplied equipment for one of our projects there that is being impacted in its ability to be delivered. It gets quarantined at the border. For our shaft sinking project there we also have some equipment coming from that part of the world that also is impacted in its ability to be delivered, although this morning we had a truck load of cable arrive on site just fine. So it is not consistent at the moment. The bigger challenge we have from our perspective is around the movement of our personnel. Given the limited access routes we have into Ulaanbaatar that is becoming more and more challenging. Now if you travel through Korea there is a 21 day self-quarantine requirement. Through Bangkok, through just about every route there is some element of that. So our ability to maintain our supervision on site is being impacted. So we are working with the client there to consolidate our work areas into some more defined space such that we can manage that more effectively. But as Henry says, at this stage we don't know what the long-term impacts will be. There will be a slowdown in work on site, and that is as definitive as we can be at this point.

Henry Laas
The challenge for us under these circumstances where we are impacted by the virus is to come to some sort of arrangement with the client, because we don't want to incur the cost impact of the delay. So it is all subject to negotiation. And whilst it is all very uncertain and nobody really knows how long this will last – is it another month or is it another six months – even the clients where we are building these projects also don't know how to respond to this and how to be

ready for whatever scenario we may be facing. We are aiming to conclude our internal work by Friday of next week and by then we should have a better feel for what the potential impact might be. So it's not as broad as one would potentially expect. As I say, currently it is essentially two projects. It's the project in South Africa where we are having problems with bringing people in from Thailand, and then this project in Mongolia which Peter has spoken about. In Australia the impact at this stage on us is minimal. It's very minimal. Even in Australia the supply chain links back to China, but very minimal impact at this stage. Further questions? Yes.

Question
I wanted to ask about the local project that has been delayed due to community unrest. What happens in the event that you are delivering the project that during execution the same thing occurs?

Henry Laas
We haven't started on the project yet. We know that we've been successful, but the official award has not been made because of the delay. But should something like this occur whilst we are implementing the project it will all be regulated by the terms of the agreement that you entered into with your client. Normally if the unrest is due to our cause then it would be for our cost. But if it is a general area thing and has got nothing to do with us we tend to get extension of time. And in some instances even cost covered by the client, almost like a type of a force majeure event.

Question
Two issues. One is TNT. What is the normal margin in that business, and how does that vary? How variable is it over time?

Henry Laas
Between 15% and 20% of revenue. That's the margin of that business. It is a specialist logistics company. Most of the work that they do is design supply. Alternatively it is EPC, going out to engineer it, procure it and construct it.

Question
And the second question is what's the way forward with ATON at this stage? Where do things stand?

Henry Laas
Who is ATON? No, as you know at the end of September last year that was the long stop date, and they did not extend the long stop date, and for that reason the offer is no longer in play. We haven't had any engagement with ATON yet. We will catch up with them as part of this results cycle. And hopefully next week or the week after next we will talk to them.

Prince
Hi. Prince from Standard Bank. Just on the debt side what would you say is the split between the local and foreign denominated?

Daniël Grobler
Self-servicing, corporate?

Prince
Across the board.

Daniël Grobler

From an overdraft point of view the bulk of the overdraft is carried here. We've got a R50 million overdraft that was utilised in Australia. The rest was used here. The JV loans we allocated between Australia and the Middle East. And the self-servicing debt, the bulk of that sits in Clough, it sits in Cementation and it sits in corporate in South Africa. About a third, a third, a third.

Henry Laas

Any further questions? Ladies and gentlemen, thank you very much. Please join us next door for something light to eat. Thank you.

END OF TRANSCRIPT