Conference call transcript

4 March 2021

INTERIM RESULTS PRESENTATION TO ANALYSTS
SIX MONTHS ENDED 31 DECEMBER 2021

Ed Jardim
Good afternoon to all our stakeholders on the webcast as well as on the conference call. This is the Murray & Roberts virtual presentation from the Murray & Roberts head office for the interim results to 31 December 2020. Welcome to the presentation. Just a reminder as this is a virtual presentation to please ask your questions during the presentation on both the webcast and the call. We will have an opportunity for those questions to be answered directly after the presentation. Please go ahead and ask your questions throughout the presentation. With that I'd like to hand over to our CEO, Henry Laas. Thank you, Henry.

Henry Laas
Thank you, Ed, and good afternoon and welcome. A special word of welcome to our Chairman, Dr Suresh Kana, who is also on the webcast call. As Ed has said, this is the results for the first six months of the 2021 financial year for the period to the 31st December 2020. I would like to follow this agenda for the presentation. You will see it starts off with me trying to create some context around the results for the first six-month period. Thereafter I will give a bit more detail and unpack the group's order book which has grown over time to an all-time high of R60.5 billion as at the end of December 2020. I will then hand over to Daniël. Daniël will get into the financial results in a lot more detail, and I will wrap up the presentation with a few key presentation take-aways.

Let's just create some context around the results for the first six months of the current year. As you know, by December 2019, which is the first six months of the previous financial year, we didn't know about the coronavirus or COVID-19. Those results were not impacted at all by the pandemic. Then in the second half of the previous financial year we had the major impact of COVID-19, and that impact continued into the first half of the current year. So we are comparing two halves, the first half of the current financial year to the first half of the previous financial year. And in the current year we had the impact of COVID-19 whereas in the previous year there was no impact in the first six months.

The group has largely recovered from the quite serious impact that COVID-19 had on us in the second half of the previous financial year. The best way for me to demonstrate it to you would be to refer you to the earnings before interest and tax for continuing operations. As you will see on the slide for the first half of the previous financial year we showed a profit of R419 million. That turned into a loss of R436 million in the second half of the previous financial year. That was the period that we really experienced a lot of COVID-19 impact. We had projects which came to a complete stop and a huge disruption to our operations. And then the first six months of the current financial year we moved out of the loss position of R436 million to earnings before interest and tax for continuing operations of R117 million for the first half of this year.

Now, if you want to have a better understanding of how COVID-19 impacted our operations, it's really in a few areas. First of all, in the second half of the previous financial year it was a hard lockdown where we were not able to do any work on our projects, and many of the projects came to a complete stop. As I said, that is now behind us and in the first six months of this year we experienced an ongoing disruption on the operation. That is because of people going into isolation or quarantine, and it is just disruptive on the operations. You cannot get your productivity up to levels that are required for you to earn a good result from a performance point of view. So that's the one element we were impacted. But secondly, as an engineering and contracting company we do make use of resources that we source internationally. And because of the travel restrictions that were imposed on us, several of our projects we were not able to mobilise the resources that were required to progress the work in accordance with the way in which we had planned it. But as I said, the major impact of the second half of the previous financial year is now behind us and you can see the improvement which came through in the first half of the current financial year.

Probably the most significant aspect of our results is this record order book of R60.5 billion. As you will see on the slide it has grown consistently. From June 2018 with every six-month reporting period the order book improved and improved, and it has now reached this figure of R60.5 billion in December 2020. And for every engineering and contracting company an order book is of critical importance. If you have an order book, you have a business. If you don't have an order book, you don't have a business. If we look forward into FY2022 we are really encouraged by this order book and we believe we are positioned for a strong return to profitability in FY2022. And after that we do expect some growth in earnings, and that will especially come from the Energy, Resources & Infrastructure and from our Mining platforms.

From an operational point of view the group is structured into three business platforms. The Energy, Resources & Infrastructure platform, or as we refer to the ERI platform, is a platform that provides its services to the global market. The Mining platform is also a business that provides its services to a global market. And the Power, Industrial & Water platform, or the PIW platform, is a business that focusses its effort on South Africa and Sub-Saharan Africa. In the following slides I will give a high level overview of each of these businesses and then unpack in a bit more detail the order books in each of the businesses.

As I've said, the ERI platform is a global business. Additionally, it is structured into three regions: North America, EMEA and the APAC region. And in each of these regions we have a dedicated and competent management team that manages our business in each of these regions. To the left bottom of the slide you can see where we have our offices, where we are located and a few of the brands in the ERI platform. Our market focus globally is in the energy sector, but in the APAC region it is energy, resources and infrastructure. And the order book as I said is R42.2 billion which for this platform is also the highest order book ever.

Now, I've been asked the question numerous times whether the group has got the capacity to deliver this order book, whether the platform has got the capacity to deliver this order book. And in anticipation of this growth – and as you've seen on the first slide the order book has been growing consistently since December 2018 – we decided to structure this business into the three regional businesses. This is a recent development. It wasn't always like that. It was always operated out of the Perth office in Australia, but now we have three independent management teams that manage these regional businesses.

Another important point to understand is that this platform predominantly five years and even maybe ten years back provided its services to the oil & gas sector while a major LNG boom in Australia was underway. It is important to remember that Clough, which is the brand under which this platform trades, is a company that has been in existence for about 100 years. Prior to the LNG boom in Australia this business did provide services to these market sectors which are currently again important for this business. So Energy, Resources & Infrastructure is not new for this platform. When we had the LNG boom in Australia during that period its focus was predominantly on the LNG sector.

The business in North America the main office is in Houston and we are busy developing quite a nice project in that region – in that market we are busy establishing partnerships with local companies in that region which we believe will set us up well for further EPC type opportunities in that market. The growth in the order book that you will see in this platform is predominantly work that has been secured in the APAC region, large projects, and the majority of them are in joint venture with other international companies.

The last bullet on the slide you will see that near orders is R5 billion. We define near orders as work that has been secured by the business. It is only subject to the contract between ourselves and the client to be concluded, and normally these near orders move into the order book in a very short period of time. And then we have R43.9 billion in Category 1. Our definition of Category 1 is tenders that this platform is working on and that they will be submitting in time. So the Energy, Resources & Infrastructure platform is a global business. It is a business which has over time changed its market focus slightly. That change has yielded excellent results, as you can see through the significant improvement in this business' order book, and we are very excited about the contribution that this platform will bring to the group earnings as from FY2022.

If I unpack the order book and pipeline, the bar on the left-hand side is the order book. As I said that is R42 billion. The middle bar represents the near orders. And you will see the table to the left has got the heading near orders. The near orders of R5 billion comprises several projects. Some of them are not disclosed on this slide for reasons of confidentiality. You will see the first two projects which are shaded in grey have already moved post December from near orders into the order book. Another important point is you will see there is an undisclosed project to the value of R2.6 billion in near orders. The award of this will be announced next week. New orders find their way into the order book and they don't stay in near orders for a long period of time.

The bar on the right-hand side is for Category 1 opportunities. R43.9 billion is the value of projects that we are currently tendering. And the first three shaded in grey, the Baroota Pumped Hydro scheme, a power station project in the UK, and then the urea fertiliser plant for Perdaman, those three are being negotiated on a sole-source basis, which means we are not in a process where we are bidding for a tender in competition with other service providers. We are in a negotiation with the project developer to bring the project to the stage that it can achieve final investment decision and then the work will commence. On all three of those opportunities we expect that the final investment decision will be taken before the end of June. And if that is the case then that value will move into the order book between now and the end of June. So a very strong performance by the Energy, Resources & Infrastructure platform. And as I said, that order book of R42 billion is a record order book for this platform, and the R60.5 billion that I've mentioned earlier on is a record order book for the group.

The Mining business is a global business. It has been organised in three regional businesses for a number of years now, the Americas, Sub-Saharan Africa and the APAC region. This business is one of the leading service providers to the mining sector. We focus on the underground mining market, and we took a decision that we communicated last year that we would like to explore some open cast opportunities as well. With the results presentation last year I indicated to you that we've been invited by a client to undertake an open cast opportunity for them. Those developments have not yet been concluded as some of the funding arrangements on this project will have to be changed, and we're not sure when that project will come back to us again. So we will be very careful the way in which we engage open pit mining and the bulk of the business as I said is really focussed on underground as we speak.

It is of significance that the order book for this business has not really grown over the past 18 month period. It has been pretty flat at the level of around R18 billion, but pretty flat. Now, the important point is that commodity prices over the recent past have really gone through the roof, and you've seen the results which have been reported by many of the mining companies. It is record results from an earnings point of view and cash flow, and we are quite confident that there will be major investments that will flow into the mining sector which will present new opportunity for this platform. We do expect that the order book will grow strongly over the next six to 12 month period as these projects get approval for development. Near orders is R14.7 billion. This is a strong near order pipeline for this business. Although the order book has been stable over the past 18 months and hasn't really improved or gone down much, we are encouraged by the near orders and R44.2 billion of Category 1 opportunities that we are currently bidding.

For the Mining platform you can see the order book is R18 billion. Near orders is R14.7 billion, and the first four projects shaded in grey have already been moved into the order book, which means that the contracts with the clients have been signed. It is now in the order book, and that happened after the December period close of the first six months. And on the right-hand side you will see the total Category 1 of R44.2 billion. And the undisclosed project which is shaded in grey is a project that we are negotiating on a sole-source basis with the client. It is an undisclosed project. It is not in the public domain yet, our involvement with this project. This is probably one which will not be achieved FID before the end of June. It may, and if it does the R8 billion will find its way into the order book. But I think it is not sure whether it's going to happen before the end of the current financial year, meaning June, or early in the new financial year.

The PIW platform is the business that focusses predominantly on Sub-Saharan Africa. This is the business which has completed its construction work on the Medupi power station and is about to complete its work on the Kusile power station. The order book as at the end of December was R400 million. Now, in comparison with the Mining platform and in comparison with the ERI platform this is a very small order book. As I said earlier on, if you have an order book, you have a business. If you don't have an order book, you actually don't have a business.

So we are suffering in this platform due to the lack of investment that we've seen in South Africa over the past number of years. There hasn't been any significant new investment or opportunity for this platform to pursue new work. This is a bit of a challenge for us. We are committed to this business. We are committed to the water sector in South Africa through this business. We are committed to the power sector in South Africa through this business. But for us to keep on providing services through this business we do need an order book.

We are encouraged by what was said in parliament last week when the budget was presented and also the President's commitment to infrastructure spend in South Africa. But we haven't really seen anything yet. So there are plans which encourage us, but unfortunately there are no real significant opportunities for this business. We haven't seen any recent awards and we don't expect any awards of any significance over the next six month period. Where we are actively pursuing work is the OptiPower business which is part of this platform. As you know, OptiPower is the company that constructs overhead power lines. There are a number of tenders under adjudication with Eskom at this stage, and hopefully we'll be successful with a number of those opportunities which will give us a bit of an injection and increase that order book to higher levels than what you currently see.

We have spoken at previous results announcements about the LNG opportunity Mozambique. We have been asked many a time what the opportunity is for Murray & Roberts. We know about the major LNG developments in the northern parts of Mozambique. What I can say is that the main contractors that were awarded work on these projects are Renaissance from Turkey and Daewoo from Korea. So we were not successful as a main contractor on these projects. But what will flow from this now will be a lot of subcontract work. Our concern is that the subcontract work will predominantly be a labour type activity. It will not include an element of procurement, which significantly increases the performance risk for us on project of this nature. And we are also very concerned about the security situation in northern Mozambique. As you know, Total has demobilised its people from its project and I'm not sure when they will bring them back. The security situation poses a significant risk. So today we don't really see the LNG opportunity in Mozambique as a major opportunity for this platform.

What we do need is government to start investing in water infrastructure and specifically in waste water treatment plants across the country. There is a major problem. We all know that the waste water treatment facilities in all the municipalities, whether it is the metropoles or smaller towns in rural areas, there is a major crisis when it comes to waste water treatment. We do have the technology. We do have the capacity. We do have the ability to play a major part in upgrading this infrastructure or even building new infrastructure. But we can only do that if there's a commitment by the public sector to start investing in these sectors that will create the opportunity for us. So today PIW is a platform that is struggling. It did reasonably well whilst the construction at Medupi and Kusile was underway, but this has now come to an end, and as I said there is very little and limited opportunity for this business.

You can also see this on this slide where we talk about the order book. Again in comparison with what you saw for Mining and for the ERI platform, this is really a very small business. An order book of R400 million, near orders of R200 million, of which some of the projects have been awarded post year-end but it hasn't been disclosed yet. And then Category 1 of R6.6 billion are tenders that we have submitted. Some of the tenders are for projects that have been on hold for a long period of time and we don't know what percentage of that R6.6 billion will actually be awarded and come to market and present an opportunity for this business to grow.

When you put all of this together and you look at the order book for the group, it is very clear that the growth in the group order book up to the R60.5 billion is predominantly due to the growth that we've experienced in the ERI platform. We don't show it on the slide, but in December 2018 the ERI platform had an order book of R4.4 billion, and it has grown to R30.6 billion to December 2019, and now it is at R42.2 billion in December 2020. And I want to give you the assurance that we've got the capacity to deliver this order book, and we believe that we've priced the tenders responsibly and that there is sufficient margin priced into these opportunities for us to earn a reasonable return and to see some profit coming through the business in the new financial year.

Mining, we're not too concerned about the fact that there has not been growth in that order book. We have seen a number of opportunities especially in the US and Canada which have not proceeded in the first six months of this financial year. And we have relied on those opportunities to go ahead. But it will change very quickly. I mentioned earlier on, I think Goldman Sachs and JP Morgan are talking about a new super-cycle in the mining sector in the commodities market. And if that is to happen, this Mining platform will certainly see quite a strong growth in the order book from the R17.9 billion that was reported in December 2020.

And then for the PIW platform there you can see the contract between the ERI and Mining platform and the order book that we have for PIW. Again it is very important for us that the South African government spend on infrastructure actually does happen and that we do get opportunity in waste water infrastructure and in the power sector to play in those markets and to secure work that will give this business the opportunity to grow further.

This is a very important slide. It's a very busy slide but let me explain it to you. On the left-hand side under the heading platform you will see there are three platforms, the ERI platform, the Mining platform and the PIW platform. To the right of that is an order book split. And we've divided it between the SADC region and international. You will see the ERI platform 100% of the order book is international, for Mining 71% is SADC region and 29% is international, and PIW 100% is in the SADC region, but that order book is very small. All of that then translates to 78% of the value in the order book in the international space and 22% is in the SADC region. And the column to the right you can just see the movement between December 2019 and December 2020. And the growth at the group level from R50.8 billion to R60.5 billion was predominantly due to the growth that we can see for the ERI platform.

Another important bit of information on this slide is when you look on the far right-hand side we give a time distribution for this order book. If I explain it for the ERI platform, they've got a R42.2 billion order book as of December 2020. Of that R42.2 billion, R5.9 billion projects will be executed in the second half of the current financial year, and then there is R15.9 billion already secured for the 2022 financial year. The significance of that is – Daniël will show you a bit later – this platform reported revenue of R5.1 billion in the first half of the year. In the second half of the year we have secured R5.9 billion. So you should expect revenue between R11 billion and R12 billion for this business in the current financial year. And already we have secured R15.9 billion for the 2022 financial year. That order book is creating an opportunity for this platform to really make a meaningful contribution to our earnings in the new financial year.

As I said, the order book does not reflect the three very large projects in the ERI Category 1 classification, and three of them are being negotiated on a sole-source basis, and we do expect that FID will be achieved for all three of them before the end of June. Again that will strengthen or further increase that R50.9 billion which is scheduled for 2022. And for that reason we are really optimistic about the new financial year. We have the same level of detail for the Mining platform and for the PIW platform.

The important message from this slide if you look at FY2022 on the right-hand side just below the time distribution you will see that we have R20.7 billion already secured for the new financial year, FY2022, at the group level. That is at the same level as the revenue of our previous financial year, and there are still a number of months to go before we start the new financial year. We are very bullish about our order book, and as I said we really believe it is a good order book. It is a quality order book and we will be able to make good returns once we start to execute work on these projects.

Just a bit more definition again. I don't want to go into much detail, but just draw your attention to the row which is highlighted in bright yellow, the 31 December 2020 row. The order book is R60.5 billion. There are near orders of R19.9 billion, and as I said, near orders is work that has been secured but the contracts with the clients still have to be signed. All of those projects will find their way into the order book very soon. Category 1 is R94.7 billion of which about R34 billion is being negotiated on a sole-source basis. And only subject to final investment decision that R34 billion will find its way into our order book. There is only R8 billion which I think will not happen before the end of June, but the balance should find its way into the order book by June this year. Category 2 of R116 billion is projects where we are working on feasibility studies or we are providing budget estimates. It is not as advanced yet that clients are asking for firm tenders.

And Category 3 is projects which we are keeping on our radar screen. We might be participating in some pre-feasibility work. The Category 3 opportunities are further out but are important for us to track, because if you have an order book of R60.5 billion you need to maintain that order book, and you can only maintain that order book if you have market intelligence and if you identify the opportunities. Even though they may be Category 3, very soon they will their way into Category 2, Category 1, and eventually into the group's order book.

Just a comment on safety. As you know, safety is very important for the Murray & Roberts group. We believe that every day all our employees should return home safely without any injury. And we do have many projects in the group that we conclude on a zero harm basis without any incident to any of our employees. But if you look at the past six months, which is the black line, you will see the lost-time injury frequency rate. That is expressed as a rate per million hours worked. And the two yellow bars are the fatalities we have in the group. The fatality reported for FY2021, the first half, unfortunately one of our employees, Wilfred Moleofi, was injured on a project within OptiPower and subsequently he passed on. And this is very sad for us when we lose one of our colleagues in a work-related incident.

And the lost-time injury frequency rate is 1 for the first six months. In the previous period, December 2019, the first half of the previous financial year it was 1.12. If you break it down for each of the platforms, the ERI platform was 0.34, the Mining platform 1.28 and the PIW platform 1.2. If you benchmark the statistics with the peer group for each of these three businesses you will conclude that this performance, although not as good as we would like it to be, is really industry leading relative to what other companies are achieving in this space.

And then just a final slide from me before I hand over to Daniël, and then I will do the wrap up towards the end. Revenue half year on half year was flat at R10.8 billion. We did report attributable loss compared to the attributable profit in the first half of the previous financial year. And as I said, it is because of the reasons that I've mentioned. Daniël will unpack it a bit more when he gives you the segmental reporting per business platform. Our continuing HEPS is a loss of 8 cents. The order book, which is the highlight of these results, at R60.5 billion.

And notwithstanding COVID, notwithstanding the losses we had in the first six months, we have a net cash position of R0.3 billion which is an improvement on the net cash position at the end of the first six months of the previous financial year. And that is after the IFRS 16 adjustments. If you ignore IFRS 16 the cash position is actually R0.9 billion, and that compared to R0.8 billion for the first half of the previous financial year. Thank you, and with that I would like to hand over to Daniël.

Daniël Grobler

Thank you Henry. I'm going to break protocol slightly by starting with a story. As we were compiling the presentation we said, look, this is a hell of a difficult presentation to put together. How do we go about that? The comment was made that we do have sympathy for Tito Mboweni. He's about to present a hell of a difficult budget. We all must understand where he's coming from and what he's got to deal with. But the factor that differentiates us from Tito Mboweni is we have a strong balance sheet. We have a strong pipeline. And I don't think he had those two factors to his benefit when he presented the budget. With that said I'm going to jump straight into the financial statements.

The turnover and EBIT slide I'm going to discuss in more detail when we get to segmentals. The two elements I want to focus on is our net interest expense as well as taxation. Net interest expense is in line with prior year, R101 million versus R91 million. We can see the debt stayed relatively the same compared to the prior year. But the one element that keeps nagging me and everyone that asks us the question, the effective tax rate remains extremely high. There are two reasons for this high effective tax rate. The first one is Murray & Roberts Ltd was designed to carry the full corporate overhead cost within the group as well as the Power & Water platform. The fact that Power & Water made a loss this year did not contribute to this problem. The corporate losses plus the Power & Water losses we could not generate a deferred tax asset to compensate for that tax loss. So that brought a loss number to the table.

The second element was withholding taxes. When you work in Namibia, Tanzania, DRC, Zambia, when you expatriate your profits from those countries you have to pay withholding tax on those amounts. And those amounts unfortunately manifest on the tax line. It is a big focus. We are looking at various ways to bring in more profitable work within the Murray & Roberts Ltd timeframe. That work has got about two months left before we try and lay and egg on that. We are definitely focussing on that, but as we stand here today we do have a problem. Discontinued operations I'll talk to on a separate slide.

ERI has got four different elements that it operates in. I think the most important one is Engineering & Construction. What we can see is a significant increase from R3 billion to R4.6 billion. We can see the order book exponentially increase from R29 billion to R41.2 billion. The main reasons for that were TransGrid as well as the Waitsia projects that were awarded. A question was asked, why the low operating margin? If you've got this increase in revenue and relatively the same overhead base, why the low 3% margin? The fact is that they were completed two loss-making projects. Both projects had their reasoning. We are busy with a commercial settlement process. If we do settle better obviously that R138 million should be looking better. But its' a process that we've got to go through with these commercial clients to try put that to bed.

If we look at Global Marine and the order book at the bottom, R382 million versus R381 million, they've have had very little movement on that project. That project is scheduled at a marine in Canada. Canada was one of the worst hit countries in terms of COVID. That project is only now starting to gain some feet and some traction. By July 2021 we're hoping to get started on that project. Commissioning & Maintenance we can see last year we had a large margin compared to the current year. Those works are ticking along. We were fortunate in the prior year that we had a project that came to an end. We carried a number of risks for reasons we were able to release. That explains the high operating margin rate for that year. And then corporate overheads. There is a big drive within Clough that as a business is putting different structures in place that they've got to drive down the overheads, so well done to Clough.

The big question that Henry asked and that we continuously get asked is, now you've got an order book of R42 billion. Last year it was R30 billion. Have you got the manpower and the structures to operate successful lump sum contracts where in the past you worked on traditional cost plus contracts? And the answer is yes for the many reasons Henry explained in terms of management structures, new people that we brought into the business. Again I want to focus on turnover, total turnover for the year. So for 2019 that was R3.3 billion. For the full year that went up to R6.8 billion. In the current year we've got R5.1 billion and R5.9 billion secured, so at best this year is going to be between R11 billion and R12 billion. Already secured for this platform is R16 billion of turnover for the next financial year. They've got a number of projects which they are sole-sourcing. They are sitting in near orders. So who knows what the 2022 turnover figure for Clough could be. It could be significant. It could be a game-changer to the group.

I'll move to Mining. Mining Africa a steady performance in terms of revenue, operating profit, order book. An overall steady performance. It's not that they have not got challenges. It's that they are managing the challenges correctly and they're getting things right. We are hoping that they at least replicate that operating performance in the next financial year. In Australia we can see a reduction in turnover as well as in profit. The reason that happened was the Mount Morgan contract, which is a contract mining contract, came to a premature end. The new contract mining projects that were due to start were delayed, and that has got a twofold impact on you. Because of the delay you are not earning profit on that revenue being burnt, and secondly, the equipment that you would have used from Mount Morgan on this mine is no longer in use and generates idle depreciation that drives down your profit.

In the Americas – and I must admit throughout the group I've got the deepest empathy with this group – they have been hit by COVID like you will not understand. And that manifests in a number of items, in project delays, new award delays, project disruptions where people have to stay at home. There have been a number of areas of impacts that have happened on them. In terms of new projects awards I do not think there are any projects bar one that we have not won. So what has happened was because of COVID delays these projects are being delayed and delayed and delayed. It's not that we're losing them. It's just that the market is shifting to post-COVID or post-vaccination or whatever the mining giants are waiting for.

That is a historical low for this entity. What we are looking for the Americas is normally on an annualised EBIT basis between R400 million and R500 million EBIT contribution to the group. Overall Mining came in with R176 million which is about 50% compared to prior year. The order book is marginally down to R17.9 billion, but we have mentioned that they've got quite a long pipeline coming out. All these mining companies that are making a lot of money at some point they will have to start spending that money, and we're hoping for the start of an upward cycle in the mining industry.

In terms of Power & Water I'll start with the easy one. Power came down. The revenue came down from R615 million to R262 million. And we can see an increase in profit. Why did we have an increase in profit? We had a number of disputes with Mitsubishi Hitachi and we won some of those disputes. We had risk provisions allocated against those items, and we were allowed to release some of those risk provisions. In terms of water they have had no projects that are being generated to help cover the overhead structure. We see they've got an order book of R114 million. The Athlone project has been awarded a long time ago, but again for a number of reasons that has not started to earn revenue. We're hoping that project will start to go in July 2021.

Transmission & Distribution, a slight reduction in turnover. Yes, they made a loss of R25 million. Again that is attributed to two projects for clients that are extremely difficult. They are in the process of following their commercial rights. Should they come right in following those rights, hopefully those losses can improve. The most important thing for Transmission & Distribution is they've got a lot of bids under adjudication both with Eskom and other parties. There has been much publicised about power units that need to be built across the country. A company like OptiPower will bring, transmit, distribute and build a substation for these powers to be brought to grid. So there is significant upside potentially for OptiPower going forward. In terms of other that is a combination of a number of projects that we've got. We've got the Sappi contract. We've got the Polokwane contract and a few other ones coming to an end.

One of those contracts made a loss due to a number of reasons. It was budgeted that we bring in specialist welders. COVID prevented us from bringing in the specialised labour that we wanted to bring in. The current labour force that we've got on site is not able to match the productivity levels of the previous guys. And believe it or not there is a slip in a few months which brings in additional P&G and holding costs in running that site. Having said that, we pursue commercial rights, and we're hoping to see where we land and make sure that we contain that loss within that platform. But overall they've got an order book of R400 million left, and that R400 million is nothing compared to the group. We really have to rethink what the best way is for this group to move forward in order to support the group.

In Bombela we had an operating profit of R107 million. And in the prior year they had R197million. So R107 million is an annualised figure that you normally would recognise at half year. That R197 million in the prior year was inflated due to the fact that we managed to secure and agree operating period disputes that went back a number of years. Once that agreement is signed a number of risks within this contract have been de-risked. And where you've taken provision for future risk you could take that out of your model. We developed a new model which gave us additional upside of about R180 million or R190 million in the prior year which was booked.

What we're also saying is on the Gautrain last year in June we had to take a view in terms of ridership and what the impact of ridership or the lack thereof would be. That impact has been taken in the previous financial year. And we've got a budget put up for this financial year, and so far we have been meeting budget and we've had some other improvements. There are a number of floating elements in that budget including insurance claims and discount rates. So a full re-budgeting process of this element will be done by the end of June and hopefully we can mitigate a potential impact of a prolonged COVID impact on this project.

Then we get to discontinued operations. In the Middle East we carried cost to commercially close out the operations in the Middle East. On top of that we recorded a foreign exchange loss of R30 million that is included in that R68 million. That loss has come to an end. There will be no future losses on that R68 million. Included in other are a number of elements. Genrec that we've closed down. But we had an investment in Mooikloof development property. When we sold Infrastructure & Building unfortunately we were forced to retain that one. And as years have gone by it has become obvious that it is more difficult to translate that asset into cash. We have now struck a deal with Balwin and they will buy the money off us. We can take a slight reduction, but at least we're going to get cash in and get the investment off the books.

In terms of the balance sheet there are only four or five items I want to talk about. We've got December 2020 versus June in the prior year. December 2020 if we go down to cash and cash equivalents we've got R3.4 billion in the bank. In the prior year we had R3.4 billion in the bank. Now, there are a number of reasons for up and down, but it's still a cash number in the bank.

If you go slightly down to shareholders' equity we can see in the prior year it was R5.619 billion. In the current year it is R5.092 billion. That is made up of two elements. The one is your attributable loss which will reduce your equity. And the second is an FCTR loss that when certain balances that have a foreign currency translation move, it doesn't go through your income statement. It goes through your equity. And then the long-term and short-term interest bearing debt, both came down which is pleasing.

And the last item I would like to flag which has not been flagged is that current liabilities went up by R816 million. Now, that relates to two contracts where we have received significant milestone payments where you achieve progress but the cost hasn't quite followed the progress. So you have to show it as a liability to potentially pay back in future or earn profit on that money.

From my point of view the balance sheet is quite strong. In the board meetings we've been asked if we've got a strong enough balance sheet to support the great pipeline going forward. And the answer is yes, from working capital facilities. What we saw on some of the ERI platform projects, they are all quite cash positive and they should be fine. As a group we've got to put the bonding facilities in place. Once those are in place I think the group is in a very good position to grow the order book into the new financial year.

The last slide I've got up is just to explain the debt structure within the group. We've got three levels of debt, self-servicing, corporate and IFRS. Self-servicing consists of asset-based finance, project specific finance and the BCC preference share. So from June on the right hand to December we can see asset-based finance came down, which is correct as your mining project is being completed. The preference share scheme in BCC did not move as there were no dividends. TNT reduces as we get quarterly repayments done on that acquisition. The overdraft facility increased marginally. So if we look at total debt it comes to R3.113 billion versus R3.5 billion in the prior year.

Equity has also come down from R5.61 billion in the prior year to R5.092 billion in the current year. And because of that and the fact that corporate debt slightly increased, we can see in terms of our gearing ratios at the bottom that the gearing ratio for corporate debt, which is the one that we keep an eye on, increased marginally from 21% to 32%. So in terms of a debt profile for the group I'm still very comfortable. If there is a significant growth in self-servicing debt it means that we're doing quite a lot of work in the mining space. That would not concern me. IFRS 16 will continue down as your leases start ramping down and you've got less future liabilities. The one area we've got to keep an eye on is your corporate debt.

Henry Laas

Thank you very much Daniël. Ladies and gentlemen, we've got one slide to follow after this divider. I want to please remind you if you have any questions to please post your questions on the webcast. Ed will facilitate the Q&A shortly. We shared a lot of information with you, and it's always important when you get to the end of a presentation to think about what the important messages are and what the key presentation take-aways are. The first point is the decision that we took a few years back to broaden our market focus has really borne fruit. You can see that through the significant growth in our order book, a very pleasing development.

Although we still had a COVID-19 impact in the previous financial year, that impact is reducing and we have largely recovered from the major impact that we experienced in the second half of the previous financial year. Daniël spoke about the balance sheet and the financial position. Of that cash R2 billion is unrestricted cash and we have R2.2 billion of unutilised credit facilities with financial institutions. That just underscores the point which Daniël has made that we do have the balance sheet and the capacity to deliver the order book which we are busy building in this business. Then just a take-away on each of the three platforms.

Firstly, the ERI platform. A significant increase in order book. Now, we don't think that this is something that has just happened. It was planned over time. As I said, the change in market focus started to bear fruit, and we find ourselves in a market today in Australia and APAC region where the Australian government has committed to significant infrastructure spend over the next decade. So that opportunity will be there for the ERI platform for the next ten years. Then in the resources sector what the ERI platform basically does is undertakes surface infrastructure work on mining projects. As I said, people are predicting the new super-cycle in commodities, and we do expect a significant investment in Australia as well over the next number of years in the resources space. So this business is really set up for success.

Mining, you will agree with me that this is just a phenomenal business. It has contributed so significantly to our profits over so many years. Notwithstanding the fact that the order book has been flat over the past 18 months we are encouraged by the signs that we see in the market that there is shortly a significant investment that will be made into the mining space. As I've said, you've seen the results of mining companies, the cash that they are generating with the current level of commodity prices. And the cash will certainly find its way into further investment.

The PIW platform is an area where we are struggling a bit. There are no projects of any real significance in the foreseeable future. And even if we do secure the project that Daniël has been talking about, it is not ever going to elevate this platform to the same level or scale as ERI and Mining. The importance for us now is to make sure, as I've said before, that we don't lose too much money on this business and that we actually will be ready for when the promise that government has made in terms of infrastructure spend becomes more visible and we start to participate in those developments.

From a group point of view in closing, a R60.5 billion order book, R19.9 billion of near orders, and well positioned for a good profit number in FY2022. I don't want to make a forecast at this point, but I just want to emphasise again the significance of what we see happening with the order book. In the first half of the financial year Daniël explained to you that we had revenue of R10.8 billion. The revenue in the second half of the year we would expect to be slightly more than that. If you take that off the R60.5 billion you can see it leaves you with about R45 billion. There are R19 billion of near orders that must still find its way into the order book, and there are all these sole-source opportunities. If we fast line [?] that correctly we could be finding ourselves in the position where we have an order book of around R80 billion by the end of June. But that obviously is subject to the FID decisions on these sole-source opportunities that I've mentioned, and that we are able to close out all the near orders and move that into the order book before the end of June.

So we are really excited about the new financial year, FY2022.We've got a strong business because we've got a strong order book. And without an order book, an engineering and contracting business does not have a business. Our net asset value is R5.1 billion and that translates to R11 per share. Ladies and gentlemen, thank you very much. That is all from me. I'm going to ask Ed now to facilitate the Q&A session and I will ask Daniël to come forward and answer the easy questions. I will answer the more difficult questions.

Ed Jardim
Henry and Daniël, thank you very much. We do have a few questions to get through. I think I'm going to start on the webcast because that's where the bulk of the questions are. The first one is: you have previously indicated that the order book has an embedded margin of around 10%. Can you reconfirm that your view has not changed on this?

Henry Laas
I think the short answer to that is yes, but I need to explain it a little bit. Every Rand or Dollar that moves through our income statement has been secured on a competitive basis. We tender for work and we compete against other companies and we then secure work if we are successful. That means that you cannot price a ridiculous margin into the tender, because you will lose the opportunity, you won't have an order book and you won't have a business. So it is competitive. But as a rule of thumb 10% at the gross level on projects is the margin that we expect from our projects and that is how we've put our tenders together. Then at the platform level after overheads when the business is really doing very well you should expect between 5% and 7.5% margin.

Now, I think the other important point to understand is the overhead cost in our three business platforms is a cost that is not very elastic with the order book. In other words we could support higher revenues and higher order book with the same type of overhead cost. So if you find yourself in a position that your revenue is growing, then your overhead as a percentage of revenue reduces. And if you price your work at the 10% gross margin level at a project after the overheads, you could be between 5% and 7.5%. And that is a very good performance for an engineering and contracting company. You cannot really do better than that, because if you do chase a higher margin you will not secure the work in a competitive market and you will lose order book and you will lose market share. So the short answer is 10% is the embedded gross margin at the project level.

Ed Jardim
Staying on the topic of margins, specifically with regards to the increased order book in ERI, we've got two questions here asking what gross margins are expected on these new projects that we've secured in ERI.

Henry Laas
Again it is in the order of about 10%. Some of them a little bit less, some of them just a bit higher. But on average you look at a gross margin of 10%. Now, sometimes when we report our results in good times where we have high revenue and overheads is a small percentage you don't sometimes see those margins because the 10% is for a portfolio of projects. And as you know from time to time we talk about a loss on a project. We never plan for a loss, but sometimes circumstances change and there are reasons for a project to go into a loss position, whether it's COVID or any other reason. And sometimes on projects we do better than what we've assumed at the tender stage and we are able to achieve a better margin. So overall 10% and on the ERI platform certainly 10% at the gross level.

Ed Jardim

Henry, still on ERI, we've seen overhead woes in the period. With the increased order book and the delivery of this order book how can we look at the overhead going forward?

Henry Laas

Before I answer that let me just get some water please. The overheads in the ERI platform used to be between A$95 million and A$100 million per annum. I've mentioned earlier on that we've restructured this business into three regional businesses and there is a concerted effort that went into the reduction of the overhead cost. The overhead cost in the current financial year is expected to be down to A$80 million compared to the A$95 million to A$100 million of the past. And we are well on track to achieve that number of A$80 million in the current year. That order book is sufficient to support the growth that we are forecasting for this business.

Ed Jardim

Thank you. Perhaps I've got an easy one for Daniël, a question on depreciation costs. It looks like they've increased. What are the main drivers behind this?

Daniël Grobler

We've had an increase in capex in the current financial year. Substantial. There has been a R400 million increase in capex in the Snowy Hydro project. That was partially offset by the disposal of assets in mining. And it's a timing issue. If you buy those assets at the start of the year and you dispose of the assets at the beginning of the year then a balance should be [unclear].

Henry Laas

Essentially it is on these large projects, the capital spend that's required.

Ed Jardim

Thank you Daniël. We've got a question asking for an update on Snowy Hydro. How is it going on the project?

Henry Laas

The project is progressing well. We had a detailed presentation to the Risk Committee and the board in November last year. The project is doing well. It is progressing in accordance with our plans and at this stage there are no red flags.

Ed Jardim

Two interesting questions. The first one is: are you intending to continue with the share buyback?

Henry Laas

You know you can only do a share buyback if you have shareholder approval for the share buyback. And at the current level buying back shares is very cheap. You would think that you would have to do it. But you will recall that at the AGM a few years back that was declined by shareholders. So we're not in a position to do any share buybacks.

Ed Jardim

A second interesting question. Now looking at Aveng in their current shape there seems to be less execution risk today than there was when you made your initial offer. Would you be interested in looking at Aveng again?

Henry Laas

That’s not something that we’ve really given a lot of consideration to at this stage. You will recall at the time we were pursuing Aveng the rationale was that we would retain the two assets, Moolmans and McConnell Dowell, which are the two important assets from our point of view. And the board and management in Aveng have come to the same conclusion, and the business today essentially is the Moolmans open pit mining business and McConnell Dowell. Yes, Ed, we haven’t given it really serious consideration. I’m not saying that it will not happen, but at this stage we’re focusing on a few other things.

Ed Jardim
Thanks Henry. Daniël, with Gautrain’s ridership levels approximately 80% lower what drives the share value recognition? Is it underpinned by cash dividends?

Daniël Grobler
Yes. What you do is you determine ridership right up until the end of the contract. There are costs coming off. But essentially the Bombela Concession Company generates dividends. Those dividends are used to repay debt and to repay shareholders. So with the dip in ridership there are obviously less dividends that could be created. We did that exercise are the end of June 2019 and we think we have accounted for the full drop in ridership. We will do that exercise again in June 2021. But yes, you take your discounts right up until the end of the project, you discount it at a rate and you get to what your fair value adjustment is.

Henry Laas
Just if I could add. The short answer is yes, the fair value adjustment is supported by cash. In terms of the current debt repayment plan debt in the concession will be repaid in…

Daniël Grobler
March 2023.

Henry Laas
2023. And as Daniël has said, the cash that is generated in the business first goes to the payment of debt and then it goes out as dividends to shareholders. So we do expect after the debt has been repaid in 2023, sometime there, there will be over the last few years quite a strike in dividends to be earned. So at the end of the concession period the profits that we’ve taken through fair value adjustments will be exactly the same, just the cash dividends which have been earned over the period.

Ed Jardim
Thank you Henry. We are coming close to the end of the questions on the webcast, but I know there is one call on the webcast as well. We will get to that question. What is the capacity in terms of performance bonds? How big could the order book get before this creates a growth strain?

Henry Laas
I think we are at a point that we are under pressure from a bonding point of view. Let’s not be naïve about this. But with the expected growth in earnings, especially also in the current financial year, we do expect the ERI platform to achieve a much better performance in the second half. And should that materialise, you will be able on the back of that performance to increase our bonding facilities with financial institutions. So currently we are a little bit stretched when it comes to bonding, but I’m pretty sure that we should be able at the end of the financial year to raise additional facilities.

Ed Jardim
Thank you Henry. Are you still considering an open cast acquisition to enter the sector?

Henry Laas
Not really an acquisition. That is a way of entering the sector. We did look at an opportunity in South Africa, and it isn't Moolmans in case somebody wants to ask that question. If we were to enter open cast mining it would be very cautiously. If it is an acquisition it will be a small player in the sector. We did look at one opportunity. We decided not to pursue it. Personally I think a better way to do it would possibly be to secure a project on commercial terms which are acceptable to us, a small project, and to grow the business organically. So the opportunity for an acquisition is always there, but as I say, we are very cautious how we try to engage open pit mining and there is nothing on the cards at this moment.

Ed Jardim
Thank you. We will take the last question on the webcast. Can you please provide any updates on the Middle East and Mafraq disputes?

Henry Laas
You know the Middle East has been reporting under discontinued operations for quite a number of years. You will recall it goes back to 2017 when we sold our business in Infrastructure & Building in South Africa. I think that transaction happened in the early parts of calendar year 2017. And at that stage the buyers of that business were not interested in taking over the Middle East, so we had to retain the Middle East. At that stage it was part of continuing operations, and it moved into discontinued operations at the time that all our construction work was completed. I think it was last year or the year before it moved into discontinued operations. We find ourselves today in the position that we've closed out all projects in the Middle East. Companies had to be de-registered.

Other than two matters, the Dubai Airport – the Dubai Airport is still in the commercial process – and then the Mafraq Hospital in Abu Dhabi. This is the question which we had. The project has been completed. It has been actually in operation for more than a year. It has been taken over by the client. There are patients in it during this COVID period in Abu Dhabi, many patients in that hospital. So it is fully functional. It is actually a fantastic project, but the commercial position hasn't been finally closed out. And we are optimistic that that would happen before the end of the current financial year. And you will recall we have signalled to the market that we would like to exit the Middle East by the end of the current calendar year. So by December 2021 hopefully all of that will be behind us. I think it's not an unrealistic expectation to say we want to be out of there by December 2021.

Ed Jardim
Thanks Henry. Last question on the webcast. Any update regarding the ATON shareholding?

Henry Laas
ATON is still a large shareholder in Murray & Roberts with 43.8%, a very large shareholder. That shareholding hasn't moved. We do engage with ATON from time to time predominantly around our results at the half year stage and at the full year stage. But yes, ATON is still there at 43.8% and we don't know what their long-term plans might be with this investment.

Ed Jardim
Thanks Henry. I see we've got one call on the conference call. It's Sizwe Dube. Could you please ask Sizwe to ask the question?

Henry Laas
For some or other reason the question is not coming through. Ed, can I ask you to contact Sizwe after the presentation and get the question so that we can provide him with an answer?

Ed Jardim
Will do. Thank you Henry. That's it on our side.

Henry Laas
Is that it?

Ed Jardim
That's it.

Henry Laas
Thank you very much. As I said at the beginning, hopefully we can have some of you in person in this room when we do our full year results at the end of August, early September. Thank you very much for your attendance, and all the best. Bye-bye.

Ed Jardim
Thank you.

END OF TRANSCRIPT