Downer EDI Limited
ABN 97 003 872 848

Triniti Business Campus
39 Delhi Road
North Ryde NSW 2113

1800 DOWNER
www.downergroup.com

FY20 Full Year Results, Investor Webcast transcript

12 August 2020, 10am

OPERATOR:
Thank you for standing by and welcome to the Downer full-year result conference call and webcast. All participant lines are in listen-only mode. It will be a presentation followed by a question and answer session. And if you wish to ask a question, you'll need to press the star key, followed by the number one on your telephone keypad. So just dial one on your telephone keypad, to ask the question, but I'd now like to hand the conference over to our CEO Mr Grant Fenn.

GRANT FENN:
Thanks very much and good morning everyone. And thanks for joining us. My name's Grant Fenn and I'm the Chief Executive Officer of Downer. And with me is Michael Ferguson, our Chief Financial Officer.

So, on 21 July, I announced a number of initiatives to create a stronger Downer. Firstly, a path to take us to 100% ownership of Spotless and finally the full benefits of acquisition. Next, we announced the exiting of poor performing and non-core businesses. We committed to shaping the Downer portfolio in line with our urban services strategy. The third initiative, we announced, was the right sizing of our cost base, reducing management layers and headcount, reducing the property footprint, systems costs, and discretionary spend. And finally, we announced an equity raising of $400 million to fund the purchase of the remaining stake in Spotless, the right sizing of the cost base and further investment in our core urban services.

The reshaped urban services portfolio revolves around the core services of transport, utilities, facilities and asset services. Over the past six months in particular, they've demonstrated their strength and resilience, and it's not hard to understand why they represent the future of Downer. They have leading market positions in essential services provided to government and industry. They're predominantly government and government-related contracts, and if not, then they're blue-chip industrials. It's a capital-light, surface-based, business model generating lower risk and long-term predictable revenues and cashflows. It leverages Downer's expertise in operations, maintenance, servicing and supply. We want to be in markets and businesses where quality service providers are valued, and relationships can truly create success over time.

If I move now to the results, the underlying EBITA for the group for FY20 was $416 million and underlying NPATA was $215 million. Michael will provide more details later, but the most telling aspect of the results can be seen in the performance of the underlying EBITA for Downer's core urban services. So, despite the impact of COVID-19, FY20 underlying EBITA for Downer's core service businesses, of transport, utilities, facilities, excluding hospitality and asset services, is comparable to EBITA for FY19, $511 million in FY20 versus $525 million in FY19.

So, despite all the issues of the COVID-19 environment, our core urban services have demonstrated amazing resilience and strength. And that is why they represent the future of Downer. Demand for our services, particularly in government, defence, road and rail, power and gas, water, health and education, has remained strong throughout the 2020 financial year and, in fact, in some areas has increased.

As predicted and, again, despite COVID-19, cash performance improved materially in the second half, with operating cash conversion at 74% of EBITDA, taking the full year operating cash conversion to just under 40%. And this is particularly pleasing result, given the position at the half year.

We'll now take a closer look at each of our urban services. And we'll start with transport. So, this part of the business includes roads services, rollingstock services, and transport projects across Australia and New Zealand. We maintain over 58,000 lane kilometres of roads and over 1,700 passenger rail cars. EBITA for FY20 at $236 million was basically the same as the FY19 result of $242 million. This is despite the lockdown in New Zealand and Yarra Trams' farebox reduction. This was a very pleasing result, but I guess not unexpected, given the critical nature of the services we provide and the strength of our end market positions. We expect demand for transport services to stay strong, as governments look to stimulate the economy and job creation through road and rail infrastructure spending, potential local manufacturing of rollingstock, and shovel-ready road maintenance.

In the transport space, customers are almost entirely government, with little risk of late or unpaid debts, and work in hand is strong at $16.9 billion over an extended period. Downer is the clear market leader in roads and rollingstock services.

Now, moving to utilities.

Utility segment includes our critical services, our power, gas, water, and telecommunication networks across Australia and New Zealand. EBITA for FY20 was $115 million.

That's 15% down on the FY19 result of $136 million. The main contributor to the reduction was the drop in NBN revenue as construction winds down. But despite the drop, this was a very strong result and has been reinforced through a number of significant contract wins and preferred positions over the last short period. We expect demand for our utility services to remain strong in FY21. Work in hand is $5.2 billion, up from $4.7 billion in FY19. Again, with a very strong mix of government and regulated private sector customers who pay on time.

And to facilities; facilities include our FM and building services for defence, government housing, health, education, and transport across Australia and New Zealand. EBITA for FY20 was $134 million, in line with the FY19 result. Despite COVID-19, our provision of FM services rolled on largely unabated. Again, this was a strong result and has been accompanied by key renewals in government and defence. Due to the critical nature of most of the facilities we manage or maintain, we expect demand for our services to remain strong in FY21. Work in hand is $12.6 billion, again, in line with FY19. We have a very high proportion of government customers in this space.

Moving on to asset services. And this is the first time we've disclosed asset services as a separate business. It holds an important set of technical capabilities that are important for our customer base and the Downer Group as a whole. The asset services business was borne out of EC&M to service the oil and gas, power generation, and industrial sectors with specialised turnaround, shut down and maintenance services. It's grown significantly over the last few years with revenue in FY20 of $672 million. EBITA for FY20 was $27 million, 102% up on the FY19 result of $13 million.

Asset services has a mix of private sector and government customers, such as Chevron, Santos, Origin Energy, BHP, and CS Energy. Revenue for FY20 was down around 13%, as non-essential maintenance and capital improvements were deferred, but the critical nature of the assets that are serviced here in this business mean that we expect demand to return in FY21, and work in hand is $1.6 billion.

Our exit from high risk construction markets in Downer's engineering and construction business unit and Spotless's infrastructure and construction business unit is now well underway with less than $100 million in out of scope work in hand remaining to be completed on a handful of projects.

The exit of capital intensive businesses, such as mining and laundries, remain a key short-term objective. Mining EBITA for FY20 was $79 million, 3% up on the FY19 result of $77 million. The business continues to perform well, despite the difficulties of COVID-19 restrictions and, in particular, operating across state and national boundaries.

The laundries business suffered in the second half, with restrictions on elective surgery across the country. EBITA for FY20 was $9.1 million, down 48% from FY19. With the return of most of the hospital volumes, the business is currently performing well. And, as announced in July, the sale process has been paused for now and will resume when investment market conditions improved. We've placed the hospitality business into hibernation to minimise costs as we await demand to recover. With cost-plus arrangements in place for those customers requiring service, we are reviewing the prospects of our hospitality business to determine which parts will continue and which parts will be exited or sold as future market demand becomes much clearer.

I'll now hand over to Michael for more on the financials.

MICHAEL FERGUSON:
Thanks, Grant. Good morning, everyone. I'll pick up from slide 22, outlining the overview of the group's results for the year ended 30 June, 2020. Grant has spoken about the revenue performance for each of the segments and the relative performance of the group's core urban services, the businesses in wind down and the businesses under review or to be sold. On a consolidated basis, the group reported total revenue of $13.4 billion, consistent with the prior year. Despite COVID, the current use or revenue increases in transport, utilities, and mining segment, offset by reduced revenue in facilities driven by hospitality and EC&M, consistent with the group's revised construction mandate. Underlying EBITA and NPATA of $416 and $215.1 million respectively sits within the earnings ranges provided as part of our market update on the 21 July. Adjusting for the after-tax impact of the items outside of underlying, the group's statutory NPATA resulted in a loss of $105.8 million. As Grant highlighted, a stronger second half operating cashflow performance resulted in a full year operating cashflow of $178.8 million and full year operating cashflow conversion of 39.5%.

Slide 23 provides further information on the financial result for the year. Consistent with our half year announcement, FY20 has seen the group's initial adoption of the new accounting standard AASB 16, accounting for leases. The new standard, in essence, requires all leases, including operating leases, to be recognised on the balance sheet. Further, and from a P&L perspective, the new standard replaces operating lease expense previously included in EBITDA with additional interest expense arising from lease obligations recognised on the balance sheet and the amortisation of a right of use asset. Downer has adopted the new standard on a modified, retrospective basis, meaning that the comparatives have not been adjusted.

Accordingly, we have included the impact of the new standard in the table to allow users to make a like-for-like comparison with the change percentage, referred to in the slide, comparing the proforma pre-AASB 16 column with the prior period. Whilst there has been very minimal impact to the groups' reported earnings at NPATA level, just $1.7 million, the table shows larger variances at EBITDA, depreciation and amortisation and net interest expense, due to the reclassification of the operating leases. On a consolidated basis, EBITDA, adjusting for the impact of AASB 16, dropped by 19% to $686.2 million from $850.2 million. Reported EBITDA, after the impact of AASB 16, was $862 million. Consistent with revenue, the full year has seen solid earnings performances, despite COVID-19, in transport, utilities, mining, and the government services divisions of Spotless. This has been offset by the performance in hospitality, EC&M and the I&C Division of Spotless. Depreciation and amortisation, on a like-for-like basis, were slightly up by 1.6%, to $294.2 million. Group EBITA was $416 million. Again, after adjusting for the impact of AASB 16 of $24 million, this decreased by 30%. Non-cash acquisition-related amortisation was $71.3 million, compared to the prior year of $70.4 million, with a slight increase due to the intangible assets arising from the acquisition of the Downer Mouchel joint venture during 2019. Net interest expense includes additional interest of $26.4 million, arising from the recognition of an additional $728 million in lease liabilities on the adoption of AASB1. Adjusting for this, lease interest has...sorry…interest has increased 3.9%, as a result of higher average debt levels, offset by lower interest base rates, and less interest from the unwind of the nRAH provision.

Tax expense of $67.5 million reflects an effective tax rate of 29%. The effective tax rate remains below the Australian statutory rate of 30%, due to non-taxable distributions from joint ventures, at a lower corporate tax rate in New Zealand. This all equates to an underlying reported net profit after tax and before amortisation, or NPATA, of $215.1 million, which is down 36.3%. Taking into account the net impact of AASB 16, comparable NPATA would have been $216.8 million. This reduction in earnings has resulted in Downer's return on funds employed reducing to 10.2%.

The Downer Board declared an interim dividend of 14 cents per share, unfranked on 12 February, and announced on the 24 March that payment of the dividend would be deferred until 25 September, 2020. Downer has not declared a final dividend for the year ended 30 June, 2020.

Slide 24, summary of earnings, highlights a number of items that have been recognised outside of the underlying earnings for FY2020. Again, these items are consistent with Downer's announcement on the 21 July. The total of these items, pre-tax, is $386 million. The full details were included in our ASX release on the 21st July, with the largest items relating to the impairment of Spotless goodwill of $165 million, portfolio restructure and exit costs of $142 million, and the settlement of a legacy Spotless class action for $34 million.

Moving on to operating cash flow on slide 25. Whilst we reported that first half FY20 saw a number of operating cashflow challenges, it has been pleasing to see the operating cashflow improve substantially in the second half of the year. Total operating cashflow, after adjusting for net interest

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paid in tax, for the second half, totalled $320.9 million with an operation cashflow to EBITDA conversion of 74.2%. Combined with the first half, full year adjusted operating cashflow was $340.4 million with a conversion of 39.5%. Included in the second half cash performance are the following items. Strong cash performance from Downer's core urban service business, including cash performance, cash conversion from Spotless of approximately 80%. Completion of the Waratah bogie overhaul program within budget in May seeing a return to predictable cash flows and higher conversions from FY21 onwards.

Improved cash flow performance from nbn as the residual programs reach practical completion. The impact of construction losses including Murra Warra generally being contained to the first half. And a slight reduction in receivables, factoring, and no factoring of payables.

Turning to overall cashflow on slide 26, net capital expenditure was $302.8. million, a reduction of 23.4% on the prior period. Consistent with prior periods, Downer's mining and the Spotless laundry business accounted for 65.2% of total capital. Other acquisitions relate to deferred purchase consideration for businesses acquired in prior periods. Downer also continues to invest in technology with capital being invested in data centre upgrades and productivity improvement platforms across the Australian and New Zealand services businesses. Financing cash inflow relates to the additional financing in the year, with the net proceeds of $348.7 million predominantly explained by the additional MTN issuance of $200 million and additional drawdowns offset by the repayment of some residual USPP debt.

Total dividends paid of $90.7 million has reduced as a result of the deferral of the FY20 interim dividend, whilst the total lease payments made totalled $152.9 million. Cash held at 30 June was $588.5 million which, when combined with undrawn facilities of $1.3 billion, provides us with significant liquidity of just under $1.9 billion.

Turning to slide 27, the Downer Group balance sheet remains strong with a strong net asset position of $2.6 billion. This has reduced from $3 billion as at 30 June 2019, predominantly as a result of the opening retained earnings impact of the adoption of AASB16 of $66 million, and a legacy payroll remediation cost of $78.4 million, and the impact of losses, arising from the recognition of the after-tax impact of the items outside of underlying, of $320.9 million, including the impairment of the Spotless goodwill. These items have also impacted gearing which has increased 35.5% on the 30 June 2020 reported basis. Taking into account the impact of the recent $400 million equity raising and the acquisition of the Spotless minority interest, proforma gearing would reduce to 29.5%.

A group debt profile is set out in slide 28. The group's total net debt is $1.48 billion, with $824 million in Downer and $656 million in Spotless. Both Downer and Spotless are in compliance with their debt covenants as at 30 June, 2020. Weighted average debt maturity has reduced from 3.6 years at 30 June, 2019, to 3.4 years predominantly due to the additional $300 million liquidity, on a two-year term, that the group attained, at the commencement of COVID-19. Whilst this facility has not been drawn, it was considered prudent to secure additional liquidity whilst the impact of COVID on the group remained uncertain. However, following the equity raise, and the acquisition of the minority interests of Spotless, Downer intends to amalgamate the Spotless debt, in accordance with the common terms deed of Downer. This will allow Downer to reduce funding costs and extend its average maturity profile as it will be able to access longer-term debt capital markets previously unavailable to Spotless. This is expected to commence in September or October of this year, as soon as the compulsory acquisition process concludes. Thanks very much. I'll now hand back to Grant.

GRANT FENN:
Thanks, Michael. Just on here, just on the outlook, as you know, we won't be providing earnings guidance for financial year 21, but there are a few points that I'll make in closing.

The acquisition of the remaining shares in Spotless will finally allow us to get the full benefits of the acquisition. Spotless is an important part of Downer's urban services strategy, driving consistent earnings and reliable cash flow from long term customers in critical sectors. Downer's strong market positions and diversification across critical services continues to deliver resilience in earnings and cash flows. Across all of our core businesses, there is a strong demand for our services and strong pipeline of opportunities. The Downer business has a bright future.

Thank you, and I'll now hand back to the coordinator for questions.

OPERATOR:
Thank you, and welcome to the Q&A session. If you would like to ask a question, you can do so by pressing star 1 on your telephone keypad, wait for your name to be announced. If you wish to cancel your question request, you can do so by pressing star 2 And if you're on a speaker phone, please pick up your handset to ask your question. We'll assemble the question queue now.

Just a reminder that star 1 on your telephone keypad to ask a question. And our first question to come through from Alex Karpos, from Goldman Sachs. Please go ahead, Alex, your line is now open.

ALEX KARPOS: Hi team, good morning, can you hear me?

GRANT FENN: Yes, we can.

ALEX KARPOS: Perfect. Just with a few on my end. First on EC&M, just on the wind-downs there, how should we think about timing, as far as any fixed price risk, any big contracts to watch? Is that risk largely gone? Or are there any kind of milestones we're gonna hit in the next couple of months to be wary of?

GRANT FENN: No, it's largely gone. Yep. It's largely gone. The out of scope work is less than a $100 million in work in hand. There's some work on Maitland Hospital and there's some work in Chevron Towers, in Western Australia. But the issues that plagued us... and that's in the I&C business within Spotless, the issues within EC&M have basically been retired.

ALEX KARPOS: Perfect. And on that asset services disclosure, it's really helpful. Thanks for that. And, you know, good growth there, obviously, and some headwind likely on COVID, you know? How should we think about growth, just from the backlog coming in and potentially kind of deferred work returning, I guess, in FY21?

GRANT FENN: Yeah, that's a good question. Look, they've done an outstanding job, over the last two to three years. They've really made a mark on the market share there. They're the leading providers now across oil, and gas, and power gen. You know, they've really done a great job. Look, I think it just depends on, you know, the impact of oil and power prices and how that relates back into maintenance and sustaining capex. You know, I make a comment in the presentation today, that we do think it will remain strong and continue to improve, but over time... but it just depends on whether there's any bumps in the road in the short term. And it's a question as much for us as it is for you.
(CROSSTALK) The only thing is the nature of the work that they do, you know, it can't be held off for that long, you know. This stuff needs to be maintained, and this work needs to get done. So, it's just a matter of timing.

ALEX KARPOS: Perfect. And one final one, just on hospitality, how should we think about the potential losses there, the run rate, I guess, losses, now that you've, kind of, right sized the cost space? Let's say we don't get a return in first half 21, what should we think about for earnings impact, just from the baseline main overhead, and all that?

GRANT FENN: Yeah, so, the nature of what we've got at the moment is the very, very vast majority of the employee base has been stood down. So, you've got a very small fraction of a handful of critical people in a number of contracts. The rest have been stood down. Now, the nature of the costs that continue on those relate to the employment costs around people that have been stood down. So, you continue to accrue annual leave and long service leave, etc. And at the moment, in a cash sense, it's not a great amount but I think it's around about $1 million a month...in (CROSSTALK).

ALEX KARPOS: Perfect. Thanks for that. That's it for me.

GRANT FENN: OK, thanks.

OPERATOR:
Alex, our next question comes through from James Byrne from Citi. James, your line's now open. Please go ahead.

JAMES BYRNE: Good morning, I just wanted to pick up on one of the remarks you made then to Alex, just around the asset services. I'm wondering whether you store much of your potential revenue, that you would have burned in second half FY20, for maintenance, deferred into FY21? And if that was the case, whether you might be able to help quantify what kind of impact that might be.

GRANT FENN: Yeah, well, we did see, certainly that, you know, quite a sizable sort of reduction in revenue in the second half, for all the reasons that you know, and we're very hopeful that that picks up into FY21. But we'll just have to wait and see, James, I guess that's the question. We think it will, but we're not on the other side of those transactions, mate, but, again, the nature of the work, the assets that we're looking after would suggest that that work's still got to be done.

JAMES BYRNE: Yeah, indeed. Any remarks that you can make on the impacts of the stage 4 lockdowns in Victoria?

GRANT FENN: Yes, at this stage, very, very little impact on Downer and Spotless.

You know, I would say no material impact, at this point. The only area that we see some impact at the moment will be, you know, elective surgeries has been postponed again in hospitals so that'll be less volume into the laundries for that short period, and we've just seen...just because of the restriction we've seen in some of the facilities, that we maintain, some pullback of, you know, non-essential maintenance, just to make sure that we comply with the requirements of the government there. But everything else that we do there, you know...most of what we do there you would see is very essential. And we're not vertical builders. So, we don't have the issues that are impacting on all of that. So, virtually anything that we're doing there is in the horizontal space, and the business continues to roll on, of course. You know what, we're all...all businesses in Victoria are working very hard on making sure that we maintain social distances and make sure that we've got the right COVIDSafe plans in place. You know, I think our people are doing a very good job on that.

JAMES BYRNE: Yep. Alright, that all makes sense. So, just think about the pipeline of opportunities in the transport segment, have you been encouraged by what governments are doing with regard to pulling forward projects or adding new projects to the pipeline? Or is it really only a small incremental benefit that you're seeing to that opportunity set?

GRANT FENN: Look, I think, governments are working hard on trying to do what they can to speed things up, and we can see that, you know, in a lot of the discussions that they're having, I think, you know, it'd be wrong to say that we're seeing a huge increase of stuff actually happening at the moment, but, certainly, it's in train and I think they're doing what they can to try and bring stuff forward. You know, and so we're not critical of them at all. They're doing their best in trying to do that. And I think that sector is an area that the government, I think, must use as a job stimulus, etc. So, you know, we're looking forward to getting on with it, as are the rest of the sector, I think.

JAMES BYRNE: Yeah indeed. Just last, quick one from me. Receivables up about 15%, year on year, just wondering whether there's anything in there that I should be concerned about... Pardon me, I should clarify that. Current receivables up 15% to $2.3 billion, anything around payment terms from non-government counterparties or anything like that?

MICHAEL FERGUSON: No, I think it's just timing of the receivables as work recommenced, particularly in our New Zealand market, but, yeah, payment terms have been very good, particularly from the government part of the business. Yeah, we've looked very closely at our private sector receivables, you know, we had some exposure with Virgin, which we've provided fully in our numbers, but otherwise we're pretty comfortable... Well, we're very comfortable with the receivables book.

JAMES BYRNE: Perfect, thanks. That's all from me, appreciate it.

OPERATOR:
Our next question comes through from Rohan Sundram, from MST Financial. Rohan, your line's now open, please go ahead.

ROHAN SUNDRAM: Hi, Grant and Michael, just a couple of questions for me. On that disclosure of the projects in winddown work in hand of less than $100 million, different context, are you able to say what that was maybe six months ago? Just keen to understand how much you've shrunk it.

GRANT FENN: Ooh, I'd have to go back and have a look six months ago, mate, but it would have been...maybe 200? I'd have to come back. Maybe you can speak to Michael Sharp. I'm sure Michael will have those numbers. But...

ROHAN SUNDRAM: Yes, no problems. And just to confirm, you mentioned a couple of projects, $100 million, how should...I guess my question is on some of those renewable projects you're working on, how close to completion are you on those, the ones that we've talked about in the past, like Clare, Beryl, Limondale, are they all practically complete?

GRANT FENN: Yes, they are...you know, in some cases there, we're just in the period of just sort of performance testing. So, they're actually working, and you've got a performance period, but, yeah, all those are just about done and dusted. So, we're spending very little money on them.

ROHAN SUNDRAM: OK, thanks, Grant.

OPERATOR:
Thanks, Rohan. Our next question comes through from John Purtell from Macquarie. John, your line's now open, please go ahead.

JOHN PURTELL: Good day, guys, how are you?

GRANT FENN: Good, John.

MICHAEL FERGUSON: Good, John.

JOHN PURTELL: Just had a few questions. Firstly, on the utility side, Grant, you made a comment that you're expecting demand for utilities to remain strong in FY21? I mean, what are the drivers of that? And you know, it does imply that you're not expecting a big nbn drop off this year.

GRANT FENN: Well, nbn's sort of converting, right? So, it was...for us, it's been mainly construction of the network. And now it's...we're very hopeful that that'll roll into maintenance. And that maintenance contract will also include construction and any movement of technologies from, you know, fibre to the node and to the curve, etc., anything that's going on to make those more consistent will be held in that contract. I doubt whether it's going to be as profitable, but we think that there's going to be plenty of revenue there. It's not just the nbn, it's also Telstra and the other sides of the whole telco space, you know, it's pretty... it's becoming more important, you know, and there's a lot happening there. So, you can see that there's a drop off in the profit for FY20 as a result of sort of the scale down of the construction. We don't think that it's gonna drop much into the next year.

So, it'll be pretty good into next year and the revenue itself will be strong but it won't be as profitable work.

JOHN PURTELL: Thank you. A question for Michael, in terms of thinking about cash conversion for the year ahead, appreciate you've got a fair amount of cash restructuring costs, which you've outlined, but how should we think about sort of that, you know, sort of target cash conversion either on a sort of pre or post cash restructuring basis?

MICHAEL FERGUSON: Yeah, John, I think, we've been able to deal to all the construction losses and quarantine those into 2020. Yeah, I think, Downer's had a history of sort of above 85% cash conversion across the services portfolio for a number of years. And we would see it sort of pre the impact of the one-offs returning to levels like that. Yeah, the difference between there and 100 is just the timing of working capital and other things across the portfolio. But for the majority of the core urban services businesses now they're...yeah, we do and get paid monthly. So, yeah, we don't see a lot of sort of variation between the earnings and the cash, going forward.

JOHN PURTELL: Thank you. That's helpful. And just the last one, look, obviously, we've got the Victorian lockdowns, but, you know, outside of that, just thinking sort of more broadly, in terms of your other states and obviously New Zealand, but to what extent are your businesses back to normal, in terms of on the ground operations and specifically thinking about labour productivity impacts, which hurt you in FY20, to what extent do they normalise in the year ahead?

GRANT FENN: Yeah, so, despite what's happening in Victoria, and also overnight what's about to happen in New Zealand, you know, those businesses...unless New Zealand goes into level four, which we don't think that will do, then the business continues, and in New Zealand, it is largely back to normal…but apart from sort of the rebuild of what is a rather small build business in hospitality over there. In the Australian side, you know, most of that is, apart from hospitality, you know, back to doing what it does. And we're getting used to managing in the COVID environment, social distancing, etc, at work and all the rest of it. So, you know, this is the way that we'll work in the future, John, and I think, you know, it'll be a matter of making sure that we continue to look at efficiencies within that environment. But, at this point, if we don't see any further lockdowns, then we're sort of, you know, back to what will be, I think, the consistent way of the future at least for the next 12 months.

JOHN PURTELL: Got you. Thank you.

OPERATOR:
Thank you, John. And our next question comes through from Nathan Reilly from UBS. Nathan, your line is now open. Please go ahead.

NATHAN REILLY: Good morning, gents thanks for taking my questions. Just the first one was in relation to the work in hand for the utilities business. So, just looking on slide nine. Looks like you've got about I think it's $1.8 billion in orders that you'd expect to convert to sales I think in FY21. So, just looking at how that sort of compares relative to the revenue generated in FY20, looks about sort of 65% work in hand coverage. So, I'm just trying to understand, is this a level of no activity, or work in hand, that you would expect to have at this point in the year, heading into the new year? Or you know still need to win a bit more work there?

GRANT FENN: No, we don't. We don't believe that we need to win much work at all in utilities, mate. We think that's largely bagged in.

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NATHAN REILLY: OK, so, would you be winning work through the year, sort of catch you up there, relative to the revenue generated
(CROSSTALK) hold those revenues flat?

GRANT FENN: Yeah, so within each of the contracts, remember that there's work that happens within those contracts that are not captured within the dollars and contract, so additional capital works, etc, that aren't factored in there. So, there's extra work that comes from the, if you like, the franchise contracts that you have in that particular business. So, you know, we've got a very high level of confidence in the revenue, moving into FY21 with utilities.

NATHAN REILLY: Understood. And then just another follow-up question in relation to the construction work in hand. So, I think, back in Feb, you had the slide in the pack where you broke down your construction exposure across the business. So, it looked like there was about $5.7 billion of construction work. And you spoke to the split between fixed price and D&C work relative to your cost class and alliance. So, I think there was about $2 billion in fixed price work. And you're now talking to this $100 million figure in terms of being out of scope. So, would you just talk to me, what is the definition of 'out of scope'? And what's, I guess, the policy with respect to onboarding fixed price work, going forward?

GRANT FENN: Yeah. So, what we said when we exited the out of scope work was that we would only be completing construction in areas where we had competitive positions and particular competency there, which set us apart from others in niche markets. So, we said that we would continue with transport-related projects, although within transport related projects, we heavily risk-manage the size of the projects in combination with the type of contract. So you'll see, and within those numbers that you're quoting, I don't have them in front of me - but if you're looking at that split, the sizable projects there were alliance-based contracting, so no risk of loss. And you'll see that the very large contracts are in New Zealand on CRL. We've also in METRONET in Perth, and we're bidding for a number of other alliances. And alliance style contracting is actually... we're seeing a lot more of it. So we, you know, we're working hard on those. In terms of hard dollar, we limit very heavily in the transport space the size of the projects that we do. But it's transport and it's power systems. And power systems, that's high voltage, construction of high voltage power lines and substations which we are the number one player in the country. But even then, we are very careful in both size and type of job. For the most part, those jobs are ECI. So we get in early and we work with the customer for pricing arrangement. So, the very vast majority, of that number that we were quoting then, relates to those two.

So, the out-of-scope relates to the mechanical and electrical in the resources sector, alright? So we've lost a lot of money on process plants, etc, for resources. It's also in major construction in buildings. So where we're working mech-elec in, you know, large-scale high-rise developments, so we're out of that, as well as out-of-scope. So, we've really...the swim lanes are pretty tight. It's transport. It's power systems. And in the I&C, so in the Spotless side of things, there's no major construction. It's down to minor construction under sort of $5 million. So that's what we talk about, when we're talking about out-of-scope.

NATHAN REILLY: That's great, very clear, thanks for that.

OPERATOR:
Thanks, Nathan. Our next question comes through from Wei-Weng Chen from JP Morgan, your line is now open, please go ahead.

WEI-WENG CHEN: Hi guys, just a couple of questions from me. First one was just on cash conversion. I'm just wondering if cash conversion in the second half benefited from cash that you were otherwise supposed to put on in first half, so specifically I guess I'm referring to rail and nbn payment timings, which you called out in the first half of FY20 to have a cumulative impact loss of $150 million.

MICHAEL FERGUSON: Yeah, so they both swung around favourably to us in the second half, as we expected they would, when we forecast it at 40%, so...yeah, we had a lockup of WIP with nbn, as the jobs got to practical completion, to trigger the final milestone payments. And we made very good progress, on those things, and so the cash from that released into the second half. There's a little bit that'll come out, first half of FY21. But, to the most part, that corrected in the second half.

WEI-WENG CHEN: OK, great, thanks. And then, just a question on your earnings in the second half, so EBITDA was roughly $200 million in the second half. Just wondering if you could give an idea of, how much of that was weighted to the third quarter as opposed to the fourth quarter?

MICHAEL FERGUSON: Yeah, would have to come back to you, on that stat. But the majority of the impact, you know, on the hospitality. So the hospitality impact was pretty much all fourth quarter. The construction loss impact, yeah ,probably equally across three and four, but, yeah, I'd have to come back to you with the specifics of what was Q3, what was Q4.

WEI-WENG CHEN: OK, thanks. And then just wondering if recent changes to JobKeeper eligibility allowed Downer to access JobKeeper, going forward?

MICHAEL FERGUSON: Yeah, we don't think so.

GRANT FENN: Yeah.

MICHAEL FERGUSON: We looked at it after the announcements came out last week, but, as we sit here today, we don't think so.

WEI-WENG CHEN: OK, great. And then, just a last one, obviously, no earning side of the FY21 today, but is there any consideration around maybe providing guidance at a later point, perhaps, at your AGM?

GRANT FENN: Oh, yeah I dunno, we'll see. So I won't give a commitment to that, but...
(WEI-WENG LAUGHS)
You know, we'll just see where we're at and how things settle down, obviously it's a difficult environment to give anybody too much comfort in anything. Apart from to, you know, spell out the type of business we are, and the type of markets and positions that we have, which is what we've done. And I guess we'll see by November whether we're in a position to do anything different.

WEI-WENG CHEN: Alright. Thank you very much, that was all from me.

OPERATOR:
Thank you, Wei Wei. And our final question comes through from Scott Ryall, from Rimor Equity Research. Scott, your line's open, please go ahead.

SCOTT RYALL: Hi, thank you very much. Grant, you gave an answer to an earlier question, which was with regards to whether or not you're seeing any step-up in pipeline from infrastructure spend out of government, and I understand the point you made. Could you just tell us, what is the thing... I have in my memory, and I don't have my notes in front of me, that historically, your roads business in particular is most leveraged to local councils as opposed to state or federal. And, so, what is it that you're, you know, hoping for, looking for, expecting in that space that would give you a little bit more of a pipeline, and how soon after we see, you know, whatever the announcement is that comes from the government bodies, how soon does it translate into earnings, typically, for you?

GRANT FENN: Yes, OK.

SCOTT RYALL: So, the second part of my question, which you may answer as well, is, you've mentioned your sustainability investments, and specifically in your annual report, sustainable asphalt, leader in the circular economy using recycled products, etc.

GRANT FENN: Yep.

SCOTT RYALL: How does that help you at the moment? Are you seeing any tangible evidence that that's helping in that discussion you're having with government?

GRANT FENN: Yeah, sure, sure. Yeah, so, just on the first point, that you made, look, we are... We have a large market share of state government network management. If you think about what our roads business is, it's a vertical business ranging from management of networks of roads, you know, also doing the maintenance, also creating the materials for the maintenance, and also importing those materials, or creating the products for the maintenance, doing the maintenance, and importing the materials for the creation of that particular bitumen. So that full chain is in action, right now, and we have a very, very strong position in the market. At the very top of that, these network management contracts which we have, we have a number in Victoria, and Queensland, in New South Wales, in South Australia, in Western Australia, they're for state government road managers, so we do a very, very large position with state governments, not just local councils, but we also do work for local councils. We don't do much for federal governments, obviously.

So the mix there, I'd have to go and have another look at... I'd have to have a look at exactly the mix between local and state governments, but both sides are very big parts of our business, and that's in the road maintenance space not in the transport projects.

So, in the timing of the projects that might come on board, well, there's a couple of things that I think the government will hopefully push here. One will be new projects being accelerated, and we will participate in that in as far as we may win those jobs in our transport projects business. But if we don't, we may participate in any case through providing road surfacing into those particular projects, and let's hope that, you know, they're on deck in the near future. But the timing of our

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earnings would be, you know, similar to the timings of what you would get from a construction of those particular elements in those projects.

The other side is maintenance. So there is a lot of shovel-ready maintenance backlog that can be accelerated here. And, of course, to the extent that is on networks and areas that we're attached to that will come directly to us. If not, then we would be bidding for that. And again, that would be, you know, as soon as the government gives the go ahead, that that's where they're gonna spend the money, then indeed we would hopefully profit from that. And the timing on the earnings would be, you know, as that amount of work rolls on. So, it's in the projects that are new, and that's both in the construction side but also in the surfacing side with our products. If they move to accelerate maintenance backlog, we'll be involved in that. And hopefully both of those can be accelerated.

On the sustainability side, look, that's been an ongoing discussion particularly with local councils who have been very keen to, I guess, show their environmental credentials. And we've had very significant success on the products that we have designed and manufactured using soft plastics, using toners, spent toner cartridges, and toner replacing bitumen as a binder, also recycled asphalt etc.

And we've seen local Councils sort of seeking us out to provide those services into the local councils' areas. And you can see, you know... I get a constant stream of very positive news from local councils around the benefits that's providing. And I think it is a differentiator for us, and we're doing very well with it. And it's also not just that, we're also investing in recycling centres. We've got a large one in Victoria, repurpose it, and we're also looking at other areas. So we're right into this circular economy in waste. You know, we're very large player in waste. You probably don't understand that, but that's what we are in detritus plants and repurpose it. So, you know, it's a whole, new and exciting area for this roads business, and we're very happy with it. But it's been going on for, you know, certainly the last two to three years. And it's very popular with the local councils.

SCOTT RYALL: OK, great, thank you.

OPERATOR:
Thank you everybody for your questions. As there are no further questions, we'll close the Q&A session. I'll hand back to Mr Fenn for any closing remarks.

GRANT FENN: Thank you very much for again interest in Downer, and I hope you all stay safe. Thanks very much.

MICHAEL FERGUSON: Thank you.

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