Balfour Beatty Plc

Q1 IMS call transcript

Tuesday 14th May 2013 – 15h00 GMT

Presenters: Andrew McNaughton, Duncan Magrath

Operator: Good day, and welcome to the Q1 IMS call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Andrew McNaughton, CEO. Please go ahead, sir.

Andrew McNaughton: Thank you. And thank you everybody for joining the call for our first quarter interim management statement that we released this morning. If you would allow me just a few minutes, I would like to make just a few observations before Duncan and I take your questions.

While we wanted to continue our practice of giving the market a good understanding of trading in all of our businesses in each quarter, there is nothing in the IMS that represents a notable change of performance since our unscheduled trading update in April. So, rather than repeat the facts in the press release, let me just pick up on a few pieces of new information.

Firstly, our order book increased from 15.3 billion at the year end to 16 billion at the end of March. The increase is predominantly in US construction, and to a lesser extent in professional services and international construction. It's important to note here that the increase in the US construction order book is the result of a conversion of our awarded of but not contracted work into signed orders. It should not be interpreted as a material pickup in our markets.

I also want to mention that in the last two weeks, we completed the internal review of the major projects business in the UK in addition to the regional business, which we've talked about in some detail in April. I'm pleased to reaffirm that we have not found anything in that review to change our estimate of the 50 million pound profit shortfall we announced two weeks ago. The resulting profile of construction profits in the year, combined with a greater than normal second-half weighting in professional services profits, means that our full year profits are expected to be more heavily skewed to the second half than in previous years.

As an update on our financial position, I can add that our average net debt for the quarter was 220 million. This is about 80 million higher than average net debt in the fourth quarter of 2012, and is in line with our expectations.

In conclusion, as the management team, we are fully aware that we have a lot to achieve this year. We are determined to start a meaningful recovery in our UK construction operations this year. We will also press on with our cost efficiency program, and the ongoing strategic initiatives. I look forward to giving a further update on our progress at the half-year results announcement in August.

But for now, Duncan and I will take your questions. Operator, over to you.

Operator: Thank you. If you would like to ask a question at this time, please press the star or asterisk key followed by the digit one on your telephone. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment. If you find that your question has already been answered, you may remove yourself from the queue by pressing *2. Again, please press *1 to ask a question. We'll pause for a moment to allow everyone to signal.

We will now take our first question from Howard Seymour from Numis. Please go ahead sir. Your line is now open.

Howard Seymour: Afternoon, all.

Andrew McNaughton: Hi.

Duncan Magrath: Hi, Howard.

Howard Seymour: A couple from me, please. One just on construction, inevitably, I suppose. Just really the timing, because obviously what you mentioned prior to this and on this is the UK construction being reduced by 50 million and trading on a break-even basis. Can you indicate what the first-half number was last year so we can sort of look at that in the context of what we'll be missing this year?

Duncan Magrath: Yes. I'll have to -- can I rack my brains? Can you ask your second question and I'll quickly look for you now?

Howard Seymour: Yes, no problem. The second question was on the investments business. You mentioned, where is it, regarding the profitability likely to be higher … expected to exceed the 40 million disposal gain target. Again, it masks a couple of peripheral questions there, but is that on the premise that you'd be looking to sell more assets down? Or, as you've mentioned before, that actually the price of the assets is actually rising at this moment in time, and therefore you'd expect to fulfil a high level of profit. And can you indicate what that target would be now, if possible?

Andrew McNaughton: Howard, thanks for that. I guess the position is that we had a planned set of assets that made up the 40 million that we were aiming for for this year. You'll have seen already that having completed the sale of a certain number of assets, we've managed to exceed what we believe the director's valuation would be, and therefore our anticipated gains. We haven't at this time got any plans to sell more assets, but we are currently concluding the sale of the last of them that would make up that portfolio. We anticipate that it's going to -- therefore, because of that, we anticipate that it's going to be a slight gain over and above the 40 million.

I can't give you a full indication of that because we're still in a process of selling the asset. But clearly, we anticipate it will be slightly more than the 40 million.

Howard Seymour: Yes, that's great. Thank you.

Duncan Magrath: And just to answer your question, Howard, I think it's around 1.5%, but I'll check that. Last year.

Howard Seymour: 1.5% EBIT margin?

Andrew McNaughton: Yes.

Howard Seymour: Okay. Thanks, gents.

Andrew McNaughton: Thanks, Howard.

Operator: As a reminder, ladies and gentlemen, if you wish to ask a question, please press *1. We will now take our next question from Mark Howson from Oriel Securities. Please go ahead.

Mark Howson: Hello, good afternoon. For the current year, I think you're still required to win and do markets of 300 million or so worth of work for the UK construction business. What confidence could you say that you could give us that you won't be taking on loss-making work within that? And what have you done on the bidding front, looking at specifically at the bidding teams, to make sure that that doesn't happen?

Andrew McNaughton: Okay, I'm going to step back just for a moment, and first of all -- when we made that statement two weeks ago, I want to make it absolutely clear, that the processes we have for bidding around the business are not broken in the wholesale position. We had a couple of business units where we had some concerns, and there was evidence where the direction and oversight that we had given was less than we would anticipate, that should have been given, and therefore there was some bidding that was at unfortunately low levels.

In the parts of the review that we've done, it's gone right the way across all of those units, and also across our major projects business. We are confident from that that the rigour that's across most of the business and the rigour that's been reinstated across the whole of the rest of the business means that we'll be bidding at margins that we should anticipate in our normal course of business.

Mark Howson: Thank you.

Operator: We'll take our next question from Joe Brent from Liberum. Please go ahead, your line is now open.

Joe Brent: Good afternoon, gentlemen.

Andrew McNaughton: Hi, Joe.

Joe Brent: Apologies, I missed the first part of your call. But just in looking at the statement, you talk about heavy skew to the second half. Could you give us a sort of H1/H2 sense of split of profits that are likely splits, just sort of percentages?

Andrew McNaughton: If I could just touch on the factors -- we talked about, obviously in the first half last year, we had the 52 million of investment gains. So that would be heavier in the first half last year than this year. We've obviously talked about the CSUK split, almost the entirely of that 50 million occuring in the first half, and if you heard Howard just ask me what the margin in the first half last year, that compares with a margin of 1.5% that roughly I think we made in the first half last year. And also we talked about the professional services being more heavily skewed into the second half this year as well. So all those factors will play to skew the overall numbers.

Joe Brent: Okay. And on the net debt position, I think the consensus for the year, I never know if it's an average or a year-end number, I think it's at the 280 level. Is that quarter number of 220 consistent with that?

Duncan Magrath: Yes, I mean we talked about being broadly around 276 a couple of weeks ago in terms of the average net debt for the year as a whole. And at the moment, I would stick with that for an average for the year and that should be consistent with the numbers that we talked about before. In terms of the actual consensus number, in terms of year-end net debt, I would have to go back and look at the numbers to be honest, but theoretically that should have moved over the last couple of weeks by the 50 million that we talked about. I honestly don't know whether that has or hasn't.

Joe Brent: Okay. And I think when you spoke to the market last, it seems that you've had a busy weekend sorting out a number of things. Have you got a sense yet of the tax implications of all these changes? How does that big shift away from the UK, which is low-tax relative to the US, slight uptick in the fairly tax-free disposal gains. What does all that mean for your tax rate?

Duncan Magrath: You're right in terms of the profile of profit mix. That will change the profile in terms of, it will obviously increase the effective tax rate in the sense of the UK going down. I haven't actually got a particular number I could quote you at the moment, Joe, but it will be putting a bit of pressure on the effective tax rate.

Joe Brent: Great. Thank you.

Operator: We have a follow up question from Mark Howson from Oriel Securities. Please go ahead, sir.

Mark Howson: Hello. Just bearing in mind what you said, this 50 million hit is kind of a one-off. How much does that play into your minds with regards to the sustainability of the dividend, if it's a one-off type situation. Clearly you said you were aiming previously for a progressive dividend policy, but there are risks that dividend might be reduced. Can you just comment on that please?

Andrew McNaughton: I think we can only repeat what we've said over the last couple of weeks on the calls that we've had in various discussions that we've had. We understand absolutely the importance of the dividend to all of our shareholders, and hence the policy that we've been adopting over the last number of years. You highlight exactly, that it's the nature of it being a one-off. The most important for us now is to have a real clear line of sight into 2014. And right now, it's a bit too early to give a position one way or another of that. But the one thing that's absolutely clear, and I think to take away from our point of view is in the policy that we have adopted, and the policy that we seek to maintain, we're not fixated on a specific cover ratio at any one point in time. The most important thing for us is to be absolutely clear and absolutely certain that we're making progress in '14.

Mark Howson: Thank you.

Operator: As a reminder, ladies and gentlemen, if you wish to ask a question, please press *1. We would now take our next question from Howard Seymour from Numis. Please go ahead.

Howard Seymour: Hi, gents. A follow up from me - just on the support services; you mention the skew on professional services and the construction from a negative point of view. But would it not be the case that support services should have a much more positive skew? I mean, not necessarily first half/second half, but clearly last year you were impacted by contract issues. We just assume you wouldn't get that again in the current year. Would that be an offsetting factor for you in the first half of this year, or at least to a degree?

Duncan Magrath: Correct. It would.

Howard Seymour: So we should assume a sort of more normal profile for that business in the current year, first half/second half?

Duncan Magrath: It would be closer to 2011 than 2012 in terms of its profile, yes.

Howard Seymour: Yes. Thanks, Duncan.

Duncan Magrath: Thank you.

Operator: We will now take our next question from Edward Donoghue from One Investments. Please go ahead.

Edward Donoghue: Good afternoon, gentlemen. A couple of questions. Could you just give an idea of the margin and how the general pricing trends that's embedded in the US business as it converts out of the pipeline into the order book? And the same with the regard to the UK business, as you get the order flow in now and execution for next year, bearing in mind last year you said it was a 1.5% business. We regard this year as a one-off; where do we go for for next year?

Andrew McNaughton: Can I tackle the US first of all? I think it's all very consistent with the discussions that we've had on this before. I mean we've said that the margin levels that were going into the order books through the last 12 months were stable, just below the 1.5%, around a 1% for the US business. And that's largely because it's dominated by the construction management-style projects. So we're seeing stability in that. What we're seeing in all the noise around orders now flowing into the order book and pick up in that - whilst we are seeing some areas of increase in that area, we are starting from a low point in terms of the volume of supply in the market. So in terms of that picking up through into 2014, we anticipate that's going to be some time before that does pick up.

In terms of the UK, we've talked about it being a one-off in terms of a break-even business for this year. We have said today that we intend to initiate to make meaningful progress back towards the operations. The question is, in our mind, with what's going into the order book we see right now and what we are bidding at, we can see that there's no reason why we can't make progress in that sense. The 1.5% to 2% business that we talked about, that there is an inevitability that some of it will take a bit of time, but there's no doubt we're going to be heading back in that direction as we move into '14.

Duncan Magrath: I would just like to add in terms of the US, the only other factor would be - we are obviously bidding on some reasonably sized design-build contracts in the civil business, and the nature of those, in terms of the profile, is if we're successful in that, and that generates a chunk of revenue - then profit recognition on those tends to be more back-end loaded. That could suppress the margin, but that would be from sort of an increased volume perspective, rather than an order book margin, as it were.

Edward Donoghue: Great. Thank you very much indeed. Appreciated.

Operator: We will take a follow up question from Mark Howson from Oriel Securities. Please go ahead.

Mark Howson: Hello, chaps. Just a couple of questions if I may. First, could you talk a little bit about the time scale and the potential sale of a chunk of the support services business? Because it's quite, and we're now into May, it has been quite some time since you said that you were interested in selling. Could you give us a bit of a timetable? That's the first question.

Andrew McNaughton: All I can say Mark is that we have a process that's ongoing of looking at a number of options for that business. And when we get to a point that we're ready to say something, we will. I'm afraid I can't give you any more any than that at the moment.

Mark Howson: Okay, and then secondly, can you give us a feel for what is happening in the international construction business, i.e. the Middle East? What's the outlook there?

Andrew McNaughton: Do you mean international construction or all of our activities across the Middle East?

Mark Howson: All of it would be quite nice, yes.

Andrew McNaughton: I mean, I think our international -- the construction part of the Middle East; we are now focusing our attention on the UAE rather than any broader than that because our concerns around the market in the Middle East. It is a very open market, and we therefore the competition for construction business - it includes a number of organizations that certainly we wouldn't go to work in the way that they would.

Secondly, the professional services side, we see some really good opportunities. We have had some great success in the last 12 months, not only in Qatar, but also in Saudi Arabia, in power and in transportation. And we see further opportunities in those areas and also some further work potentially in our business that's been well established in Kuwait. So the market outlook in the Middle East is growing in a number of areas, and we see more than stability, we see some growth coming back to the UAE as well.

Mark Howson: Okay, and just finally from me -- just in terms of you yourself taking over running the UK construction business. I mean, clearly, there's a job to be done in terms of the group level, making sure the professional services guys play ball in terms of the overall enhancement of where you want to take the group longer term. I mean how do you manage to run the UK construction on one side and making that sure that is effective on the other?

Andrew McNaughton: Yes, I mean we made it clear a couple of weeks ago the fact that I've stepped back in to actually ensure that it gets the rigour and the focus and the attention that is required. We've management changes in that area. It doesn't rule out that there won't be further management changes, but whatever happens, my focus is in the very, very short term to ensure that we can give you the confidence in exactly the questions you've asked today. And what I want to do is at the appropriate point in time, move on with that business so that we can focus our attention on the overall growth, because that's where we really want to be in the long term.

So what I'm doing at the moment is balancing something that we've got to absolutely focus on to give confidence over the next few months, and then expand back out to take the business forward strategically.

Mark Howson: Okay, thank you.

Operator: As there are no further questions in the queue, that will conclude today's Q&A session. I would like to turn back over to your host for today's call.

Andrew McNaughton: Well, thanks very much. So that brings us to the end of the call. Clearly, if you've got any further comments or questions, Duncan, Basak and myself, we're all available for the rest of the day. And as always, any time that you might need us in the future. But thanks very much for joining us this afternoon.

Operator: That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

END