WORLD TELEVISION

Balfour Beatty

2015 Full Year Results Presentation
15th March 2016

BALFOUR BEATTY

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Summary and Operational Overview

Leo Quinn, Group Chief Executive
Welcome, everybody, to Balfour Beatty's final year-end results for 2015. I'm Leo Quinn, the Chief Executive, and I'm joined today by Philip Harrison, my Finance Director.

We'll start off with a brief introduction and summary from myself, which will be followed by Phil, and he'll give some detailed financials. And then I'll give you an update on our Build to Last progress.

So let me start with a few observations. I started with Balfour Beatty 12 months ago, and at that time I announced what effectively was our 24-month self-help plan. And that was a very, very deliberate decision, both in terms of the timing and the things that we would have to do.

I think what's key about self-help is that we were going to actually manage this transformation using our own assets and resources. We weren't going to go outside to the market and look for help, which would mean an equity call or some other form of cash raising.

So the last 12 months have been very, very challenging and, we've turned in what I think is a very strong performance. There's no doubt that - I don't want anybody to forget that we're 12 months in to a 24-month plan, therefore we're halfway through, if anybody can't do the maths on that. So we still have the other half to go. So I don't want to be declaring victory in any way, shape, form or size.

The first 12 months was a steep slope. My experience is that the second 12 months is always a steeper slope, so we have a lot to do.

I think we've made rapid and meaningful progress in that period of time. We've effectively simplified a lot of the organisation, and there's still more to go. We've upgraded leadership, something that we will continue to relentlessly do in the company. Our governance and controls have improved dramatically, and we're starting to see a culture change based around, you know, measurement and transparency. So in that count, good progress, but still a long way to go.

We've seen our order book start to stabilise, and we still have one of the strongest sector balance sheets. In terms of our orders, we've taken a good, hard look at them and in areas where we've had the legacy projects and the loss-making contracts; we've looked to reduce our exposure in those areas. And we've also made meaningful progress in respect of some of our contracts which effectively were just loss-making, and we've negotiated an exit from many of those.

In terms of our governance and controls, I'll take you through in more detail later, but we've actually implemented our gated lifecycle process, so we're actually looking at actively managing jobs all the way through the cycle.

But I think more importantly now, on the back of our investment in R12, we've now put into place what effectively is a cost-to-complete project on a page, which was extracted from a single database and one version of the truth, so to speak. And again, that means we can track and monitor things through their lifecycle.

Our employees are responding to the transformation in two ways. A recent employee survey saw 67% levels of response, but in terms of our campaign around cash and Cash is our Compass, if you look at our cash performance, I think it's been not short of stellar, and that happens because 35,000 people are all actually contributing towards making us a better, more commercially astute company.

We're still working through our legacy contracts. Phil will show you a slide that shows you that we're 60% complete at the end of last year and we're still hoping to be 90% complete by the end of this year, 2016. We're certainly making progress. These contracts are not without their challenges, and although we may have reached practical completion, we still have to reach financial close on those contracts as well.

We're doing all of this against a backdrop of what is a favourable market, and I do have one slide just to sort of run round the globe and talk about the market per se. But this favourable market allows us to be selective, but at the same time what we're doing is maintaining our investment in both our capability and our assets, and I'll talk about that in my presentation as well.

So on that note, I'm going to hand over to Phil, our Finance Director, and he's going to take you through the numbers. Phil, over to you.

Financial Review

Phil Harrison, Finance Director
Thanks, Leo. Morning, everybody.

Let's go through the headline results from 2015. I'll cover off most of these items in separate slides later, so just to make a few comments on the overall numbers.

Group revenue was £8.2bn; underlying loss from Operations of £106m for the year reflects the losses booked in the first half of £120m, therefore the group did generate a small £14m profit from Operations in the second half.

Total pre-tax losses reduced to £199m from £304m. This reflects the much lower losses in 2015 from Rail Germany and the legacy engineering services contracts, compared to 2014.

Directors' valuation will be covered later, but only a small decline, despite a £145m of disposals during the year.

And finally the dividend, despite the losses shown here in 2015, we expect that we'll be able to reinstate the dividend at an appropriate level at the interim results in August 2016.

Now moving to the order book. During 2015 we focused on improving the quality of new orders. New orders are now being won with more realistic cost assumptions and with better terms and conditions. This has resulted in a small overall decrease in the order book, from £11.4bn to £11.0bn, but the corresponding positive is that we did see an increase in the overall margin of the Group order book.

We've done this by stabilising the parts of the Group where we had the greatest historic problems, such as the UK, and growing the business where we have seen good opportunities, such as in the US.

Looking at Construction Services, the order book was actually flat at £7.9bn, but there are few moving parts within the segment. In the US we continue to experience a good market for new orders, with the order book increasing by £400m to £4.1bn. £150m came from growth in the infrastructure business, with wins in highways, rail and water. In the US building business, the growth came in the West region, particularly northern California, and up into Washington state.

In the UK, the focus has been on improving the quality of new orders, and as a result the UK construction order book fell by £400m to £1.9bn. This was a direct result from us being more selective in the work we bid on. The decline was in our regional business, and there should be no surprises that the greatest decline came in the regions with the most problems historically. For example, London and South East declined by over £200m.

And to illustrate how the quality of the UK order book is improving, we have seen 140 basis points increase in the order book margins over the last 12 months for UK construction. This is the result of the low margin work unwinding and new wins with better implied margins coming in. However, we still need to work hard to deliver to cost and realise those order book margins.

Turning to Support Services, where the order book finished the year at £3.1bn, it's worth remembering that the Support Services business wins large multi-year contracts, which we book in one year, then unwind over the following years. About 80% of the decline was simply this - the natural unwind of the order book on big long-term utilities and transport contracts. The remaining 20% was largely due to our decision to exit a poor performing local authority contract.

So in summary, we've made solid progress in stabilising the historic problems and improving the order book quality. It is worth remembering that we are only halfway through the initial 24-month self-help phase, so we still need to work hard to continue to deliver against these goals that we've set ourselves.

This is the start of a good foundation to achieve our medium-term aim of industry standard margins and Leo will cover more of the market opportunities in his section.

Now a slide on the financial performance of each segment. I'm going to start with Construction Services. Looking at the Construction Services segment now, which has been the source of the Group's poor performance over the last few years, total revenue was down 3%, but the overall message is the same as I just explained in regard to the order book. The UK declined by 14%. This was a result of the order book decline in 2014, but also much lower levels win and do work in 2015, as we became increasingly more selective. We may continue to see some further declines in 2016, as the lower order book at the year-end flows into 2016.

Revenue in the US was down 4% at constant exchange rates. There was also good growth in the Far East from our Gammon joint venture.

Now looking at the profit from Operations, losses largely reflect the historic issues in the UK, US and Middle East, and were in the main booked in the first half. The US losses of £22m includes a £19m profit in the second half, representing a 1.2% margin for the second half.

In the UK, losses increased from the first half by £42m. We did see some additional costs in the historic contracts in H2 as we moved to close them out, but this is also partially due to the unrecovered overheads on projects that we had already written down in the first half.

Middle East losses are predominantly due to the mechanical and electrical business, with a further £9m of losses booked in H2. We are actually trying to reduce our risk profile in the Middle East, but expect to see continued difficult trading conditions in 2016.

The Far East performed well in 2015; however, it is worth nothing that the two contracts that we highlighted at half year, that are currently traded at breakeven, which have a material range of outcomes, are still being actively worked. And we're hopeful that we'll make progress in resolving those issues in 2016.

Looking at non-underlying, it's worth noting the greatly improved performance on the engineering service contracts. This reflects good progress in closing out on those projects.

Finally, comments on the improvements that we've made in our processes and controls during the year. Leo will talk about this in more detail, but as an example, the roll-out of Oracle R12 into most of the UK business is already having demonstrable improvements in our visibility of financial performance.

If we now move to Support Services. Revenues in 2015 were stable as we continued to execute on our long-term orders. However, profits effectively halved in the year to £24m. There are quite a few different businesses included within this segment, many of them which are heavily influenced by their regulatory cycle, such as in gas, water and the power businesses. So we do expect some variability in the margin between years, but the movement in 2015 is outside these normal tolerances, driven by three factors. We realised lower lifecycle cost benefits in the gas and water business in 2015. However, this is just a timing difference and we still expect to realise them in 2016 and beyond. In 2015, we had much lower volumes from overhead power line projects, as we had several big projects complete in 2014 and early 2015. Firstly, this means lower profits, but it also leaves you with undeployed costs as you seek to retain the skilled staff for attractive near-term opportunities. And Leo will cover some of these later in his presentation.

The prior year number was boosted by one-off contract settlements and gains in transportation that didn't repeat in the current year. Our performance in the second half was greatly improved, with £20m of the profit generated in H2 representing a 3.1% margin.

Now moving to the infrastructure investments. A very strong performance for the investment business. Predisposal profits grew by £3m to £37m. That's a good performance considering the disposals we've made over the last few years. Disposal gains were £95m as we made four disposals during the year, including interest income which makes up a sizable part of the overall investment income. The pre-tax profits were flat on the prior year at £161m.

Now if we look at the new project wins and Directors' valuation in more detail. Looking at the new project wins and financial closures, you'll see that we're continuing to invest in the front end of the business. These are the projects that will generate the future growth in the investment portfolio.

We were appointed bidder on eight new equity projects in the year; two university student accommodation projects in the UK, three private rental housing projects in the US, one OFTO in the UK, one healthcare project in the UK and also one energy project, also in the UK. Four of these reached financial close in 2015, along with another three projects where we were appointed preferred bidder in 2014.

Looking at the two columns on the far right, you'll see that a number of the projects included in the Directors' valuation increased during the year from £66 to £71, once disposals had been taken into account. This level of new project wins in 2015 really says three things. We're investing into new projects for future growth and not just disposing of assets; the strategy to diversify the portfolio away from PFI and PPP projects and into new sectors is paying dividends, and that we are not constrained by market opportunity, so we can afford to be selective in how we grow and how we allocate our capital.

If we now move to the Directors' valuation of the portfolio. The Directors' valuation of £1.24bn is flat on the half year position, and only down slightly over the year. This is despite receiving a net £125m of cash from the portfolio from disposal proceeds and distributions, less the £102m that we invested back into the portfolio. Importantly, all four of the disposals made in 2015 were in line with the Directors' valuation, which was revised upwards twice in 2014.

In terms of the other moving parts of the valuation, new project wins boosted the portfolio valuation by £45m; the unwind of the discount on MPV added £93m, and offsetting this was a £69m reduction relating to operational performance and FX. This was largely in the UK due to lower inflation rate and deposit interest rates, some higher lifecycle costs and an increase in the assumed tax burden for potential purchasers.

Overall, a very strong performance with no material change in value, despite the net £125m cash received from the portfolio.

If we now move to the underlying items in the year. £10m of the trading losses from Rail Germany and the engineering services contracts - as I said earlier, this is a marked improvement on the prior year, and when they collectively contributed £111m of our losses. Within the impairments and amortisation, there is £17m relating to the transformation of our IT estate - and of course this is a non-cash item. Within disposals we have also included a £16m gain on the disposal of SSL, which was a non-core rail joint venture which we sold in the first half.

Finally, it's worth pointing out the £23m of restructuring costs relating to the Build to Last transformation. This is in relation to delivering the £60m of annualised cost savings we announced today. Looking into 2016, we do expect further costs relating to the transformation as we continue to restructure our business processes, such as Purchase-to-Pay and Order-to-Cash. Overall, we are still confident of delivering the £100m of annualised savings by the end of 2016.

If we move on to look at the closing out of the historic contracts in the UK. This is the same slide as I presented at the half year. It's a tracker of the 89 historic UK contracts that have been distorting the profit and cash performance of the Group. We said we were focused on closing these contracts out as soon as possible. Only once you've got off the job, do you stop spending the cash, and then we're able to move on to new projects written at better margins and with realistic cost assumptions, and in the end, better contractual terms.

We are now at practical or financial completion on 60% of these projects, up from 31% at the half year. This is a result of a lot of hard work, focus and determination by the teams involved. And as these contracts finally close out in 2016, we should see the final cost and cash flows happen at the back end of the year. So in conclusion, we are still on course to be at practical or financial completion on 90% of these projects by the end of 2016.

We'll now move on and look at the cash flow performance for the Group. This slide shows the cash flow performance of the Group in 2015, which was a strong performance considering the headwinds we faced. There was an operating cash outflow of £247m before movements in working capital and pension deficit payments. This represents the losses and provisions booked in 2015. Offsetting this is a £178m improvement in working capital, shown in detail on the table on the right hand side.

If I give you a little explanation on the right hand table. The construction contract balances had an inflow of £313m. These balances reflect the net, unbilled contract positions and traded profit and loss for each individual construction contract. A portion of this inflow is a result of risk contingencies recognised on specific construction contracts. Trade and other receivables had an inflow of £74m, reflecting the Group's continued focus of driving working capital inflows from improvements in its billing and WIP management. Offsetting this is a working capital outflow in trade and other payables of £236m. This is important as it demonstrates that working capital improvement wasn't driven by delaying payments to suppliers. In fact, as you can see on our creditor days, we saw a reduction in our days.

If we then move back to the left hand side of the cash flow, I've discussed investments already. In terms of the other major headwinds we face, we made £66m of pension deficit payments. In Other, there was a small movement in 2015. In 2014, other movements of £172m included higher levels of capex, and the £96m of plc dividends in that period.

So the total cash outflow in 2015 was £56m, which was a strong cash flow performance in light of the losses in the year and the other headwinds we faced.

If we compare this performance to the prior year, 2014 included £723m of net cash from the disposal of Parsons Brinckerhoff. Stripping out the Parsons Brinckerhoff proceeds gives an adjusted cash outflow of £438m in 2014. And therefore we have seen a year on year cash flow improvement from the businesses of £357m.

Looking forward, we still see a cash outflow in 2016, as the final effect of the losses over the two-year period unwind into cash. I would expect roughly a half to two thirds of the working capital inflow in 2015 to unwind in 2016. When you take into account all the moving parts, we expect to be cash positive at full year in 2016, although lower than the £163m we had at the year end.

I'll now turn to my final slide showing the Group balance sheet. We've already spoken about most of these items, so I'll only highlight a few items.

Retirement benefit obligations of £146m were relatively stable in the year, considering the size of the scheme and the poor performance from the equity markets during the year. More detail is given in the appendix, but it's worth noting that this year is the triennial valuation of our major scheme and we'll report on the outcome in 2016.

It's also worth reminding everyone that the investments portfolio, which is held within investments, joint ventures and associates, is included on the balance sheet under IFRS measurement rules. Therefore, the balance sheet doesn't fully reflect the £1.24bn of value held within the portfolio.

And finally, cash. As detailed on the previous slide, to have £163m of net cash at the year-end is a very strong performance in the light of our trading losses during the year. On the back of this strength, we refinanced our banking facilities, putting in place a £400m facility for three years, with the option for two further one-year extensions, subject to bank approval.

I'll now hand you back to Leo.

Build to Last

Leo Quinn, Chief Executive Officer
Thanks Phil, I'll now try and make up all the time that Phil used. Build to Last transformation, just very quickly - where did it come from, what was the origin? We build things which last for decades, the company has been around for 100 years, so the basis of Build to Last is really a case of we want to put a foundation in place for Balfour Beatty where it's going to be around for the next 100 years.

I'd like to think we could become a share in the future, that you buy, you put in your drawer and ten years later you pull it out and you say, oh hasn't that done well. Unfortunately it's far too early to declare that, but we'll get there one day.

The four planks of Build to Last really around Lean, Expert, Trusted and Safe. Lean is about leaning out the company and our supply chain and we set the goals of £200m cash in, £100m cost out. Expert is about the fact that people buy from us because of our expert engineering capability, project management delivery and it's about honing those skills and actually building on them. Trusted is about doing what we say we will do, both in terms of customers, shareholders, banks and employees. Safe is our licence to operate.

I'm going to take you through the next four or five slides, which I won't tell you the story again, it's really about demonstrable proof and measurement in terms of evidence that we're making progress in all of these areas. And then I'll save my time for the backend when we talk about the markets. So if you want to leave early you're going to miss the best slides.

So cash flow, £200m cash in, this graph on the left hand side here actually shows at the quarter points, the actual cash within the company and I want to draw your attention to effectively the pink line here at the bottom which is 2014, which is effectively the cash flow, ex Parsons Brinkerhoff sale. So you can see very clearly from that if Parsons Brinkerhoff had not sold for £600 to £700m that number would be quite a way down from where it is.

I want to draw your attention to the dark blue line, which is the 2015 performance. And this is the cycle of cash within the Balfour Beatty business, but I would contest that it's the cycle of cash within every construction business. So you get these peaks and troughs in the period. And you can see at the half year, '14 over '15 we were actually £362m better.

We maintained that for the full year at £357m better, and that was largely driven out of two big factors, well three to be honest. The first was improvement in working capital, the second big factor was actually the dividend suspension, capex contributed towards it, but also within our Investment portfolio, which I have to say is a standout performer, we sold £145m worth of assets which were mature and we achieved Directors' valuation for them. But we also had a record year in terms of our investment of £102m in terms of new assets.

So part of the theme as you go through this presentation is that you know we're harvesting in some areas, but we're putting back and equal amount in order to protect the future of the company.

In terms of the £100m cost out, very interesting, one of the revelations over the last year and the more and more you get into this company, what you find is that we're effectively integrating 45 different businesses, which were actually procured and purchased over the last decade, which have not been properly integrated. And whereas that might feel like a horror story it's a great opportunity to lean the company out and to actually extract those benefits.

What we're doing is effectively simplifying the structure and the processes in terms of management layers, removing loss makers and continuing to integrate the back office systems.

Phil talked about purchase to pay and all the other supporting functions. In the HR area alone, when we looked at the statistics I think we said we've got 200 different policies all set up over different companies that they - came to the company with, we're now rationalising those down to five or six. So there's a systematic way to actually deliver those services to our employees.

In terms of cost reduction, £60m of annualised savings already achieved, £39m in back office costs, £13m in IT and IT is a bigger opportunity for us going forward and also £8m in procurement, indirect procurement. We're investing in our direct procurement, as you know we procure £7 - £7.5bn a year and that's an area where we think there's - there's still significant opportunity, although all of the benefits and savings here won't accrue to us because we contract on the basis that we sometimes share the savings, other times the savings go back to the customer. So what we are doing is we're extracting the benefits of a legacy acquisitive organisation here.

In terms of Expert, in a market where the supply is outstripping the demand it's very, very important that we maintain our expertise. And so what we're doing is we're looking to recruit, train and retain the best and the brightest. That doesn't mean we won't be turning over our organisation as we constantly upgrade, but demonstrable signs of proof for me are you know circa 300 apprentices and graduates recruited this year. That's a record year in terms of bringing people into the company. And this is interesting how it brings energy into the organisation, new ideas and new ways of thinking.

We had our first leadership conference where we had the top 300 people in the company come along. Interestingly enough that was a great way of aligning the organisation and actually sort of meeting people who in the past have not always met. But this time we did something different, we had half a dozen apprentices, we had a dozen graduates, so what we're looking to do is actually get the message right throughout the organisation, not just the top down.

In terms of retention, our employees are participating in our survey, 67% response levels. Our scores average around 600 which is actually not a bad place, US had a much stronger performance than the UK. But that's an opportunity to improve.

As you know we moved out of our London office, not only did we save £2m, but we now have a much more productive working environment. It's interesting when you think of the image of construction companies, I'd look at our offices and think we're more like design consultants. So excellent.

And then this year we awarded 344 people with CEO awards, you know recognising their special efforts and recognising their contribution towards the company. It's very, very important that people understand that they're valued and in our world they are.

In terms of Trusted, this is about in my view doing what we say we will do. If you look at the fact that we still have one of the strongest balance sheets in the sector. We finished with positive net cash, our banks have supported us with the refinancing, our shareholder register is quite stable, our employees and customers are still supporting us. We're still winning marquee landmark contracts all over the world, which is extremely satisfying.

The basis of trust for me is built on the following two slides; the first one is our gated lifecycle process. I've taken you through this in the past as to what it means, but fundamentally this is about ensuring that we sell what we can deliver and then ensuring that we deliver what we sell.

It’s quite interesting to me, you can get caught up around a number of things here but there's a couple of things which are important to me. The first is not that our margins have improved or our book margins by 1% or 1.5%, it’s about whether we’ve got adequate cost in the job to deliver it. And if we had delivered our contracts over the last three years at zero margin we’d have half a billion pounds extra in our balance sheet today. So it’s - you know people get obsessed about one and two points of margin, I care about do we have adequate cost in the job to deliver it. So it’s really important that we actually execute this flawlessly.

It’s also important that we start to step back and look at the business. So when I actually do a risk review or any of my colleagues at the senior level in this room, I'm looking at who’s the customer we’re engaging with, do we have experience of that customer and do we actually like working with them and is their former contract acceptable to us? And it isn’t then at stage one we’re going to decline the opportunity. There's too many contractors out there at the moment chasing business that they’re inappropriately qualified to actually deliver.

The second thing I look at is do we have the project management capability that we have confidence in that can actually deliver that job. Too often if you look in the past we’ve actually won a job and we actually then don’t have the people to put on the job, let alone the leader to make sure it happens.

And then of course do we have a trusted supply chain whereby that supply chain can then deliver the job that we’ve actually sold. And again if I look at many examples both the US and the UK, we've actually taken a job, we've exposed ourselves to risk and we don't even have the supply chain lined up that can actually do it. And today we have challenges on jobs where we've got a good supply chain but we've overextended it, you know we've got one M&EA provider who is actually on two or three critical jobs, and of course with the shortage of labour it's very difficult to resource those jobs properly. It's incumbent on us not to overtrade as a company because the supply chain is our limiting factor.

The second thing is that we've done a hell of a lot by the way in our IT infrastructure in sorting it out. I wouldn't even go through the pains of the last 12 months, but we're starting to make real progress. Phil talked about the fact that we've put in our R12. You know I've never known an ERP system save a company. I've known it sink companies but we're starting to - we've put the system in, it's not the best ERP system in the world but it's adequate and now the challenge is how do we get real value out of it. And unfortunately you can't do that in two months or three months or six months, it takes two to three years. But we're working it really hard.

This is an innovation which has been put together by one of our guys, and I just think it's just sheer genius. What we've done is we've taken the R12 database and we've applied a data analytics model across it. We can now pull real time, and I'll qualify real time is monthly for us, all the data on every single job. So we can look at forecast final margin, recognised revenue, margin to date, certified by client, cash flow. We can look at simple things like value recognised, cost incurred to date, time in terms of schedule. So you get a very quick view of how that's performing.

Now why is this important? In the past if I had wanted to know how a job's performing I'd have to phone probably three layers of management and finally some poor guy at the end of the branch would actually put together a forecast and send it back. That would take days and invariably it wouldn't be very accurate. What this is, is that this is a real time version of the truth which we can invasively go in and pull and extract any contract centrally for the company and get an answer.

So for example I visited a customer two to three weeks ago, and in the morning I said could somebody actually give me where we are in terms of the cost on this job. So when I talk to the customer if he actually owes us cash I can talk about it, or if there's a cost overrun I can understand why. I was given the sheet, it printed off, it had all of this information, I took it into the customer meeting, and although it was a meeting to talk about performance it was a meeting also to talk about their obligations in terms of ensuring that we were being paid and that we were recognising costs correctly. So this is a great piece of work and it just shows that when you've got geniuses in your organisation just what you can turn out from the infrastructure we're putting into place.

In terms of safety again I cannot emphasise enough this is our licence to operate. If you are not safe you will not be in business, you will not be awarded contracts. The great news is that the whole industry is responding to this. This is an inherently dangerous place to work. Construction sites kill people and we have to make sure that we are at the forefront of good safety practices. And by the way it doesn't cost you money. I'm fundamentally a believer that safety is free, because if you look at the downstream costs of getting it wrong you would make sure that you invest upstream so it doesn't happen.

You know our employees feedback that we have good attitude towards safety. We're increasing our leading indicators in terms of safety observations so we're into prevention, and lost time accidents. Generally speaking I think we're moving in the right direction but it is a marathon and it's something you have to stay on top of every single day.

I'm going to go back because I've lost a slide and I got the order wrong. I'm going to go back to this slide here in terms of trusted. And what this slide was actually demonstrated to do was actually to show how we have performed in terms of our gated lifecycle process around the bidding of jobs. These are three jobs which we bid through our Infrastructure business in the United States and this is the output of the discipline that we've installed.

This first job here, by the way this is publicly available information that's why I picked on this, this first job here is Echo is a water treatment plant in California. It's known as a hard bid, lowest price wins and this is a case where Balfour Beatty bid $442m and the lowest bid was $415. Now you may think that's within the margin of error and I probably look at it and think the same way, but it is quite interesting is that we're actually - we know the customer, we know the plant, we know the application and we work in territory. So that is a very, very accurate bid in terms of what it would require to do the job and make a profit and cover the degree of difficulty.

This is a bid from a company that actually has - is experienced in water treatment but have not worked in California, do not have a local workforce and so you really question around the fact that is it possible to deliver that bid for that price? So the fact that it's gone at that price we're really comfortable but we know the cost that we put into that job was the right cost. So we lost that.

In the case of Georgia 400 which is in Atlanta, it's the intersection of 400 and 285, big complex job. 80% on price, 20% on technical capability. We scored the highest technical competency. We bid $783m and the competition won it at $460m. You know that is completely nuts that anybody could deliver that job for that price. And so do you know where I am on it? Fantastic, let them take it because they've got five years of pain. And we have an expression in the company called two minutes of champagne and two years of pain. I think, you know, they better enjoy the champagne because that's going to be very painful over the next few years.

Finally one that we actually won, the Bergstrom Express, it's in Austin, Texas. 70% price, 30% technical score. We had the highest technical score. We won the job at $100m premium over our competition because we actually bid what was required to do that job. So I just want to use this as an example about how it's really important to do our bit about maintaining these disciplines, otherwise you can get so carried away in terms of just trying to bid to win and I'd rather have less business at a good margin than lots of bad business which will leak out over the next five years.

Moving onto the market for a few seconds, market growth. I think we're living in a very, very favourable world for construction at this moment in time, I think particularly Civils and Infrastructure going forward. So if I just do a quick fly around the world, if I look at

UK, we're mostly Brits in this room, I mean we read every day about HS2, Crossrail Thames Tideway, energy projects, airports such as Heathrow, tall buildings, you know the UK market I think is very, very favourable. And the challenge is going to be which ones do you want to do that you're prepared to do with the right customer, with the right supply chain. And I think these things are going to be very - they'll be hard fought over but I think there's so much business out there it's a question of being very, very selective.

In the case of US Construction, the building side of the US I think is growing at 2% to 3%. I think it will have a strong year this year. Moving into the future I think you'll see it flattening a little bit from there. But on the infrastructure side, roads, railways, water treatment, they've just passed the first highways budget I think in five or six years and it's about $300bn over the next five years or so, so I think you're going to have strong US demand on the infrastructure side.

And I like our Infrastructure business in the US, strong capability in roads, strong capability in railways, strong capability in water and we're very selective, we only play in the states that we play in today. So we don't believe in taking our expertise and moving into another state. Even though it's the United States it's another world in many cases.

I'll go to, before I go onto international, I'll just talk about our Support Services which is effectively for us UK rail, power, gas and water. Gas and water for me is sort of a flat market going forwards. There's a lot of work going on but the nature of the contracting in these areas and some of the contracts over the next eight years on a pain gain, I think one wants to limit their exposure to them because how you can forecast eight years ahead is a bit of a mystery to me. So I think we'll continue to support what we've got but I don't think we want to increase our exposure.

If I look at power you know to me a great business is a business that doubles over five years and I think mathematically it's about 15% compound. But if I look at what's going on in interconnectors in terms of connecting power to Europe, to Iceland, to Norway I think this is a very attractive market. We need to be very careful, it's a different risk profile to what we're doing today. We're in transmission distribution. But I see that as a strong growth area. And it's actually - this year it's actually one of its lowest performance because of the regulator and the new billings and the regime means that effectively the likes of National Grid and utilities are all trying to work out what work they can place and what volume. But I think looking forward this is a strong growth area.

In our rail market we've been consolidating over the last few years and we've been exiting what effectively are some very difficult contracts. We're now at a point where I think we're very stable. I think Network Rail is a really challenged customer, a great customer. They're going to spend £38bn over the next five years and what we want to do is we want to make sure we're there to support them in a way that's meaningful that we can actually deliver on their demands and that we can make the right sort of return. So we're encouraged in this area.

If I look at - I'll do investments, very strong pipeline of investment opportunity. We're going to continue to sell assets when they're mature in their cycle, and we're actually going to continue to invest in the cycle. But you see all the things around Network Rail and whatever, this is a very strong market and the great news is we've got a very strong capable team which perform consistently over the years.

Finally in the area of international, international to us means two things, Hong Kong and the Middle East. Hong Kong where we're partners with Jardine Matheson, very professional organisation, good structure, good process. The team is doing very well. Buildings has been growing over the last three years, there's been a dearth of Civils type jobs, the Civils market is now starting to come back where we're very strong. So I think Hong Kong, you know, will carry on and it will be quite steady for us.

If I look at the Middle East you know I think that's a very difficult market. It's the most aggressive contracting market I've ever seen. I'm not a lover of that amount of aggression. Our revenues have grown. We would like to have kept them stable to slightly declining, but the growth has really been along the lines of customer diversification which is actually quite good. We've got exposure into different markets and customers that we want to do business with going forward, and they're also good historical customers. So the Middle East I think is going to be the single most challenging area in the portfolio for us. There is a lot of growth there. Oil price is at $40. I think there's a real liquidity challenge in that area. So I'm not comfortable being overexposed there. So that's just a sense of what I see around the world. A very interesting time to be in Construction, very interesting.

Finally my last slide and just to remind everybody, we're halfway into our 24 month self help plan. Far too early to declare any sort of victory but there is a thread through the presentation I will remind people of. You know we're investing in over 300 graduates and apprentices for the future. We had our record year in terms of £100m into our investment portfolio. We've cleaned up one hell of a lot of crap in terms of contracts, but also in terms of infrastructure and our IT and we're now starting to turn these into enabling tools. So you know at the end of our 24 months I'd like to think we're in a really good position for the next 24 months, whereby we're looking at how do we take Balfour Beatty to industry standard margins. And then beyond that we are the largest player. We should have economies of scale so in the long term I'd like to think that we're actually generating returns which are commensurate with the market leader.

So I'm sure we'll deliver on our 200 in and our 100 out. But there's still 12 months to go and we've got a great team sort of delivering on it and I'm hoping to come back in 12 months time and report some good results. Thank you.

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Questions and Answers

Howard Seymour, Numis

It's probably a couple of questions around the same focal point really and that is the regional Construction business in UK. You've given us the top line numbers but I don't know if you're going to give us the numbers breaking down going forward, but firstly is it safe to assume that much of the revenue decline in the UK would have been the regional business in the past year?

And secondly and sort of going forward, a lot of what you mentioned in the UK is the sort of major projects, the tall buildings, which isn't regional. Just some sort of idea as how you see the shape of the business, both in terms of overall and clearly on the regions and those regions that have been problems. Thank you.

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Leo Quinn, Chief Executive Officer
I can hit on that, both of those if it helps. Look you're dead right, I mean most of the revenue decline and the booking decline is in areas that we've had problems or we've been challenged. And I think that's only sensible. In those areas what we want to ensure is that we've got a strong foundation and base before we start to grow. There's no point in over trading, especially at a time like now where the real challenge is skill shortage across the industry.

In terms of the mix between the regions and major projects, obviously there is a lot of infrastructure which sort of falls into the major projects areas, both in terms of roads, coastal defences and the like. But if you think about our regional business there's a great opportunity to feed business locally, but also to be feed stock for our major projects because those people are actually of the same ilk, the same training and the same capability, it's just that they move up onto larger scale projects. So I'm comfortable that if we don't have the regional business that we want we're in a good position to redeploy skilled, trained people into bigger projects.

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Gregor Kuglitsch, UBS
Can I ask a few questions, two are a bit detailed just to be clear, and then one is on the sort of midterm where you see the business heading.

The first one is just on the UK. Can you give us a sense when you think the UK Construction business will actually hit breakeven point? Do you think that's possible in '16 or is it more a '17 story? I understand there's obviously the unwind of the legacy still to play with.

The second is on Support Services, you sort of flagged a few one off issues in 2015, can you give us a sense - I think you've traditionally spoken around the sort of 4% margin - 3.5%, 4% kind of margin, is that something that you think you can achieve already this year or will it take a little bit longer until some of these positive dynamics come through?

And then maybe a bigger picture question, obviously you're talking about selectivity return to profitability. Can you give us a sense where you see sort of perhaps by the main segments your midterm margins, and perhaps also sort of a view of directionality of revenues, i.e. do you think you will have to shrink the business to get there or do you think you can hold the roughly I think you were £8.2bn of Group revenues, is that something that you think you will broadly hold steady so giving a bit of a sense? Thank you.

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Leo Quinn, Chief Executive Officer
Let me take them in reverse order. You know if you're going to drive and create value you can't shrink businesses in the long term. So I think the way I think about it is we're going to look to stabilise the business around what is our capability in the short term, and then we're going to look to grow from that stronger base. Whether that's 12 or 18 months I wouldn't like to say, but it's that order of magnitude.

And to drive value there's only three levers, you need some top line growth, it doesn't have to be a lot, you need some margin improvement and you need some overhead reduction. And I think the way I think about it is we're pulling all three of those levers at this time.

In terms of Support Services I think we're on record as saying that we see that market performance in the 3% to 5% range. So obviously we'd like to think in the short term we'd get to the 3% and then shortly after be heading towards the 5%. But then I think beyond that I'd like to consider that we should be having market leading performance in those areas and that market average is not really acceptable given that we've got the largest market share in some of those services areas in what we do.

In terms of UK Construction, you know it's still a challenge and I mean to be fair and not to give you the answer that says you know as a CEO I'm not a magician, I can't sort of conjure up these answers, I'd have to say that I think you'd be safe in assuming that you would be returning to profitability in '17 around UK Construction. And if we do it earlier than that wouldn't that be a nice surprise for all of us.

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Stephen Rawlinson
Just three questions if I may please. Firstly on the working capital improvement obviously it's quite a major change but the creditor days still stand at 91 and within the industry I just wondered whether that's actually rather high and what we might expect this year in terms of a working capital improvement during the course of the year?

Secondly with regard to the PPP PFI, you've got £100m reduction in the operating margin there. Obviously when you recalculated the portfolio in the early part of the year I think the £375m of the improvement in the value of the portfolio up to £1.3bn came from operational performance improvement. You're now saying that well maybe £100m of that wasn't quite right is one way of interpreting that. Could you just help me understand how better to interpret that number?

Third one, on the pension deficit it may be starting to rear its head again. You did allude to the fact that there's a triennial valuation but if you take into account the fact it's gone up by about £20m and you stuffed in £66m during the course of the year as well, the shift in the underlying areas is quite strong. So if you could just help me out with those three points at the moment I'd be really grateful. Thank you.

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Leo Quinn, Chief Executive Officer

Those are so straightforward and easy I'm going to give those to the Finance Director.

Laughter

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Phil Harrison, Financial Director
So on pension, working back, pension clearly it's IAS 19 - it's accounting, when we do the actuarial valuation it will be on a completely different basis. And remember the £66m that we're putting in on deficit is related to the actuarial valuation that we did three years ago. So they can be different and I think if you look at IAS 19 it's typically just the movement of discount rates and how they move. So I'm not - I don't think you should look at both of those in the same way. And clearly we'll report back on where we get with the actuarial valuation in 2016. So it's a kind of an apple and pears there so I think at the moment given where we are on the pension fund I think we're in reasonably good shape.

On the £69m operational cost in terms of the director's valuation, as always you're going to assess - you have to assess this at your yearend points. Clearly the assessment that I've taken this year is if you look at where we are on inflation - the two big movements are inflation rate and deposit interest, and the other one is actually the tax benefits that could appreciate to other purchasers. We've had to take a look at those because clearly coming down the line on tax is BEPS 4, that will have an impact going forward and therefore we've made what we think is prudent assumptions around that. And in inflation we just modified that down to the lower rates of inflation that we're actually seeing. And that's the judgements we've taken this year.

And on the working capital I just can't remember -

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Stephen Rawlinson
You've got creditor days down to 91 but quite clearly but there's both in that - that 91 is a long period in this sector from obviously you've got a range of geographic exposure there which will vary the traditional relationships in those territories. And the other element of that is there might be a trade off there with margin as well. So it was just to explore that a little bit. I know it's a complex question for this type of meeting but the creditor date is an important number.

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Phil Harrison, Financial Director
No it's fine. If you go to - in our appendix if you go to slide 32 we actually plot out to '07. And I have to say when I look at this on creditor days 91 is the lowest period that we've ever had since December '07 by about three days. We typically have averaged even 108. So actually it's I have to say a very good performance off Balfour Beatty statistics back to 2007.

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Stephen Rawlinson
What would you regard as the stable number going forward then Philip in terms of actually also getting that trade off with margin which might arise from earlier payments?

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Phil Harrison, Financial Director
I don't think there's necessarily a trade off on margin. I think we can - what we're trying to do in procurement is actually look at long term relationship with suppliers that drive a better outcome for both parties. And therefore I would anticipate we may actually reduce our creditor days down in relationship to actually providing a better base in terms of consistency, quality going forward. So I don't want to commit as yet to where we think the creditor days is, I think we could certainly see them going down. I certainly wouldn't want to see them go back up to the high levels that we saw in '10s and '11s.

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Stephen Rawlinson
Thanks. And can I ask just one further question if I may. On page ten of the text you talk about a small number of long term complex projects where significant judgements have been taken over contractual entitlements. Could you just give us a clue if you can about the range of likely outcomes that you see on that, because obviously that's quite important for the way investors see the future and it's quite a heavy duty sentence in the way it's expressed there?

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Leo Quinn, Chief Executive Officer
I was going to give that to Phil actually because that's worthy of him, but what I would say is it's exactly the same sentence that we had in a year ago. Just on payables for two seconds just while I remember is that in terms of our balance sheet we're clean in terms of there's no factoring, historically there had been some, so there's none of that goes on, there's no supply chain financing going on in it either so it's a very clean number that you're seeing. And Phil in terms of the range of outcomes on those material contracts?

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Phil Harrison, Financial Director
I mean we put it in the statement because there is a wide range of outcomes. And it would be - I can't definitively give you a figure around that Stephen. What we're trying to draw your attention to, we are a very large contracting business, our business is in dealing with some major projects which will have big outcomes. I did say in my words though Hong Kong we have a couple of big ones, that's where you should look at.

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Marcin Wojtal, Bank of America Merrill Lynch

Could you please clarify a little bit your comment regarding reaching industry standard margins, in particular in the Construction sector? What do you consider to be standard margins with that mix of geographies that you have?

And then when you say that will be reached in the next 24 months, do you mean you will be there in 2017 or it's more 2018, if you could give some clarity on that?

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Leo Quinn, Chief Executive Officer
Before that I'll just give a little bit of a preamble which is quite interesting, because I think the expectations on margins are changing as well. The historical model of Construction, the business model, was that effectively you would start a job and you would get a large mobilisation payment and you'd sort of earn 5% on your money in the bank and you'd earn 2% on your construction business, and so you'd make more money with the money you have on deposit than you actually would make from running the business.

Unfortunately that's all changed because with low interest rates there's no return on cash. So I do encourage my customers to be aware of this and to pay us even sooner and faster because they can't get any interest on the money either.

In terms of margins, let's just run around the world. UK, very clear, 2% to 3% is the market number and I've said this before. In the US where we do offer a managed service so we're not the constructor per se, we're the manager of the construction, and that's typically a business that, you know, a really good year you'd do 2%, in a more normal year you'd sort of do 1.5%. And that's where we should be operating. And the new incentive scheme in the US is designed around getting them to perform at those sorts of levels, and if they fall below that then there's very little incentive payout. So I'm sure that will see a remarkable improvement in behaviour around bid margins. In the case of Hong Kong 2% is sort of - 2% to 3% in the case of Hong Kong.

And in terms of timing, obviously 24 months takes us to the end of 2016 and I think I would like to be at a run rate of industry standard margins by the end of 2017. And so therefore '18 would be a good year for us. Beyond that, you know I've said it before and I say it internally, we are the largest market player. You know why we aren't garnering returns which are commensurate with our scale is a challenge that we're taking on board internally to see how we can do it.

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James, JP Morgan
Just picking up that point on your margin recovery and trying to get to the industry standard, you talked a little bit about the margin on new work coming through. Is that sort of consistent and how do you recognise that as that moves through, is that giving you confidence that you can get to that industry standard by the run rate 2017?

And then just on the Middle East, you talked about the conditions there being very challenging, you sort of alluded to that being more due to competition. Are you seeing anything in terms of the market environment given the lower oil price?

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Leo Quinn, Chief Executive Officer
Right okay, let's just take the first one. You know we have set thresholds within the company as to the margins that we want to bid at and those have risen substantially in the last 12 months. So the examples I gave are real live examples of how that's sort of coming into effect. We are bidding and we're achieving those new margins, but we have an order book to trade through, so you know I see nothing at this moment in time that tells me we shouldn't get there. Now you have to remember the industry is full of surprises. You know good surprises, and we've had some of those, and bad surprises. So you are managing and running the business within those parallel lines. So we are performing at a higher book margin and - but that's still has to be proven. You've got to deliver at that margin.

In terms of the Middle East, the signs we're seeing there's a lot of demand out there. I think it just comes with a lot of contracting risk. And if you look at the write offs in the Middle East in the last couple of years which is really the legacy of the last five years, those are very big numbers. I don't see things changing in a way that would give me confidence that we're bidding at cost plus or different forms of contract. So you know in our M&E side we would certainly want to see our exposure being reduced dramatically in the Middle East because we're only losing money at it at the moment.

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James, JP Morgan
Just a follow up on the dividend you talked about for the interim 2016, what will factor into your mind about your thinking about that? Is that going to be a level of EPS cover or cash flow, how should we think about that?

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Leo Quinn, Chief Executive Officer
It's a decision for the Board but it will be cash flow. And confidence in a forward order book. You know we're no different to you, we're pragmatic business people. If it's something that we think is sustainable and affordable we'll be very enthusiastic about it. If we're worried about it we'll say now is not the right time. We'll only make a decision based on the facts we have in front of us at the time.

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James, JP Morgan
Thank you.

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Leo Quinn, Chief Executive Officer
Well on that note it looks like there's no more questions. Can I thank you for your continuing support, much appreciated, and look forward to working with you this year. Bye-bye.

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