Media release

Tuesday 26th September, 2017
For immediate release

ANNOUNCEMENT OF RESULTS FOR THE FULL YEAR ENDED 30 JUNE 2017 AND RESIGNATION OF CHIEF EXECUTIVE OFFICER

Salient features

- Net loss of R6,7 billion and headline loss of R6,4 billion
- Non-cash impairments and write-downs on long-outstanding uncertified revenue of R5,9 billion
- Headline loss of R630 million excluding non-recurring write-downs and charges
- Queensland Curtis Liquefied Natural Gas Pipeline Project (“QCLNG”) award of R508 million (AUD50,5 million)
- Fixed overhead expenses reduced by R503 million or 18%
- Unacceptable operating performance, hence operational intervention
- Net asset value (“NAV”) of R14,56 per share
- Contracting business’ order book for FY18 100% secured
- Agreement reached with major funding banks to renew and extend facilities
- Mr Kobus Verster has resigned as Chief Executive Officer with immediate effect and Mr Eric Diack will assume duties of Chief Executive Officer and Executive Chairman

Johannesburg, 26 September 2017: Aveng announced its annual financial results for the year ending 30 June 2017. It further announced the resignation of Kobus Verster as Chief Executive Officer and Executive Director with immediate effect. Eric Diack, current Executive Chairman, will assume the duties of CEO until such time as a new CEO has been appointed.

The company reported a headline loss of R6,4 billion and a net loss of R6,7 billion. This loss included impairments and write-downs of long-outstanding uncertified revenue of R5,1 billion, and resultant deferred tax asset write-downs of R531 million.

“During the year to 30 June 2017, Aveng reported a headline loss of R6,4 billion (2016: R299 million loss) attributable to a number of detrimental events,” said Aveng’s Executive Chairman, Eric Diack.

“During the first half of the year, arbitration rulings for the Kenmare Resources and Mokolo Water Augmentation contracts resulted in awards well below our expectation. This together with a highly litigious environment precipitated a review of long-outstanding uncertified revenue. In addition, subsequent to the year-end, the long-running dispute with the Queensland Curtis Liquefied Natural Gas (QCLNG) pipeline project, which McConnell Dowell executed with a joint venture partner, were concluded, resulting in an award of AUD50,5 million (R508 million). This was substantially lower than the value of our claims. The Board decided to write-down a non-cash amount of R5,1 billion in uncertified revenue (R2,4 billion of which relates to the QCLNG award)and various other impairments which have resulted in derisking of our balance sheet. The change of approach has resulted in six major commercial settlements and arbitration awards being concluded, resulting in positive cash inflows and further reducing uncertainty.”

The decline in performance was partially offset by improved performance at Aveng Mining’s open cut division, largely due to better commodity prices that resulted in new contracts as well as existing clients increasing volumes.

Furthermore, Group overheads were significantly reduced by 18% overall. “This decrease is the determined result of the Group’s strategic interventions over the last few years, which include improved cost management within most operating units,” said Diack.

Despite a very difficult past year, the Group’s outlook and prospects for next year are more encouraging. The Group’s two-year order book amounted to R29,9 billion at 30 June 2017, increasing by 8% from the R27,7 billion reported at 31 December 2016. This includes a 1% increase in AUD terms in McConnell Dowell’s book, translating into a 3% increase in Rand terms. The Aveng Mining order book increased by a significant 29% or R1,7 billion, in line with increased activity in the commodities sector. Aveng Grinaker-LTA’s order book increased by 2%.

The geographic split of the order book at 30 June 2017 was 51% Australasia and Asia (December 2016: 53%), 41% South Africa (December 2016: 41%) and 8% other (December 2016: 6%).

“Securing quality work at targeted margins remains a key priority,” said Diack.

A number of new projects were awarded in the period under review:

- Aveng Grinaker-LTA has been awarded various mechanical & electrical maintenance contracts, Mtentu bridge in the Eastern Cape, Pampoennek road project in Northwest, and the Fincorp office development in Mbabane, Swaziland
- McConnell Dowell was awarded the Dryandra Road in Australia, the Amrun Export Facility in Australia, the Murray Basin Rail upgrade also in Australia, the Tangguh LNG Export Facility in New Zealand, and the U2 on Waymouth development in Australia
- Aveng Mining was contracted to the Karowe (Botswana) and Gamsberg (South Africa) mines.

Liquidity

Post-year end, the proceeds from the QCLNG award improved the Group’s net cash position by R508 million. This award and the write-downs remove significant risk and uncertainty from the Group’s balance sheet. The NAV of the business is now R14,56 per share after recognising the various write-downs and impairments.

Subsequent to the year end, and following the reported outcome of the QCLNG award, the Group engaged with its major funding banks who currently provide various facilities under existing agreements. This engagement resulted in the conclusion of an overarching term sheet, renewing and extending these facilities.

Following the QCLNG award and the re-evaluation of the long-outstanding uncertified revenue, the Group executed a recapitalisation and working capital injection into its Australian-based operating subsidiaries through McConnell Dowell. The purpose of the plan is to ensure an adequate capital base and working capital.

On 12 December 2016, Aveng successfully disposed of Steelmetals’ N3TC equity interest for a purchase price of R195 million. On 6 February 2017, the conditions precedent were fulfilled in respect of the Blue Falcon equity interest and the Windfall equity interest. R600 million from these disposals was received on 13 February 2017. A total amount of R821 million was received in respect of the sale of these assets.

Furthermore, the long outstanding dispute between Genrec Engineering (Pty) Limited (“Genrec”) and the Aveng Steel Fabrication division, and which relates to Aveng’s entitlement to compensation as determined by an arbitration award in August 2014, the Dispute Adjudication Board (“DAB”) ordered Genrec to pay to Aveng the sum of R123 million; and in addition, to pay interest on such sum at the simple interest rate of 15.5% from 1 September 2011 to date of payment. The DAB is currently curing calculation errors in its award, which amended award has not yet been delivered to the parties. The parties have agreed that the final value of the Award is R124 million (excluding interest). In terms of the initial award, the total cash award payable to Aveng is R238 million. Genrec is obliged to promptly give effect to the terms of the award and make payment. The award will remain binding unless and until overturned by way of an arbitration process which may follow.

Strategic review

The Board has initiated a robust strategic review, in conjunction with an independent advisor, to evaluate Aveng's financial and operational structure. The objective is to determine the key requirements to ensure the Group's medium-and long-term sustainability. The review will identify the core operating businesses and assets that will be part of the Group's long term strategy.

"The review will include the development of a sustainable capital and funding model, which will address the future funding of McConnell Dowell and the Group's convertible bond which matures in July 2019. The review will be completed by 30 November, after which I will communicate its outcomes. Non-core assets have been identified for disposal and proceeds will be earmarked for the reduction of debt or the creation of additional liquidity headroom," commented Diack.

Remedial actions to date

"Aveng continuously assesses its recognised uncertified revenue. This review resulted in a significant write-down, which has derisked the Group's balance sheet. The Group has further enhanced its internal controls regarding the recognition of uncertified revenue and renewed its focus on cash flow and performance monitoring across the Group," continued, Diack.

Furthermore, taking the current economic environment into account the Group overheads were significantly down-sized to reflect the current operating environment. The Profit Improvement Programme initiated at Aveng Manufacturing, during the second half of the 2017 financial year, is expected to yield results in the next financial year.

The McConnell Dowell organisational reset has been completed and is now moving towards a stabilised operation preparing for growth. This reset process has resulted in a simplified organisation with new operating model, empowering its business units, strengthening the technical and operational capabilities, improved project and business governance, enhanced its efficiency and client focus, and refreshed the executive leadership of the business.

Eric Diack was appointed as Executive Chairman on 23 August 2017 and served on the Aveng Board since 2012. Eric's extensive commercial experience will support the management team as it enhances its strategy to enable the company to realise its significant underlying value.

Operational review

There is an enhanced focus on cash flow and performance monitoring across the Group. An operational review will be commenced immediately, focussed on Aveng Manufacturing and Aveng Grinaker-LTA.

At Aveng Manufacturing, over the course of the last year, the top management of this business has been enhanced and strengthened. The Profit Improvement Plan was commissioned and commenced and executive focus is now required on unlocking the identified benefits. This programme is focussed on markets, procurement, production efficiency and the rationalisation of production capacity in line with market demand. The targeted improvements will be quantified and reported on by half-year.

Aveng Grinaker-LTA, the appointment of a managing director is a priority and a search is currently underway. An appointment is expected to be made early in the new calendar year. In the interim the organisational design will be reviewed in order to achieve an efficient and effective operating structure. In addition, a comprehensive review of major Civil Engineering projects will be conducted and the Building and Coastal divisions will be subject to a margin enhancement intervention. The Mechanical & Electrical, Aveng Water and Aveng Rand Road divisions are performing according to plan. The results of these interventions will be fully reported by half-year.

Market review

The South African infrastructure market remains subdued, reflecting the marginal economic growth experienced in the country. Aveng Grinaker-LTA continues to operate in a tough market environment with its financial performance adversely affected by low revenue and continued underperformance in project execution, mainly in the civil engineering division. Despite current building projects under construction, it is expected that building activity will reduce and shift to demand in healthcare, student accommodation and other smaller projects. The civil engineering industry remains competitive, with limited new opportunities coming to market. Road rehabilitation work remains dominant. Current public infrastructure spend is focussed on the transportation, energy and water segments.

The pace of expansion in the Australia and Asia Pacific construction industry steadied over the past 12 months, however, the Australian construction industry is expected to grow at a steady rate over the next five years. Despite the limited growth in the mining and energy sectors, the outlook remains positive. The growth will largely be driven by significant private and public sector investments in road, rail and power infrastructure projects. The Australian building industry remains robust with spending set to expand on affordable housing programmes and commercial projects. The growth in Southeast Asia remains very healthy and driven by investments in infrastructure, water utilities and energy projects. In addition, the market in New Zealand continues to gain momentum, with government investment in large-scale transport and water projects which will continue to fuel growth for the region and expansion of the construction industry.

The mining industry in South Africa and globally is cautiously optimistic with mining companies looking to increase output and make new investments in assets. The current rally in commodity prices provides opportunities for the Aveng Mining operating group.

The South African manufacturing industry is experiencing some headwinds due to weak economic activities and difficult trading conditions. The sector had a negative annual growth over the past 12 months and it is not expected to improve in the short term. However, having access to a diverse product portfolio with multiple manufacturing facilities and the ability to access markets in various geographies, provides an opportunity to improve the overall performance of the Aveng Manufacturing business.

The economic environment facing the steel industry continues to be challenging. Oversupply continues to weigh on the steel sector. The improvements experienced in the current year were mainly due to the increase in raw material prices and increased protection measures rather than any significant improvement in the demand of steel. The recently announced safeguard duties on imports of certain steel products will improve the local market and should benefit the Aveng Steel operating group during the next financial year.

Outlook and prospects

The markets serviced by McConnell Dowell are expected to offer growth opportunities over the medium-term. In Australia, the continued roll-out of large- and medium-sized projects in the major cities is set to continue. In Southeast Asia, opportunities exist in infrastructure in Singapore, Malaysia, Thailand and the Philippines. Government investment in large scale transport and water projects will fuel growth in New Zealand.

Domestically the outlook for the infrastructure market remains subdued with limited visibility on large scale projects. The muted outlook is expected to extend into the manufacturing sector. However, there are opportunities to increase the penetration into selected international markets.

The local construction and manufacturing businesses will remain focussed on improving financial performance in what is expected to be a continuingly difficult market environment.

The improved contract mining environment and some notable contract wins place the operating group in a strong position to pursue its longer-term growth strategy in selected markets.

Furthermore, the focus will remain on optimisation efforts in Aveng Steel to deliver a break-even result in the current depressed market conditions, which are expected to persist.

The immediate priority for the Group will be the completion of the strategic and operational reviews.   Non-core assets have been identified and a disposal process has begun.

The improvement of liquidity headroom will remain a key focus in the immediate term.

"Aveng commences the 2018 financial year with a more certain financial position and a stronger two-year order book of R29,9 billion at 30 June 2017, with 100% of revenue secured for 2018," concluded Diack.

The Aveng Board and executive management teams are determined to realise the Group's potential and deliver value for all of our stakeholders.