SGH | Industrial Services, Media, Energy and Investments

Results Release – Half-Year Ended 31 December 2016

Slide 1 – Ryan Stokes

Opening Slide

Good morning.

Welcome to the SGH results release for the half-year ended 31 December 2016. I am Ryan Stokes, CEO and Managing Director. With me today is Richard Richards, our Chief Financial Officer.

Slide 2 – Ryan Stokes

Disclaimer

This is our standard disclaimer. On to slide 3.

Slide 3 – Ryan Stokes

Group Overview: Our Businesses

This table provides an overview of our businesses and their strategic positioning and some perspective to the component parts of SGH.

The Group has diverse interests across a few key sectors. We're pleased to say that many of our businesses, including WesTrac, Coates, and Seven West Media, are the market leaders within their respective areas.

More on this later as we go through the operational reviews.

Slide 4 – Ryan Stokes

Group Overview: People

We focus on safety at all levels of our organisation and we are driving our safety culture through leadership and special initiatives, such as the Take 5 Program in WesTrac and Coates.

Our aim is to make sure that everyone goes home safely every day. The statistics here show that we are continuing to improve across all of our businesses, with the exception of Allight, where there has been a significant reduction in hours worked which impacted the measure.

Our company culture is one of the three pillars of our strategy and is a key focus for SGH. Work ethic, safety, efficiency and employee engagement across all of our operating companies is important to us.

Slide 5 – Ryan Stokes

Group Overview: Highlights

We achieved an underlying EBIT of $176 million for the half-year, which is up 5 per cent on the prior comparative period and ahead of earlier expectations. The Group posted a statutory net loss of $41 million for the half after taking into account the non-cash impairment of Seven West Media.

The underlying profit result reflects the recovery in Coates performance, the strong performance of the equity accounted interest in Beach, and the mining production cycle as fleets age and customers continue to manage operating costs effectively. We are seeing the aging fleets start to require component exchanges. Whilst intervals were extended there is increasing demand for maintenance support. Our focus on cost management continues and our businesses are well placed to benefit from an improved operating environment.

While the segment result for WesTrac Australia is down, there has been a 10 percent increase in product support sales in WesTrac. This mainly relates to a strong parts performance with opportunities to capitalise on the related service demand. We are expecting this activity to continue.

We are pleased with the performance of WesTrac China and Coates Hire, which posted improvements in underlying earnings of 83 per cent and 40 per cent, respectively. There was solid momentum provided by infrastructure demand in Australia and some encouraging signs in the Chinese excavator market.

No ordinary or TELYS4 shares were bought back in the period. However, the Group is prepared to take advantage of any opportunities to enhance shareholder value and we have therefore refreshed the ordinary share buy-back for another 12 months.

Today we have declared an interim fully-franked ordinary dividend of 20 cents per share, which has remained constant since 2013. The dividend reflects our confidence in the strong free cash flow of the Group and the strength of the balance sheet with ample liquidity and undrawn facilities.

Slide 6 – Ryan Stokes

Market: Economic Backdrop

As I alluded to earlier, the market drivers are improving for our industrial services businesses. Iron ore and thermal coal volumes and prices have increased significantly over the last six months. At the same time, NSW and Victoria continue to benefit from major new infrastructure projects with peak spending anticipated to occur over the next three years.

We are well positioned to take advantage of the continued rebound in the resource cycle and infrastructure activity.

Similarly, oil and gas prices have recovered over the last six months which is positive for our energy assets, especially those that are leveraged to the east coast gas market where there is limited availability of uncontracted gas.

In media, we are also seeing more encouraging signs for the free to air advertising market and we hope this continues.

Slide 7 – Ryan Stokes

Group Overview: Key Financials

Underlying EBIT for the period was $176 million and up 5 per cent for the half. Underlying net profit after tax was down 7 per cent to $104 million. This is due to an increase in the effective tax rate in the period. Underlying earnings per share was 32 cents. The interim dividend represents a 62 per cent payout ratio on underlying earnings.

The statutory net loss after tax for the period of $41 million primarily reflects the impact of $166 million in non-cash impairment provisions for the Group's investment in Seven West Media. It is included in the $145 million in significant items that form the bridge to the Group's underlying result.

I will now hand over to Richard to take you through the Group's financials for the period.

Slide 8 – Richard Richards

Financials: Profit and Loss

Thanks, Ryan, and good morning.

Slide 8 provides a summary of both the statutory and underlying net profit after tax for the period and I refer you to the Financial Statements within the Appendix 4D for the detailed statutory presentation and reconciliation of Significant Items.

Underlying EBIT of $176 million was up 5 per cent on the prior corresponding half. This reflects the strength of our industrial services business through the cycle, coupled with a higher contribution from our investment in Beach Energy.

Consolidated revenue was down by 5 per cent to $1.3 billion. Pleasingly, product support revenue of $902 million was up by 11 per cent which includes the sale of parts which grew 14 per cent, reflecting escalating component maintenance on an aging mining fleet.

Product sales revenue of $412 million was down by 25 per cent, due to lower sales of mining equipment reflecting the impact of the Roy Hill deliveries in the prior corresponding half. However, there was growth in equipment sales to the construction sector in Australia and a notable recovery in hydraulic excavator sales in China.

Ryan will discuss each segment's specific financial result later in his presentation.

Other income reduced, principally as a result of foreign exchange gains of $9.4 million that were included in the prior corresponding half. The share of results from equity accounted investees improved, with contributions from Beach Energy up by $19 million and Coates Hire up by $10 million, partially offset by a $19 million decline in the Seven West Media contribution.

Expenses, excluding depreciation and amortisation, reduced by $78 million, reflecting the ongoing work being done across our businesses to optimise costs. Cost of sales reduced by $59 million, employee benefits expense reduced by $8 million and operating lease rental also reduced by $4 million.

Depreciation and amortisation decreased by 19 per cent, or $4 million reflecting the benefits of WesTrac's disciplined capital investment over the past three years and lower reservoir depletion recognised within our energy assets.

Net financing costs decreased by $1 million reflecting lower borrowing rates on renegotiated facilities partially offset by increased drawn debt. Excluded from this is interest income of $5 million related to legal judgement reached during the period which has been treated as a Significant Item.

The Group's underlying effective tax rate was 22 per cent, lower than the prevailing corporate tax rate reflecting the proportion of franked dividends within underlying income. It was however higher than the 10 per cent rate in the prior corresponding year which included the recognition of tax free property gains.

Slide 9 – Richard Richards

Financials: Significant Items

Consistent with prior years, Significant Items reflect potentially non-recurrent items that arose during the year. These items totalled $145 million after tax and reduced the underlying net profit after tax of $104 million to a net loss after tax of $41 million on a statutory basis.

Significant Items primarily related to a $140 million impairment of our investment in Seven West Media, based on the adverse share price movement during the period, along with recognition of our $33 million share of Seven West Media's impairment of its Yahoo!7 investment.

The share of equity accounted investee's significant items also included $6 million referable to redundancy and restructuring costs in Coates Hire, offset by $19 million referable to the gain on sale of the REVY buildings at Jones Bay Wharf, and $10 million referable to the gain on sale of Beach Energy's Egyptian Assets.

Other redundancy and restructuring costs within the Group totalled $5 million; net gain on sale of investments totalled $2 million; net derivative mark-to-market movements totalled $1 million; and other items relate primarily to favourable legal judgement totalled $2 million.

Significant items also included the previously mentioned interest income of $5 million and a tax benefit of $3 million. It should be noted that $45 million in deferred tax referable to the Seven West Media impairment was not recognised, as it did not satisfy relevant accounting requirements.

Slide 10 – Richard Richards

Financials: Earnings Summary

Slide 10 details the underlying EBIT result across each segment, providing reconciliation to Statutory EBIT with an allocation of the significant items from Slide 9.

Slide 11 – Richard Richards

Financials: Cash Flow

Operating cash flow for the Group was $93 million representing an underlying EBITDA cash conversion ratio of 48 per cent. This is lower than we have seen in recent periods, predominantly as a result of parts inventory investment in WesTrac Australia and new equipment inventory in WesTrac China, reflecting strengthening underlying demand in both businesses. Earnings in the half-year also included a higher proportion of non-cash profits referable to equity accounted investments with no corresponding cash flows.

We expect operating cash flow to be stronger in the second half as we realise the benefits of the inventory investments made in the first half.

Cash flow from investing activities provided $9 million, including $33 million in net sales from the listed investment portfolio, partially offset by $17 million in capital expenditure and $7 million in other investments and derivatives.

Cash flow from financing activities consumed $144 million, comprising $69 million in ordinary and TELYS4 dividends paid and $75 million in net repayment of borrowings.

The Group finished the half with cash and cash equivalents of $295 million, down $77 million during the period. Net debt, after taking into account foreign exchange movements, increased by $21 million to $1.39 billion.

Slide 12 – Richard Richards

Financials: Balance Sheet

A summary consolidated balance sheet is detailed on slide 12.

The Group's net assets decreased by $193 million to $2.5 billion predominantly due to unfavourable movements in the carrying value of investments including Seven West Media.

Trade and other receivables were relatively flat with improvements in AR being offset by increases in promissory notes in China. Inventory increased by $29 million of which $37 million was parts offset by a $10 million reduction in new equipment. In China, the inventory investment primarily related to new equipment for delivery on specific projects in the second-half.

The value of investments and other financial assets reduced by $198 million. Included in this figure is a $158 million reduction in the carrying value of the Seven West Media investment, unrealised mark-to-market losses on the listed investment portfolio of $46 million and $33 million in net sales from the portfolio. It should be noted that the investment in Beach Energy was required to be reclassified from a Financial Asset to an Equity Accounted Investment on obtaining Significant Influence when Ryan was appointed to the Board of Beach.

Property, plant and equipment reduced by $7 million, mainly relating to a reduction in workshop plant and tooling in WesTrac.

The $7 million increase in intangible assets primarily related to a favourable foreign exchange revaluation gain referable to the WesTrac China distribution network.

Trade and other payables increased by $37 million mainly in WesTrac Australia and China relating to increased parts and machines acquired in December.

Deferred income decreased by $58 million referable to the termination of MARC contracts and reduced customer slot fees deposits.

Net tax liabilities have decreased by $3 million which excludes the deferred tax impact on the reduction in carrying value of Seven West Media.

The $57 million decrease in net derivative financial instruments principally relates to a reclassification from the fair value reserve in relation to USPP cross-currency hedges with the hedging no longer satisfying the cash flow hedge requirements and thus the debt is held at amortised costs not fair value.

Slide 13 – Richard Richards

Financials: Debt Maturity Profile

Slide 13 presents our debt maturity profile which demonstrates a strong and diversified funding base available to the Group. At 31 December 2016, the Group held $2.5 billion in total facilities with $924 million currently available to be drawn and $295 million in available cash.

Our facilities provide an average tenor of 3.7 years on a weighted basis while the drawn component of our debt has an average maturity of 5.1 years. The relative difference reflects the long-term funding provided by the USPP notes which have maturities extending to 2041. The fixed proportion of debt is currently 58 per cent.

Short-term facilities relate to OEM financing and China facilities which are largely undrawn and are reported as current and have historically been renewed on a consistent basis.

In terms of current debt, $80 million relates to OEM financing with a three year $30 million bank loan in China set to mature in the second half. These repayments will be financed out of existing cash reserves.

The large undrawn facilities, cash reserves and the value of the listed investment portfolio have provided the Group with significant liquidity and balance sheet flexibility to be resilient in the face of challenging market conditions in recent years.

The Group's leverage is effectively 36 per cent after adjusting for debt related derivatives or 22 per cent when further adjusting for the value of the listed investment portfolio.

Slide 14 – Richard Richards

Financials: Capital Management

The Group has declared an unchanged fully franked interim dividend of 20 cents per share, in line with the policy of maintaining the dividend through the cycle. The dividend represents a payout ratio of 62 per cent of underlying earnings and provides a pre-tax yield of 6.0 per cent calculated on yesterday's closing share price of $9.57.

While we did not buy back any ordinary or TELYS4 shares during the half, the Group is willing to take advantage of any future market dislocations in order to enhance shareholder value. We have therefore announced today an extension of the ordinary share buy-back for a further 12 months.

Now I'll hand you back to Ryan who will provide a more detailed review of the operating performance of our businesses.

Slide 16 – Ryan Stokes

WesTrac Australia Overview

Thank you, Richard.

On to slide 16: the WesTrac Australia overview. The result is down on the prior comparative period, which we are expecting to recover in the second half. The continued focus on costs, along with realising the opportunity available, is a focus for SGH and WesTrac management. We are particularly focused on improving our result in New South Wales.

Australian iron ore and coal export volumes continue to grow, as shown in the earlier slides. Both aspects are relevant for our Western Australian and New South Wales territories operated by WesTrac.

This presents a number of opportunities for WesTrac – the deferral of replacement expenditure together with increased fleet usage requires ongoing maintenance support in the form of parts and service, along with more component exchange activity. The increased production volumes will eventually require further mine investment and development to address aspects, such as aging fleets and increased overburden removal. Higher commodity prices will provide increased support for this investment.

The numbers on this slide show that the average age of the utilised mining fleet continues to increase, and is now just over 8 years. Resource companies have been very effective at managing costs and capex.

As fleets age, this will require the review of fleet profiles and we anticipate the replacement process will eventually occur. The technology of Autonomous Haulage and product quality of CAT ensures we're well positioned for that next stage. However, at this point our focus remains on securing the immediate product support, particularly service work that underpins our customers increased productivity levels.

Slide 17 – Ryan Stokes

WesTrac Australia Case Studies

I want to mention two good examples where WesTrac's value proposition has played an important role in helping mining organisations achieve some of the world's lowest unit production costs.

WesTrac's team on the maintenance contract at one of our customer's sites has helped transform the way truck maintenance is delivered. Offering an in-pit maintenance service has eliminated transit times to the workshop and significantly reduced the time required to perform regular maintenance checks. The result has been better fuel consumption, less downtime and greater utilisation.

A second example has seen a 20 per cent productivity improvement with the autonomous haulage solution, which has moved over 200 million tonnes of material to date. This 20 per cent efficiency improvement would not have been possible with a regular fleet. This productivity gain, along with autonomous haulage, aided in the customer's reduction in C1 production costs by 43 per cent.

Our objective is to work closely with our customers and continue to offer them the best support in the market. We want to convert these activities and support to the delivery of financial results for WesTrac.

Slide 18 – Ryan Stokes

WesTrac Australia Results

WesTrac Australia posted EBIT of $75 million, $10 million below the $85 million EBIT of the prior comparative period. Trading revenue was 4 per cent down, with a 32 per cent decrease in product sales partially offset by a 10 per cent increase in product support revenue.

The decrease in product sales is due to declines in mining equipment sales partly as a result of the deliveries for the Roy Hill project in the prior comparative period. However, construction equipment sales grew during this period as we support the level of infrastructure activity.

The increase in product support revenue was driven by improvements in parts sales, which were up 14 per cent in the last six months. WesTrac has invested in parts inventory to ensure that we continue to capture these opportunities in the second half.

The decline in trading revenue resulted in a decline in the EBIT margin, despite the benefits of the restructuring and cost reduction initiatives of prior periods. This is pronounced in the interim results and we are implementing activities to address this in the full year. In addition we continue to further refine our cost base to match market demand, with a particular focus in the New South Wales business.

Slide 20 – Ryan Stokes

WesTrac China Results

WesTrac China's EBIT of US$13 million represented a 72 per cent increase on the prior comparative period. While there was a slight decline in overall trading revenue for the six months, there was a change in product sales mix, with an increase in higher margin excavator sales offset by a decline in lower margin engine sales.

The improved market for hydraulic excavators reflects increased infrastructure activity in our territories. This is the first time in many years we have seen growth in this market.

Notwithstanding the decline in product service revenue of 8 per cent, WesTrac China recorded a solid EBIT result with an improvement in EBIT margin from 4.2 per cent to 7.4 per cent. This result reflects the significant cost reductions carried out over the last couple of years, together with improved market conditions for mining and infrastructure. The business is positioned to perform through the cycle.

Slide 22 – Ryan Stokes

Coates Hire Results

Coates Hire continues to be Australia's market leading equipment hire company, with a focus on the construction and infrastructure sectors. Last year Coates executed a strategic relocation of fleet from WA to NSW to take advantage of the buoyant east coast infrastructure market.

Coates has had a dual focus on cost control, as evidenced by the 290 FTE headcount reduction over the prior comparative period, and improving price realisation. This is reflected in the improved EBIT result of $74 million, up 40 per cent on the prior comparative six months, and the 4 per cent improvement in EBIT margin to 16 per cent.

With new management in place the company is performing well, but still requires more work and ongoing focus on streamlining of costs to improve performance. Debt management has also been a keen focus with net debt reduced by approximately $100m over the past 12 months.

Slide 24 – Ryan Stokes

Media Investments Results

The reduced contribution to SGH Group NPAT from SWM of $38.5 million follows the guidance SWM provided at their AGM and is down 33 per cent on the prior period. This result follows the soft metro television advertising revenue market and additional costs associated with large contract events.

This six month period saw continued leadership in TV with Seven ranked Number 1 in rating and revenue share in a metro advertising market which reduced by 4.5 per cent. It is the 21st consecutive half year period of ratings leadership.

The operating model continues to evolve with multi-platform delivery of major content including the Rio Olympics, AFL, 7Tennis and key programming.

SWM has maintained its full year guidance, based on current visibility, of underlying FY17 EBIT down 20 per cent on the previous year. Encouragingly, the team are seeing a stronger advertising market for free-to-air TV in February and March as the market moves longer.

Seven West has a strong balance sheet with net debt of $681 million and a net debt to EBITDA ratio of 2.2x.

Slide 25 – Ryan Stokes

SWM Strategy

SWM continues to evolve its operating model and is now the largest production company in Australia with increased program sales to the US and UK. SWM produces over 850 hours of content across multiple genres each year. The company predicts the

EBITDA from program sales and third party commissions will be greater than 20 per cent of television earnings by the end of FY17.

Free to air TV remains the media platform with the greatest audience reach. Independent studies reflect the ROI of advertising spend across different media, resulting in some advertisers, particularly in FMCG, increasing their television advertising budget with SWM.

Media reform is an increasingly important and urgent initiative for the sector to ensure the industry can evolve and companies can remain competitive in the changing landscape. This includes significant licence fee relief and comprehensive reform of regulations.

Slide 27 – Ryan Stokes

Energy Results and Asset Overview

As highlighted earlier, the market dynamics are improving for our Energy business, with solid increases in oil and gas prices in the period. Beach Energy contributed $18.5 million in the half, driven by record production volumes and lower field operating costs.

As the largest onshore producer of oil in Australia, and the lowest cost operator in the Cooper Basin, Beach is well positioned to take advantage of the improved market.

During the period we also completed the offshore inspection and testing campaign at Longtom. As a result, we have approximately 20 PJ of gas from the Longtom 3 & 4 wells ready for production, subject to the availability of gas processing facilities.

In addition, there is the added potential for first gas from Longtom 5 in 12 to 18 months. This gives a combined opportunity to supply 80 PJ of uncontracted gas to Victorian and other East Coast gas users, who have approached us and are keen to secure supply in a tightening market.

Slide 29 – Ryan Stokes

Property and Listed Portfolios

Our listed investment portfolio provided the Group with $19 million in dividend income at a gross yield of 7.5 per cent in the period. In addition, the Group realised a gain of $19 million relating to the share of the REVY building in Pyrmont, which was included in significant items for the period.

The sale of sites at the old Seven Perth studios has been impacted by the slowdown in the Perth residential market with 28 lots sold to date. This has covered the development costs of Stage 1. The development of Stage 2 will be considered once we see a turnaround in this market.

The listed investment portfolio has performed well over the long term with $146 million of unrealised gains recognised in reserves. However during the period, the market value of the portfolio declined by $46 million leaving the portfolio with a market value of $543 million at 31 December 2016.

Slide 30 – Ryan Stokes

Outlook: Key Takeaways and Questions

In closing, I would like to emphasise some key takeaways:

We have a strong balance sheet with significant undrawn facilities and access to additional liquidity through the listed investment portfolio. Our confidence in the Group's continued free cash flow generation supports the unchanged dividend. We anticipate improved operating cashflow in the second half following the working capital investment made during the first six months.

The improved performance of Coates Hire and WesTrac China are expected to continue with further upside from growing infrastructure demand in their respective markets.

Our investment in Beach Energy provides opportunities for the Group to benefit from improved market conditions, with increased production at higher prices.

At WesTrac, while we are pleased with our parts performance, there are opportunities to deliver enhanced service solutions to support the productivity demands of a market benefiting from greater volumes at higher prices.

We anticipate that the improved market conditions, underpinned by increased iron ore and coal production, higher commodity prices and greater infrastructure activity, will continue into the second half.

On this basis we have raised our full year guidance that underlying EBIT will now be 5 to 10 per cent up on last year.

Thank you. We would be pleased to take your questions at this time.