# Balfour Beatty

Half-year Results Presentation

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## Balfour Beatty

Leo Quinn, Group Chief Executive

Phil Harrison, Chief Financial Officer

## Questions From

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## Introduction & Key Highlights

**Leo Quinn, Group Chief Executive**

Good morning everybody, thank you for coming and changing the venue at short notice, there is a bit of an echo in this room, but we'll make do with it.

Phil is going to take you through the numbers in the usual way so you'll hear those and I'll start off and just give you a sense of how things have changed in Balfour Beatty and just how different it is compared to two years ago.

First and foremost two years ago if you remember I think we delivered our 8th profit warning, we had 89 distressed projects, the company was in a bit of a crisis and we were on the edge of a sort of potential takeover bid from Carillion. You wouldn't identify or recognise just how different the company looks and feels internally today. And I think that's a real credit and a testament to our Build to Last programme.

You know we've simplified our organisation and I'll take you all the way back to remember we divested Parsons Brinkerhoff right at the beginning of my tenure. We have in the intervening period divested our entire interest in the Middle East, with no ongoing liability. The company is much more transparent in terms of how we work and how we go about business. And that all drives to the simplification that we have in the company.

We continue to focus on leadership; you know there are no comfortable corners. We have got a top team at the top of the company and in the level below the Ex Com in the last year we've upgraded six of our executives. So we're not stopping the momentum at all.

The area where we've made the biggest impact is really around short interval control, around governance of the company and our gated lifecycle process, our digital briefcase, our project on a page, all of these allow us to actually inspect what's going on, what we're bidding, what terms we're taking onboard, and really the risk that we're assuming. And all these things are driving a very different culture, a very different company, but they are all for nought unless we embed them into the values and the culture of the company. Because we talked about Build to Last and Build to Last is about how we create a foundation for the next hundred years. It's not a quick fix in terms of how do you deliver tomorrow's results, it's around how do we deliver a company that can deliver sustainable performance half in half out.

And we all know that people respect what you inspect, so we spend an awful lot of time rigorously, even boringly going through reviews, looking at numbers, looking at customers. It's around how do we ensure that we reinforce what are the behaviours and what are the things that you have to do around here in order to be successful. And that is going to be part of Balfour Beatty's long term transformation.

These are all very good things to say, but how do we actually know it's working, you know where's the proof in all of this? And if you actually look at the results that we've just announced, I mean first and foremost, you know, average net cash in the last period of £45m positive, if you compare that with a year ago, we were £65m negative, or £65m debt, that's in excess of £100m per month improvement in cash flow. That says something is going on, profits are now starting to turn to cash, and especially if you look at our working capital, I think we're about 13.1%, 13.2% of revenue and that's been consistent for the last three halves.

What's even more interesting in this, and I'll give you some great detail in my slides later, but the fact is there have been no material divestments in this, so this is really saying that the operations are actually delivering. And that to me gives me really great confidence.

If you look at the underlying profit of £39m, that's interesting - but the fact is we see the momentum in the business to carry on delivering into the full year in terms of expectations and we've got a target on delivering industry standard margins in the second half of 2018 and we're confident about that as well.

In terms of our chosen markets, if we look at how the sort of macro market is working, there is definitely a shift both in the United States and in the UK towards larger infrastructure projects. And if you go right back to where Balfour Beatty came from, you know we are an infrastructure company and therefore the confidence that I have in the markets is that we're sort of the largest company with the largest market share in the UK and we're on a rising tide; so I feel good about the outlook. And remember outlooks aren't six months or twelve months, I'm looking over the next five to ten years. This is a great place to be at this particular time.

And then finally all that confidence is really wrapped up in the fact that we're prepared to commit to a 33% increase in dividends and that's still going to be a progressive dividend going into the future.

So what I'll do is I'll now hand over to Phil and Phil will take you through some of the numbers and then when I return I'll take you through some of the really exciting things that are going on within the company, Phil.

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## Financial Review

**Phil Harrison, Chief Financial Officer**

Thanks Leo. If we go to financial highlights, in the first six months of the year the Group reported profit from operations of £39m and we're on track to deliver full year expectations. We have continued to build strong cash discipline and cost control across the Group. Net cash at the 30th of June was £161m with average net cash during the period at £45m.

Our cash position, coupled with the Directors' valuation of the investment portfolio, which now stands at £1.235bn emphasises the strength of Balfour Beatty's balance sheet.

All this gives the Board confidence to increase the dividend, a 33% increase on prior year and we continue to anticipate a progressive dividend policy going forward.

Moving to the next slide this is a summary of our half year numbers. The only thing I'd like to say on this is that our financial metrics are improving, driven by our focus on delivering on our Build to Last transformation and I'll go into more detail over the next few slides on how these numbers come together.

If we look at underlying profit from operations the Group reported an underlying profit from operations of £39m and here we show the breakdown. I'll look at each segment separately on the coming slides, but importantly there were material year on year improvements in each earning based business, with Support Services reporting profits in the range of industry standard margins and Construction Services reporting a profit which is a substantial improvement from prior year losses.

For our asset based business, Infrastructure Investments, the profit from operations was lower than the prior year, predominantly due to a reduction in profit on disposals. In March we highlighted that we did not expect material disposals in the first half of 2017 and this has been the case.

Overall good progress and the Group is confident of achieving industry standard margins in the second half of 2018 as we drive three key levers for improved financial performance; managing the remaining historical project base through to completion, reducing costs across the Group, and executing on the improved order book.

Now moving to the order book, as you'll see the order book was down 8% in the first six months of the year, 6% at constant exchange rate. Our focus continues to be the quality of the order book: higher margin and lower risk terms and conditions. The Construction order book decreased by 10% at constant exchange rate, due in part to phasing and lower orders in the US and Far East. We don't included preferred bidder or pipeline estimates in our numbers, so you will see some more timing variations on order book.

In the UK we saw a small decline; we continue to shift the mix of UK business to a lower risk contract portfolio, with a reduction in the number of fixed price contracts. The value of regional work won in the first half of 2017 from traditional fixed price contracts only accounted for around 30% of total orders, down from approximately 50% in 2016. This reduction has been offset by an increase in target cost contracts and framework agreements. These types of contracts have a better risk profile for the company.

In July 2017 we were very pleased that HS2 awarded Balfour Beatty's joint venture the maximum two sections of Phase One and this is characteristic of the strong pipeline of projects in the Group's key markets.

Turning to Support Services the order book was up 6% at £3.3bn, that's following the delivery of a number of successful projects, the Group has subsequently won more work in the period.

Now a slide on the financial performance of each segment, starting with Construction Services; the segment continued its financial recovery, with all geographies reporting profit from operations in the first half of the year. Underlying revenue increased by 12%, 4% at constant exchange rate, with growth in both the US and Far East.

As expected, underlying revenues in the UK fell by 2% as the improved bidding disciplines adopted in Build to Last resulted in lower levels of contracts in previous problem areas.

Looking at the US revenues, revenues increased by 7% in constant currency, the PFO margin at 0.9%, gives us confidence that we're well positioned to achieve our 1 to 2% target range for the full year.

UK Construction continues to make progress, reporting a profit from operations of £2m, the business is continuing to manage historical projects through to completion. At the half year 92% of the 89 historical contracts had reached practical completion with over 75% now at financial completion. Of the remaining seven ongoing projects, two are expected to reach financial completion in 2017, with the remainder in 2018.

In the Far East both revenues and profits were up at Gammon.

Now moving to Support Services, as expected revenues in the year were down 5% as an increase in utilities was more than offset by a decrease in transportation, reflecting lower volumes from local authorities. Profit rebounded to more normal levels compared to the first half of 2016, with underlying profit from operations of £16m.

In Support Services, the outlook for the power transmission and distribution market is positive, gas and water operates in a stable market as a cost plus business, with a fee on recovery. Water is in the middle of its asset management period, the AMP cycle, with the next round of new contracts to be awarded in 2020. Transportation, which includes road and rail maintenance contracts, is expected to remain stable.

Support Services reported a 3.1% PFO margin in the first six months of the year and we continue to expect the margin percentage to increase as power transmission and distribution profitability increases and the gas and water business benefits from the middle part of the AMP cycle.

If we turn to the Infrastructure Investments business, they had a relatively quiet six months with only one new project and one disposal in the period. From a financial perspective the key difference from prior year is the profit on disposal being lower by £52m. Operating profit was also down due to the prior year disposals. In March I highlighted that the Group was not expecting to make any material disposals and this has been the case in the year to date.

We continue to see opportunities to invest in attractive projects with good returns and we will sell investment asset at a time to maximise value to shareholders. For our asset based business valuation rather than earnings is the key metric.

Therefore turning to the Directors' valuation we can see that the overall value saw a small increase to £1.235bn in the period. The size of the portfolio was maintained at 69 projects, with the increase in valuation due to unwind of the discount and partially offset by negative exchange rate movements. The Group received £26m of distributions and the Group continued to invest in new projects, with £24m spent predominantly on two hospitals in Canada and a student accommodation project at the University of Texas.

In the second half we would expect to invest a further £10m to £15m into projects.

If we go to our half year cash flow - another very good cash performance from the Group, with average net cash of £45m in the first six months of 2017, compared to an average net debt of £68m in the first six months of 2016.

The Group had positive cash flows generated from operations of £7m in the first half, the £106m improvement compared to the first half of 2016 is primarily the result of the continuing recovery in profitability of the Group's earnings based businesses, specifically UK Construction.

The total cash movements in the period resulted in a reduction to the Group's net cash position as expected to £161m. Excluding non-recourse net borrowings, unlike previous periods there were no material investment disposals in the period.

Turning to working capital on the right hand side you can see the details behind an outflow of £9m. The increase in both trade payable and trade receivables is predominantly driven by the cash profiles of several large projects in the US, with a net effect being a cash outflow of £6m.

On our historical contract cash flows we outflowed £10m in the first half of the expected £50m that I talked about at full year. I still see the additional £40m outflowing over the second half. For full year we now see average net cash in the range of £25m to £50m.

I'll now turn to the balance sheet; most of the items such as cash and working capital have been covered in previous slides. As seen in the previous slide again there is less volatility across balance sheet items for this period.

It's worth remembering we hold the Investment assets on our balance sheet at book value, rather than the Directors' valuation. I think the one item to highlight on this slide is the net retirement benefit liabilities of £208m, which is £23m lower than the year end.

The decrease in pension deficit in the period is due to a small reduction in life expectancy based on the latest mortality studies, together with cash deficit payments made by the company, partially offset by a small reduction in corporate bond yields.

It is worth noting that the cash deficit payments of £10m were materially lower than the £29m in the first half of 2016 following the latest triennial funding agreement with the trustees of the Balfour Beatty pension fund. The full year pension deficits will be around £25m.

In conclusion, all businesses are making progress on profitability and we continue to maintain a strong balance sheet, underpinned with average net cash and an Investment portfolio of £1.2bn. I'll now hand you back to Leo.

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## Build to Last

**Leo Quinn, Group Chief Executive**

Thanks Phil. It is interesting looking at those numbers just what a clean set of financials they are and just how understandable they are. So that's a real credit to the progress that we're making.

Just to touch on Build to Last, I've given you the background to that but there are four main planks or tenants and that's Lean, Expert, Trusted and Safe and I'm just going to take you through what these actually mean and the progress that we're making, because this underpins everything that we're doing within the transformation.

This to me - if you stay awake for any slide this is the one to stay awake for. This actually to my mind really shows the progress that we've made. The one thing I'm adamant about is that cash doesn't lie. So if I can just avert your gaze to the 2014 pink line on there. That was the cash flow in that year and you can see in the first half it peaked at about £450m outflow and then proceeded to go downhill fast to peaking at nearly £600m of outflow in 12 months. I mean that's just a phenomenal pouring of cash.

If you look at the 2015/'16, which is the blue and the dotted green line what you can see is an improvement that was generated through better working capital management, cancellation of the dividend, sales of £300m odd worth of investment assets in order to shore up the losses. If you look at the yellow line which is 2017 you can see the substantial year over year improvement from about £150m to just over £300m so there is circa £250m to £300m of cash improvement in the first half. And that is actually with no material divestments in it at all, so that's like operating cash flow.

If I take that yellow line and project it through to the second half you're going to see a similar profile. If I then take you through to 2018 and you look at those two halves you're almost going to be flat lining on that and that just underpins the real progress we're making. So to my mind this is really exciting and demonstrates that we're actually delivering on all of the outputs that we've promised under Build to Last.

The other point I'd made here is that if you remember in Phase One, Lean was about £200m cash in £100m of cost out. We're still focused on taking cost out and in the first half we took about £18m of cost out, we're still targeting another £20m odd in the second half of the year. And that actually is around delayering, but it's primarily around just leaning out processes. As we start to actually make our R12 effective in the UK, as we put in a standard system right across the United States, what we're seeing is that all the costs, the extraneous costs and the manual efforts falls away from behind it.

So it's just a continual programme of leaning and that will go into 2018 as well. So, really, really strong progress in this area.

If I look at the area of Expert, you know forget the slide for two seconds, the only thing you need to think about is that Expert is around a market that we're about to head into which is going to be capacity constrained. Go back five years there was more capacity to deliver than there was demand, as I go forward for the next five and ten years there is more demand than the capable capacity can deliver.

So what we have been doing over the past two and a half years despite all the changes we've been making is we haven't compromised on our investment in terms of recruiting people, training people, and actually making sure that people are retained within the company. I do laugh sometimes at meetings when I have the senior managers; there is an awful lot of grey hair in the room, including my own. And I have a declaration about ensuring that all of our senior leaders have their hand on someone's shoulder and that they are actually training someone up to do their job. So we're not going to allow anybody in

Balfour Beatty to retire until they've brought through and trained a successor and passed on their skills and their expertise, which is quite disappointing because some people thought they could go at 60, not any more.

Really important here that we understand that the confidence that you see today in our numbers around Balfour Beatty is we're building a stronger brand, we've got upgraded leaders; you know at the end of the day people join companies and they leave leaders. What we're doing is constantly upgrading our leaders so that we've got the best and the brightest. And at the end of the day we want our leaders to be people that the people joining the company want to work for.

We're also finding that iconic projects are really important in attracting and retaining the best people. The news of HS2 was a great shot in the arm in terms of giving us courage and confidence that we've got the right capability, the right skills and we can deliver competitive bids into the market. And I'll explain that to you in a few minutes.

We're investing in people and capability, we talked about how we're upgrading our project managers, we're training all of our commercial people, we're also investing in our engineering. And all of this is delivering the results that you see on the left hand side where voluntary terminations have dropped from about 16% to just over 12%. And that is on a trend downwards, we've got far more engagement in the company.

So Expert is about recruiting, training and retaining the capability that we're going to need to deliver demand in the future. And it is going to be a market which is actually going to be capacity constrained.

If I also think about Expert, we're moving beyond the image of muddy boots. You know this is an industry which is incredibly professional and high tech - we just don't give it credit. And we've launched our Innovation 2050 paper where we talk about nobody on site, everything being done by robots. A little bit tongue in cheek there, but we have to have a vision in order to make these things happen. And if I think about a digital Balfour Beatty, the things that we're doing around BIM and 360, how that's driving efficiency and productivity on our sites and delivering the benefits. Things around virtual reality incorporated into safety exercises and the likes of this. 3D surveys and scanning, whereby we get better data, better baseline information.

All these things are sets of skills that don’t come in what we think of as a traditional normal engineer. And it's this image that actually is going to attract a very different set of people into the industry. The people that are coming through today, these digital warriors they are not built in the same way that I am. And we actually need them in order to take Balfour Beatty to the future. So we are putting a lot of emphasis in terms of getting this right.

Some of the stuff that some of our people are doing in data analytics is just astounding in terms of the insights and the transparency it's providing. We've got all the data we just haven't been using it, now we're using it to help us drive productivity.

In terms of Trusted, this is really around our governance and controls and how we ensure at the end of the day when we risk our capital we get and adequate return from it. And it's not complicated; it's really, really simple stuff. If I divert your gaze to the circles of risk on the left hand side, you know the single most important thing for us is do we have a matching - an alignment of behaviours in terms of the way we want to work and the way the customer wants to engage with us. So the single most important thing is, is the customer or the client somebody that we want to work for? And there are many customers that we do, we have a great history with, we know how they act and behave in good times and bad. And that is the core of Balfour Beatty and it's taken us tens of years to build that up.

So once we've decided on the customer it's a question of can we actually deliver the application. And then it's a question - do we have the internal resources and the team that knows how to deliver that job and that application. And then it's about the contract and is it in a geography that we can actually service. It's incredible when you look back over the learnings from the 89 legacy projects how many of them actually fail in two or three of these areas. It's all common sense, but believe you me, common sense goes out of the window when you're chasing a goal or an incentive. So our governance and control is very strict around this.

So we have established a very strong platform around how we manage risk in terms of the gated lifecycle, the digital briefcase, projects on a page, and that's actually being inculcated into our leadership behaviours. And we actually have cross divisional collaboration where other divisions review the bids that go out from other divisions in the company. And that is a real credit to our leadership.

Selective bidding I've talked about in terms of the margin and taking on the appropriate risk. It's really important that we ensure that the contract that we sign up to is something that we can engage in. If we do all of those things what we will do is successfully deliver on all of our promises.

Safety, I won't spend too much time on this to say without being safe we don't have a licence to operate. You know we have seen situations in the market where contracts have actually been denied or pulled because the safety record of the supplier is not adequate, so we have to take this very seriously. And by the way we should take it very seriously, it's important.

But the way I look at safety is it's just another indicator in terms of the transformation of the company. It's all well and good saying my numbers are going up, but if your numbers are going up and your safety is going down and your other indicators are going in the wrong direction you ultimately aren't going to end up with a successful business that's going to be here for the long term.

This demonstrates as you see on the left hand side how our LTIRs are actually reducing over time. And again they are still in my view too high; our goal is to get to zero harm. The number of observations that we're seeing, which is a measure of engagement is going up, which actually ties and correlates directly with safety instances. And around our initiative at the bottom here called 2025, that's to ensure that 25% of our onsite activities today are done offsite in the future. And again, what that leads to is actually a safer construction site, it leads to better productivity and it leads to better quality. So don't mistake safety as something that we're doing for safety's sake, it ties into every facet of how we run our business.

If I look at the market for a few seconds the thing I would say here is that there is really no change from what I presented six months ago and 12 months ago. If I look at the US you've still got the very large investment from the FAST Act, you've still got the California Education Bonds, you've got infrastructure bonds, now the states are now starting to levy a gasoline tax, which will add another $5bn to infrastructure spend.

It's quite interesting if you go back over the last ten years there has been a lack of expenditure in infrastructure in the United States. What that has led to is that the capability to deliver that infrastructure is actually at an all-time low. The fact that we've got a 700 million business that is actually equipped to deliver infrastructure and that we're bringing on joint venture partners says that we're in a very good place to take the right business at the right time on the right terms. So we're excited about the US.

In the UK again it's HS2, it's Heathrow, it's Highways England, and it's Hinkley and we're effectively a major supplier to all four of those customers. And it's only going to grow in those areas.

And in Hong Kong, even in the Hong Kong market we're seeing more investment in the airport and runways, we've seen a downturn in the last 12 to 24 months in the areas of infrastructure and civils, but that will come back once they start to get their act together through parliament.

So fundamentally a strong market and our growth is going to be limited by our ability to supply not the size of the market.

I want to spend a few seconds on HS2, which is High Speed 2, partly because this is exciting and it's also very material to the Group. This is what Balfour Beatty does at its best and that's the way to think about it. As you know we were successful in joint venture with VINCI winning sections N1 and N2, which is the blue area in the middle there around the Birmingham hub. HS2 will see a selection of tunnels, cuttings, highway diversions, viaducts, all of those civil infrastructure projects that we do and do at our heart blood. So this is uniquely very exciting.

But this in itself starts off the next 16 months in that it's working under what I would call and NEC Version C contract whereas Phil mentioned in his presentation we take a target cost. So we will work with the client in collaborative way to effectively put together a target cost based on the design, based on the soils and the ground engineering and we will agree that with the customer. We will then deliver that over the next few years after the 16 month period and we will take a fee on that target cost. There will be a pain/gain share on that, which is 60/40. The point here is that we are collaboratively putting together the design, the engineering, the schedule and the delivery and we agree what that is and then we actually look to implement it.

In that period of time, over the next 16 months while we do that, the customer actually pays for all the costs associated with that. So that is a much better way of working in terms of understanding the risk and then delivering against that risk. So that is what HS2 represents to us today.

There is one challenge in it and that challenge is that there is an overall budget for the programme and HS2 leadership team have to bring the project in within that budget. So it's going to be quite a - there are going to be pressures in terms of the scope, the design and the budget and the affordability. So affordability is a factor that still has to be taken into account.

What's even more exciting about this is if I actually look at HS2 in the future - you've still got on top of what's already been awarded and won, £4.2bn which will be assigned to stations. And again, we have the expertise to deliver on those stations, in the case of the rail system; within our rail division we have the electrification of the catenary and the signalling. So if you look at the £2.7bn that's assigned against that we can provide the civils, the rail, the power in terms of the transmission and the power cables and the traction controls and also the M&E.

So in a way if you look at it, if you were to actually lay out the requirements of HS2 and the capability of Balfour Beatty they almost perfectly align. In the case of the Birmingham to Crewe that was announced recently that will be another £3.7bn and that actually ties directly to the sections N1 and N2 that we're looking at. And again, our capabilities match. And then into the future the line up to Manchester and Leeds is another £24bn.

We are obviously not going to bid all of this and we're going to be selective, but you know this is a great opportunity for Balfour Beatty. And if you put that alongside what's going to happen at Heathrow which is a customer of ours, if you look at Highways England which is one of our largest customers and if you look at what's going on at Hinkley this is pretty exciting stuff. So you can understand the investment we have made over the last two years in bringing on apprentices, graduates, training people, moving towards a digital Balfour Beatty, all of that is going to come to the fore in delivery of these projects.

In terms of our expectations, no changes there, we're still saying the same for 2017/'18, the same for 2019 and beyond. I feel pretty confident in where we are here.

And then finally, it's very interesting, two and a half years ago I think when I took this job a lot of people phoned me up and said to me - you know have you lost your marbles so to speak? I don't suppose there's one of those people today that wouldn't willingly change places with me to be in my position running this company in this market.

And if you look at what we've delivered in the first half of the year, you know net cash of £45m versus last year net debt of £65m. If you look at the fact that we're on track to deliver full year expectations with a marked improvement in the first half of the year. We've substantially de-risked the portfolio with another six months of trading, but we're actually focused on those areas that cater to Balfour Beatty's strength. And that is all underpinned by the fact that we're confident enough to raise the dividend and still have a progressive dividend going forward in the future.

This is a great place to be at this moment in time. So on that note I will hand you back to us two to answer questions.

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## Questions and Answers

**Gregor Kuglitsch, UBS**

Good morning, I've got three questions. The first one is to the competitive landscape, obviously the last six months was pretty eventful for the sector, I wanted to understand to what extend you think that impacts you, helps you perhaps in recruiting people, others becoming more selective, or any other opportunities that may be thrown up as a result of that? That's the first question.

The second question is you obviously paint a pretty positive picture on end markets, but I think some of these projects if I'm not mistaken kind of ramp up in '19 and '20 at the same time your order books kind of come down. Is there anything we need to think about in terms of revenues dipping before they kind of start rising, just maybe any colour on that?

And then finally on working capital, I'm looking at your accounts and it appears that particularly Support Services has gone into a negative position, which is pretty unusual, I wanted to understand if there is anything one off there in nature, or do you think that can be sustainably in negative - it will be a negative working capital business? Thank you.

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**Leo Quinn, Group Chief Executive**

On the first one just to clarify you said and interesting landscape, what did you - was there a more detailed question around that?

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**Gregor Kuglitsch, UBS**

Well obviously there has been a string of profit warnings from a number of your peers, some of them going into some financial distress, I want to understand if you think that throws up any opportunity in either recruiting people, being able to bid perhaps on better terms because these people are to - or these companies will perhaps become more selective, anything that you're seeing perhaps already?

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**Leo Quinn, Group Chief Executive**

Right a couple of things, first of all the landscape is always interesting and construction would never bore anybody would it? Look, first of all in terms of the profit warnings if you look back over the history of the industry, there have been a number of companies that from time to time have stalled and even some have failed, it just seems to be a characteristic of the industry. The root cause of that is a longer discussion.

I'm focused on ensuring that Balfour Beatty is a winner out of all of this. We are focused on ensuring that our margins are rising and that we're playing in a market and with customers that we want to play with and that we have experience with.

In terms of recruiting people, look the winning of HS2 saw a flood of résumés come through our door because people are attracted to effectively good companies, good brands, good leadership and iconic projects. And again in that area we'll be selective. But I still believe in my heart that there is ample capacity within the Group that can be absorbed so therefore we don't have to bring on more costs, we can actually take on more revenue.

We are managing our cost base in line with our revenue, so we are constantly looking at how we can do things more productively, how we can take out cost right across the Group. And we are not in the slightest bit concerned about where we sit in terms of backlog and orders because we know that if we look towards the future there is going to be strong demand coming through.

On your working capital question, Phil will grab that if you've got it at your fingertips?

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**Phil Harrison, Chief Financial Officer**

Predominantly on Support Services we actually run positive cash - positive sorry working capital not negative working capital. We have had a couple of mobilisations in that area that has made us go negative. So I would think that will move back actually into positive territory for the full year.

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**Howard Seymour, Numis**

A couple if I may on specifically the industry standard margins because you alluded to the fact of the confidence on that. I note you saying in the statement that US and also Support Services get there this year. Is your greater confidence that they are getting there quicker as opposed to the UK, or is it across the piece that you'd be expecting that greater confidence?

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**Leo Quinn, Group Chief Executive**

I think our confidence really goes across the piece, obviously it helps when you're already there doesn't it, you know if you're already at 3% or 1%. I think what we're seeing is that it's as the settlements on the legacy projects and the commercials trade through, you know there is a wide range of outcomes. And by the second half of 2018 most of those should all be done and settled. So you're almost running a true run rate at that time, so that's why we put it out there.

You know if somebody sort of settles early and gives us a large amount of money, it does change the financial outcome doesn't it, but you can't sort of forecast that can you?

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**Howard Seymour, Numis**

And secondly you alluded to the costs coming out of the business, 1) are they as expected and 2) you always alluded to the UK would be a greater source of that than potentially the US, is that still the case - are you still in the case where a lot of that is UK driven or is the US part of that as well?

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**Leo Quinn, Group Chief Executive**

Yeah no in actual fact the US is quite substantial, I can't put - I won't put an exact number on it, but I know in the last two years it's over $40m that we've taken out of the US. And you know the US actually runs six to nine months behind the UK, so they are going to be benefitting from a sort of US wide single version of JD Edwards which goes in at the end of the year. That standardisation gives better transparency, better control of jobs, less bureaucracy and manual work around the numbers and things like that.

So I think my confidence around the cost out is just how do we continue to drive productivity. We've made great inroads on our procurement initiatives as well on both sides of the Atlantic. And you know there's sort of still a long way to go on those activities.

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**Howard Seymour, Numis**

Thank you.

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**Joe Brent, Liberum**

Good morning, three questions probably best to take one at a time. Firstly thanks for the update on the legacy contracts can you tell us if any other problems contracts have come into the order book in your tenure.

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**Leo Quinn, Group Chief Executive**

Go on Phil.

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**Phil Harrison, Chief Financial Officer**

You might be alluding to Aberdeen Western Peripheral maybe, I don't know?

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**Leo Quinn, Group Chief Executive**

Let me try and answer that and then Phil can chip in. In the normal course of business I think if you look at this set of results as we go forward in the future I think you're looking at a much more normal construction company, so effectively you could look at us and judge us on the basis of infrastructure and construction. And I think within that you're always going to have a range of projects, you're going have to have some that's over performed.

We did have one contract which actually performed at 30% gross margin in the last period, unfortunately it wasn't a large contract which is a great shame, but again you are going to have some troubled contracts. For example Aberdeen Peripheral is a very challenging contract, it's a contract where you know when you've got a contract like that your focus has to be how do we get it delivered and how do we get it finished and how do you make sure that the benefits accrue to the customer because that's going to put them in the best place.

It's a project which over the last year has probably weathered some of the worst weather conditions on record in Scotland. And at this moment in time we're looking at, we're delivering approximately 30 million a month in terms of production. And every morning I get up and I look at the weather because it's going to be the weather that's going to determine our success.

So we're targeted on delivering everything but the bridge over the River Don and the whole southern section finished by the end of this year. And if we do that you know that will be quite an optimistic outcome I think. However if we slip because of weather it will be a little bit more challenging so there's always a range of outcomes around these things. We've got the normal, we have upsides and we have downsides but I'd say nothing in our current portfolio compares to where we were two years ago.

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**Joe Brent, Liberum**

Thank you and the second question if I may …

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**Leo Quinn, Group Chief Executive**

Just for the record we're quite good at managing these projects by now.

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**Joe Brent, Liberum**

And on your PPP disposal it was sold at zero profit which I presume means it was sold at book value, that's unusual isn't it for an asset to be sold only at book, what happened there?

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**Phil Harrison, Chief Financial Officer**

This was a PRS scheme, private rental scheme in the US and on that basis actually if I remember rightly we don't carry a huge book value on that in the sense of it matches the market value. Typically the big increases are in our PFIs which are predominantly UK, that's where you see large disposal gains.

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**Leo Quinn, Group Chief Executive**

Remind me of the size of the transaction I've forgotten now?

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**Phil Harrison, Chief Financial Officer**

£2m.

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**Leo Quinn, Group Chief Executive**

I don't think that's statistically meaningful in £1.2bn

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**Joe Brent, Liberum**

And finally in the back of the slides you show your geographical structure of your US Construction Business, clearly it does look very much sort of West Coast, South Coast, East Coast. Are there infills that you'd like to make to start to build out that geographical spread?

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**Leo Quinn, Group Chief Executive**

I'm clear on that, no none whatsoever and we're enjoying a pretty optimistic picture at the moment. If you look at California and Oregon, Seattle where we are we're seeing growth around Seattle, Portland, IT centres, backup power supplying establishments, education in Southern California.

Dallas has gone through a period of correction but I think Dallas is refocussed now on a very strong market. Just for information Dallas is a single branch is about $1bn of turnover so it's a pretty big business. We've recently put a new leader in charge of it who's been with the company 20 odd years, doing a fantastic job in moving that business forward.

We're concentrating on Florida, we've recently upgraded the leadership in Florida and in Georgia, we've combined our Georgia operations with our Charlotte operations so we've got strong leadership in there, Washington DC is strong. So I think we've got a very strong footprint in very attractive markets where they're urbanising and people are actually moving south. So I think we've got enough to cope within just this indigenous growth within those markets without thinking about going outside of them. And if anything we'd be retrenching into those established centres.

One other piece of information which might be helpful we, in the last half, we closed our Houston operation, that was bought three or four years ago, it was a refurbishment business that had then ventured in to selling hospitals. In the same period we cancelled a very large hospital contract and we negotiated the liabilities on that down to $4m where it could have been substantially more. So we're exiting where we shouldn't be playing and in effect and where we don't have the concentration of expertise.

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**Andrew Nussey, Peel Hunt**

Again a couple of questions maybe take each in turn as well. First of all when we look at the UK Construction order book what will be the impact from HS2 is it just 50% of the overall project value?

And then as we look at the order book progression over the next 6 to 12 months by major project, rail and regional how would you expect that to trend?

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**Phil Harrison, Chief Financial Officer**

On HS2 we don't anticipate, it will be 50% of the £2.5bn that we'll book. The bulk of that order won't be booked until late 2018 so it won't hit our order book until late 2018, maybe early 2019. And that's when if you remember as Leo said the target cost will be agreed and we'll have a value to put on. There will be a small order probably I think circa £80m that we'll book in the second half which is the ECI and it will be half of that.

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**Leo Quinn, Group Chief Executive**

And in terms of regional and rail as I look forward, let's take the rail construction. Two years ago we withdrew from a number of projects around the UK where the terms that were agreed were just unsatisfactory and we were just basically losing money. What we have continued to do is I'd have to say almost exemplary delivery, if you look at many of the electrification projects around the UK they've all not been delivered or they've been over on budget. We delivered the London to Maidenhead line and delivered it very, very successfully.

On the back of that performance we are now engaged with Network Rail to actually look at other opportunities where they're confident in our ability to deliver. So we're very excited about it so we will see growth in that business and that's performing very strongly yes.

In terms of the regional I'm very happy for the revenue to stay flat to slightly declining depending on the area. Now Living Places for example which is our roads business which is local authorities you know the right contract in that area at the right returns we'd look to expand but if not we'll stay as we are.

So I'd say the outlook for regional is largely flat to steady and it's shrunk a little bit over the last couple of years but if you think that the majority of losses occurred in that area we've only given away revenue that was effectively loss making. So we're now in a much stronger position, much, much stronger.

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**Andrew Nussey, Peel Hunt**

And secondly if I wrote it down correctly, taken out £18m of costs in the first half and £20m in the second, to what extent does some of that have to be reinvested in the business as opposed to ultimately drop through to profit?

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**Leo Quinn, Group Chief Executive**

And it was £18m in the first half; it would be nice if it was 80 but 18 and 20. If you look at the bullet on the slide I put investing to take out cost, you know the investments we're making today in the IT infrastructure and the likes of that and the digital analytics, my view would be in the first half the majority will flow through, in the second half you know let's assume half of it will flow through otherwise Phil will be kicking me under the table saying that you're raising estimates and there's no intention to do that.

Did I get the right answer?

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**Phil Harrison, Chief Financial Officer**

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**Marcin Wojtal, Bank of America Merrill Lynch**

Hello, the first one on Support Services, can you explain what is driving the improvement in the margin as revenue was down, is it more the cost cutting or is it more the phasing of projects?

And number two is on HS2, I think you mentioned that your win ratio was the highest allowed if I understand that correctly and also if I'm not mistaken your market share is not too far from 20% considering what was awarded in July.

Do you believe you could be close to that with all those new tenders that are coming up and do you actually have enough people, enough engineers to actually be targeting a market share that would be let's say high teens or 20% or that would maybe going a bit too far?

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**Phil Harrison, Chief Financial Officer**

Support Services I think predominantly we've tackled cost; we've tackled cost in our power and transmission business and in gas and water. There's also in gas and water we're pretty conservative in terms of pain gain, it's a pain gain kind of process so we're just entering into a period of gain at this point so there's some effect of that coming in as we go through that AMP cycle. So we don't recognise any gain until we've actually established that the gain can't be reversed, others might not do that so that's Support Services.

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**Leo Quinn, Group Chief Executive**

HS2 I think the question was around win rate, we won about 40% in winning N1 and N2 which was the largest market share. We won it in conjunction with VINCI that was around first of all Balfour Beatty's brand and our capability, also VINCI's experience in the likes of Tours De Bordeaux which is the Poitiers to Bordeaux high speed line. So I'm not quite sure what the rest of the question was?

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**Marcin Wojtal, Bank of America Merrill Lynch**

Do you think your win ratio can be as high as that in the new tenders that you flagged, do you have enough people, do you have enough engineers, are they capable of serving so much work?

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**Leo Quinn, Group Chief Executive**

I wonder if I can flick back to that slide for a second it's worth looking at this, if I look at without revealing my win strategy if I look at rail systems you know our M&E capability is industry leading, our power capability is industry leading, our traction controls is industry leading in rail, rail electrification we're probably the market leader in delivery and then civils. So if I look at rail, power and M&E are not involved today so I'd be looking to take a substantial part of that and then the civils would be very complementary.

If I look at the Birmingham to Crewe that's the adjoining section to what we're building so you know we've got to have a unique understanding in terms of what's in that area. What's going to be key by the way for all of this is the behaviour of the contractors, and that's going to have a big impact.

So I'd say that stations are interesting, the rail system is very interesting and Crewe is very, very interesting. I won't look at the Manchester or the Leeds bit so you'll have to judge yourself from that I mean it's a big prize and then you're right, I mean your appetite can be too big. So we're going to bid selectively where we have capability to deliver.

And remember that's one thing but think about what's happening with Highways England you know if I go back a couple of slides I mean there's a programme there that directly impacts on us and Highways England is £15bn and we're Highways England's probably largest overall supplier. You can match that up with Hinkley I mean we're going to have to be very, very discerning and we're going to have to be very careful that we don't eat too much.

But if I go back and I won't go back any more slides but if I look at our strategy around Expert, throughout all the things we've been doing in the leaning out of the company we've sort of been maintaining our investment in key skills, key capabilities, those things that differentiate Balfour Beatty. So you know we're in as good a place as we can be, we'll be increasing our investment in that area as we go forward because it takes five years to get good engineers up to speed with the right sort of knowledge and experience.

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**Sam Bland, JP Morgan**

A couple of questions please. The first one was I think you said in the UK business fixed price contracts were about 50% of work one, now about 30%, would you categorise that as mainly a market movement and the market generally has moved towards lower risk bidding structures or is that more a decision that you've taken to move more in that direction?

And the second question was on the HS2 contract where it's a target cost contract. Is the terms of that target cost arrangement typically across the industry and in the event or is it possible for that target cost estimate to turn out to be a long way wrong of what actually happens? And in that event what would the outcome be, I think you said it's a 60/40 gain share, how does that work in practice? Thanks.

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**Leo Quinn, Group Chief Executive**

I think Phil can answer it because it was his presentation but fundamentally I think there is a shift especially in the London market where things have moved more to two bid or two steps where you do an early engagement with a contractor ECI and then you work up the scope together. But also from us being more selective I mean there are bids we just won't enter in to and you know there are clients that we don't want to sort of play with, that's for other people. So I think our selectivity has been more important than just a general market movement.

And then in terms of targeted cost look you're absolutely right you know we're only as good as our ability to estimate and to engineer. The idea of putting something together in terms of the ground conditions, the scope, how you would deliver it in conjunction with the client you would hope would get you to a fair, balanced and reasonable estimate of what actually is required, the time to do it, etc.

It's important that we don't take on risks that we don't control or that we price that risk and in many cases there are instances where we've priced the risk at a certain level, the client's decided not to take it and it has been substantially in excess of that when the project's been implemented and that lies on the client side. Things like archaeological risk is a classic example of that, how do you determine that in advance?

In terms of your pain gain, the 60/40 that's not untypical, just 50/50 is the usual mark and 60/40 is not far from that. In a way I think that's sort of like an incentive on both sides that says if you do get it wrong you're not going to take all the pain but if you do get it right you're not going to get all of the upside. And the key point in all of these things when I talk about risk and archaeological and other risks is that you've got to be very careful in terms of what costs are allowed and what costs are disallowed and making sure all those things are established.

Why do I feel confident that this is a better way to work? If I look at all of our contracts over the last 10, 20 years the areas that we manage better and have experienced this type of twostep process with an ECI and early engagement, that is our core competency.

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**Chris Moore, Investec**

Just one very quick question on the UK Construction business, what was the profit from rail which I think was moved back into UK Construction in the first half?

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**Leo Quinn, Group Chief Executive**

I don't think we actually disclose that do we but rail has made an improvement along with regional construction and what else is in that part - and majors of course yes. So they've all made material progression the last six months or year over year whichever way you look at it.

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**Chris Moore, Investec**

And maybe just one other follow up, you pulled out in the comments about the London market being a bit weaker, I just wondered how important that is for your regional business in terms of revenue, whether it's that material?

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**Leo Quinn, Group Chief Executive**

Phil just said it's about £100m per annum over a £1.5bn business - so London I'd say is not necessarily material. And we're maintaining a presence there, the projects we've got have all been won in the last two years, they've gone through our gated lifecycles and we think they're on, what I call good terms and good understanding the risk.

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**Phil Harrison, Chief Financial Officer**

Yes our biggest losses is two years in the London market so we downsized the London market two years ago and we've been very selective in the capabilities that we'll do in London. So to some extent we have less exposure to what we see is a downturn in the London market at the moment.

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**Leo Quinn, Group Chief Executive**

Yes I think London will naturally soften and we'll maintain a footprint there. I'm quite relaxed about not being over exposed to London.

If there are no more questions thank you all for coming and I'm sure we'll talk to you in the next few days, thank you.

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