Investor Day
3 December 2012
Chief Executive's opening remarks
Ian Tyler, Chief Executive Officer

<u>Title slide</u>

Good afternoon and welcome to our Investor Day. Two years on from our Investor Seminar in November 2010, we thought it was time to give you an update, and I am very pleased to see so many of you here in person.

<u>Agenda</u>

The afternoon will be devoted to exploring the Group's strategic opportunities, demonstrating our progress to date – and re-affirming our overall vision for the Group. It is important for us today to show you that not only is our strategy gaining momentum, but it is also proving to be exactly the right strategy to be driving as construction markets evolve globally.

We will run the afternoon in three parts:

- The first part will consist of presentations in this room to all of you.
- Then, after a tea break, we will have break-out sessions in small groups where you will have the opportunity to meet other members of the team. They will take you through their businesses to give you a good understanding of their aspirations and a deeper dive into their plans. We hope these sessions will give you a more tangible feel for the Group's direction.
- And finally, after the break-outs, we'll come back to this room for an open Q&A session.

But first, I'd like to devote some time to the near-term environment and its implications for the business.

<u>Trading</u>

Our last communication with you was the Q3 Interim Management Statement. There is nothing new to tell you about trading, and I certainly don't want to repeat everything we said at the time, but I think a summary is helpful to put our near-term plans into context.

Very briefly, most of the Group's businesses are performing well and in line with our expectations.

But in the construction business the picture is more mixed. Some parts of the business are doing very well, like Gammon in Hong Kong. However, at the present time, our construction business is weighted heavily to the UK and US, and this business which has served us very well over the last ten years, is exposed to cyclical downsides, particularly in the buildings sector.

Volumes in the US buildings market remain at a depressed but stable level, and we probably won't see our business benefit from market recovery as soon as we might have expected. On the other hand, prospects in the economic infrastructure market, whilst proportionately a smaller part of our business, are actually quite encouraging. You may have seen that we won the £500m Dallas Horseshoe Project in joint venture with Fluor – and we have several similar projects in our sights.

In UK construction, we have seen market volume continue to deteriorate with three factors coming together as we go into 2013: reduced public sector spending, no recovery in private sector investment such as in commercial buildings, and delays in projects that are awaiting certainty around government policies such as power. These three factors together reduce substantially the number of large, technically complex projects which allow us to differentiate ourselves from much of the competition and achieve higher margins – projects like the M25 or Birmingham Hospital. So the business mix is shifting to less complex, lower-margin regional business and our supply chain is reaching a level where it can't take any more stress.

Overall, then, 2013 will be a difficult year for our construction business. However, we <u>are</u> actively managing the business to mitigate these headwinds as much as possible, so let me now talk about what we are doing.

<u>Mitigating actions</u>

It's worth reminding you that we have already done a great deal to focus the group on less cyclical markets as part of our long-term strategy. However, this is a long-term programme and we're only part way through it.

More tactically, we have seen the downturn in our construction markets for some time and, partly with this in mind, and partly to drive long-term competitive advantage, we currently have two cost efficiency programmes in place. Phase 1, which we launched in 2010, will reach its target run rate of £30m by the end of this year. We moved onto Phase 2 in March. This is a deeper and broader programme with global implications, and it's expected to deliver an additional £50m of annual savings by the end of 2015.

So what more can we do?

Firstly, the most important thing we, as a management team, must do at this point in the cycle is to manage risk. There are two elements to this. One, we must ensure that our fight for market share in current conditions does not drive us to import risk that we can't manage. Two, we have to ensure that we do not fill our order book with low value work which increases risk without reward. Carrying risk without commensurate value is something we will avoid, even at the cost of losing volume. So risk management and pricing control become our key focus. We have a strong track record in this area and we are confident we can deliver.

Secondly, there is the question of adjusting the cost base to an inevitably lower level of activity. As you know, the operational delivery part of our business flexes naturally with the volume of project activity. For example, since the beginning of the year about 1,400 people have left the UK construction business as we completed projects and haven't moved them on to a new one.

But what about the support functions? Can we drive costs lower than currently envisaged? Well, overlaying a third phase of cost reduction on top of the two existing programmes has its challenges but there is further scope for adding to the current cost efficiency programme. These further savings would underpin 2013 performance, and also drive the underlying cost efficiency of the Group even further with additional benefits from 2014 onwards. We will update you on this front in the coming months.

Rail business

One other headwind we brought to the market's attention in the IMS was in Rail in Europe. This business has performed well over many years. However, there are two issues which we need to respond to. Firstly, there is a clear and probably long-term structural change in Italy and Spain, where volumes are now becoming critically low. Secondly, we are seeing the progressive commoditisation of some of the work we do – particularly renewals and smaller project work – in the UK and Germany.

We will redefine our Rail business so that we focus on those sectors where we can deliver most value and withdraw progressively from those areas where a lack of long-term differentiation will lead to progressive commoditisation.

We will come back to you with specifics over the coming months, but there is one thing I can be absolutely clear about- this will not side-track us from the delivery of complex major projects internationally. This is a market in which we have been very successful over many years. Projects like the West Coast Electrification, Rwang Ipoh in Malaysia and the North East Corridor Electrification in the US are part of our heritage. With PB now an integral part of the Group, more recent projects such as Denver, Melbourne and East Kent Spur are central to our focus and the creation of a strong Rail vertical remains at the heart of our strategy.

Capital allocation - Balance sheet

So that's all I'm going to say for the moment on the immediate trading outlook for the Group. Before we turn to the main subject of the day, our longer-term strategic opportunities, I'm going to spend just a few minutes on capital allocation.

Firstly, let me re-emphasise a point I've made many times before. A strong balance sheet is a pre-requisite in our sector and in particular, when we're entrusted with the responsibility for delivering our clients' assets.

A strong balance sheet means having the liquidity to manage large swings in working capital and, as a pretty good rule of thumb, it necessitates having monetisable assets broadly equal to our negative working capital. And that's not just our rule. It's how our customers and the US Sureties see the world. This is how we've run our business over many years. It's why we held so much cash at the top of the cycle and it's why we've been able to manage the impact of cyclical downturn with minimal difficulty.

Monetisable assets mean not just cash but also assets which can be readily sold for cash, such as from our PPP and PFI portfolio. So, our balance sheet requirements mean that any conversion of such assets into cash does not necessarily increase the amount of capital we have available to invest in the business.

The capital we do have to invest is the total of the excess of our monetisable assets over our negative working capital, plus our free cash flow excluding any working capital movements plus the proceeds from any part of our operating portfolio which we sell.

Capital allocation – Investments portfolio

So, let's talk about our strategy for the investments portfolio.

Last year we started a programme of disposals. Our declared aim was to sell £200-300m of mature assets over four to five years. Our objective was and still is to realise the value of these assets at the point when that realisation maximises value for us. Ian Rylatt, who manages the investments business, will give you an overview of this programme later.

The question investors have been asking us since then is: could we accelerate these disposals? It's a fair question, and one we consider all the time.

Disposals do support earnings and dividends to shareholders, but beyond that, there are several factors we have to take into account.

- Firstly, by selling assets arguably before their point of maturity, we would forgo some value and furthermore any significant reduction in the scale of our business would have some impact in operating efficiencies on the remaining assets.

- Secondly, we have to weigh up a number of macro factors. Discount rates would increase with any increase in interest rates, but only at the very long end of the yield curve. Conversely, the strong inflation hedge within these assets means that demand for them increases as concerns about inflation grow.
- Thirdly, we have to think how political risk could impact value. At the present time, with the government focused on bringing significant new private capital into the infrastructure sector, we judge this risk to be relatively low.
- Finally, we need to bear in mind the point I made just now. Any disposal of these assets would not necessarily increase the capital available to invest in the business.

Taking all these factors into consideration, we believe our current strategy remains the right one. However, looking at how the portfolio will develop over the next few years, it is our intention to accelerate the programme. We currently envisage disposing of assets with £200m of Directors' value over the next three years. This would increase the £30m disposal gain target we indicated in August to around £40m per annum - approximately double our original estimate of £20-25m underpinning short-term profitability.

<u>Capital allocation - Moving capital into verticals and growth markets</u>

So, let's step away from Investments now and look at the rest of the Group in terms of capital allocation.

Balfour Beatty is transitioning. Hence, it is natural that some parts of the business will be more essential to the strategy we are driving than other parts, and this will require careful management. One thing is certain though. We will inevitably be shifting our capital over time to businesses that are in our chosen vertical sectors and growth markets.

Over the rest of the afternoon you'll hear more about this strategy and how we're implementing it. I'd like to offer a few words to set the scene.

For many years, Balfour Beatty has been a world class constructor and we have a reputation as such around the world. We've developed and broadened our skills, we've developed related businesses in support services and investments, and we've made a lot of money for shareholders in the process. However, there are a few drawbacks to this. As a constructor, we only really have true differentiation in our home markets. Elsewhere, we don't have the local knowledge to be truly competitive. So without taking unwarranted risks, we are mostly tied to our home markets – largely the UK and more recently the US. Our capacity to grow market share is constrained and, as Peter will explain in a minute, our core geographies are generally less likely to grow than other major infrastructure markets. Of course, with a narrow geographical focus, this business is also very cyclical, as our outlook for 2013 demonstrates.

There is another part of the infrastructure value chain which has none of these drawbacks – professional services and particularly design and programme management. PB has historically been a world class professional services firm in the same fields of infrastructure as Balfour Beatty. The trouble that PB had, apart from its ownership structure, is that, trading purely on asset knowledge, with limited ability to take execution risk, it's very hard to maintain a lead over the competition and creating scale in any market is a very long game.

Meanwhile, infrastructure owners are under inevitable pressure to deliver more for less, whether through fiscal pressure, the inexorable process of regulation or the simple need to deliver shareholder returns. These pressures vary and so do the solutions which asset owners seek. But, across the world and across sectors, there is a general trend to break down the traditional boundaries in the value chain and seek more effective outcomes.

The effective combination of world class asset knowledge and world class asset delivery in one delivery system makes a business which is sustainably differentiated across sector and across geography. This is the essence of our long term strategy. To achieve it will require us to focus on sectors where asset knowledge and delivery complexity provide the greatest opportunity for value and this inevitably leads us to economic infrastructure – transport, rail, power and water. In turn, this focus allows us to enter new geographical markets in which as a constructor we couldn't have been competitive and as a professional services player we would have struggled to achieve scale. And in time, these new geographies will take us into new sectors such as mining and the wider resources industry.

We have demonstrated that we can run a successful construction business. We have also shown that we create and grow related businesses, such as services and investments, on the back of that business. I think we have also shown that we can add value to a global professional services business. But our strategy is to take those elements and deliver more. To build a higher value – and higher margin – business, exposed to higher growth markets with less cyclicality and greater long-term visibility.

It's perhaps worth talking briefly about timing. This is a long-term move for the Group and there are a number of elements to it. One element is internal. We are making good progress with the structural changes that will facilitate the strategy and we've also embarked on a process of cultural change. We'll talk about some of these this afternoon, but please be assured that we are determined not to risk damaging the inherent value with the group in driving these changes.

A second element is organic entry into new markets and you will hear later on today about the steps we've already taken to realise that goal. I must add though, that history tells us such developments have to be taken steadily. The alternative of throwing caution to the wind in pursuit of market share in a market you don't fully understand is not appealing.

Finally, where entry into new markets can be facilitated through acquisition, again we have to be thoughtful about time scales. Not only do the right opportunities rarely present themselves at exactly the right time but our experience suggests there is a strong correlation between the success of an acquisition and the gestation period of the transaction – particularly where you are entering a market about which your knowledge is limited. PB took us four years from start to finish. Centex Construction took us three years. As we move into new geographies and sectors, a process in which we are already well underway, we will move as fast as opportunity and sound judgement allow, but it's reasonable to assume timescales will be similar. This is a long distance race not a sprint.

Now, at the very beginning of my speech I said that today, we would brief you on the progress we've made on the strategy we presented to you in November 2010.   That strategy remains unchanged – focusing the business on higher growth and higher value markets and recycling capital from our investments business. We'll cover all this this afternoon.

I will now hand you over to Andrew who will tell you how we're going to go about that.

Andrew…

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Agenda
Andrew McNaughton, Deputy CEO and COO

Title slide

Agenda

Thank you Ian… and a very warm welcome to all of you.

In a minute, you are going to hear from the team about our immediate plans and medium-term aspirations in all areas of our business. You'll appreciate that it is almost impossible to do justice to all of these topics in one afternoon, but we will do the best we can.

To illustrate the various themes, you will then see each of three break-out sessions, so that we can discuss and go deeper into the nuts and bolts with you. In order to gain some synergy from the combination of the break-out sessions, we've focused them all on the power sector.

To begin, Peter Zinkin, our Planning and Development Director, will update you on the global infrastructure markets and in particular will discuss the rationale behind the verticals and geographies we have chosen.

Peter's presentation will be followed by a double act from me and George. I will focus on where our competitive advantage lies and outline the strategies we are employing to build our industry verticals. Transport, power, water and mining – are areas where our differentiation is strongest and they already account for about 60% of our order book.

George Pierson, who joined us with Parsons Brinckerhoff, heads up our Professional Services business, and has been leading much of our effort to grow our presence in these growth markets. After all, PB has been present in these markets for much longer than Balfour Beatty. These markets offer huge opportunities for the future and successful penetration could mean generating a quarter of our business in higher growth markets in the medium term.

We also wanted to give you an update today on our Investments business. Ian Rylatt will discuss, not only our portfolio and disposal strategy, but also the evolution of the business and its role in the long-term strategy of the Group. Ian is the chief executive of the Investments division, and has been building this business for the last ten years.

That should all take just over an hour. We will then take a break for tea before proceeding with the break-out sessions. Peter…

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3 December 2012
Infrastructure is a good place to be
Peter Zinkin, Planning and Development Director

Title slide

Good afternoon

We have titled this session "infrastructure is a good place to be". The presentation builds on the propositions that we put forward at our investor seminar in 2010 where we started to explore the strength of the infrastructure market and our belief that in the medium and long-term infrastructure is a good place to be whatever the short term vicissitudes of individual economies. This is entirely consistent with our own experience where our infrastructure business is much stronger than the building market.

Infrastructure is a good place to be

Today we shall be discussing a number of propositions which build on what we said in 2010:

- First that economic infrastructure markets being transport, power and water are relatively resilient. They are less affected by economic shocks and cycles than other markets with which we (or our peers) are involved. In actual fact, all of our recent major contract wins have been in infrastructure.
- Second that sustainable economic growth requires infrastructure investment. Moreover, there is a virtuous circle as the infrastructure investment itself generates employment and economic growth; and economic growth itself enhances government revenue and ability to finance infrastructure investment – a very virtuous circle.
- Third that in developed countries investment is being driven by both the need to replace aging infrastructure and the sustainability and carbon agendas.
- Fourth that in emerging markets investment is being driven by the need for new infrastructure, to support urbanisation and strong economic growth. Indeed infrastructure bottlenecks are often identified as the barriers to growth. We also anticipate there will be a halo effect on the key resource and mining economies, including Australia, Canada, South Africa and Brazil stimulated in the medium term by the economic growth in China and other emerging markets.
- Finally infrastructure is high on the policy agenda of many governments, which recognize the importance of infrastructure in their growth agenda.

What I would like to do now is to take each of these propositions in turn, present our evidence for believing them and explain how they are informing the development of the Balfour Beatty growth strategy.

Infrastructure markets are relatively resilient

Our first proposition was that infrastructure markets are relatively resilient and that they are less affected by economic cycles than other markets in which we operate. The slide shows the activity, in nominal terms, in the infrastructure market and, by way of contrast, the private building market in the UK and the US over the past decade. You can see clearly that the infrastructure market when compared to the private building market is remarkably more stable. In fact, in absolute terms it is pretty consistent year on year. The very significant reduction in the UK activity that we have seen is concentrated in the building market and will be exacerbated by the reductions in government spending on education and health. The story in the US is broadly similar. Our experience mirrors this and you will have seen our recent announcements of the highways maintenance contract in Scotland and the major highways contract in Texas.

We have looked at the relationship between the building and infrastructure markets across a number of cycles and countries in the last 30 years and the story is very much the same. There are obviously many complex reasons driving this relationship but we believe the key factors are:

1. Major infrastructure projects are many more years in the planning and execution than building projects and so are harder for governments, which fund most of infrastructure directly or indirectly, to turn on and off.
2. Governments use infrastructure spending as a counter-cyclical policy tool in recessions mainly based on shovel ready projects which inevitably given our earlier point tend to be the smaller projects.
3. A significant part of the infrastructure market is regulated and the regulated industries have specific multiyear infrastructure capital expenditure commitments.

The much higher volatility in private building can at least in part be explained by behaviour. In a recession private developers will simply stop projects in an uncompleted state when they can see cash is tight but will start the work again as soon as there is a sign of recovery.

Infrastructure is a prerequisite to growth

Our second proposition is that infrastructure investment is a pre-requisite to economic growth. We have updated the analysis we presented two years ago. It now includes India, South Africa, Brazil, Indonesia, Australia, Canada, China, the USA and the UK. I think you can see from the chart (which uses Gross Fixed Capital Formation as a proxy for infrastructure investment) that there is a strong correlation over many years between the rate of growth of spending on infrastructure and economic growth. Causality is straightforward, there is a simple explanation: economic growth cannot occur unless the infrastructure, including power, water and transport networks, is in place to support that growth.

Drivers in developed economies

The third proposition is that in the medium and long term infrastructure will be a growth market in both the developed world and emerging markets. In the UK we are seeing the replacement of the aging nuclear plants, the dash for gas and the carbon and sustainability agendas which are forcing the debate on investments in wind and other alternative technologies. These are typical examples of what is happening in the developed world. You will see from the slide where in the UK we are showing the pattern of expenditure on the power transmission and distribution network and how we might expect that to be replicated over the coming years as the assets reach the end of their lives. In the US we are showing the age of the power generation fleet much of which is approaching the end of its life and replacement of one sort or another will have to occur in the medium term, or, as recent press comment has noted, the lights will start to go out – indeed, they did temporarily go out in the Northeast of the US not so long ago. In addition, the carbon commitment and increasing societal concern about long term sustainability are causing investment in lower carbon but relatively expensive alternative technologies. Just consider the recent energy act discussions. This is not limited to the power sector and we are seeing equivalent investment themes starting to emerge in both transport and water. Two other factors we need to remember are first the impact of demographic changes – just think about population movements within the US to the south and second bottlenecks - just think about the London airport debate.

Drivers in emerging economies

In emerging markets, where economic growth is expected to be stronger and where there have often been governments that have failed to deliver sufficient infrastructure in the past, the need for investment is pressing. This is evident when we look at data that reflects the extent of a country's infrastructure, for example, energy consumption or cars per head of population, or access to sanitation facilities. You can see that there is a vast gulf to be spanned to bring these countries to the levels seen in the developed world if that is what they ultimately decide to do. Moreover, the inexorable rise in urbanisation in emerging markets stimulates the need for even greater infrastructure investment in areas such as mass transit systems and sophisticated water treatment plants that are needed to deal with the consequences of urbanisation. Once the core networks are in place and therefore in the longer term, we expect that social infrastructure investment will then start to catch up, as wealth increases.

Infrastructure investment in emerging economies is accelerating

In most emerging countries infrastructure investment is accelerating and infrastructure accounts for a much greater proportion of construction activity. You can clearly see both these phenomena in the slide, which contrasts the UK with India.

This differential growth will move the balance of infrastructure investment to emerging economies

From a Balfour Beatty perspective we believe that this high relative growth in emerging countries leads to one of the most important changes that will be occurring over the next decade: that is, where infrastructure expenditure is actually going to be taking place. Although there are many different forecasts as to the growth rates in emerging markets compared to developed markets almost all of them lead to the conclusion which is illustrated on the slide that by 2025 the majority of infrastructure expenditure will be in emerging markets. This contrasts to the current position where the majority of expenditure is in the developed world.

Balfour Beatty is a global scale infrastructure player but based on strong positions in a few mainly developed countries. We intend to continue to be such a player but this means that over the next 10 years or so we will have to establish additional strong market positions in our chosen vertical markets in some of those countries where the growth in infrastructure expenditure is going to be taking place.

There will be a halo effect on resource economies

As resource economies in the developed world, Australia and Canada have benefited hugely from the demand for their natural resources and the infrastructure investment necessary to extract them. In the medium and long term we believe that this will continue. If we look at the spending on infrastructure as a percentage of GDP in Australia and Canada over recent decades you can see the acceleration as their resource and mining industries have built up. The level of infrastructure expenditure in these economies is higher than that seen in a traditional developed economy as a result of this. Consequently, the market opportunity is equivalent to that in a much larger developed but non-resource economy such as the UK. We see significant opportunity in both these and our chosen emerging market economies and Andrew and George will be developing this theme in their sessions that follow.

Customers in the resource sector have significant demands for infrastructure in our chosen vertical markets. Bulk materials such as coal or iron require investment in transport (usually rail) and ports to help move the extracted material to the ultimate customers. Unconventional gas requires heavy investment in water supply and water treatment to allow extraction to occur. Both of these industries have substantial power requirements. Overall we believe that 25 to 40% of the cost of the major projects required to deliver these commodities to customers is in our chosen vertical markets. We recognise that actual levels of investment will depend on commodity prices, which have fallen. However, we believe that the current, somewhat depressed state of the market could lead to opportunities to strengthen further our position in anticipation of a medium term recovery in commodity prices and the restarting of deferred projects.

Financing infrastructure investment

It would be reasonable to ask how all this infrastructure expenditure is going to be funded and whether this is a sound basis on which to build the strategy. We recognise this is a complex subject which we can't do full justice to today but a few thoughts to consider. In addition to the virtuous relationship between infrastructure investment and economic growth, we see two other near-global trends which helpfully should play to our strengths. In many countries there is a growing recognition that, one way or another, the user is going to have to pay for the infrastructure. This has encouraged much greater involvement of the private sector in the development and financing of infrastructure. First, a number of governments have concluded that rather than raise general taxation it is better to adjust the regulatory regime under which the relevant infrastructure market operates. This often results in the privatisation or quasi-privatisation of infrastructure networks. Second, governments have encouraged greater direct participation of the private sector in infrastructure projects, including through PPP and concessions, which they have found is a mechanism which is particularly suitable to the funding of infrastructure. This is illustrated by the current acceleration of PPP in the USA, where it has been a long time coming, and rising direct private participation in India. We are finding - and Ian Rylatt is going to develop this in his session - that our experience in PPP is definitely valued by both potential local industry partners and government agencies.

Long-term view of infrastructure market

So to summarise our view of the market: we see a large and sustainable infrastructure market in transport, power and water, in the developed world, emerging markets and in the resource economies. We think that in the shorter term there will be more spending on power because of the age of the estate and the critical need for power in many emerging markets. The focus will then move to transport and water particularly in emerging markets which as I have said will account for an ever increasing share of global infrastructure investment. Ultimately across longer periods it is necessary that the social infrastructure of education and health is also in place to support the increasing aspirations of the wealthier society that result from growth.

We are intensifying our focus on emerging and resource economies

We have been considering very carefully which of these geographies we should focus our growth efforts on. Although China is much the biggest of these markets that does not mean that it is easily accessible to our range of skills. We believe that in the developed world the resource economies of Australia, where we have a strong and established market position, and Canada, where we are building one, are the developed markets where we should put our growth efforts. In emerging markets we have identified India, Brazil and South Africa as countries where we have the potential to build significant businesses in our chosen vertical markets. Our choice of countries reflects our assessment of a number of factors, including scale, growth potential and competition, as indicated on the slide. You can also see the scale of these markets compared to the UK. We will be developing these themes across the conference and in the breakout sessions that follow.

<u>We are progressively reinforcing our position in specific verticals – transport, power, water</u>

This belief in the long term strength of the infrastructure market and in the customers who we can supply in this market underpins our strategy. Consistent with this world view we have concluded that we should concentrate our sectoral growth initiatives on the vertical markets of transport, power, water and the provision of these to resources customers – sectors which are particularly relevant to our target countries and where the Balfour Beatty Group has real comparative strengths and can provide something distinctive to the key infrastructure customers.

<u>Infrastructure is a good place to be</u>

So for our growth initiatives: our chosen vertical markets of power, transport, water and resources and our chosen geographies, of Australia, Canada, India, Brazil and South Africa are derived from the propositions we have discussed.

I hope you will agree that we have provided you today with the evidence to validate these propositions.

And our simple conclusion that infrastructure really is a good place to be.

I will now hand over to Andrew.

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Seizing growth opportunity
Andrew McNaughton, Deputy CEO and COO

Title slide

Thank you Peter.

I'd now like to do two things. I'd like to set out our overall strategy for how we intend to seize the growth opportunities Peter has just outlined. And then I'd like to talk in particular about how we will put this into action in some of our chosen verticals.

Our strategy: Leveraging three key strengths in target markets for incremental growth

Our target verticals and geographies are where we intend to increase the Group's exposure over the coming years. This is not to say we are neglecting our existing core markets in the UK, US, parts of South East Asia and the Middle East – indeed we expect those to continue to be strong performing businesses and essential ingredients for our future success. Instead these target markets are where we see the greatest incremental value for the Group and where we will need to position the business to ensure we are appropriately exposed to long term growth opportunities.

Of course, it's easy enough to identify these attractive opportunities.

But what makes us think we can access them successfully?

Well, we've done it before. Over the past 10 years we've gone into the US and Hong Kong, for example, and built successful businesses. So we know what it takes to succeed.

And based on that knowledge, I'd point to three critical strengths that we possess as a group and that we firmly believe will be the foundation of our future success:

- Firstly, we have deep-rooted, local presence in multiple geographies
- Secondly, we have end-to-end asset knowledge which we've gained from working across all stages of the asset lifecycle, around the world. And we can harness this to create powerful solutions that address our customers' critical infrastructure needs
- And thirdly, we have the capability to develop, structure, finance and deliver investment and PPP projects

Bringing these strengths together creates a powerful and distinctive offer. So let's look at them in a bit more detail…

Local presence – Closer to customers and markets

Local presence allows us to align with our customers - most of whom are based in a single country - and be closer to them. That allows us to better understand and respond to their needs.

It also means that, as local organisations, our clients value the commitment we show to the communities we serve. By committing to and investing in these communities, we provide training and development, create long-term employment opportunities, and support sustainable economic growth. This can be seen across our business through our apprenticeship, training and outreach programmes.

Finally, with deep roots in a community we are also able to create resilient businesses by developing a rigorous approach to risk management. Being on-the-ground gives us an intimate understanding of the local operating environment and crucially, its local supply chain. As most projects in our industry are delivered through that supply chain, local presence helps in every part of our business; and where we take delivery risk ourselves, it's absolutely critical.

Building deep-rooted local businesses

We have this deep rooted presence in a number of countries around the world already.

The light-blue boxes on the slide indicate regions where our presence is long-established.

From our foundation in the UK we've built strong domestic businesses in the US, Hong Kong and the Middle East. Experience has taught us that this model works much better than an expeditionary, fly-in-fly-out approach.

We've then continued to expand our coverage into our chosen target geographies – which are the dark blue boxes. We aren't starting from scratch in these countries: we already have a presence, in some cases a significant one – gained largely through our acquisition of Parsons Brinckerhoff three years ago.

For example, we now have over 3000 people in Australia, around 350 in Canada, 300 in South Africa and 300 in India.

These are solid foundations on which to expand our activities in these regions. And they bring some strong, long-standing client relationships – which George will talk about later.

End-to-end asset knowledge – Stronger engagement, better solutions

Combined with our local presence, we also have global, end-to-end experience and understanding of infrastructure assets. That gives us an edge on three levels:

- Through design and planning, we can leverage strategic relationships and early engagement with clients – this means we can get early visibility of opportunities, help to shape how projects come to market, and generate opportunities ourselves.

- We can design better because we understand the construction and operational issues – and conversely, we can construct and operate more effectively because we understand the engineering issues.

- And being investors and developers, we also understand the owner's perspective. In fact, more than that – we can actually develop, structure and finance investment projects as well as deliver them.

More on this from Ian Rylatt later.

So this end-to-end knowledge adds value to all our work. Not just on integrated contracts where we're providing all these skills to one project, but also in single-service contracts where our understanding of the full lifecycle makes us a better designer, or constructor, or maintainer, or operator.

<u>Global expertise across the whole asset lifecycle</u>

Now this knowledge isn't just end-to-end. It also cuts across all of our core geographies.

And we are using this international expertise, across the whole asset lifecycle, to help us grow in our target verticals. We are doing this through global vertical teams that link up all the different parts of the Group around the world that are active in these sectors. These teams are responsible for knowledge flow, specialist resources, global strategy, and coordination of global customers.

David will talk you through the way we are doing this in Power generation in his break-out session.

<u>A leading global player in economic infrastructure</u>

So, with all these strengths, how do we compare with other players active in infrastructure?

Let us consider a couple of metrics. Firstly scale.

The slide lists the companies with the highest revenues in economic infrastructure in the Western World. We now rank number eight amongst a broad and international peer group – one that is very different to our peer set from only four years ago when we would largely be compared with UK construction companies. This scale gives us a breadth and depth of understanding of infrastructure assets that only a few can compete with.

Scale is not the only metric though. Indeed in the analysis you can see that our professional services peers wouldn't be classed as leading players on the measure of scale alone.

A distinctive combination of strengths

We believe that a more important consideration is, therefore, the combination of strengths that differentiates us from our peers.

Here we've taken a cross section of players from different disciplines that we regularly compete with in economic infrastructure. When you look at these different types of organisations, you see that what we have to offer - including our financing skills, knowledge across the asset lifecycle, and local presence - is very distinctive.

Although there are other players that can match us in some of these dimensions, there's arguably none that can match us across the board. And it's this combination of strengths that sets us apart.

So how do we put this model to work, to "seize growth opportunities" as I called it on my title slide? I'll show you, by looking at our key chosen growth verticals in a little more detail.

Transport market: strong growth drivers

We'll start with Transport.

This is a large market. Taking highways, rail, ports and aviation together, it's worth around £710 billion a year.

It has strong growth drivers in both developed and emerging economies, including capacity constraints, environmental targets and the poor state of existing networks.

Importantly, the procurement trends are also positive. We're seeing more design-build and PPP - and I'll talk about this in more detail in a minute - more outsourcing of operations and maintenance, and a more sophisticated style of engagement between clients and suppliers.

A leading player in Transport

In this very attractive market, Balfour Beatty is the sixth largest player in the Western World. We're active in Transport across the whole Group – in markets all round the world, and in all stages of the asset lifecycle. So, as with infrastructure generally, we have deep understanding of the sector, its clients and its particular asset types – be it in Highways, Rail or Aviation.

Group approach: leverage our strengths in major projects

Our strategy in this market is to leverage this depth of knowledge, along with our local presence in specific geographies, to target major projects.

We do this in two ways:

- In our 'home markets' we offer a full service model. The 'home markets' were those light blue boxes on the map I showed earlier, namely the UK , US, Hong Kong, and the Gulf States – all places we have a strong construction presence. The contracts we're looking for in these territories may be integrated projects or standalone services – but either way, they'll be contracts where end-to-end asset knowledge adds real value.

- In our 'growth geographies' on the other hand – the dark blue boxes on the previous map - we lead on professional services and leverage this platform to take on selective delivery risk, drawing on our asset knowledge and delivery experience from our home markets.

This approach ensures that, wherever we operate in the world, we get full leverage from our existing businesses and maximise the value we capture in each project. It also means we effectively manage risk and only target opportunities where we can command higher returns.

As you can imagine, this approach is most effective on major projects or large programmes of work. That's where our end-to-end expertise adds most value. So that's where we'll increasingly concentrate our efforts – particularly in our growth geographies.

<u>Strategies in Roads, Rail and Aviation</u>

This approach runs through all of our separate strategies for Roads, Rail and Aviation.

In Roads, we see significant opportunities in integrated projects at home. In our growth geographies, however, we will address selective opportunities where we have competitive advantage - avoiding smaller projects which are better served by the local supply-base. In particular, we see a real opportunity to export our skills in asset management and O&M in highways as outsourcing gains momentum around the world.

In Rail, Ian referred earlier to the measures we are currently undertaking to address issues in Europe. Alongside this, we continue to implement our international rail vertical strategy – focussing on integrated and complex projects in our home markets, and aligning our international activities to the Group's target growth regions.

And in Aviation, we are already capitalising on integrated opportunities here in the UK, and we will look to take this model to the US. In Hong Kong, we are very well positioned with a sizeable pipeline in this area. In the other parts of South East Asia though, we are yet to exploit the opportunities arising in aviation – and this is something we'll be looking to do over the coming years – initially through our professional services business.

Transport strategy in action

So, we think our combination of local presence and global asset knowledge is powerful in Transport and here is some evidence:

The F-Bane Rail project in Denmark is a 10 year, £320m re-signalling programme that we secured in combination with Thales, our technology partner. The opportunity to bid for this project came about by combining the design and systems integration skills of PB together with the local delivery capability and customer knowledge from our Scandinavian business. This is an excellent example of how, having broadened the skillset of the Group through the acquisition of PB, we were able to win work we wouldn't have been able to bid for previously.

In Qatar, we recently won two programme management contracts in Roads and Drainage for Ashghal and Rail for QRail. The bids were led by PB's Middle East team – but we won them by drawing on the whole Group, including our downstream construction delivery experience and our global credentials in roads and rail.

And our US Highways team has recently been named best-value bidder for the upgrades and replacements of river crossings in Dallas, Texas – known as the Dallas Horseshoe project. This is an $800m contract, on which Parsons Brinckerhoff, Balfour Beatty and our construction partner, Fluor, offer an integrated design-build package.

In the States we're seeing an increasing level of design-build activity like this, as well the emergence of PPP in Transportation. You may recall that this was a trend we predicted when we acquired Parsons Brinckerhoff. It is good to see the US market developing as anticipated in this way.

In all of these examples, where we are able to combine our strengths like this, we can generate superior returns. These projects are large and complex which reduces the level of competition, but crucially by working together we are also able to eliminate interfaces, promote value engineering and manage delivery risks in an integrated way. This provides a more efficient and higher quality product for our customers, and higher returns for us.

Power: a large and sustainable market

Like transport, power is another large, sustainable market.

It is worth around £440bn a year, with transmission and generation accounting for roughly half of this each.

As with transport, there are some strong growth drivers around the world.

In developed markets the carbon agenda and the need to replace ageing assets is driving demand; whilst in developing countries, increased capacity is being driven by economic and population growth.

Whilst uncertainty remains in some countries regarding policy on generation mix, there can be no doubt that new capacity has to be delivered. And for our part we are technology agnostic as we have skills in Gas, Coal, Hydropower, Geothermal and other renewables.

Also, whatever the mix of generation required, the power transmission market will remain strong throughout the world. The focus in developed markets is on strengthening and renewing established grids as well as bringing new renewable energy generation into the grid. At the same time, developing markets continue to build infrastructure to support growing communities.

<u>A solid base to build on</u>

Again, as with Transport, we are well established in the Power sector, and able to build on our international capability.

In professional services we are already a Top 10 player globally.

In Power Transmission, we have a strong track record of delivering transmission projects, both in the UK - where are the market leader - and internationally - with current operations in the US, Indonesia, Hong Kong, Australia and New Zealand.

Alongside this delivery capability we have been building a track record as an investor and developer in the UK Power Market, most notably in the biomass and waste-to-energy sectors and in off-shore transmission assets.

<u>Strategy: harness local presence, global knowledge</u>

So we're strong in power but aiming to be stronger internationally.

As with Transport, our strategy is focussed on combining local presence and global expertise. In this case, we will use our global engineering and procurement capability to selectively take on and manage more delivery risk.

We also aim to extend our relationships with international power and resource clients, in particular by harnessing our experience in PPP and as a project developer. There is strong evidence that global procurement trends support this approach. There is already a high level of private sector ownership in the sector. And the use of PPP and concessions is increasing in both transmission and generation – especially in emerging market economies such as India and Brazil.

In addition, in Power Generation, the frequent use of integrated engineering, procurement and construction contracts (known as EPC) allows us to build on our existing capability in the US, and leverage that across the world. There are three strands to our strategy in Generation:

- Strengthening the consistency of our professional services offer internationally.
- Further developing our existing EPC activity in the sub-100MW market
- And ultimately increasing our EPC capability in the over-100MW market.

Later this afternoon you will hear from David Rutherford about progress we are making in this area, as well as from Sandip Mahajan about recent successes and future potential in combining investment expertise with engineering and delivery capability in the global power market.

<u>Good progress in mining and water</u>

Before I close, I'll just spend a moment on our other two Global Verticals – Water and Mining.

We are making good progress in both these markets:

- In Water, we have a good position in the UK and a significant and growing one in the US – boosted by the Frucon acquisition in 2011.

In the near term we want to grow in the US, where the water market is very local, by building on our enhanced regional capabilities and leveraging them nationally. We've already made progress on this, winning new projects such as the Galveston treatment plant, in Texas.

In the medium term, we aim to bring our enhanced skills to bear on our target growth markets, particularly Australia. Here, our experience of working within the UK regulatory framework gives us a distinctive edge as many customers seek to learn from and adopt the UK model.

- In Mining, we are responding to the needs of our international Tier 1 mining clients such as Xstrata, Anglo-American, BHP and Vale. We're doing this by leveraging the local presence we have in the places where they operate – Australia, South Africa and, most recently, Brazil. And outside Tier 1 clients, there is also growing demand for end-to-end DBFO contracts including power assets, rail links and miners' housing.

Summary

So to summarise:

- Our key strengths are local presence, asset knowledge and investment capability. It is through these that we will unlock the growth opportunities in our target verticals and geographies

- The breadth and depth of our business in key infrastructure markets is something few can match – the combination of our strengths is very distinctive

- And finally, harnessing the strengths of the Group provides significant opportunities in both mature and growth economies. We're already seeing this through our verticals in Transport and Power, and expect more to come from Water and Mining in future

I'll now hand over to George Pierson – who will explain how this strategy is working specifically in our target growth geographies.

Investor Day
3 December 2012
Accessing growth markets and resource economies
George Pierson, CEO - Professional Services

Title slide

Thank you Andrew.

So far today, we've spoken about how we've identified certain growth geographies and verticals, our overall strategy and how we will differentiate ourselves in these markets, as well as our specific plans in the target verticals.

I'd now like to focus on our strategy in our growth geographies. And like Andrew, I'll take a couple of example markets to examine in more detail.

Before we start I'd like to repeat a couple of points Andrew made.

Firstly, it's worth making clear that, although we're talking about "Accessing growth markets and resource economies" these markets are not virgin territory for us.

They are all areas where Parsons Brinckerhoff has been active, or at least preparing the ground, for some time. PB's presence, as well as our understanding of these markets, provides the platform for Group expansion in these regions, and it's this Group expansion that I'd like to address today.

Secondly, I want to stress again that although we're focusing on target growth geographies today, we're not neglecting our existing geographies. These have not become in any way less important to us – and indeed, Andrew has already explained how our core businesses will be instrumental in accessing new territories. Our focus today, though, is on what we're adding to the Group.

Our target geographies – Large markets with strong growth prospects

So to recap quickly, these are our targets geographically.

As Peter explained earlier, having looked across the world, the areas where we see the best opportunities for growth are in five geographies: Australia, Canada, South Africa, India and Brazil.

On this slide we've also shown the UK - just for comparison purposes. The size of the pie charts reflect the overall spend on economic and social infrastructure and private buildings, with the darker blue and labels referring to the economic proportion of this.

Our five target growth countries share several common themes:

- In all five, the opportunity is large – in most cases, larger even than the UK.

- In all five, economic infrastructure is a key sector.

In fact it's typically the largest sector for the reasons Peter outlined earlier. What's more, the opportunities for the Group cut across multiple areas of economic infrastructure, such as Power, Transport, Water and so on. Multi-sector geographies are key to building scale and achieving the necessary efficiencies to reach our target margins.

- In all five, infrastructure spend has been accelerating and has excellent prospects in the medium to long term.

- In four at least, infrastructure investment is further underpinned by resource-related spending – though not so much in India.

- And in most of these countries, PPP is expected to play an increasing role.

- One word of caution, however. While in all but one of these geographies the size of the opportunity is larger than the UK, exploiting these opportunities will not happen overnight. The business environments are different and in each the Group is at differing stages of development.

<u>Our strategy – Professional services platform and delivery risk</u>

But the growth opportunity is definitely there. So what's our strategy for taking a slice of it?

In all these geographies, what makes us different to other firms is our strategy of starting with a professional services platform from which we can expand and progressively add delivery risk.

The professional services platform is key as it forms the basis for understanding the business environment and local supply chain, but most importantly it provides customer knowledge and intimacy. In a word, it allows us to be "local."

With our local presence, we are able to broaden our professional services offer into new sectors by importing professional services capabilities from elsewhere. And at the same time, we can capture progressively greater value from the local markets by drawing on our world-class ability in delivery from the rest of the Group.

The strategy is the same in all these places – but we're at different stages.

At one end of the scale is Australia, where we have a sizeable professional services platform in several markets and have been selectively taking delivery risk for some time.

At the other is Brazil, where we're still in the process of establishing the platform.

As you can imagine, this approach to new markets will have implications for where acquisitions will need to be made, and what type of acquisitions they might be. I'll come back to this later.

I think it would be illustrative to now look at two of these geographies in detail: the top two on this table, Australia and Canada.

I'll cover our current status of development for each and some of the successes that have resulted.

And then I'll give you a brief overview of our plans for the other three countries.

Australia/New Zealand – strong drivers and favourable procurement

Although Balfour Beatty has been active in Australia for some time, it was the acquisition of PB in 2009 that gave us a major presence there.

We now have around 3000 people in Australia in total.

The majority of these work in professional services – where we are a Top-5 player, focused on infrastructure and resources. Until recently our at-risk delivery work was limited, with a small presence through our rail construction and power transmission businesses. But that's changing – as we'll see in a moment.

The market is large, with about £38 billion spent on economic infrastructure each year. It's been growing strongly for the past couple of decades and there is still a large pipeline of projects outstanding.

The market is also underpinned by large volumes of work in the resources sector. The reduction in commodity prices has led to a slowdown here, but probably quite a healthy one because growth rates had become unsustainable. Going forward, although the market has come off its peak, we expect volumes to remain healthy and sustainable, providing plenty of opportunities for our mining business.

Another key characteristic of the Australian market is its progressive approach to procurement. PPP and design-build are commonplace, and there's a clear public-sector view that private investment will be key to the infrastructure solutions needed over the coming years. The nature of engagement between customers and suppliers is sophisticated and plays to our strengths – especially given the strategic-level relationships we have with clients in PB. And what's more, outsourcing opportunities are opening up in highways, rail and water – all following similar models to the UK. So that means we are well positioned to be a leader in these markets.

To complete the picture, it's worth pointing out that there are two very large general contracting groups operating in the Australian market. For this reason, we are not setting out to replicate our UK-type model where we span all sectors. Australia is a big market, and initially we are targeting those parts where our existing presence and global capabilities will differentiate us best.

Already seeing results

This selective approach is already starting to pay off. We are already making significant headway with our leading professional services platform and our ability to take delivery risk in selected parts of the market. We are leveraging the strong client relationships that PB has already built up, and importing specific global capabilities that add value to the local market.

The Melbourne Rail project is a good example of this. PB held the local client relationship, and also had the right reputation to attract the right local partner. Into this we could import our experience of at-risk delivery work in complex rail environments – particularly our track record on the East London Line in the UK.

Similarly, in power transmission we partner with UGL locally and draw on our international Power Transmission business

And this model is also paying dividends on power generation projects – such as the Te Mihi geothermal plant in New Zealand or the Karratha gas plant, where we're drawing on our EPC skills from the US. David Rutherford will tell you more about some of these projects later.

Taking delivery risk in target verticals

If professional services is the growth platform, at-risk delivery is the engine. By taking more delivery risk, focused on our target verticals, we expect to see many more opportunities of this sort going forward:

- Right now, we're actively bidding on more opportunities in power generation…
- We're pursuing development opportunities in Waste To Energy, which Sandip will tell you about later…
- We expect bidding to start next year for a first-generation outsourced highways maintenance contract in New South Wales – an opportunity that arose from the relationship PB had with the State Department of Transport. PB introduced the client to our Highways Maintenance business in the UK, who helped them review the different outsourcing models available and showed them the benefits we bring to our UK clients.
- In the resources sector we're starting to see opportunities in end-to-end services for Tier 2 miners – including transmission, housing and pit-to-port rail assets…

- And we believe the rail market generally provides us with a lot of opportunity – both in projects and potentially, in the longer term, in rail maintenance

Professional services platform creates opportunities in Canada

Let's turn now to Canada. Unlike Australia, PB has not been present in Canada for long. But it's a market that we've been interested in for some time – in fact, Parsons Brinckerhoff was actively considering entering when we were acquired by Balfour Beatty.

Since then, through the Group we've been able to buy Halsall – a leading professional services firm in the building sector, with around 350 people. This business is now providing the platform for tapping into infrastructure opportunities, as we organically import our transport and power capabilities from the US and elsewhere in the Group.

In addition to this, other parts of the Group are also active in Canada – most notably the Power Transmission business and our Investments team.

Like Australia, Canada is a large and healthy infrastructure market. The total spend on economic infrastructure is currently around £38 billion a year. Growth in Canada has been resilient, with an economy relatively unscathed by the banking crisis that hit the US and Europe and with a good spread of drivers. These drivers include population and economic growth, environmental pressures, and a substantial diverse resources sector.

In addition there's a well-functioning PPP market, on a model which is very similar to the UK's. Design-build is on the increase, and we also have a cultural edge: Canadian customers are generally predisposed to like the British more than the Americans, and I can say that with my accent!

Importing Transport skills: further opportunities from adding delivery risk

As with Australia, we've already been able to broaden our offering beyond the initial buildings professional services offering. We have successfully leveraged the original Halsall platform to secure several important transportation projects, including one in Waterloo Ontario where we were named as the General Engineering Consultant on one of the largest infrastructure projects ever to be constructed in the region.

This project, and others, was won on the basis of our local knowledge of the market through the Halsall platform and by importing transport capabilities from both the US and UK.

Having crossed that threshold, we are now actively moving into at-risk delivery work, again using local knowledge and global capability. We see opportunities in power generation and transmission, transportation and PPP.

Our other target geographies

In addition to Australia and Canada we have three other target geographies: South Africa, India and Brazil. I'm not going to describe these in detail, but let me give you the essential points.

I'll start with South Africa. We have 300 people there at present, all working in professional services and mainly focused on power.

South Africa clearly has a significant need for infrastructure. The pace at which that need will be addressed is not entirely clear because of political uncertainties, but the pipeline is certainly there. There are also questions about the public sector's capacity to manage large-scale infrastructure programmes – but that in itself presents an opportunity for us.

What we do know is that we are already seeing results from importing delivery capability. A case in point is Medupi, where we are working in partnership with the local electricity utility, Eskom, to build the world's fourth largest coal power station.

So where do we see the next opportunities arising for us in South Africa?

Certainly in the management of large-scale infrastructure programmes, because of the public sector capacity issues I mentioned. In power generation and transmission. In South Africa's very large mining sector. And more generally across the infrastructure spectrum, but particularly in our target verticals. Ian Maclean will talk about this in more detail in his break out session.

In India we have an established professional services presence with 300 people and eight offices in key cities. We've also substantially enhanced our local connections and influence by forming a joint venture with the engineering procurement and construction business of Tata Group, one of India's largest companies. This will give us considerable edge in pursuing urban infrastructure opportunities.

India's economic growth and relentless urbanisation provide strong long-term growth drivers with significant opportunities coming through the 12th National Development Plan.

The opportunities we see for Balfour Beatty in India are focused on our power and transportation verticals. In power we see particular opportunities in transmission infrastructure, including PPPs. In transportation, specifically rail, we see opportunities in urban transit and India's ambitious programme to build dedicated freight corridors to relieve the pressure on its national rail network.

We also see international growth opportunities for our low-cost design centre in India.

In Brazil, the fifth of our growth geographies, we are at a much earlier stage. We established our São Paulo office earlier this year and currently have five staff there.

But I don't have to tell you what a vibrant economy Brazil has – nor that it has all the infrastructure growth drivers that you'd expect in a rapidly developing and urbanising economy. Its Growth Acceleration Programme envisages $526 billion of infrastructure investment between 2011 and 2014. Other significant market drivers include the next World Cup and Olympics, and a buoyant resources sector.

If we're going to exploit these opportunities fully, we will need to build scale quickly. That will mean some kind of joint venture or acquisition, and we're actively investigating our options.

A footnote to all three of these geographies is that the ethical and health & safety environments require careful attention and management. We will need to be selective about where we work, and that will to some extent circumscribe the opportunities that are open to us.

<u>Acquisitions: creating a platform for growth</u>

As you'll have noted from our story so far, acquisitions have already provided a valuable platform for growth in these geographies. And they are likely to be part of our strategy going forward.

The acquisitions of PB and Halsall have provided the platform for growth in Australia, South Africa, Canada and India. We are now leveraging these to grow organically, drawing on our global capabilities. To step-up the pace of our development in these markets, we may well look to further acquisitions that build scale in one or more of our chosen verticals.

Likewise in Brazil, we are looking for a JV or acquisition that will enable us to build our presence faster. But even though we're looking for acceleration, it's not something we're going to rush. It's very important to us that we find the right partner – and we accept that it could take some time.

<u>Summary</u>

So, to summarise:

- We're targeting five geographies for international expansion.

- Our strategy in these markets is to start with a professional services platform and import capabilities from across the Group to broaden our activities in target verticals and selectively take delivery risk.

- In four of these geographies we already have a strong platform for growth with our existing professional services business. Our approach here is yielding results and we see a strong pipeline of future opportunities.

- Acquisitions and joint ventures will be pursued if and when the right opportunities present themselves – either to accelerate growth in our target verticals where we already have a presence, or to provide an initial entry into Brazil.

Thank you very much.

Investor Day
3 December 2012
Realising sustainable returns in Investments
Ian Rylatt, CEO – Infrastructure Investments

Title slide

Good afternoon everyone,

In 2010, we announced our intention to realise some of the value in our investments - through the disposal of mature assets - over a planned five-year period. We are now some two years into that process, which is a good point to give you an update on our progress so far.

As Ian outlined in his introduction, some of the considerations we take into account before proceeding with any asset sale are Group considerations – around balance sheet structure, for instance - and others relate to value maximisation and the day to day operation of the Investments business itself.

In my presentation today, I'm going to:

- briefly outline our business objectives for the Investments business,
- summarise our disposal performance to date,
- and, give you an overview of some of the considerations we take into account in selecting an asset for disposal.

When we dispose of an asset it gives rise to an immediate gain. But of course you then forgo any future investment returns. So I'll also give you a high-level overview of the relationship between the two.

Investments – Business objectives

But first of all - what is our Investments business seeking to do?

We actually serve a number of strategic purposes.

Our primary objective is to invest in projects where we can use our investment skills and expertise to maximise the broader benefit to the Group's growth and development. Our initial investment activity centred on PFI. But now we're increasingly diversifying away from this. Why? Partly because the UK PFI market has reduced in size. But also in response to the change in the activity of the Group as a whole – which is now considerably larger and more diverse.

The Investments business plays an active role in supporting the Group as it seeks to develop market verticals, new markets and new geographies.

We need to be able to respond to changing procurement needs – and we have played an active part in supporting the UK Government in its desire to reform PFI.

And finally, an important aspect of our business is the ongoing release of value from our investments - which is the focus of my presentation today.

Disposal strategy – Announced in 2010

This is just to remind you of the objectives we set ourselves back in 2010, when we announced our intention to begin disposing of assets on a continuing basis.

The original programme envisaged the disposal of £200-300m of asset value over a five-year period. And we expected this to generate profits of £20-25m per annum.

Over the period the Investment business was to be self-funding, and a net cash contributor to the Group.

Disposals programme - Performance to date

So how are we doing so far?

Since 2010, we have sold, either in whole or in part, our interest in four assets which represented £83m of our Directors' Valuation.

In all cases we have sold at a value above the Directors' valuation – generating cash proceeds of £112m and disposal profits of £72m.

Despite these disposals, the Directors' valuation of our retained investments has continued to increase – up by £40m to £711m at this half year.

Directors' valuation movements

Here I've shown the various elements that have contributed to the net increase in Directors' valuation from January 2011 to June this year.

On the plus side: we've made additional investments… there has been an increase resulting from the unwind of the Directors' valuation discount rate… we have secured new projects and recognised the income element that they will generate… and, importantly, we've realised operational performance enhancements as we maximise value.

Reductions in Directors' valuation have come from the disposals themselves… and distributions received during the period.

So there’s a range of factors that impact on the Directors’ valuation, and we consider the magnitude and timing of all of these as part of our disposal assessment process.

<u>Cash movements</u>

The previous slide considered changes in Directors’ valuation. On this slide I’ve shown the cash position.

Over the same period we made investments of £91m, - most notably in the M25. We received distributions of £112m and disposal proceeds of £112m. This generated net cash of £133m to fund the Group, - and the Investments business.

<u>A diverse portfolio</u>

Today, our portfolio remains both substantial and diverse: it’s currently made up of just over 60 assets - across a range of projects, market sectors and geographies.

As you would expect, there are some differences in risk profile across these assets – due to investment type and/or the stage in a particular project’s development cycle. In looking at any possible disposal we, therefore, consider its potential effect on the robustness of the remaining portfolio and the resultant income it will generate.

<u>Portfolio maturity</u>

In this slide I’ve shown our portfolio, not by asset class, but by maturity.

Just under 45%, by valuation, is less than a year post final investment.

We’ve held about 20% for less than 3 years.

And the balance – about a third – is three years or more.

It’s important to consider maturity in looking at which assets we can dispose of and when. But it’s not the only consideration – because yield maximisation is a key factor. Even a mature asset may offer either yield enhancement or contracting opportunities to the Group, which can add value - that you won’t see in simply looking at the Directors’ Valuation.

<u>Portfolio characteristics</u>

On this slide I’ve taken the maturity analysis a step further, and summarised some more of the key considerations at each level of maturity.

Anything we have held for a year or less is likely to have a lock-in provision which prevents the sale of our equity. That would make disposal difficult without consent and probably not in our economic interest. We are also unlikely to have maximised value.

Between 1 and 3 years post investment, lock-in provisions typically expire - we are establishing a demonstrable income track record for the asset and seeking to maximise value.

Of the remainder, which we have held for over three years, some are still generating significant additional value for the Group or are projects we wish to retain because of future market or strategic considerations.

So overall, you'll see that there are about £100m of assets which are more likely to be considered as potential disposal opportunities at this time.

Disposal considerations

To summarise our approach to disposals:

Our objective is to maximise the value of our assets.

So we look to dispose of assets where the value has been maximised, if we can.

We look to hold assets where there is a strategic benefit or where we can capture additional downstream value to the Group.

There are a number of additional considerations which I've listed here to give you a fuller picture.

- There are operational efficiencies, which essentially relate to economies of scale,
- It's important to retain a presence in key markets, or verticals, where we see future growth opportunities.
- Asset performance is important – is the income stream stable and predictable?
- We've become experienced in managing lifecycle funds, which can often result in additional downstream work for the Group.
- And there's the trade-off between disposal profit at the time of sale - and the ongoing income which we forego as a consequence of a disposal. I'll come back to this in a moment.

Expanding portfolio with no wins or disposals

But first I'd like to talk a little more about the overall value of our Investments portfolio.

How do we expect disposals and new project wins to affect the Directors' valuation?

This is how we would expect the Directors' valuation to grow over time if we neither disposed of anything nor won any new projects. The growth is driven primarily by the timing of committed investments being made, the unwind of the Directors' valuation discount rate, offset by dividend payments. The growth is not linear due to the timing of some of these factors.

Opportunities for future wins

But we don't expect the world to remain static - and we do see a strong pipeline of future opportunities.

In the UK, PFI bidding levels may have reduced but there are still opportunities coming up. We are still active in the market - there is a significant programme of similar, Not for Profit Distribution, projects in Scotland - and we expect there will be some investment opportunities in the Priority School Building Programme. The decline in PFI has been offset by opportunities in new markets such as student accommodation and the waste sector.

I should comment that we welcome the Government's objective of reforming PFI and look forward to the Autumn Statement in a few days' time. At present, our future bidding plans only include projects or programmes that have already been announced. There is no underlying assumption in our plans that PFI bidding will return to the levels we experienced a few years ago.

In the US, the PPP market is slowly growing and a number of the states have announced plans to use this procurement route. We are also seeing significant opportunities in student accommodation.

In other markets, we are pursuing opportunities in Canada, India and Australia and supporting the Group's interest in Brazil.

Many of these opportunities are aligned with our chosen industry verticals.

UK bidding

In the UK, these are the opportunities where we are currently either at the preferred bidder stage or actively bidding or developing a project. As you can see, there are a considerable number of projects - and this list does not include the projects we are tracking but have yet to actively start work on.

You'll see that just under half our current bidding activity is either PFI or the Scottish, Not for Profit Distribution model. If I exclude Scotland a relatively small part of our activity is currently PFI.

Importantly, over half of our activity is neither PFI, nor NPD, demonstrating our ability to apply our bidding, financing, structuring and development skills in new markets. Sandip will talk more about this and how we are applying and broadening skills in the breakout sessions later.

Looking at this list from an infrastructure market perspective – about 60% of our UK activity is currently in the infrastructure space and the verticals we are aligning ourselves to.

<u>US and Canada bidding</u>

By contrast - in the US and Canada, most of our current bidding is non-PPP and is in the social infrastructure market. This reflects our existing social infrastructure capability based around our extensive Military Housing business and the capabilities of Balfour Beatty Construction.

As I mentioned earlier, we are starting to see an increasing number of projects procured through a PPP route. We are bidding some already, and we expect this to grow.

In 2013, we are anticipating a number of significant infrastructure opportunities coming to market. We believe we are well positioned to bid these - given our proven infrastructure investment skills - the Parsons Brinkerhoff presence in the US - the infrastructure capabilities of our other US businesses - and the rest of the Group.

<u>Portfolio significantly larger with potential wins</u>

How might these bids affect our Investments portfolio?

Let's assume a pretty conservative win rate of something less than one in three… make a few broad assumptions on factors like timing and project size… and this is how we might reasonably expect the Directors' valuation to grow over the next five years.

On this basis – if we made no disposals and simply carried on bidding – you might reasonably expect the Directors' valuation to reach about £1.2bn by the end of 2017.

<u>Accelerated disposal model</u>

So now let's take disposal profits into account…

It's against the backdrop of a rising Directors' valuation that we intend to accelerate our disposal programme, given - the growth opportunities we see in the market – the maturity profile of our portfolio – and the broader considerations I outlined earlier.

In the next three years we expect to sell assets with a Directors' valuation totalling £200m - and generate approximately £40m of disposal gains per annum.

This is an annual profit increase of £15-£20m above our original plan and is expected to generate an additional £100m of cash proceeds over the period.

On this chart I've shown the anticipated effect on the Directors' valuation assuming new wins, and disposal profits of £40m per annum for the next three years and a more conservative assumption of £30m of annual gains thereafter.

With this disposal profile we would expect the resultant Directors' valuation to be around £700-£750m over the period.

When comparing individual disposals, it's important to note that the relationship between Directors' valuation, disposal proceeds and profit is not necessarily the same over time. This will depend on the opportunity within each project to maximise value. By way of example, our early PFI investments had inherently greater opportunity to maximise value than more recent PFI projects, which have been more competitively bid as markets have matured.

<u>Effect of disposals on operating profit</u>

As I mentioned earlier, when we consider disposing of an asset, we need to take account of the annual income, or running yield, that we would have to forgo.

On this slide I've shown the cumulative effect of disposals on the underlying operating profit of the business, ignoring the disposal income itself. A significant one-off disposal in any one year, while providing a one-off gain, would naturally accelerate this effect.

<u>Summary</u>

So to conclude…

Our disposal plans are underpinned by the continuing visibility of investment opportunities in our existing markets, although the mix of opportunities has changed.

We're seeing an increasing number of opportunities in new markets.

We continue to view an active disposal programme as a sensible means of realising the value in mature assets.

We intend to accelerate our disposal programme over the next three years by selling assets with a directors' valuation totalling £200m and generating total disposal profits of £40m per annum.

This will release significant amounts of cash for the Group, while maintaining a relatively stable directors' valuation of around £700-750m.

Thank you.

Investor Day
3 December 2012
Concluding remarks
Andrew McNaughton, Deputy CEO and COO

Title slide

Welcome back everyone.

I hope that you found the break-out sessions both interesting in their own right but more importantly helpful to expand on the points that we made in the earlier presentations.

Before I hand back to Ian to lead us through the Q and A session, I would like to draw out the key points from this afternoon.

On track to deliver strategy in the medium term

Our overall aim has been to demonstrate not only that we have made good progress on our established strategy, but that we have a clear view of our direction and focus going forward.

We have previously set out that in order to address the cyclical nature of construction, we would focus on the more resilient and stable economic infrastructure markets. Our actions to date in this respect have significantly changed the nature of our order book and also moved us to a position of scale on the global stage. You will remember our presentations today. The forecast future investment around the world in our core vertical markets provides clear opportunities for further progress.

The breadth of skills now evident across the Group, application of an end-to-end service and harnessing our ability to take on and manage delivery risk are all factors that underpin our ability to deliver our target of enhanced margins. Our success in the growing design and build market in USA and in EPC power contracts are evidence of this. You heard from David Rutherford about one area where we can move forward both in scale and performance.

We have developed a platform to drive forward in key growth markets. Ian Maclean gave one example of how we can achieve significant growth through the development of key customer relationships - particularly as a business embedded in the local community. We are confident that the economic drivers in our chosen target geographies will provide the environment for strong growth. Organic growth through knowledge transfer and strategic acquisition will each play a significant role.

Our disposal strategy has successfully delivered higher than expected returns and the ability to create further value in the asset portfolio. Sandip demonstrated how our skills are transferable into opportunities that deliver significantly higher returns than we have experienced in accommodation projects in the UK. This validates our strategy to increase the target for gains from disposal whilst continuing to sustain our asset portfolio as a key strength of the Group through reinvestment in future assets and the generation of asset knowledge.

We therefore remain convinced that the strategy we have been following, driven by a focus on infrastructure, a strong commitment to developing our footprint in growth markets and continuing to invest both in expanding our capability in vertical sectors and infrastructure assets will provide greater resilience, drive growth and generate sustainable long term value.

Ian…