Company: **Balfour Beatty**

Conference Title: **Half Year 2011 Results**

Presenters: **Ian Tyler, Duncan Magrath**

Date: **Wednesday 17th August 2011 – 15h00 BST**

Operator: Good day ladies and gentlemen and welcome to the Balfour Beatty Half Year Results Conference Call. For your information today's conference is being recorded. At this time I would like to turn the conference over to Ian Tyler, CEO. Please go ahead.

Ian Tyler: Ok, thanks for joining the conference today. I'm going to spend just a couple of minutes summarising the developments in the period just before Duncan and I take your questions. In the first six months of 2011 trading has evolved broadly in line with our expectations in all of our markets. The diversity and flexibility of our business allowed us to increase our focus on the areas of greatest opportunity and therefore we continue to grow both revenue and order book in tough markets. The order book has grown by 6% over the last 12 months to £15.5 billion. Since year end it has grown by 2%, in line after extracting the impact of exchange and acquisitions. Given the market conditions we believe that this was a good performance. Revenue increased to £5.2 billion representing 1% growth in revenue compared to the same period in 2010 or 3% at constant currency. Acquisitions added 1% to revenue in the period.

Profit from operations before non-underlying items reduced by 5% or 3% at constant currency to £136 million. The impact of acquisitions and disposals broadly offset each other in the period. Pre-tax profits before non-underlying items rose to £138 million, a 4% increase. Underlying earnings per share are up 3% on last year at 14.7p. The interim dividend will be increased by 5% to 5.3p ahead of EPS growth reflecting confidence in our ability to deliver growth over the medium term.

I mentioned tough markets a few minutes ago. I'm not going to dwell on the challenges caused mainly by funding limitations of governments in our major markets as I believe you are all aware, however I would like to emphasise that the actions that we have been taking in line with our strategy have been effective. Firstly we have continued to develop our business. In June we completed the Howard S. Wright acquisition to fill the gap in our US construction coverage on the West Coast of the US which is a significant growth market that is emerging from the downturn. We've also launched our infrastructure funds management business to leverage the skills of our investment and professional services business. Secondly we've increased our focus on markets with the greatest opportunities. In the period we made further progress in renewables while becoming a preferred bidder on our second OFTO asset and this will become a leading investor in the offshore transmission assets.

We are also broadening our capabilities to take advantage of the UK power market which offers substantial value. Thirdly the major cost efficiency programmes we started implementing in 2010 have proven to be timely and effective. We have been rolling out our procurement of back office initiatives successfully and are on track to reach an annualised cost reduction target of £30 million by 2013.

Finally we have sharpened our focus on strengthening our core skills. We are developing the culture and mechanisms to share and transfer knowledge around the group. We believe that combining our skills and building on our asset knowledge gives us clear competitive advantage.

By way of conclusion let me repeat that although there are significant challenges in many of our markets, the nature and magnitude of those challenges are very much as we expected and planned for and consequently we are confident of making progress this year. Looking ahead we will continue to manage the business on the basis that market conditions will remain tough. The clear strategy we have in place, the scale and capabilities being built over the last several years, the actions we've taken in individual markets and the cost measures we started implementing in 2010 will stand us in good stead. We expect recovery in our markets in the medium term and we have positioned ourselves to take advantage of the growing demand longer term for infrastructure across the globe.

Now I will turn the call over to the operator for questions. Thank you.

Operator: Thank you sir. Ladies and gentlemen, if you wish to ask your question today you will need to press *1 on your telephone keypad. Please ensure that the mute function on your telephone is turned off or we will not receive your signal. If for any reason you need to remove yourself from the queue you can do so by pressing *2. Once again to ask a question today that will be *1 on your telephone keypad.

As a reminder ladies and gentlemen if you are attempting to signal for a question today you will need to press *1 on your telephone keypad ensuring that the mute function on your telephone is disabled. As a final reminder if you wish to ask a question that will be *1 on your telephone keypad.

We currently have no questions over the phone.

We will take our first question today from Niamh Lewis of SSGA Ireland. Your line is open, please go ahead.

Niamh Lewis: Hi there. Could you maybe give some clarification around the margins in the professional services division? I guess with Parsons Brinckerhoff being added to that division and that being a higher margin business I suppose we would have expected that that might help boost margins in that division. Maybe you could give some colour around how the integration of Parsons Brinckerhoff has affected margins in that division and what your longer term expectation for the overall margin in Professional Services is?

Duncan Magrath: Hi, it's Duncan here. If I could take the margin comment first and perhaps pass over to Ian in terms of integration. You're right, the Professional Services division is largely the PB business that we acquired. Within there was the old Balfour Beatty management business in the UK that we had and also Parsons Brinckerhoff which is more an architectural engineering firm in the US. In terms of the margins in the first half they were at 4.5% for the first half of the year. That compares with 5.9% first half last year but last year we did have a very high degree of incentive income which we flagged up last year that would be a one-off and wouldn't be repeated. So the 4.5% at the half year, I think that will tick up a bit probably in the second half so that I think the margin for the full year will be slightly higher than that, and that will be broadly in line with the 4.8% underlying margin we had last year. I think going forwards we stand by what we said last November which is that over time we do see the ability to move those margins up for a number of reasons, one around potentially a different mix of business particularly perhaps involving some more of that incentive income that we might be able to leverage through PB; but secondly also working with the rest of the group; and thirdly through just a degree of cost efficiency as well. But perhaps Ian if you talk about how it's leveraged with the rest of the group?

Ian Tyler: Yes, I think our view of the future profitability generally, the margin position and indeed the interaction from the rest of the group of the PB is very much where we were before. I think the business has the capability to deliver substantially higher margins and the management team now are very much in the process of delivering that. That is exactly as Duncan says around cost reduction and heavier focus around the delivery side of infrastructure as opposed to purely acting which they do in the main on the client side. There's a lot of scope in leveraging their capability there. The first half as Duncan said is largely driven by history rather than the underlying position of the business and we are making very good progress within PB in delivering those higher margins, so I'm absolutely confident that we will deliver those in the timescale that we said.

Duncan Magrath: I think the other thing is where they're adding to the capability of the rest of the group, for instance there may be benefits that are within the Construction Services division that would appear in Construction than rather specifically in the Professional Services element as well and over time that will probably increase.

Niamh Lewis: Ok, thank you. Just a follow-up on margin, when I look back at the H1 2010 versus H2 2010 margins, we saw a significant improvement even though you didn't have that level of incentive income in the Professional Services division in H2 of 2010. Would you expect a similar trend of improved margins in the second half of this year?

Duncan Magrath: I think in relation to last year the margin in the first half was 5.9 and the margin for the full year was 5.3, so I think…

Niamh Lewis: Sorry, I meant at an overall level, for the total company margins improved in the second half?

Duncan Magrath: Right. Yes, I think the effects that we would see, we would expect better margins in the second half in the Construction and the Support Services segments as well. There is always a sort of improvement in profitability. Very simplistically we've got broadly in those divisions a sort of 40-60 profit split based on a reasonably even revenue split and that has been very traditional over a number of years, so in a normal cycle the second half will have a higher margin than the first half.

Niamh Lewis: Ok. Could I maybe just ask one more question? You mentioned the fact that the move from public contracts to private contracts in Construction Services would shrink the amount of negative working capital. Could you maybe give some more information around the reasons behind that?

Duncan Magrath: Yes. I guess what I was just flagging up was that I think generally where projects are project financed and that could be public sector projects, there could be other projects that are potentially financed through that way and particularly some projects we did in America. Where the funding effectively goes into the project right at the start through some bank debt etc, then as long as the bank is getting in return, how the cash flow works beyond that, they're more indifferent to. Those sorts of projects we can negotiate in conjunction with the margin and delivery, we can negotiate some good phasing of cash. I think as we see more private sector work probably coming into our order book, the private sector depending on how they fund the project are probably going to be much more focused on the cash flow of the project and consequently their terms might not be so favourable on the cash flow. Ultimately if the cash flow changes then obviously we have to take that into account in terms of the margin which we price the work, so it's all interwoven between the margin and the cash flow element. All I was flagging up was I was thinking just going forwards that at the moment I would anticipate possibly an element of working capital unwinding. The other angle on this is sort of the other end of the spectrum is we do continue to get opportunities where we might look to invest and do the construction financing ourselves and we haven't actually taken up really very many of those at the moment, but that again is a possibility going forwards which would consume working capital as well. So I guess I was flagging up potentially those trends. The latter one would be relatively small.

Ian Tyler: I think really the point that we're making there is that we have seen in particular in that sector working capital as a percentage of sales increase over the last two or three years and I think what we're going to see, we're going to see factoring coming back to where it started from, not the wholesale outflow of working capital.

Niamh Lewis: Ok. So if I was to try and explain it in a nutshell I guess, it's a mix effect of moving to more private than public rather than any kind of change in the structure of a public contractor or a private contractor.

Ian Tyler: Absolutely correct.

Niamh Lewis: Ok, that's great. Thank you very much.

Operator: As a reminder ladies and gentlemen if you wish to ask a question today that will be *1 on your telephone keypad. We have no questions over the phone at this time.

As we have no further questions over the phone I would like to hand the call back to Mr. Tyler for any additional or closing remarks. Thank you.

Ian Tyler: No, just very quickly to say thanks very much for your participation. Obviously any other questions very happy to take them individually. Thank you.

Operator: Ladies and gentlemen, this will conclude today's conference call. Thank you for your participation, you may now disconnect.