HY23 Results

Tuesday, 22nd August 2023

Introduction

Ken Gilmartin

CEO, Wood Group

Good morning and welcome to our half-year results presentation. We're here in London this morning for this virtual event. I'm Ken Gilmartin, CEO of Wood, and I'm really pleased to host you today as we share our latest results. I'm joined today by David Kemp, our CFO. So the agenda for this morning will be a summary of the highlights from the first half from me. David will then present the financials, and I will then talk about how we're delivering on our strategy and the positive momentum that is creating. We will then take our – take your questions at the end. So our standard disclaimer here, for the record.

Highlights

So, starting with a quick overview of the key highlights from the first half of 2023. So, following a transformative 12 months for Wood, we entered 2023 with a clear strategy and a laser focus on performance excellence and predictable delivery. Six months in, that remains, and we're seeing good trading and momentum. So let me talk to a few themes that illustrate my point.

Good trading across business

So, firstly, we've seen good trading across our business in the first half of the year. As David will walk you through, both revenue and EBITDA were up, and we saw much improvement in our operating cash flow. We have increased our full-year guidance today, underpinned by the delivery of our strategy.

Delivering on our strategy

We shared the strategy at our capital markets day last year. I will come back to our progress here in more detail, but highlights include double-digit growth in revenue and pipeline across key focus markets, significant contract wins and a major improvement in employee engagement.

Continuing to build momentum

And finally, we'll continue to build momentum. Our order book was up, our sustainable revenues grew by 20% and we have increased our employee headcount as a key marker of growth.

Retirement of David Kemp

Now, you will have seen this morning that we announced that David Kemp, our CFO, has advised the board of his intention to retire as CFO after 10 years with Wood. I've really valued his support and leadership since I joined Wood, and he has been instrumental in the challenges – in the changes that we have made to transform the company, so let me put on record my thanks to David. He'll remain in post until his successor is in place and will continue to support myself and the board in our strategic delivery. So, with that, I will now pass you on to David to cover our financial results.

Financial Review

David Kemp

CFO, Wood Group

Thank you, Ken, and good morning, everyone. I will now talk you through our financial performance in the half, and I'll cover the strong trading we saw across revenue and EBITDA in the first half, the progress in our order book and our improving cash performance. I'll also cover the increase to our full-year guidance.

Good trading in the first half

Overall, we saw good trading in the half. Both our revenue and EBITDA performance were ahead of the estimate we provided at the July trading update, and that reflected a strong close to the half. We saw strong revenue growth, up 20% at constant currency, and this was helped by a significant increase in low-margin pass-through revenue, and that was about a third of the growth. We delivered EBITDA of 202 million, and that was up 12% at constant currency. The EBITDA margin was lower at 6.8%, but this partly reflects the increased pass-through activity, plus the OPEX investments we're making to deliver future growth. The adjusted diluted EPS of 1.1 cents reflects the sale of the Built Environment, which contributed significantly a year ago, plus a relatively high adjusted tax charge on our results. The net debt was in line with our expectations, and our cash turnaround story remains on track. The improved operating cash performance and consistency of exceptionals reflects this, and I'll come back to this in a few slides.

Revenue up 20% (constant currency)

Looking at revenue, you know, we saw strong revenue growth in the half, up 20% at constant currency. And you can see in this chart that our revenue across all of our business units, with particularly strong growth in Projects, and that reflects the effectiveness of our strategy and the delivery of the strong backlog build last year. The growth in Projects also reflects a weak comparator to last year. The revenue growth was also helped by the increase in low-margin pass-through, which was approximately a third of the growth. Especially pleasing was the growth of our sustainable revenue, which was up 20% to 600 million, and that was despite our pull-back from lump sum renewables projects.

Adjusted EBITDA up 12% (constant currency)

Then on to adjusted EBITDA. An FX impact of around 6 million in the half, so growth at constant currency was 12%, and this was led by strong performance of Projects, along with lower central costs. I'll cover the performances by the business units shortly.

Order book up 5% since December 2022

Our order book at June '23 was around 6 billion, and that's up 5% since December after adjusting for FX and the sale of our Gulf of Mexico labour operations business. As Ken will pick up shortly, we continue to win significant contracts across our business units, and our focus markets reflect our strategy delivering. Growth was most pronounced in Consulting, driven by the strength of our energy offering, but we're pleased how our order book has developed across all of our business units. The strength of our order book gives us in excess of 90% coverage of our revenue expectation.

Consulting: strong revenue growth

So looking at the business units in a bit more detail, starting first with Consulting. We had strong revenue growth of 17% at constant currency, with good growth across energy and across digital. Adjusted EBITDA was 38 million, with the margin lower at 10.6%, and that reflects the exit of higher-margin work in Russia last year, OPEX investments we're making in SMEs in high-growth markets, and the weighting of our energy asset development business performance to the second half. Our energy asset development business develops renewables projects from concept to shovel-ready, and as such this is a low-volume, high-margin business with a lumpy profit stream. The order book was up 8% at constant currency, with good growth right across the business. Looking ahead to the second half, we expect continued revenue growth and a stronger margin, partly reflecting the performance of the energy asset development business.

Projects: strong revenue and EBITDA growth

Moving next on to Projects, here we had strong headline revenue growth of 30% at constant currency, and the growth represents good performance across oil, gas and chemicals, and that's more than offsetting the impact of running down LSTK activities, which were principally in US renewables projects. Around half of this growth relates to increased low-margin pass-through activity, and we are comparing to a weak comparator for the first half of '22. Adjusted EBITDA increased from 81 million to 92 million, with a lower margin reflecting that pass-through increase. The order book was up 2% at constant currency, with lower year-on-year growth following a very strong recovery last year. Looking ahead, we expect slower growth in the second half of this year and a broadly similar margin.

Operations: solid performance

Finally, moving on to Operations, in a very solid performance in the half, revenue was up 9% at constant currency, with growth from higher activity levels and some benefit from pass-through activity. The slightly lower margin reflects this, and so adjusted EBITDA was slightly higher at 77 million. The order book was down 10% at constant currency and down 7% when adjusting for the Gulf of Mexico sale. This reduction reflects the multiyear phasing of large contracts in our Operations business and, due to expected award timing, we expect a stronger second half. Looking ahead, we expect continued growth in the second half and an improved margin, and that's driven by lower pass-through and improving delivery margins.

Significantly improved operating cash flow

Running through our cash flow now. There was a free cash outflow of 219 million, and you can see all the moving parts in this table in detail. Operating cash flow improved by 120 million, and that was despite a 64 million contribution from Built Environment in '22. The improved position was driven by lower provision outflows and a lower working capital outflow. The working capital was an outflow of 94 million, and that was a significant improvement on last year. And we typically have an outflow in the first half, and some of this will unwind in the second half. CAPEX and intangibles was higher at 76 million, and much of this was a phasing between the halves. We expect a total of around 130 million for the year, and that's higher than previously guided, primarily due to additional engineering software licences. Exceptionals were also weighted to H1, and I'll cover these in detail shortly.

Net debt in line with our expectations

Moving on to net debt, net debt was in line with our expectations. We had net M&A flows of 20 million, with inflows from the sale of our Gulf of Mexico and Built Environment completion, and that was offset by the 62 million of tax paid on the Built Environment sale. FX was 20 million, so net debt, excluding leases, was 654 million, and that represents 2x net debt to EBITDA. And, as a reminder, our covenants are set at 3.5x.

Reducing legacy liabilities (unchanged since CMD)

Our expectations around legacy liabilities are unchanged from the capital market day last year. As we've said previously, we expect our legacy liability costs to come down significantly in '23, and again in '24, and further in '25.

On track for positive free cash flow from 2024

So now looking at our cash turnaround story as a whole. This is an update to the slide we presented at the capital markets day last November. The blue shows our operating cash flow, which we expect to grow above EBITDA given our focus on working capital and improvements to come in our Projects business. We saw significantly improved performance already in the half. The bars below the line show CAPEX, which we expect to come down as we complete our ERP implementation, and then we have legacy liabilities, which, as I just walked through, will reduce significantly in '24 to 65 million and will come down to just 30 million in 2025. Adding that all together, you get the inflection in free cash flow in 2024, albeit at a modest level, and then we get significant growth beyond this.

Our capital allocation policy

Our capital allocation policy remains unchanged. It's relatively straightforward and starts with having a strong balance sheet. We articulate this in our medium-term target leverage range of 0.5 to 1.5x net debt, excluding leases, to adjusted EBITDA pre-IFRS 16. Beyond this, we always consider how best to create value for our shareholders from dividends, share buybacks or attractive acquisition. We have made good progress in the first half, and we look forward to updating our shareholders on our thinking on capital allocation, including how to deliver value through dividends or buybacks, alongside our full-year results in March.

Outlook for 2023

So, bringing all of this together, I'd like to take you through the outlook for the group. We anticipate ongoing revenue growth in the second half, albeit a lower level than the first half, with revenue for the full year expected to be around 6 billion. Adjusted EBITDA is expected to be ahead of our original expectations, but within our medium-term target of mid to high single-digit growth. We expect adjusted EBITDA margins to be flat in the nearer term at around 7%, partly as we reinvest in the business to secure growth and reflecting a level of low-margin pass-through revenue activity. On cash, we expect positive free cash flow in the second half of this year, with no change to our expectations for net debt at year end. So, with that, I'll now hand back to Ken.

Delivering on our Strategy

Ken Gilmartin

CEO, Wood Group

All right. Thanks, David. So, underpinned by our consistent financial performance, I'd like to now turn your attention to Wood's strategy and the progress we're making in delivering on it.

Our strategy

So, as a reminder, let me recap the key elements of Wood's strategy to 2025, which we outlined at our capital markets day last November. The pillars of our strategy centre on a commitment to delivering profitable growth; an unrelenting focus on performance excellence, both in the work we do for our clients and in how we manage the business; passion for building an inspired culture that helps us retain and attract the industry's best skills and talent. We're focused on growing in two end markets, energy and materials, with digitalisation and decarbonisation being the cross [cutting drivers] of a competitive advantage in everything we do.

Firstly, in engineering – in energy, we're driven by the need for energy security and a commitment to energy transition, and we are well positioned for growth opportunities in oil and gas, hydrogen and carbon capture markets. Our second core market is materials, where we're focused on metals and minerals, chemicals and life sciences, driven by the demand for sustainable raw materials to enable the energy transition and growth in life sciences post pandemic.

Our strategy is ultimately about focus and prioritisation, delivering for all of our stakeholders by concentrating on where Wood can bring the greatest value and achieve the highest growth. We're nine months into our three-year strategy, and I'm pleased to say we are continuing to make good strategic progress. We're measuring our performance against the three pillars of our strategy. Let me share some of what we're achieving against our targets.

Good progress since our CMD in November 2022

Profitable growth

First, in profitable growth terms, we grew our EBITDA by 12% and saw significant improvement in operating cash flow. Aligned to our commitment to de-risk the business, lump sum turnkey contracts now account for only 1% of our order book. Looking ahead, we will further drive profitable growth by being highly selective in the markets we work in and continue to improve our pricing. We will also optimise our portfolio and, like any good business, continue to review our portfolio to ensure it fits our strategic goals. Finally, and importantly, we will continue to improve our cash generation.

Performance excellence

In terms of delivering performance excellence, we have grown our order book by 5%, we're expanding our global execution centres to deliver global engineering support with more than 3,000 people now in our GECs, and we've seen a 20% increase in revenues from sustainable solutions. Our focus will be to maintain the critical discipline we have established in what work we bid, on further growing our global execution centre workshare model to deliver more for our clients, and of course in growing our sustainable solutions to support decarbonisation, digitalisation and sustainable energy and materials growth.

Inspired culture

When it comes to inspired culture, I am really pleased with the tremendous progress we're making in ensuring Wood is a great place to work. As a people business, this is critical to retention and attraction. We measure our employee engagement via an all-employee survey, and we've seen a 23-point increase on our employee net promoter score compared to this time last year. This is fantastic and real sign of employee loyalty and engagement. Linked to this, we're now seeing lower voluntary employee turnover and continue to make important progress on our gender diversity. Indeed, 35% of our leaders are female, which is up three percentage points, and we're on track to meet our target of more than 40% of leaders in Wood by 2030.

Let me reiterate, we're nine months into a three-year strategy. We're making good strides, with lots more to do. Clarity of priorities, coupled with a strong sense of accountability and high energy levels across our business, lead me to believe we're continuing to build the momentum necessary to meet our longer-term goals.

The opportunity: well-positioned for market growth

Turning now to the markets that offer the greatest growth opportunities for Wood. So our total addressable opportunity in six primary markets in 2025 has increased slightly to $235 billion. The combined market CAGR remains unchanged at around 5%, which we expect to consistently outperform. We categorised our markets into three areas: large markets where we already hold a strong market share and provide solid growth potential, namely oil and gas and chemicals; small markets like carbon capture and hydrogen, which are growing substantially; and the large markets where we are smaller today but focused on significantly growing our market share; and for Wood, that's minerals and life sciences.

Growing and improving our pipeline

So, moving on to our growing pipeline, we've made some great progress here since our capital markets day. Firstly, we cleaned up our pipeline in late 2022 to align with our strategy, removing lump sum turnkey and large-scale EPC opportunities. So, from this position, we've seen double-digit growth in our factored pipeline, reflecting both market growth and increasing demand for what we do: advising, designing and delivering complex projects. The pie chart here shows the market split of our pipeline across our two end markets. This shows you improved diversification, greater balance and that we are growing across both markets. Sustainable solutions now make up one third of our pipeline, and we expect this proportion to continue to grow. And finally, we're seeing some signs of improved pricing. The gross margin bid as a percentage of revenue is increasing. There's a lot of work to convert this to bookings and then deliver, but this is a great early sign that our strategy to prioritise and be selective is working.

Lower risk business model

So a reminder here that we now have a lower-risk business model. Revenue is shown on the left and our order book on the right. So you can see that we're running down the lump sum turnkey exposure, now only 3% of revenue and around 1% of our order book. Most of the work we do is either cost reimbursable or fixed-price services work, and this fixed-price work is across contracts that average less than $10 million.

Contract win: upgrading a global specialty medicine production facility

So let me now bring to life what we do by sharing a few examples of recent work we have won, and these projects showcase the incredible work our teams to deliver to ensure success for our clients. So you'll recall I just talked about life sciences being a large market where we're focused on significantly growing our market share, so a recent project win with GSK in the US marks progress in our life sciences growth and evidences our capabilities. We're working with GSK to upgrade a specialty facility for the production of global medicines under a $50 million contract to deliver engineering, procurement, construction management and validation. Wood won this work because of the strength of our subject matter experts. We have some of the industry's leading authorities in advanced manufacturing for life science facilities and, of course, significant experience in capital project delivery, bringing digital tools and solutions to accelerate the construction of this critical project. And if there's one thing that drives pharmaceutical projects, it's pace to ensure critical health products come to the market.

Contract win: maximising national energy production in Brunei

Turning to oil and gas, so in July we renewed a major contract in Brunei to rejuvenate 20 critical offshore installations, ensuring energy security and efficiency for the region. Bringing our expertise in brownfield engineering and procurement through construction and commissioning, Wood employs around 1,500 skilled employees under this contract. And, as with almost every oil and gas contract we have, we're also bringing decarbonisation solutions to our clients to optimise their assets.

Contract win: designing Europe's largest high-purity manganese facility

The demand for sustainable minerals is increasing, and Wood won a major contract this year by Euro Manganese to deliver a unique mineral project critical to the energy transition. So, in the Czech Republic, Wood is delivering FEED and EPCM solutions for Europe's largest proposed high-purity manganese processing facility. As a mineral used in most lithium-ion batteries, it's deemed a critical mineral, and this is the only significant source of manganese in the European Union today. With mineral reserves of 27 million tonnes, this project could provide up to 20% of projected European demand for high-purity manganese. This innovative project holds real significance for Wood as we continue to lead the development of critical mineral projects with specialist expertise in hydrometallurgy and a passion for designing sustainable energy and materials infrastructure.

Hydrogen and Carbon Capture: Wood has leading capabilities

So I'm also keen to highlight some of the fantastic capabilities we have in delivering hydrogen and carbon capture projects as two of our focused growth markets. So Wood has performed over 175 carbon capture studies. We're helping deliver the world's largest CCUS hub in the Middle East and designing 400 kilometres of CCUS pipeline in Canada today, all of which leads us to play a role in setting industry standards in this space. Looking at what we're doing in the hydrogen markets, our experience in hydrogen goes back over 40 years, and we have designed and delivered more than 130 global hydrogen plants. We have blue hydrogen technology that can capture up to 95% of CO2, which is in demand amongst our clients. Wood is involved in three industrial cluster projects in the UK, and we're working in the US Gulf Coast on feed studies to eliminate 95% of CO2 emissions from some onshore complexes. I'm really pleased with the progress we're making in delivering across all of our key markets.

Sustainable solutions revenue up 20% to c.$600m

Now moving to the sustainable solutions we offer across Wood. So carbon capture and hydrogen are a significant part of this, but, as you can see here, we do lots more. Sustainability is core to what we do as engineers and consultants, and we're passionate about delivering the net zero solutions important to both our energy and materials clients the world over. Wood's skills and expertise are critical to the world meeting its net zero goals, and it's important to remember that we deliberately set a really high sustainability bar for the work we include in our sustainable revenue metrics, based on the principles set out in the EU taxonomy guidelines. All that said, even against a high measurement bar, over $600 million of our revenue in the first half was from sustainable solutions. That's a run rate of 1.2 billion alone this year, and growing at 20%. This is progress, and we will continue to focus on increasing our sustainable solutions.

People focus: Energised and skilled workforce

We've covered how we're delivering in our markets, growing our pipeline and performing. I now want to talk for a minute about Wood's greatest pride: our people. We have around 36,000 remarkable people, delivering some of the most complex and awe-inspiring projects for clients every day, and we continue to grow and attract new people to meet the demand for our expertise. Already we have increased our headcount by 5%. Culture is so important to us strategically. To be able to retain and attract the best in the industry, we need to create a great place to work where people are energised and see opportunities, and that's why it's really encouraging to see our employee engagement score increase so significantly compared to this time last year, up 23 points. And I'm always proud of the recognition our experts receive in the market, and this year we have seen Wood SMEs recognised globally across many areas, with Suzie Ferguson and Valentina Depetri recognised as two of the top 50 women in hydrogen, as an example. And that industry recognition continues with the recent ENR rankings, which showed Wood remains in the top 10 international design firms, with top-five positions across North America and globally across petroleum, industrial and manufacturing markets. All of these steps help us to create an inspired culture for our people and bring significant competitive differentiation to Wood.

Conclusion

So, to conclude, I'll go back to where I started and reiterate what I believe are the important takeaways from our results. We saw good trading across our business in the first half and have raised our full-year guidance. We're delivering on our strategy, as evidenced by the work we're winning and improved employee satisfaction. And we continue to build momentum, with a clear focus on sustainable solutions, an increasing order book and growth in critical expertise.

So, with that, I'll close and move on to your questions, and we'll now hand over to the operator.

Q&A

Operator: Thank you. To ask a question, please press star, one, one on your telephone and wait for your name to be announced. To withdraw your question, please press star, one and one again. Please stand by while we compile the Q&A roster.

We will now take the first question, which is coming from the line of Rachel Fletcher from Morgan Stanley. Please go ahead.

Rachel Fletcher (Morgan Stanley): Good morning, gentlemen, and sad to hear that you're leaving, David. Thank you for all of your help. My question is on the sustainable solutions revenue. So this is up 20% to $600 million. It's now 20% of revenues, I think you said, and 33% of the pipeline. Firstly, I was wondering what drove the sharp increase in this revenue year-on-year. And then, on this topic, is a third of revenues the target level for sustainable revenues for Wood, or are you aiming for a – for a higher proportion of revenue? Thank you.

Ken Gilmartin: Yeah. Yeah. Good morning, Rachel. Great question, and thanks for that. I think, as you – as you outlined, you know, moving from 500 to 600 million, right, so that 20% increase compared to where we were last year, is a significant improvement for us and something that we're really proud of. I think – and we also need to underscore that on the movement that we had away from our, you know, lump sum turnkey renewables pieces of work that we were doing. So what we're seeing, Rachel, is growth in our sustainable solutions across all of our end markets. What we're seeing, however, is particularly strong growth in energy transition. And I think you're right; you know, as we move through our strategic cycle, as we're seeing increased investment in various parts of the world in the areas of energy transition that we're really strong at – carbon capture, hydrogen – you know, that pipeline – the two-year pipeline jumping to 33% is a great indicator. Will we move towards that as we're going through the strategic cycle? Let's see. Let's see how we go, because our platform is a diversified one, but we're very confident that we're going to see continued momentum and traject- – and a better trajectory as we're moving forward on that. So, short answer is yes, we're going to see it continue to grow.

David Kemp: Think the only thing I would add, Rachel, is just to remind you, you know, we have a fairly strict definition of sustainable revenue, so it's – it's really closely aligned to the EU taxonomy. So, as Ken says, we're really proud of the growth we've had. You know, the – it doesn't – it doesn't fully capture everything we're doing in an energy transition space. There's lots of decarbonisation activities that don't meet the definition that are right the way across our business as well.

Rachel Fletcher: Great. Thank you very much.

David Kemp: Thanks, Rachel.

Operator: Thank you. We will now take the next question from the line of Nikhil Gupta from Citi. Please go ahead.

Nikhil Gupta (Citi): Hi. Firstly, I would like to thank David for all the help. My question is, you know, overall, the medium-term guidance is unchanged, but, you know, as I understand, you know, the activity in the factored pipeline has increased. The gross margins or, you know, the pricing is looking to increase. So, you know, just wanted to understand, you know, is the guidance, like, being conservative or, you know, why – why do you see it unchanged, like, over the medium term?

Ken Gilmartin: Yeah. Look – and, again, great question. So, probably a couple of things that I'd point you to here. So – so, first of all, again, we would've always said that we're on a three-year strategic cycle, and, you know, this company is about – is about gaining momentum, discipline, intensity and focus on where – that we want to play, and we're going to continue to do that. And we've always said that, as we go through this strategic cycle, we want to see that momentum increasing, and that's what's reflected in our mid-range guidance. I think particularly as it pertains to pricing, you know, what we are seeing is, in our bidding pipeline and as we're bidding, we're seeing that selectivity and focus and discipline in the areas where we're really good starting to parlay into us being able to bid at higher – at higher margins. You know, where we are as a company, however, a lot of those are in large, multiyear framework agreements. So, from bidding into award, from award turning into purchase order and purchase order turning into engagement takes a period of time for that to really reflect in the performance that we have. So, while we're seeing good signs now, really we're – we are building, and we're building the platform for what we hope will be increased and improved performance as we're moving into 2024.

Nikhil Gupta: Got it. Thank you.

Operator: Thank you. As a reminder, if you wish to ask a question, please press star one and one on your telephone – that's star one and one if you wish to ask a question. And the next question comes from the line of Mick Pickup from Barclays. Please go ahead.

Mick Pickup (Barclays): Morning, all. Quick question on costs in your business. Clear that you're talking about tightening market, bid margins, gross margins going up. Can you just talk about the inflation that you're seeing and how tough it is to get the new headcount growth that you've got in the business?

Ken Gilmartin: Yeah. Thanks, Mick. You know, first of all, let's say, from an inflation standpoint, you know, the one thing that we do point everybody to is how we've de-risked our portfolio and how we've continued to move away from lump sum turnkey work and really doubling down on both reimbursable work as well as fixed-price services. And I suppose why that's important, Mick, from an inflationary standpoint, is means that we're not exposed. And because it's a reimbursable and – a predominantly reimbursable services model that we have, we're able to pass on those inflationary pressures, particularly as it pertains to kind of wages from our staff, to our clients, and our clients are willing to accept that. So I think what we've seen last year and what we've seen this is, you know, minimal or no kind of inflationary pressures kind of pushing through.

You'll have to remind me the second part of the question.

Mick Pickup: No, that – that was it. It was people, pricing and hiring people. Obviously you've had 5% headcount increase [inaudible] –

Ken Gilmartin: Yeah, look, I – yeah, I think, Mick, look, 5% headcount increase, lower kind of voluntary turnover, net promoter score and engagement kind of moving up the 23 basis points – jump significantly from where it was last year – just all underpins that we've got a good strategy, the strategy is resonating with our people, it's resonated with our clients; our pipeline is continuing to build, we've got exciting opportunity. And I think I've always been impressed by Wood's ability to attract new talent. That's been consistent, and that continues to be consistent, in all of the geographies that we serve, Mick. So, that's as a result of just that fantastic brand recognition through the years, the complexity of the projects that we work on, and – you know, and we continue to see that being demonstrated all across the sectors that we work in, as well as all of the geographies that we play in.

David Kemp: We're also seeing our voluntary turnover in white collar coming down slightly as well, Mick, which is another great indicator for us and aligns with all the other people metrics that we're seeing.

Mick Pickup: Thank you.

Operator: Thank you. We will now take the next question from the line of Alex Paterson from Peel Hunt. Please go ahead.

Alex Paterson from Peel Hunt, please go ahead.

Alex Paterson (Peel Hunt): Morning, everybody. I've got three questions, please. Just on your CAPEX, you highlighted that you were – your CAPEX had gone up because of additional software licences. Could you just talk a bit about where these are coming from? Is this a function of more activity, more employees, therefore needing more licences, or are you buying licences in different areas?

Secondly, could you talk a bit about the effect of higher interest rates on your interest costs and also what that means? You know, your – well, I suppose thirdly, your tax rate seemed to be quite high in the first half. Could you talk about what you'd expect for the full year?

And then finally, just on the free cash flow chart that you have put up, it seems to be slightly different from the previous one, because you've explicitly identified CAPEX. Was the CAPEX previously in 'Interest, tax and other', or is that a change on – is there any change to your expectation for free cash flow? Thank you.

Ken Gilmartin: Yeah. Morning, Alex. Maybe I'll take the first one on the – on the licences piece, and maybe then I'll hand over to David for the next two. So, specifically around the licences, there's probably a couple of things that are happening there, Alex. So one is around obviously, as we're growing, headcount is growing, we need more licences, right? So, in order to – for the engineering software and for the – in order to be able to do the designs that we need to do for our clients, so that's one portion of kind of why the – why the licences are increasing. It's a reflection of where we're growing. Also, renegotiating with some of our key vendors and key people as well – there's also a portion of that. So, overarching from a licences standpoint, the main piece is, yeah, uptick in – uptick in demand, which we think is a positive piece.

David Kemp: I've – I'll pick up the other elements. I counted four questions there, Alex, actually, so I'm not sure whether my counting is getting worse with age. Maybe just as well I'm retiring.

I guess, in terms of interest rates, most of our – most of our debt does vary with changes in the base rate. We've USPP debt, which is about 350 million, which is fixed. Our rate just now is – is about 6.7%. You saw the rate in the first half being slightly higher because we'd had increased margins related to the higher covenant levels that we had in the second half of '22, and so that fed through until we had submitted our full-year accounts for '22. So, going forward, just now we're at about 6.7%.

In terms of the tax rate, our expectation is that it will be broadly similar for the full year, and so that guidance was 36%, you'll see in the accounts. Just maybe building that out as a thematic, you know, our tax rate is relatively high just now, and that reflects we're at almost a minimum level of tax just now. And so, within the UK, we're not able to recover all of our withholding tax and our interest just now. So, as we look forward, the opportunity is really around as growth delivers in the UK in particular and the US, our tax rate will start to come down. So the minimum tax rate will stay constant, but our actual rate will reduce.

Your next question I think was on – what was your final one, Alex?

Alex Paterson: It was just on the slide on sustainable free cash flow. You've now explicitly put CAPEX in. That didn't seem to be on the previous charts. Is that – is that a – an addition, or was it previously in the 'Interest, tax and other'?

David Kemp: Yes, no, you're right. It was previously in the – with the 'Other', so we've just split it out to give a bit more clarity. It's maybe worthwhile just building out just where we are and, you know, what we're trying to say in terms of that cash flow slide. You know, firstly, when we look at the first half of '23, there's been some really significant progress. You know, we've seen a bit improvement in our operating cash flow. If you stripped out the Built Environment there, our operating cash flow's improved by over 180 million, driven by lower provisions and lower working capital. So that's been a significant improvement, and you see that coming through as we go through '24 and '25. The exceptionals have remained consistent. You know, there's no change to our guidance around that. We still have to deliver that, but we've got that consistency, so the legacy items are coming in as we expected. You know, the overall picture – we've made some good progress in H1. In the second half of '24, we expect to have positive free cash flow. But we also recognise there's still more work to do. You know, we need to play out the – the legacy items. They'll reduce significantly in '23, '24 and '25, and there's further improvement around our Projects cash conversion. As we've had in an – you know, almost every year really excellent cash conversion in Operations and Consulting. Projects – we're seeing the improvement, but still a bit more work to do there. And we also have some pressure on – from growth, and you picked it – you picked up the CAPEX element of that, but we also have a pressure on our working capital as well, as we continue to grow. And all of that, you know, comes to the overall headline message: we expect to be free-cash-flow-positive in the second half of '23, we have a modest free cash flow for '24, and a significantly more free cash flow in '25.

Alex Paterson: Thank you.

Ken Gilmartin: Thanks, Alex.

Operator: Thank you. There are no further questions at this time. I would like to hand back over to Ken Gilmartin for closing remarks.

Ken Gilmartin: Yeah, well, listen, thanks, everybody, for joining today. Thanks for the quest – thanks for the questions. Look, we announced our growth strategy in November of last year. We set out a plan kind of to deliver on that potential, and I think what we're seeing here is good results –

Speaker: One more question.

Ken Gilmartin: Sorry, we've got one more question. Okay, well, right at the death, one more.

Operator: Thank you. Just one moment, please. The next question comes from the line of Jamie Franklin from Jefferies. Please go ahead.

Jamie Franklin (Jefferies): Hi there. Thank you very much for taking my final question. I just wanted to go back on that free cash flow guidance again. So you mentioned potentially some working capital unwind in the second half. Just want to clarify whether your guidance for positive free cash flow in 2H is on the basis that there will be some positive working capital inflow, and if so, what's the magnitude of that, or should it be the case that operating cash flow will be positive even if working capital is flat?

And then second part of that, if you could just remind us how the working capital profile should change from 2024 onwards as you move away from lumpsum work. Thanks.

David Kemp: Yeah, let me take that up, Jamie. So, we do expect an unwind of part, unwind of that capital built in the first half. And that's included in our guidance for '23 second half in the positive free cash flow. It's probably worthwhile to stepping back and understanding our business. So, typically what we expect in our business is that we build working capital into the summer. So, summer is typically our peak revenue months, and then we release working capital as we come into November-December. And December is typically a lower-revenue month. So that will be the shape of our working capital going forward.

The de-risking element around lumpsum turnkey is largely achieved now. So, if you look in – we pulled out the last unwind of the lumpsum turnkey into our exceptionals cashflow, and so our guidance for '23 is 25 million there. And we don't see any further in '24. So, in '24, our working capital becomes much more straightforward. It's largely driven by DSO, and our DSO varies typically between 65-70 days or that order of magnitude. So, from a modelling perspective, it should be must more straightforward as we go forward.

Jamie Franklin: That's very clear. Thank you.

Operator: Thank you. I would like to hand back to Ken for final remarks.

Ken Gilmartin: Take two. Well, listen, thanks, everybody, again for joining us today. I'll go to the abridged version, which is, look, we've had a very strong first half. We're very pleased that we're in a position to raise a guidance for the year; confidence is growing, there's more to come. Thank you, all.

[END OF TRANSCRIPT]