Q1 Trading Update

Thursday, 9th May 2024

Operator: Good day and thank you for standing by. Welcome to the Wood Q1 Trading Update. At this time, all participants are in a listen-only mode. After the speakers presentation, there will be a question and answer session. To ask a question during the session, you will need to press star one one on your telephone. You will then hear an automated message advising your hand is raised. To withdraw your question, please press star one one again. Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Ken Gilmartin, CEO, please go ahead.

Introduction and Business Overview

Ken Gilmartin

CEO, Wood

Thank you very much. Good morning, and welcome to our Q1 Trading Update Call. So I'm really pleased to be joined today by our new CFO, Arvin Balan. Arvin has been with us just shy of a month now and is already a force for good, making a strong and positive impact in the company.

So, as you will have seen yesterday, we are now in an official offer period. Following an unsolicited preliminary and conditional proposal from Sidara. Wood's board rejected the proposal unanimously yesterday, and, as you would expect, being a public company, we are extremely limited on what more we can say at this stage. What I will say is that our resolute focus remains on business as usual, building on our current growth momentum and delivering against our strategic priorities.

So, accordingly, today, we're pleased to talk with you about our Q1 performance as part of our latest trading statement. And we'll then take your questions.

Key highlights

So I'll start with some of the key strategic highlights from the first quarter of 2024. So firstly, we're continuing to deliver on our growth strategy, with EBITDA growth, margin expansion and a higher order book all being strong signals of success. This strong start to the year supports our confirmed outlook and underlines our confidence in what we are building here at Wood.

Since the start of the year, we've welcomed three new executive leaders to the team with Arvind as the CFO, Marla Storm as CHRO and Michael Rasumuson as Group General Counsel. And in addition to this, Jennifer Richmond was recently appointed as Chief Strategy Officer. This means we now have a new leadership across all of our functions, and I'm really pleased with the strength and the experience of the team.

Our simplification programme, which has been put into place to enhance our growth strategy, is progressing well with the first phase already complete. So as a reminder, our simplification programme is designed to enhance the quality and margins of our business over and above our strategic growth plans. So we expect to generate annualised savings of around $60 million from 2025 onwards, and this will lead to a significant step-up in our margins and will also create a stronger quality Wood as we reduce complexity for our people to do what they do best, which is deliver for our clients.

Financial highlights

So turning to the financials in a little bit more detail, then, the key points to note are adjusted EBITDA was up 4% in Q1 with margin expansion across all business units. This margin performance was a result of improved pricing and our strategic focus on building a higher quality business with our move away from EPC work. Revenue in Q1 was around $1.4 billion, which is 6% lower than last year, and this partly reflects our strategic move away from lump sum EPC and lower pass-through revenue.

So business unit term's, Projects revenue was down because of these key factors and some weakness in the minerals market business. Consulting was broadly flat, and operations revenue was up. So while revenue is slightly down, EBITDA and margins are all up, which to me signals better quality growth.

Business momentum

So I'd like now to talk about the strategic and high-quality work we are winning for our clients. So our order book remains strong. So it's up 9% to $6.2 billion. We continue to see good momentum across the majority of our business, winning work across all our primary markets, delivering energy security, energy transition and sustainable materials. So today, we are a company winning many, many contracts rather than a company banking on a few major contracts. We saw breadth of consultancy wins in the first part of this year, with many high margin front end consulting and technical contracts. Indeed, we were awarded more than 1,300 consulting scopes in Q1, including being selected by Woodside Partners as the consultant for the Greater Sunrise development in Asia Pacific, which is a really exciting project.

We also saw the award of a number of highly complex EPCM contracts for oil and gas and chemicals, as well as several critical operations contracts for maintenance, brownfield engineering and specialist decarbonisation solutions, like flare gas recovery on offshore platforms. This is evidenced by a recent decarbonisation contract with TotalEnergies here in the UK for exactly this.

One market we are seeing some signs of weakness is minerals, with some of our clients delaying projects. We continue to grow our sustainable solutions, and our pipeline reflects around 40% of sustainable opportunities, which is really encouraging and reflective of our client spend in energy transition and the demand for sustainable materials.

Simplification 2024

So let me talk to the progress we're making in our simplification programme, which we launched in March. And as I said, the programme is designed to drive higher margins over and above our pre-existing targets. So in the first phase of the programme, we focused on streamlining our central functions and putting more ownership and accountability for priority functional activities into our business units, in turn reducing the number of functional roles and reducing central costs. So the second phase of the programme is focused on reducing complexity in our processes and procedures, making it simpler and faster to get things done and reducing our external spend. So as we previously shared, we expect to realise annualised savings of around $60 million from 2025, with around $10 million of savings in 2024. I'm pleased with the progress we're making to deliver the programme, and the first phase to reduce central functional costs is now complete.

2024 Outlook

So our continued progress means that I remain really positive and indeed excited about Wood story this year. So following this Q1 update, we're confirming our full year EBITDA outlook for 2024. And that means high single-digit growth in adjusted EBITDA. Operating cash flow is expected to continue to improve, partly through improved cash management across our business. And net debt at December 2024 is expected to be at a similar level to December 2023, after the proceeds from planned disposals, which are due to complete in the second half of this year.

2025 Outlook

And finally, I want to emphasise what we're building here at Wood. We're a business in strong markets, trusted client relationships, a deep talent pool, and we are improving the quality of our business, reducing our risk profile, expanding our margins and we are laser focused on returning to cash generation. We continue to expect EBITDA growth in 2025 to exceed our medium-term target, with an annualised benefits from our simplification programme of around $60 million on top of growth consistent with our strategy. With this improving profitability and continued improvements in cash conversions, we expect to deliver significant free cash flow in 2025. Arvind will be driving this cash focus across the group and already has many ideas that he's looking forward to discussing with you all.

So with that, Arvind and I will now take your questions.

Q&A

Operator: Thank you. To ask a question, you will need to press star one one on your telephone keypad and wait for your name to be announced. To withdraw your question, you can press star one one again. We will now take our first question. Please stand by. And the first question comes from the line of Alex Smith from Investec. Please go ahead. Your line is now open.

Alex Smith (Investec): Morning, guys. Thanks for the call this morning. Just a quick one. You alluded to pricing power coming back into your comments there. I’m just wondering, that's been mentioned by a few of your peers. Is that thematic that we could see growing through 2024 and beyond?

And then just a second question on the Ethos disposal, you said expected in H2 and expect net debt to be roughly flat year-on-year. So just, maybe you give some colour on how that process is going or anything more you could give would be great. Thank you.

Ken Gilmartin: Yeah, thanks for that. Alex. I think back to the first part of the question, yeah, we are seeing improved ability to win margin across all of our business units. Part of that is due to the selectivity of where we are choosing to play. Or said another way, Alex, where our clients really understand how we're differentiated and the complexity of the design that we do, that we're able to start to generate better premiums on that.

I think the other piece to this is, yes, we will see, and we expect to see, a continued improvement there as we go through 2024 and on into 2025. As we said in the comments, Alex, we are materially improving the quality of the business, and that's going to parlay into better margins.

I think on the second part, as it pertains to Ethos, look, I think we've said we're looking to see that close in the second half. It's a process. It's moving well, no further updates that we could give or – at this point, but as in comments, expected to close in the second half.

Alex Smith: Great, thank you very much.

Operator: Thank you. We will now take our next question. Please stand by. The next question comes from the line of Guilherme Levy from Morgan Stanley. Please go ahead. Your line is now open.

Guilherme Levy (Morgan Stanley): Hi. Good morning everyone. Thank you for taking my questions. I have two, please. The first one, as a follow-up to the question before on the change on the net debt guidance for the end of this year, has something else changed compared to a couple of weeks ago in terms of working capital expectations? Anything that you can say that that is behind that change on the net debt guidance would be great.

And then the second one, on your order book, could you maybe try to strip out for us how much of the order book one year ago compared to now came in the form of pass-through activity, just for us to try to estimate the type of growth that you are seeing year-on-year without that component. Thank you.

Ken Gilmartin: Yeah, thanks for that Gui. So first of all, back to the net debt. So look, as you've said, look, we now expect net debt December 2024 to be at a similar level to December 2023 after the proceeds from the planned disposals. I think that the main driver for this really is working capital. So I think we've seen a little bit of weakness in the minerals. We're also going to see a waving in the second half as we start to recover from a revenue standpoint. And of course, as that starts to recover in the second half, we're going to see a little bit of pressure in working capital as we're trying to get to collectibles.

I think the other bit is – that we're working on is that continued increase in strengthening our cash management and really continuing to drive down that DSO, particularly in our Projects business. And I think that's the real change.

I think, to the second part, I think really when you look at order book, maybe the way I'll put it in our order book and see where the growth is and maybe break it into our business units a little bit. Strong in consulting, up double digits. Our consulting business, however, is becoming more of a book-and-burn business with shorter duration. So while that's really encouraging and gives us a lot of confidence for where we're going in the second half, it's less of an indicator for us now because of that short three-month duration. Significant uptick in operations as well, long-term contracts, double-digit growth there. The area where we're looking and where we need to continue to press is in Projects. Good growth in oil and gas, good growth in process and chemicals, some weakness in mining and minerals. Predominantly where we're seeing that play out is clients delaying spend. So the macro in minerals, from a strategic direction, still remains very positive. The world needs the minerals on this journey to net zero. We're seeing some shorter-term headwinds as clients are just not progressing with projects at the pace that we had anticipated.

Guilherme Levy: Thank you.

Operator: Thank you. We will now take our next question. Please stand by. And the next question comes from the line of Richard Dawson from Berenberg. Please go ahead. Your line is now open.

Richard Dawson (Berenberg): Hi. Good morning, guys, and thank you for taking my questions. Just a follow-up to the previous question on working capital. I just wanted to understand what actions are being undertaken to improve that working capital management. And given results are expected to be H2 weighted, how much influence can you actually have on accelerating those cash collections if the work is done towards the end of the year?

And then secondly, I appreciate there's only so much you can say regarding the Sidara bid, but has the approach and the second approach in second year, has that changed any of management's priorities at all, for example, potentially bringing forward shareholder distributions or any change to the strategy? Thank you.

Ken Gilmartin: Yeah, maybe I'll start with the second question, and maybe then I'll hand over to Arvind, who can talk a little bit about working capital and some of the measures that that we're taking, we're initiating. Look, obviously, the news from yesterday, I really can only repeat what we said yesterday. So just for all of you, we did receive that unsolicited. And it was a preliminary and conditional proposal from Sidara and a possible cash offer of 205p. The board carefully considered the proposal, together with its financial advisors, and we concluded that it fundamentally undervalued Wood and our future prospects. So accordingly, the board rejected the proposal unanimously yesterday.

I think from a company standpoint, we're still in the second year of a three-year strategic turnaround. We have generated significant momentum in the business, and we're continuing to be very robust in driving what has been really strong performance and growing the business, growing the margin profile, continuing to be very selective in the areas that we work. And by doing that, demonstrating consistent, superior value to our clients. Build momentum, we're going to continue to do that, and that's going to be the focus for all of us as we go through this period. Continue to grow the business and return to significant free cash flow in 2025.

With that, maybe I'll hand over to Arvind.

Arvind Balan: Thanks, Ken. And thanks, Richard, for that question. So, in most of the transformations that I've seen and in – like ours, we are at that point where the focus has been on higher quality margin, and now there has to be a pivot into putting focus more on cash. That is essentially where most of our energy is going. So we've got a whole series of actions right from simple ones around changing the way we design our internal management information, the cadence at which we look at cash, into, if you like, tighter ones, which really drive behaviour and drive incentive within the organisation. But the focus is there. I've got an eight-point plan, which we're already executing at the moment.

Fundamentally, our working capital is very lumpy. A big chunk of our payables goes out quite early in the year, and a big chunk of our receivables comes in the back end of the year. And essentially, that means our predictability around working capital is low. And so the levers we have to actually pull become very weak as we get to the end of the year. So we're looking at the shape of the working capital curve. We're looking at the steps that we take and definitely putting a lot of focus on it. But your question is, 'Can you pull it off this year?' That's a difficult one to answer. There are lots of variables in that space. Of course, our intention is to do as much as possible early, but you'll have to give me a bit more time to come back with a very clear view on how long this will take to take effect.

Richard Dawson: Perfect, thank you very much. And I just wonder if I just have a quick follow-up just on the net debt as well. I mean, so obviously you mentioned the working capital there. And the other part to that is the disposals. Is there any change in your view on what your potential cash proceeds are for those disposals?

Ken Gilmartin: No, no change at this point.

Richard Dawson: Perfect. Thank you very much.

Operator: Thank you. We will now take our next question. Please stand by. The next question comes from the line of Mark Wilson from Jefferies. Please go ahead. Your line is now open.

Mark Wilson (Jefferies): Thanks. Good morning, gentlemen. And my first question, it follows on from what has just been asked about working capital. One question I'd like to say on that is when you speak to such a broad-based set of projects across the company, why would working capital and receipts not be more spread across the year? And frankly, why is it that prediction of such things does seem to be a moving target?

Ken Gilmartin: Yeah. Thanks, Mark. Good question. Look, I think the way to answer that is as a company, very strong discipline, very strong focus, really driving to half year performance. I think part of the piece that we have and part of the nine-point plan that Arvind – that we're working on at the moment is making sure that we're changing that cadence, that rigor, that discipline to be much more week-on-week focused rather than really driving towards the half year. That's a change. That's a significant change for us, Mark. That's going to take a period of time for us to drive through the organisation, but that's the path that we're on.

Mark Wilson: Okay, that's good to hear. Then more broadly based, you spoke, Ken, about the revenues and work you've seen in sustainability, good growth in oil and gas and, okay, maybe some shorter-term headwinds in minerals. One theme we've seen broader in the industry, in the conventional oil and gas, is the international growth in offshore versus somewhat softer US onshore expectations. Now, this offshore side of things has been quite a tailwind for various companies. Can you speak to Wood's exposure to that? And I think I'm talking beyond, say, North Sea O&M projects. Thank you.

Ken Gilmartin: Yeah. Look, I think that's a fair question. I think, again, very proud of our of our ability to win work, very proud of our long-term relationships with our key clients in the oil and gas space, and also very proud of our ability to be able to provide those specialised engineering services in offshore CAPEX. So what we're seeing, Mark, is in offshore, really strong growth in our consulting business, looking at various services that we provide there. What we're also seeing in our projects business is decent growth as we're looking at the offshore component. I think the bit that where we're seeing probably more growth for us though, when you look across all of our portfolio, is that continued growth in brownfield modifications, right? So really looking at squeezing more out of existing installed assets, both offshore and onshore, and we're really, really happy about our position in that. It's highly specialised, high barrier of entry for competition, really strong relationships, something where we've got a differentiated offering, and that goes across all – well outside of the North Sea and into other geographies that we serve. And it's a higher margin, low risk business. That's the other piece that's very key for us. So a growth vector for us for sure.

Mark Wilson: Okay. Thank you. I'll turn it over, and welcome Arvind, and good luck with it sir.

Arvind Balan: Thank you.

Operator: Thank you. We will now take our next question. Please stand by. And the next question comes from the line of Mike Pickup from Barclays. Please go ahead. Your line is now open.

Mark Pickup (Barclays): Good morning everyone. A couple of questions, if I may. Firstly to Arvind, obviously you've mentioned working capital as an initial focus, but I think Ken mentioned you've got several ideas. Can you talk about the areas you're looking at? Obviously you've inherited a simplification programme. Can you just talk about what are some of these ideas you're thinking about?

Arvind Balan: All right. I'll rattle on through my notes, Mick, for you, but I'll just give you a flavour, right? Changing management information to be first cash, then everything else. Changing the frequency at which we performance-manage to going to weekly on cash. Changing the metrics that we have to track cash to track recoverability. Smoothing out the payables and receivables curve in a way that we spend after we earn. Looking at cutting some optional costs, like less travel, etc. Teach-ins. A large chunk of the management, if you like, if you go down the organisation, understand revenue and profit, but perhaps need to truly understand the balance sheet and what it means so when they talk to clients, they can trade between margin and cash. So education. Tweaking the incentive mechanisms that we have where we put a much greater focus on cash collection; you don't collect cash, you don't get paid incentives. I could go on, but that's the plan.

All that's in play already. But I don't want to leave you with the idea that it's about doing these things. It's ultimately about changing a culture where you have the whole organisation who understand cash. Everyone in the top 100, 200 in the organisation understands what that cash position is, understands what they need to do and is able to find that balance between growth and cash. And that cultural change will come as we start embedding these changes in process, metrics, KPIs, cadence, etc. And we'll have to wait till you get that switch. But I'm fairly confident that we'll get to that point.

Mark Pickup: Okay. Thank you. And Ken, I think you mentioned in one of your earlier answers, your clients are just slower on projects than you thought. What do you think is holding them back?

Ken Gilmartin: Yeah. Morning, Mick. That was – that commentary was mining and minerals. That was in the mining and minerals space. And I think there's probably a few things that are pushing. It’s probably fair to say that when you look at commodity prices, there's been some fluctuation there. So there's been a little bit of delay with some of our larger clients going after some of those projects. We don't think it's a macro. We think it's a timing issue, Mick. I think the vector in mining and minerals still remains really strong. I think the growth targets that we have in our five and ten-year plan remain really strong. But it's short-term headwinds in the mineral space, Mick.

Mark Pickup: Okay. Thanks a lot. Cheers.

Ken Gilmartin: All right.

Operator: Thank you. We will now take our next question. Please stand by. And the next question comes from the line of Alex Paterson from Peel Hunt. Please go ahead. Your line is now open.

Alex Paterson (Peel Hunt): Yes. Morning, everybody. Could I just ask three questions, please? Firstly, just on the disposals. Could I clarify? Clearly, you're looking to sell Ethos in the second half of the year. Are you also expecting to make the other smaller disposals in the second half, or do you think they will come later?

Secondly, if net debt is flat year-on-year after disposals, but clearly you've sold some businesses so your EBITDA would be lower because of that, then your net debt to EBITDA is actually going to be higher. With your positive free cash flow in 2025, would you expect that net debt to EBITDA to fall again in 2025?

And then lastly, just on that weaker minerals comment, you mentioned it was minerals relating to net zero. Are they sort of all sustainability projects, or is it something else, please? Thank you.

Ken Gilmartin: Yeah. Thanks. Thanks for that, Alex. All right. So the first question was on disposals. It was Ethos and the other smaller disposals. Yes, we expect both Ethos and the smaller disposals to be executed in the second half of the year.

Second question was around net debt and I think – 2025 net debt. Yes, we will expect to see that going down in 2025.

And then the final question was around the mineral processing piece. I think that the nuance there, Alex, is where we play in minerals is where there's a high degree of chemical processing required to look at those minerals. So think, a copper goes through a copper concentrator. And typically what we're seeing as well is in that – where that chemical processing is high, it is generally minerals associated with that journey to net zero. I think there's an overarching piece, just delay in the minerals and mining sector as an overarching piece. But where we're playing is where there is that high degree of chemical processing to be done. That's where we differentiate, and there's also consistent delays there. The macro is still very strong.

Alex Paterson: Thank you.

Ken Gilmartin: Thanks.

Operator: Thank you. As there are no further questions, I would now like to hand back to Ken Gilmartin, CEO, for any closing remarks.

Ken Gilmartin: Yeah. Listen, thanks very much, everybody, for your questions and listening this morning. Again, good momentum, good Q1 with a lot of more opportunity for us to continue to improve. So we look forward to talking to you all again soon. Have a great week. Thanks.

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