Full Year Results Announcement

ASX & media announcement

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Highlights

- **Underlying trading NPAT of $5.4m up 29% on FY15**
- **$41.8m cash and no debt at 30 June**
- **Fully franked final dividend of 1.35cps maintains full year dividend at 2.70cps**
- **Secured a number of strategically significant contract awards**
- **Transitioning from construction to maintenance phase in resources**
- **Datatel acquisition provides scalable telecommunications platform**
- **Targeting further acquisitions to deliver strategic diversification**

Southern Cross Electrical Engineering Limited ("SCEE") today released its results for the year ended 30 June 2016 announcing an underlying trading net profit after tax of $5.4m after adjusting for acquisition costs in the year. This represents a 29% increase on the prior year underlying trading NPAT. Statutory net profit after tax for the full year was $5.1m.

SCEE also actioned a number of strategic diversification initiatives during the year including organic entry into new sectors and the acquisition of Datatel which provides immediate entry into the communications and telecommunications markets, offering significant growth opportunities across Australia as the NBN roll-out gathers pace.

<u>2016 Full Year Results</u>

Revenue for the year was $207.6m, down 13.7% on prior year underlying trading revenue[1]. The Datatel acquisition was completed on 29 June 2016 and made no contribution to FY16 trading results.

Activity in the first half of the year was high as a result of contributions from construction projects at CITIC Pacific Sino Iron, Samsung Roy Hill and Tecnicas Reunidas TAN Burrup. These projects were successfully completed and closed out during the second half of the year. Work continued throughout the year on BHP Billiton Iron Ore Sustaining Capital projects, Rio Tinto Iron Ore Electrical Infrastructure Replacement and Bechtel Australia Pacific LNG at Curtis Island. SCEE also performed works for Western Power under their Major Works Panel as well as a number of jobs for industrial clients.

Gross margins for the year were 16.1% compared to underlying trading gross margins of 14.8%[2] in FY15 and were driven by strong performance on the larger lump sum construction contracts that completed during the year.

Underlying trading overheads for the year were $21.4m after adjusting for $0.4m of costs relating to the Datatel acquisition, down $0.9m against underlying trading overheads[3] in the prior year. Cost control remains a priority and a streamlining of the organisation structure towards the end of the year combined with various productivity initiatives, such as growing assistance from our new Philippines Support Centre, is expected to result in further efficiency gains in FY17.

Depreciation expense decreased by 30% to $4.8m as a result of a combination of the asset rationalisations in FY15 and lower capex spend in more recent years.

Underlying trading NPAT for the year was $5.4m after adjusting for the Datatel acquisition costs noted above. This represents a 29% increase on FY15 underlying trading NPAT of $4.2m[4].

The Company maintained a strong balance sheet throughout the year and at 30 June 2016 had cash of $41.8m and no debt. This has been achieved after absorbing cash outflows of $6.6m to complete the Datatel acquisition.

The acquisition has resulted in the recognition of additional goodwill of $12.3m and an $8.7m non-current liability for the payment of deferred consideration which represents our assessment of the fair value of potential future earn-out payments. Approximately $2.5m of net tangible assets were acquired and these have been included in the 30 June balance sheet.

The Board has declared a fully franked final dividend for the year of 1.35 cps which maintains the full year dividend payment of 2.70 cps at the same absolute level as in the prior three years. The franking account balance at 30 June 2016 was $18.5m.

<u>Outlook</u>

SCEE entered FY17 at relatively low activity levels as a result of successfully completing large scale iron ore construction projects early in the second half of FY16 and consequently the order book at 30 June was $24m which as a headline number is lower than in previous years.

However the Company has recently secured a number of strategically significant contracts which are providing greater visibility of activity which is forecast to ramp-up over the coming months. These include:

- KSJV, SCEE’s LNG-focussed joint venture, has secured a contract with Bechtel to deliver electrical and instrumentation installation services on the Chevron-operated Wheatstone Project;
- A Master Services Agreement with Newmont Mining Services for the provision of general electrical services at the Boddington Gold Mine in Western Australia for a three year term;
- Datatel has been awarded a new Master Subcontract for NBN construction works and has commenced work in both Victoria and Tasmania; and
- SCEE’s first transport infrastructure award for approximately $2m of electrical works on a freeway project.

Unless stated otherwise the contracts have been awarded on a zero-value basis and set out the terms under which work will be performed. Initial work orders have been received and first personnel mobilised on these projects.

The Company also continues to win work under its existing framework agreements with major iron ore and CSG clients as well as securing a range of minor awards in the resources, infrastructure and industrial sectors on both the West Coast and East Coast.

It should be noted that the market move away from large scale lump-sum contracts to smaller projects of shorter duration and almost immediate lead times awarded under framework agreements generally has a moderating effect on the headline order book number. Importantly this order book number does not include any estimate of future revenues to be derived from reimbursable or recurring works which are a significant part of forecast activity.

Tendering activity across the business remains high with the Company’s diversification into new sectors resulting in a broader pool of work being targeted.

Markets

Conditions in the resources sector are not expected to change significantly in the near term although visibility of some larger capital projects has returned to the medium term pipeline from expenditure to maintain production levels in iron ore and new investment in certain commodities.

In mining SCEE continues to perform work in the iron ore, gold and copper markets and expects LNG construction work to carry on through FY17. The capability and capacity to perform large scale international work has been retained and strategically appropriate opportunities will be tendered as they arise.

The NBN roll-out will continue to ramp up significantly. In addition wireless networks and data providers are also investing heavily in their capacity and technology driving forecast construction spend across the Australian telecommunications sector of over $30bn by 2019. The acquisition of Datatel gives SCEE immediate market entry into the sector and a platform which can be used to achieve national expansion.

Datatel also brings an opportunity to leverage their presence in the education, health and commercial sectors, where they perform electrical services works, and to broaden SCEE's service offering to existing clients.

In the utilities sector SCEE continues to perform works for Western Power under their Major Works Panel and has the capability to expand this offering to other utilities providers.

SCEE has a history of successfully delivering large scale construction projects in the resources sector and these skills are transferable to other sectors with a significant identified pipeline of opportunity. In the transport infrastructure sector there is over $100bn forecast construction spend in Australia by 2019 while social and commercial infrastructure has forecast construction spend of over $80bn in the same period. SCEE's award of freeway works is a first entry into the transport infrastructure sector.

Strategy

SCEE primarily sees itself as an electrical contractor. The Board's strategic objective is to create shareholder value by:

- Transitioning to a sustainable resources business through exposure to sustaining capital and maintenance markets; and
- Growing through expansion into adjacent and complementary sectors and new geographies.

As the resources sector shifts from the capex phase to a sustaining capital and maintenance phase it is essential that the Company aligns with this change in order to continue its long term relationships with major clients. A number of key framework agreements are in place and activity is expected to increase as the year progresses. Regional offices have been established in key locations and opportunities to widen existing service offerings to clients continue to be evaluated.

Having completed the acquisition of Datatel at the end of the year focus has now turned to driving profitable growth from the business as it expands nationally.

Management is continuing to invest significant effort into investigating further acquisition opportunities aligned with achieving sector and geographical expansion in the markets discussed above.

CEO Comment

Commenting on the results, SCEE's CEO Graeme Dunn said "I am pleased to be able to announce a solid full year result with a 29% increase in underlying trading NPAT.

This has been achieved in competitive market conditions with the last expansion projects for the time being in the Australian iron ore sector completed during the year. The resources sector continues to move from the capex phase to a sustaining capital and maintenance phase and the Company has taken actions that will help us better meet clients' changing needs and allow us to maintain a sustainable resources business.

2016 has also seen us perform some other important strategic actions that will stand us in good stead to grow in future years.

We are now active in a diverse range of sectors, both organically and via the acquisition of Datatel.

Datatel gives SCEE immediate market entry into the telecommunications sector and, by combining SCEE's resources and their operational excellence, a platform which can be leveraged for national expansion outside of WA. The commencement of Victorian and Tasmanian works validates this vision as the NBN roll-out accelerates.

We are actively evaluating other acquisition opportunities that would further broaden our geographic and sector footprint and enter 2017 with a strong balance sheet capable of supporting these growth initiatives.

We have continued to manage our cost base through significant efficiency initiatives to ensure that it remains appropriately sized for our activity levels."

Notes

1 – Statutory revenue for the year ended 30 June 2015 of $238.3m included $2.3m of claims write downs which have been excluded from underlying trading revenue.

2 – Statutory gross profit for the year ended 30 June 2015 of $33.0m included the $2.3m of claims write downs noted above and $0.3m of inventory write downs which have both been excluded from the calculation of underlying trading gross margin.

3 – Overheads for the year ended 30 June 2015 included $1.1m of organisational restructuring costs which have been excluded from the calculation of underlying trading overheads.

4 – Statutory NPAT loss for the year ended 30 June 2015 of $9.8m included $2.3m of claims write downs, $0.3m of inventory write downs, $2.3m of organisational restructuring costs, $1.3m of lease provisions, $1.4m of asset write-downs, $8.4m of goodwill impairment and $2.0m tax benefit relating from these items. All of these have been excluded from underlying trading NPAT.

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