Emeco

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ASX: EHL ('EMECO' OR 'THE COMPANY')

Managing Director's Annual General Meeting Address and 1H20 Guidance

Thankyou Mr Chairman.

Good afternoon everyone.

At last year's AGM, I outlined Emeco's strategy for FY19. This included continuing the increase in our fleet utilisation and rates, whilst managing costs to improve margins. We also highlighted our focus on asset management and expanding our asset maintenance capabilities to extend component lives. The aim of these initiatives was to maximise our return on capital, generate strong cash flows and to continue to aggressively deleverage the business.

FY19 recap

As our Chairman touched on, one area which demands continuous improvement in the business is safety. Although we incurred no lost time injuries during FY19, our total recordable injury frequency rate disappointingly increased from 1.2 to 4.6. We take this very seriously and, in response, we have significantly increased our safety resources and taken actions to enhance our health and safety systems, processes and reporting. We will continue to emphasise our target of zero harm and management is dedicated to reducing workplace injuries.

I am otherwise proud to talk though our FY19 results and our success in achieving our strategic objectives.

Emeco achieved strong growth in FY19. FY19 operating NPAT was up 214% on FY18 to $63 million. The Company generated operating EBIT of $125 million and EBITDA of $214 million. This is an increase of 51% and 40% on FY18, respectively.

Operating EBITDA margin increased 590 basis points to 46.1%. This was driven by increases in operating utilisation and rates, tightly managing costs, and realising the benefits from the Force and Matilda acquisitions.

On the back of the strong profitability in the year, Emeco generated free cash flow of $90 million. This is before our investment in growth capex of $85.1 million, but net of our sustaining capex of $88.5 million, which is mainly engine and component replacements on our existing fleet.

Facilitated by technology, and supported by rigorous engineering and commercial analysis, Emeco invests heavily in its asset management tools to ensure we monitor component health and optimise our major component replacement plan, identifying opportunities for improvement compared to industry practices. We have successfully extended the useful life of many of our major components. Combined with our high-quality Force workshops expertise, we are also able to undertake the works cost effectively. We will continue to adopt asset management best practices to maintain our commitment to delivering our customers cost effective, high reliability equipment hours for their project requirements.

Emeco's strong free cash flow enabled us to invest in a package of strategic growth assets during the 2019 financial year. It was our vast global procurement network and the Force workshop rebuild expertise which allowed us to take advantage of these key assets required to optimise our fleet configuration. These are high demand assets which are expected to achieve 17%-20% IRR through their economic life.

In addition to this growth investment, we also reduced our gross debt by US$33.8 million in FY19, decreasing our ongoing interest expense.

Emeco's growing earnings and cash flow reduced our net leverage to below 2.0x at the end of FY19, down from 2.6x in FY18. Deleveraging to 2.0x is an important milestone in our deleveraging journey, and was achieved a year earlier than forecast.

In addition, executing on our operational and financial goals resulted in a historically high FY19 return on capital of 21%. This is up from 13% in the previous cycle peak.

FY20 update and outlook

The Company has had a strong start to FY20.

I am pleased to advise that we are currently expecting Emeco's first half operating EBITDA to be between $118 million and $120 million, with further earnings growth expected in the second half.

Growth in revenue and earnings in FY20 is both from rate and utilisation improvement on our existing fleet, together with the additional earnings generated by the growth assets acquired in FY19.

The Western Region has secured new work in iron ore and gold projects. The team has been very focused on project-managing the preparation and redeployment of assets from completed projects into new projects. I am pleased with how quickly these assets have been put back to work. Recovery and growth of the Western Region is gaining momentum and aligns with our strategy of diversifying our commodity exposure.

Demand in the Eastern Region continues to be robust, particularly as we see customers remaining disciplined with capital expenditure allocation. As a result, utilisation in the Eastern Region remains high, particularly in metallurgical coal. Our projects in thermal coal continue to provide us with stable earnings.

The growth assets acquired are now all working across various projects and remain on track to generate $25 million in EBITDA this financial year. These growth assets have expanded our earnings capacity, and do not replace any of our pre-existing rental fleet working at existing projects.

In the Force workshops, FY20 is about building on the excellent growth we generated in FY19 as a result of capacity expansion across the regions. We will continue to concentrate on increasing throughput in the workshops, both with our internal fleet requirements and also for our customers.

We believe there are synergies between our rental and maintenance businesses which allow us to provide our customers with a complete solution from our assets, our asset management capability and our highly skilled workforce.

Strategically, we continue to carefully pursue opportunities to further build on our business model and widen our value proposition to achieve growth and sustainability. The Force workshops have been a transformational acquisition for us and we are exploring how we can expand our offering and provide more services and value to our customers.

In addition, although coal (and that's primarily coking coal) continues to contribute to Emeco's growth, we are consciously driving growth in other commodities such as iron ore and gold, particularly with the opportunities we are seeing in the Western Region.

Management and the board also remain committed to deleveraging and reducing the gross debt of the business. We are expecting to generate strong cash flows in FY20 and beyond. This will allow us to reduce our gross debt and we also expect the pace of deleveraging to accelerate in FY20, with leverage expected to be 1.5x by the end of FY20, and targeting 1.0x by the end of FY21.

Emeco's strategy is very clear – we are ensuring the business is more stable and resilient through the cycle.

Our management team believes the business is on the strongest footing it has been in in years and we hope to reward shareholders for their support with dividends in the future.

Thank you

In closing, I would like to thank our shareholders, debtholders, customers, suppliers and advisers for their support over the year.

I would also like to thank my fellow directors and the whole Emeco team for their ongoing dedication and hard work.

The future is very exciting for Emeco and we look forward to the year ahead.

Ian Testrow
Managing Director & Chief Executive Officer

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