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11 November 2021 – AJ Lucas Group Limited AGM

Group CEO Address – Brett Tredinnick

Thank you all for joining us today for the 2021 annual general meeting. While we are not meeting in person, I hope to still be able to provide you with valuable insight into your company's progress.

As you know, AJ Lucas is essentially two separate businesses. In Australia, we operate a highly respected and profitable drilling business, while in the UK, we hold the largest area of petroleum exploration licences onshore England. The different businesses have a markedly different impact on our performance and are affected by very different external factors.

I will start today by providing an overview of our group's financial performance in the year under review before highlighting some of our achievements in the drilling business. Finally, I will conclude with an update of the UK operations and some of our priorities for the current year.

Before jumping into the detail, I would like to acknowledge the contribution of the 400-plus Lucas employees and our long-term loyal customers who both have made our results over the last 12 months possible.

Many of you will recall that in July 2020, at the start of the year in review, the world was still learning how to deal with the pandemic. Now, here we are today, 16 months later, with high vaccination levels, nearing the end of broader restrictions and talk of a return to international travel, what a period it was.

The pace and efficiency at which our people adapted to the challenges of the pandemic is one of the key reasons we were able to deliver a positive financial result for the year. We continue to prove we the most dynamic and capable team in our industry, and this will continue to be a competitive advantage for us well into the future.

Financially, the year to end of June 2021 was a good one in the unusual and trying circumstances that confronted us all. The result was built on the underlying strength of our drilling business with a continued focus on well construction times, the restructuring of our cost base, a favourable foreign exchange gain and receipt of R&D credits in the UK, all contributing to the turnaround.

Given the external challenges, it was particularly pleasing to report a significant improvement in our cash generation, with cash flow from operations increasing from $2 million in the previous year to $19.6 million. This was driven mainly by a reduction in interest and other finance costs, which fell from $20.2 million to $6.2 million, and the $4.3 million worth of R&D credits received in the UK.

In a year where our key clients were affected by some significant delays the strong cash flow was critical to providing the Board and management with the flexibility to develop and implement strategies that will help build a sustainable and profitable business over the long term.

As a direct result of those operational delays by key customers, our revenue fell by 24.3% to $111.08 million compared to the previous year. The delays, which impacted the first half but became more pronounced in the second half, prompted us to prioritise cash-generating activities

Group EBITDA of $20.85 million represented a margin of 18.8%, a major improvement on the already strong previous year where the EBITDA margin was 15.5 %.

The improvement in operational cash flows from our Australian drilling operations was enhanced by significantly lower expenditure on our UK operations. We also continued to find efficiencies wherever possible and decided to close our Sydney office and restructure the Board and senior management team.

The bulk of the nearly $19.6 million in cash generated by the business was used to pay down our debt facilities, and together with positive foreign exchange movements and capitalised interest, resulted in a decrease in total interest-bearing liabilities of $7.2 million to $107.4 million at the end of the year.

As discussed earlier, our people play a key role in the success of our business. While we have an excellent team of managers in place, we are aware of the need to empower more of our people and develop the next generation of leaders.

To this end, we have continued to invest heavily in our leadership development program that is designed to identify and grow the strategic, operational and safety skills of people across all facets of our business.

During the year, we refined and expanded our Operational Excellence program and, as a result, witnessed further significant improvements in productivity while maintaining our superior safety record. One of the best examples of the program's success is a measurable improvement in the productivity and effectiveness of our drilling teams.

During the current year, we will be moving to the program's final phase with the implementation of a new High-Performing Team project. Under the project, our Rig Managers and crews are given ownership and accountability for the continuous improvement of our drilling rigs. This high level of responsibility has proven to be one of the best ways to maximise efficiency and problem-solving on site.

Having the people to grow a business is one thing; we also need a unique product that clients are willing to pay a premium for. This means we need to meet and exceed the safety, operational and environmental expectations of our clients on a consistent basis.

Over many years, Lucas has built a reputation for delivering specialised and technically challenging projects in a highly efficient manner. Continuing to invest in expanding our expertise and capacity in directional drilling will be critical to our future success. This type of drilling is a relatively new and highly complex field, but when it is done successfully, it has significant environmental, social, and commercial benefits.
Utilising directional drilling means we can reduce the number of horizontal boreholes that need to be drilled, which saves significant time, money, resources and lowers the above-ground footprint of our operations.

At Lucas, we also take tremendous pride in our safety record. The key measure of success in this area, the Total Recordable Injury Frequency Rate (TRIFR), fell by 16% to 3.07 in the year under review.

We achieved TRIFR of ZERO on 100% of our customer sites for the first time in our history. Given the scale and complexity of our operations, this is not just an industry-leading result for Australia but an exceptional outcome that cements us as a global leader in safety.
As you can see, our Australian business is performing strongly and we are well placed to deal with the opportunities and challenges we know are coming, as well as those things we can't predict.

As I mentioned earlier, Lucas is a business of two parts, and it would be remiss of me not to provide some insights into our approach to extracting value from our Cuadrilla shale gas investments in the UK. Since acquiring the asset, as we are all aware the UK government has placed a moratorium on hydraulic fracturing.

Since the moratorium was enacted, our priority has been to significantly reduce the cost base of the operation while still maintaining enough presence and expertise to engage with relevant authorities and campaign for a lifting of the moratorium. Until the moratorium is lifted, the assets remain largely uncommercial.

Our Chief Executive Officer of Oil and Gas, Francis Egan, continues to work with a small, dedicated team to navigate an extremely complex situation. The moratorium on hydraulic fracturing means we have made no progress in developing the clean and probably abundant gas resource contained within our licence areas at a time when gas has become critical to the debate about the UK's net zero climate commitments and the cost of achieving those commitments.

As a result of policy settings the UK is currently buying massive amounts of expensive, highly carbon-intensive gas from countries like Russia and Qatar while its own, cheaper, cleaner resources are untapped. The crisis is likely to become more critical over the winter as high prices and shortages affect people's ability to heat their homes.

Ultimately, all we can do as a business is clearly and consistently put our case to UK regulators that a safe, affordable, domestic supply of shale gas is achievable with the right regulations and oversight. We will continue to make this case to whoever we need to.
Turning now to our priorities for the current year.

The outlook for the metallurgical coal market that underpins demand for our services remains healthy and robust. The price of metallurgical coal has risen to record levels in recent weeks as rising demand and poor domestic supply in China pushed up demand for international supplies.

The price of coking coal surged to $US410 a tonne in September, representing a more than tripling in price since early 2020. While the price has eased in recent weeks, demand is expected to remain high as economies emerge from the pandemic and steel production ramps up. As a result of the price increases, coking coal is now overtaking iron ore as the highest input cost for many of the world's steel mills.

Thankfully, Australia and Queensland have some of the highest quality coking coal globally, and we work for some of the biggest producers.

We entered the new year with a sizeable order book and continue to seek out new opportunities to grow our revenue and profits. Much of the hard work of reducing our costs has now been done, and we are confident we have the right foundations to grow profitably and sustainably.

We are in a good position to begin the process of renegotiating and, if required, restructuring our debt profile. While we have no debt expiring in FY22 it is important we start this complex process well in advance of expiry and carefully manage the de-leveraging of the business. A low-cost base, increasing revenues and strong cash flow will make this complex process a little easier.

Finally, I would like to thank Chairman Andrew Purcell and his fellow Directors for their support and guidance throughout the year. We have built a great team at Lucas and are looking forward to the future.

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