ASX Release

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ASX: EHL (EMECO OR THE COMPANY)

Emeco delivers a strong 2H23 performance

Results Overview

Emeco today reported its FY23 financial results in what has been another solid year. Strong conditions in commodity markets fuelled exceptional demand and activity levels across the business. We are also experiencing new demand coming from mining customers seeking to retain flexibility as they assess new technology options and navigate ESG considerations for their fleet requirements, and others, particularly mining contractors, seeking to preserve balance sheet capacity.

Emeco's financial performance can be considered a story of two halves. The Company delivered a strong turnaround performance in the second half, with growth in revenue and earnings across each business, including the benefit of the successful renegotiation of rates and contractual terms with a key Pit N Portal ("PNP") customer. This followed a disappointing first half which was largely attributable to the underperformance of PNP. Credit losses taken in 1H23 were sufficient to cover de-risking and reset of the project portfolio, including Aurora project termination in 2H23. A comprehensive counterparty risk review has been completed and additional credit management resources have been injected into the finance function to improve counterparty risk exposure going forward.

The outlook for FY24 is positive, with momentum achieved in 2H23 expected to drive earnings growth. The business continues to focus on cost efficiencies and contract repricing, to drive margins and returns.

Capital investment continues to target 'high demand' Rental fleet. Emeco's mid-life asset rebuild model, delivered through Force workshops, underpins the Company's ability to replace and grow its Rental fleet to meet customer demand in a capital and cost-efficient manner, maximising financial returns.

Emeco's balance sheet remains strong with net leverage of 1.1x, providing flexibility to respond to the changing needs of the business and to pursue opportunities for growth.

The Board has approved a 2H23 capital management package of $13.8 million, which includes a share buy-back of $7.3 million and a final fully franked dividend of 1.25 cents per share, which represents a 35% payout of 2H23 Operating NPAT.

Financial Highlights

- Record **Group Revenue** of $875 million**,** up 16% on pcp, with strong growth in the Rental and Force businesses reflecting ongoing high demand for equipment and services
- **Strong 2H23 performance** with a 21% uplift in Operating EBITDA on 1H23. Earnings growth in each business and Operating free cash flow generation of $44 million (excl. growth capex)
- Solid **Operating EBITDA** of $250 million, in line with pcp, tempered by 1H23 underperformance of the PNP business, now de-risked and reset
- **Operating EBIT** of $105 million, down 13% vs pcp
- **Operating NPAT** of $59 million, down 14% vs pcp
- **Return on capital** at 13%. ROC excluding PNP of 18%, well above cost of capital
- **Capital management** package of $20 million paid in FY23, including $13 million in dividends and $7 million in on-market buy-back program

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Operating and Financial Performance

Emeco reported record revenue of $875 million, up 16% on FY22 driven by strong rental and workshop demand and an increase in fully maintained projects.

Second half earnings recovered strongly, after a disappointing first half. Second half Operating EBITDA of $136.9 million was an increase of 21% on the first half, and a 6% increase on the prior corresponding period, reflecting earnings growth across each business. First half earnings were impacted by the poor performance of PNP. Full year Operating EBITDA of $250.4 million was just ahead of FY22.

Full year Operating EBIT of $105 million declined 13% on FY22, however second half Operating EBIT improved by 56% over the first half. Operating NPAT of $59 million and Statutory NPAT of $41 million declined vs FY22 driven by the underperformance of PNP and higher interest expenses.

Group returns remain robust despite the challenges at PNP during the year. Reported ROC was 13%, however when excluding PNP the core Rental and Force business's generated strong returns of 18%, well above the cost of capital.

The Board has today announced a 2H23 capital management package of $13.8 million (35% of 2H23 Operating NPAT), including a 1.25 cents per share fully franked final dividend and $7.3 million to be applied to the share buy-back program. This capital management package, when combined with the 1H23 fully franked dividend of 1.25 cents paid during the year brings the total amount allocated to capital management in respect of the FY23 year to approximately $20 million.

Earnings per share of 8.0 cents declined on FY22 in line with Statutory NPAT, noting the reduced share count as a result of share buy-back announced in relation to the 2H22 capital management package and executed during 1H23.

FY23 Operating Financial Performance[1,2]

$m unless otherwise stated	FY22	1H23	2H23	FY23
Revenue	754.4	429.5	445.4	874.9
Operating EBITDA[1]	250.2	113.5	136.9	250.4
Operating EBITDA margin	33%	26%	31%	29%
Operating EBIT[1]	120.7	40.8	63.8	104.6
Operating EBIT margin	16%	10%	14%	12%
Operating NPAT[1,2]	68.9	19.6	39.5	59.1
Return on capital (ROC)[3]	16%	13%	13%	13%

Notes:

1. Operating financial metrics are non-IFRS measures. Refer to Statutory to Operating reconciliations in the Appendices
2. Operating NPAT assumes 30% notional tax expense on non-operating items
3. Return on capital (ROC) calculated as LTM Operating EBIT over average capital employed. ROC excluding PNP assumes allocation of corporate overheads to PNP based on revenue

Emeco's CEO and Managing Director Ian Testrow said: "FY23 has been both an exciting and challenging year for Emeco. Our results have been delivered against a backdrop of record demand for our equipment and services but tested by ongoing inflationary pressures across the business. Our Pit N Portal portfolio was successfully de-risked and reset, including the renegotiation of rates with a key customer. Our business is resilient, and our dedicated team continues to tackle each new challenge and create new opportunities always motivated by delivering strong returns for our shareholders.

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Rental

"Our Rental business revenue grew by 19% over the year as we deployed fleet to meet strong customer demand and increased the number of fully maintained projects, in line with our strategy. Gross fleet utilisation increased to 93% driven by this new work. Rental Operating EBITDA increased by $19.5 million to $259.7 million, an increase of 8% on FY22. Margins declined on FY22 as a result of the increase in fully maintained projects, use of cross-hired fleet to meet customer demand and ongoing parts and labour cost inflation, including subcontractor costs. Margins stabilised during the second half with the application of contractual and out-of-cycle pricing and fleet deployment."

Force Workshops

"Our Force business continued its strong performance, driven by a significant increase in retail customer activity, whilst also supporting increased internal rebuild and maintenance activity, with 125 equipment rebuilds completed during the year. Revenue from retail customers increased by 73% to $156.5 million and Operating EBITDA increased by 30% to $11.8 million compared to FY22. Our mid-life asset rebuild model continues to underpin our ability to replace and grow our Rental fleet to meet customer demand in a capital and cost-efficient manner, maximising our financial returns. We have also significantly increased the proportion of Force built components to both counter parts price inflation and to ensure security of supply in a challenging market."

Pit N Portal

"Pit N Portal's revenue decreased by 10% to $223.6 million over the year reflecting completion of a number of projects as well as the de-risking and reset of the project portfolio. A strong second half turnaround performance was underpinned by the successful renegotiation of a key customer contract as well as the commencement of several new projects. First half earnings were disappointing, reflecting the termination of several projects, as we de-risked our project portfolio. This negatively impacted Operating EBITDA which declined to $17.2 million for FY23, as we demobilised equipment and people. A $22.9 million credit loss provision was recognised in the first half to account for losses associated with terminated projects, with all amounts now written-off. We have recently invested in additional resources and capability across our credit management, tendering and customer selection processes."

Balance Sheet and Cash Flow

Emeco's balance sheet remains strong with net leverage of 1.1x at 30 June 2023, in line with the long term target of 1.0x. The Company has total liquidity of $141.7 million, including cash of $46.7 million and an undrawn $95 million revolving credit facility.

In February 2023, Fitch Ratings upgraded their long-term issuer default rating to BB- from B+. In doing so, they noted the improvement in the Company's revenue diversity and visibility.

Emeco's Operating free cash flow (before growth capex) of $52.3 million was impacted by a working capital outflow of $18.2 million, predominantly due to the non-collection of impaired Pit N Portal receivables of $23.0 million which was provided for fully in the first half.

Net sustaining capital expenditure totalled $154.1 million. Emeco also invested $21.8 million in growth capex during the year, including approximately $20.0 million for the rebuild of a second-hand fleet of 18 trucks purchased in FY22. This fleet is now fully deployed and generating strong earnings and returns (IRR 21%), demonstrating the competitive advantage Emeco's mid-life asset model delivers.

Higher drawn debt levels and interest rates during the period, resulted in net finance costs being $6.5 million higher compared to FY22.

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Outlook, Guidance and Strategy

The outlook for FY24 is positive with demand across all businesses expected to remain robust, driving earnings growth.

Rental earnings growth is expected to be driven predominantly by high fleet utilisation and fleet growth. The Company will continue to focus on cost improvement, targeting the replacement of cross-hired fleet with our own equipment and converting subcontracted labour to full time employees.

A strong portfolio of contracted retail projects will underpin growth at Force workshops, whilst continuing to support the Rental business through a growing internal rebuild program.

PNP earnings expected to be lower in 1H24 compared with 2H23, following the de-risking and reset of the project portfolio, with full year earnings expected to be higher than FY23. An ongoing review of the business is in process to consider options to improve returns.

Emeco has a strong track-record of achieving high returns on capital investments in its core Rental business through the Company's mid-life asset rebuild model.

Net sustaining capex for the year ahead is expected to be approximately $160 million, largely in line with FY23 and in line with depreciation.

The Company's FY24 capex program also includes: growth capital expenditure of approximately $7 million to rebuild five 789C trucks to replace cross-hired fleet, with an expected IRR of 19%. Further, growth capital expenditure of approximately $19 million has been committed to acquire 18 'high demand' 240-tonne 793D fleet cores. A staged rebuild program, linked to customer demand will bring the total investment for this 793D fleet to $24 – 37 million. This investment is expected to generate an IRR of ~20%, once equipment is rebuilt and deployed into projects.

Emeco has also committed to the upgrade of its ERP over the next 3 years, with an approved project spend of ~$8 million for FY24. This investment in technology is critical to the sustained success and growth of the business.

Leverage is expected to remain around the Company's long-term target of 1.0x Operating EBITDA.

Ian Testrow concluded: "We enter FY24 with strong momentum and are confident that our business model will enable us to deliver sustainable growth and deliver increased shareholder returns in FY24."

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This announcement was authorised to be provided to the ASX by Penny Young, Company Secretary of Emeco Holdings Limited.