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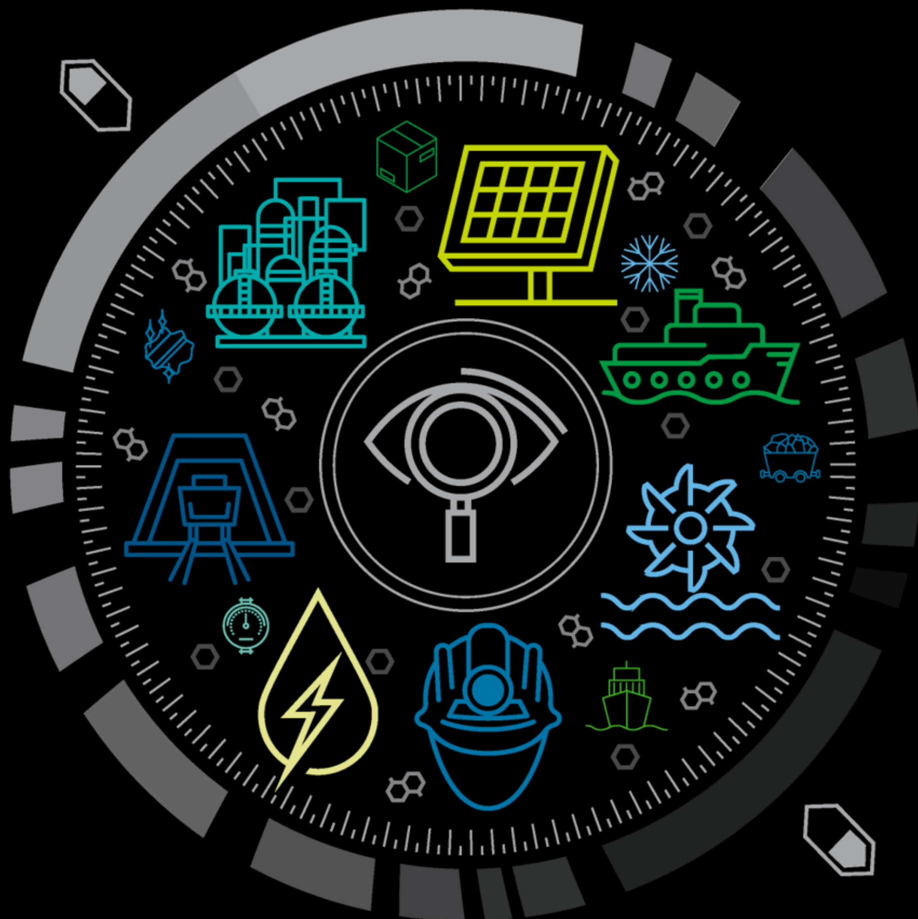


WA Index Special Report

Mining Services

Lead indicator for the health of the energy and resources sector or an industry with a much bigger agenda

October 2018

Over the past ten years, the Australian economy and WA in particular, has been highly leveraged to the demand for Australia's rich mineral resources from markets in China, and the broader Asian region.

The first half of the current decade was underpinned by astounding growth in the mining sector. The industry significantly increased the number of active mining projects in Australia, and companies rapidly expanded their production capacity to keep up with insatiable demand.

To meet growing global expectations meant increased demand for construction and engineering services, which saw the mining services and contracting industry reap the rewards of this expanding market. It was not until 2012-2013 that the start of a decline in mining capital expenditure signaled the end of the most recent mining investment boom.

Since that time, mining and mining services companies suffered through the global commodity market downturn, with our local WA economy hit hard. Despite the challenge posed for many WA companies during this time, the industry's resilience and focus to stay the course sees these same companies well positioned to benefit into the next cycle. To that end, 2018 looks to be well on the way to being a very positive year for the industry.

In fact, it was in the Deloitte WA Index Diggers & Dealers Special Edition of 2017 where we highlighted early signs of positivity observed through mining services company performance, where we had noted that mining services companies had arrested market capitalisation declines for the first time in several years.

We referred to mining services being a lead indicator for the overall health of the mining industry, and that indicator had turned.

Since that report's release, we have seen a continued uptick in the market capitalisation for many of the top 100 WA listed mining and mining services companies, which confirmed our thinking that we were steering the right way to a once again healthy energy and resources sector. Global economic stability, improved commodity prices and a less anxious investment community has certainly helped.

This special report looks at the performance of WA mining service providers since our 2017 report, indexing market capitalisation performance, reviewing the relative performance amongst peer group companies and highlighting what drivers are behind a revitalisation in the mining services sector.

"In our resources rich State, demand for mining services often acts as a lead-indicator for the overall health of the energy and resources sector"

Deloitte WA Index – Diggers and Dealers Special Edition 2017

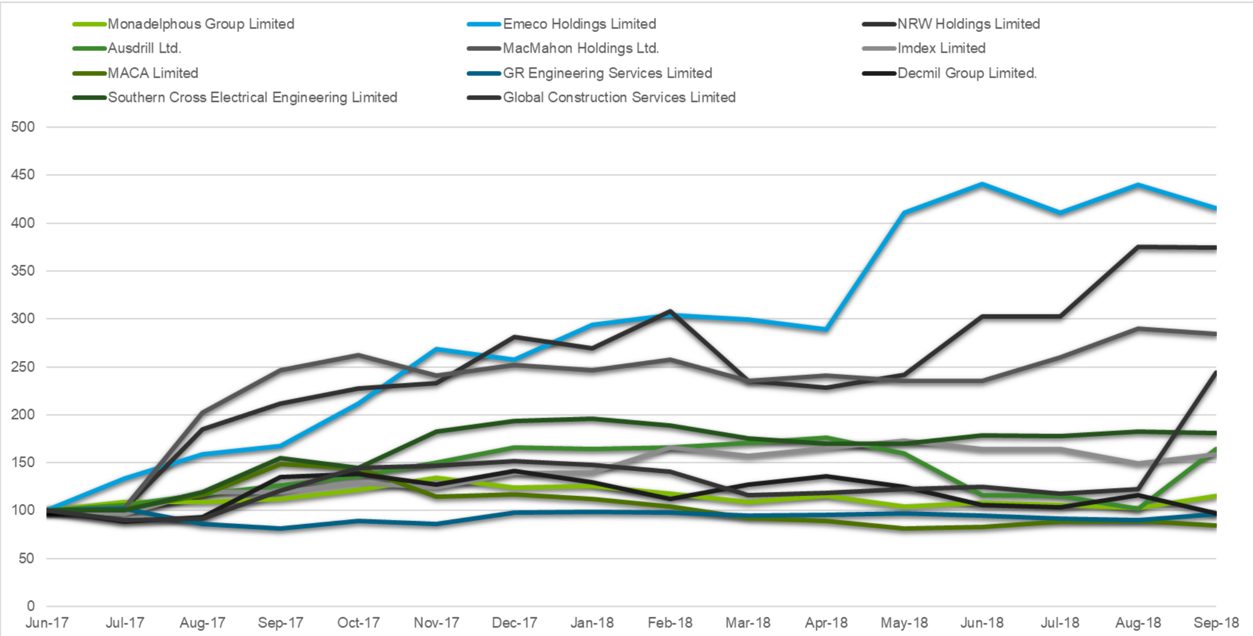
Since observing a positive directional change in mining services companies market capitalisation during 2017, we have indexed the market capitalisation of mining service companies in the WA Index as at 30 June 2017 to compare performance amongst peers and consider what factors may lead to more recent relative outperformance.

The contracting sector generally has been the welcome recipient of large-scale national infrastructure project approvals, committed energy related projects and major mine development decisions over the last 12-18 months. This level of support is thanks in part to a degree of stability across global economies and global commodity prices and a need to be prepared for the future.

While commodity prices across the board have not moved significantly upward or downward over the last 12 months - the exception being demand driven pressures in energy-related bulks and battery metals such as nickel - the mining services sector has enjoyed increased tendering activity and a more favourable operating environment than that of recent years.

Increased activity typically lends itself to increased turnover for participants and consequently a more positive industry shall prevail. This is evident through a recent tightening in the contract labour force market and the improved market capitalisation performance across most mining services companies since 30 June 2017.

Figure 1: Mining Services market capitalisation performance (30 June 2017 indexed to 100)

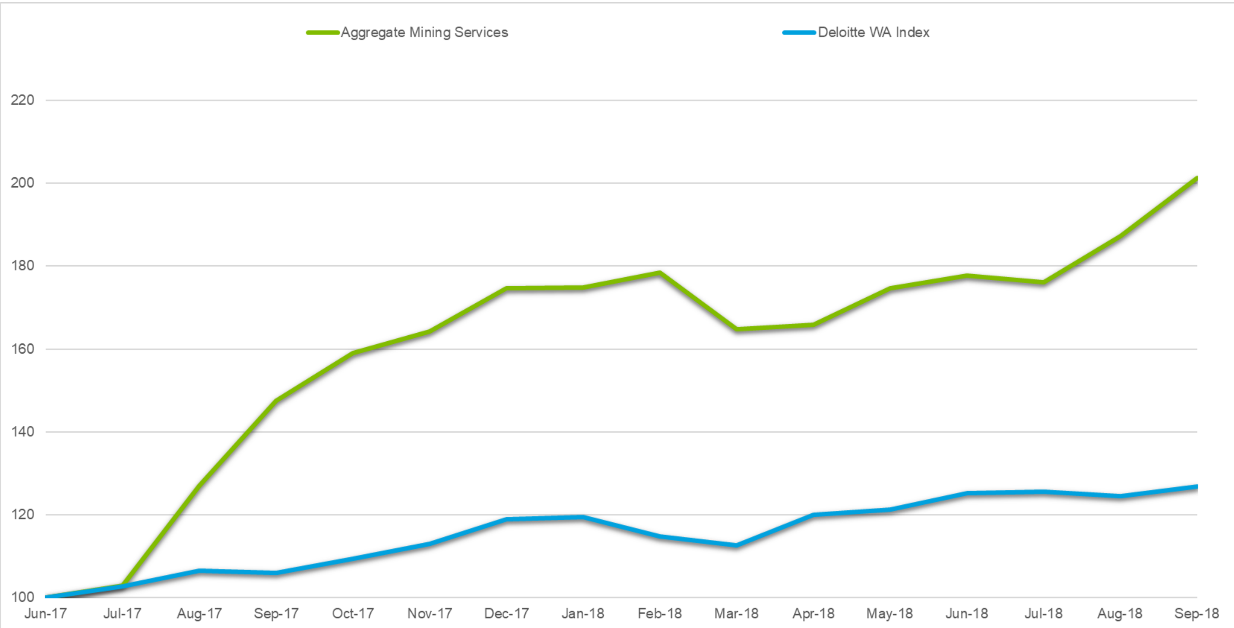


As shown in Figure 1, of the 11 companies tracked in our Deloitte WA Index categorised to mining services, over 80% demonstrated positive growth, with only two companies closing lower (down 3%) over the 15 months from 30 June 2017 to 30 September 2018.

At the top end of the performers, we see outstanding growth achieved by Emeco Holdings Ltd ("Emeco") and NRW Holdings Ltd ("NRW"), each delivering in excess of 250% returns for shareholders over the last 15 months. Also of note is Macmahon Holdings ("Macmahon") which achieved 185% return over this period.

These are significant returns without doubt, but we also need stand back to acknowledge the sector as a whole. Aggregating the 11 Deloitte WA Index mining services companies included in the table above, the average return across this basket of companies was 100%. That is, with an equal weight investment made across these companies on 1 July 2017, the investment value would have doubled in value over the last 15 months. Not many sectors that can demonstrate that level of performance; particularly considering the Deloitte WA Index 100 itself achieved 27% growth over the same period.

Figure 2: Aggregate of mining services market capitalisation compared to Deloitte WA Index (30 June 2017 indexed to 100)



In terms of individual company performances, Emeco took an early mover advantage, starting its acquisitive strategy back in March 2017 with the mergers of both Orionstone and Andy's Earthmovers. Emeco since acquired two further companies, Force Equipment and Matilda Equipment, both national equipment rental and maintenance businesses. The mergers provided Emeco with increased scale, a more diversified customer base, and an expanded equipment portfolio.

NRW followed shortly after in acquiring Golding Group, a leading civil infrastructure, urban and mining services company with significant East Coast presence during August 2017. This acquisition enabled NRW to grow its service offerings into adjacent and complementary sectors.

Interestingly, NRW has been somewhat a quiet achiever in our Deloitte WA Index. Whilst we have not observed significant individual monthly market capitalisation increases sufficient to see NRW recognised as a top mover in our monthly summaries, the aggregate performance over recent time has been outstanding.

The decision to increase exposure to the east coast of Australia, and in particular the buoyant infrastructure and coal markets of QLD and NSW, opened up new customers and diversified revenue streams for both Emeco and NRW which complemented existing business platforms.

Not surprisingly, the continued strength in the east coast coal industry over this time has helped these companies prosper. In addition, government and corporate spend in infrastructure projects of significance to the States has seen contractor pipelines increasing.

Bulk commodity performance has remained strong across this same period with a number of contract extensions and renegotiations underpinning earnings performance. Thermal coal pricing remains at record levels as energy demand from Asia continues to outstrip supply. Contractors involved in bulk commodity contracts and the recent early-works tendering in both coal and iron ore projects have benefited.

Figure 2: Bulk commodity price performance (30 June 2017 indexed to 100)

Macmahon, having been subject to CIMIC takeover offer from early 2017, rebounded strongly after announcing a significant life of mine contract and strategic alliance with AMNT over its Batu Hijau copper/gold project in Indonesia, with conditions precedent to the transaction being satisfied during August 2017. Surety over cash flows and contractual revenues provided much needed investor confidence as the company reaffirmed itself as a standalone contractor.

Each of these strategic M&A deals were significant in the context of these respective companies.

This M&A focus reflected a confidence from the leadership teams to bet big early on in the cycle, while the subsequent share price performance confirms the market's support of being bold during difficult times. In comparison to peers, this early move on M&A activity saw sharp market capitalisation growth that has proven difficult for other sector players to catch.

More recently, Ausdrill announced its acquisition of Barminco, and Global Construction Services announced a merger of equals with SRG Limited. Both M&A related announcements saw the respective company's market capitalisations spike in September 2018 on this news.

Additionally, Southern Cross Electrical Engineering Limited ("Southern Cross") and Imdex Ltd performed well over this period, largely relying on organic opportunities to fuel performance. Both companies have secured key contracts in chosen markets and markedly improved earnings performances over recent reporting periods has not gone unnoticed.

Southern Cross in particular has recently secured a number of significant infrastructure-based contracts, including works at both WestConnex and Northlink WA. Imdex has continued to enhance its intellectual property and customer solution offerings, and has seen strength in demand across a number of geographies as the global mining outlook continues to improve.

A key consistency of the high performing mining services companies has been the ability to secure work and fill the pipeline, but doing this in a balanced way; with stable, accretive and deleveraged earnings profiles. Maintaining a strong balance sheet with adequate capacity and flexibility is top of mind.

So where to from here? Global economies and commodity prices have both demonstrated some much-needed stability that has allowed mining and infrastructure companies to commit to growth and ongoing sustainability of production volumes. This has seen a raft of new project approvals and activity across these sectors.

Global demand forecasts remain robust over most of our locally important commodities and as such, we would expect the contracting industry to continue to secure additional work to bolster their work pipelines.

Inevitably, not everyone can be a winner. However, as we looked back over the last 15 months of performance, the mining services companies in the Deloitte WA Index certainly have a good number of success stories to celebrate.

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