Austal Limited (Austral) (ASX: ASB) has today reported its results for the six months ended 31 December 2016, with a Net Profit After Tax of $9.3 million.

Austal’s financial engine room in the USA, delivered a strong turnaround in earnings, with segment EBIT up 53% on the prior corresponding period (“pcp”) to $41.1 million. The earnings contribution from the Australian shipyard was lower than the half year prior as anticipated, as major vessel programs progressed through their design phase. Earnings at the Group level, were impacted by a one-off event of a $13.2 million provision relating to the recent settlement of an arbitration matter from a commercial vessel delivered seven years ago.
Austal Chief Executive Officer David Singleton said the result demonstrated the benefit of Austal’s global scale.

“Austal’s diversity across geographies and vessel programs meant the Company was able to deliver a profit and maintained dividends to shareholders despite two of our shipyards being in a transition period” Mr Singleton said.

“Earnings from the US shipyard bounced back strongly from FY2016, with the performance on our two multi-billion-dollar navy vessel programs improving as each ship is delivered.”

“This performance in the USA offset the expected lower result from our Australian shipyard which is in a transition year. The 21-vessel, $305 million, Pacific Patrol Boat program and a circa $90 million, 109-metre ferry have been going through their design phase although construction on these ships will have commenced by the end of the financial year.

“Our Philippines shipyard ran below full capacity in the half due to the delay of an expected order related to customer financing. We remain confident that this will be a temporary issue given the very strong pipeline of new enquiries from around the world which is running at levels not seen since before 2008.”

SEGMENT RESULTS

USA

Austal’s USA segment reported revenue of $594.3 million (FY2016 H1: $638.4 million), with a segment EBIT of $41.1 million (FY2016 H1: $26.9 million). This was driven by work on thirteen ship construction projects across Austal’s two major vessel contracts for the U.S. Navy; the ~US$4 billion Littoral Combat Ship (LCS) contract and ~US$1.9 billion Expeditionary Fast Transport (EPF) contract.

Revenue in the support business has continued to grow, up 78% on the same period to $55.8 million. The EBIT margin on support at 12.5% was above our normal expectations as a result of the benefit of profit awarded by the US Navy in FY017 H1 that related to FY2016 activity. Nonetheless overall profit margins in support are continuing to improve.

USA shipbuilding EBIT margin was 6.6% per cent, in line with the Company’s previous guidance of 5 – 7%. Austal’s confidence in the LCS program continued to grow in FY2017 H1 as the Company moved further along the production learning curve, with findings from the LCS program review completed in July 2016 being progressively implemented. The number of new requested modifications to vessels already well advanced has dropped dramatically and existing required
modifications are now being incorporated much earlier in the build cycle which reduces costs. In addition, the shipyards strategy to continually bring forward work normally carried out at the waterfront into the module manufacturing facility is reducing costs and increasing speed particularly in the final stages of build. This approach is allowing Austal to maximise the benefits of its leading edge production facilities designed to facilitate just this approach to construction. However, the company advises that further evidence of progress over at least the next 6 months will be necessary to provide real confidence that the turnaround is complete. Meanwhile, the EPF program, which is utilising the production techniques described above, is performing exceptionally well and above expectations. The program was extended from 10 to 12 ships with the award of 2 additional vessels, extending Austal USA’s contracted production schedule into FY2021 although we would like to see additional orders in the next 18 months to maintain the tempo now being achieved

Austal has previously advised that it has made a series of financial claims related to the modifications requested by the US Navy on the LCS program. Advice is maintained that based on experience, any potential settlement of these claims, if achieved, may not be for up to 2 years and accordingly no account has been made of their potential value.

Australia

Austal’s Australian segment reported revenue of $47.4 million (FY2016 H1: $105.6 million), with a segment EBIT of $1.7 million (FY2016 H1: $11.3 million). Austal expects FY2017 to be a year of lower profitability in Australia, as stated at its FY2016 results, given that the shipyard is completing previous programs and is now in the front-end design phase on two significant vessel programs; the $305 million Pacific Patrol Boat program and ~$90 million 109 metre Mols vehicle passenger ferry. Austal’s revised profit recognition treatment follows a more conservative process announced during the full year results in 2016 whereby profit will only be recognised progressively as significant first in class risks are eliminated. It is therefore likely that profit will not be recognised on the first PPB vessel until delivery scheduled for October 2018, although profit maybe recognised on the Mols ferry which is a more standard ship type. In addition, current year profitability will also be affected by the two Cape Class vessels being completed for the Royal Australian Navy under a bank leasing arrangement. These ships will only generate accounting profit during the lease period rather than during construction as would normally be the case.

Austal delivered a 70-metre fast crew boat to Caspian Marine Services ahead of schedule in September 2016 under a US$34 million contract in a ‘hybrid’ build between the Australia and Philippines shipyards. This production approach can generate time and cost savings which will continue to enhance our offering to customers.
Sustainment activities have generally been generating strong returns for the Australian business. Cape and Armidale vessel repair and maintenance activities, in Henderson and Darwin, have been running successfully and at a significantly higher level than in the past. This activity will be augmented in the second half with a substantial amount of support work on the Armidale remediation contracts in Henderson. Austal has recently increased its staffing levels in Cairns after taking over activities, from another party, to support Cape vessels now and Pacific Patrol Boats in the future and this will further increase profitable work. Offsetting this, the Cape Class management support contract is currently losing money because Austal has had to provide significantly more resources than was anticipated in the contract. Our priority has been to ensure that Border Force is fully supported as it carries out its important mission and we anticipate a contract amendment to recognise the additional resources required in due course.

**Philippines**

Austral’s Philippines segment reported revenue of $12.7 million (FY2016 H1: $16.3 million), with a segment EBIT loss of $(2.8) million (FY2016 H1: $0.6 million EBIT profit). Three smaller commercial vessels were under construction at the shipyard in the half but the low revenue levels do not meet the breakeven run rate for the yard. A fourth vessel which in our plans had been expected for the yard and which would have lifted revenue to the necessary level was signed but the contract has been delayed due to completion issues for the buyer. The construction slot was eventually filled by the FRS vessel signed in December 2016 on which design is now complete and actual shipbuilding is just starting. The commercial vessel pipeline includes several larger ferries which will maintain revenue in the Philippines beyond the economic breakeven point if contracted. Importantly following the management and organisational improvements implemented at the beginning of the year, construction of the vessels is currently performing well and within schedule. We continue to believe that the yard provides the basis to protect our market in fast ferries and now that the sales pipeline is improving we anticipate the profitability of the yard to make a significant contribution to the group in future years.
Group

Austal took an opportunity to settle a long standing arbitration matter after the end of the financial half year. The arbitration related to a latent defect in a commercial vessel delivered to a European customer seven years ago. The settlement avoids the risk of an adverse arbitration outcome and the cost of continuing complex arbitration in the United Kingdom and was judged to be a prudent outcome for the business. Austal had previously fully provided for the actual repair costs associated with the claim but not for a settlement. This settlement was negotiated subsequent to the end of the reporting period and is a material post balance date adjustment, and was therefore included in the FY2017 H1 accounts. Austal has no further arbitration or significant legal actions underway.

The effective rate of tax was inflated by the high proportion of earnings from the USA relative to Australia, and conservative treatment of technical matters that are the subject of an ATO audit.

CASH AND CAPITAL MANAGEMENT

Austal transitioned to a net debt position of $32.6 million at 31 December 2016 from a net cash position of $51.7 million at 30 June 2016. Austal has historically experienced significant working capital movements driven by the nature of its business as can be seen from the chart in the associated company results presentation. Importantly, Austal has trended towards net cash over the past five years and ended the FY2017 H1 with a strong cash at bank balance of $153.5 million, supporting the ongoing payment of dividends.

A major factor impacting Austal’s debt position is its contract to construct two additional Cape Class Patrol Boats. These vessels will be chartered by NAB to the Commonwealth of Australia (Royal Australian Navy) for a minimum term of three years. Austal entered into a financing arrangement under the contract which results in the construction costs being recognised as capital expenditure and the progress payments from NAB recognised as vessel finance (debt). This vessel finance totalled $45.5 million at 31 December 2016 ($25.8 million at 30 June 2016) and is expected to rise to ~$65 million prior to delivery.

INTERIM DIVIDEND

Austal’s Board has declared an interim dividend of 2 cents per share, fully franked, in line with FY2016 H1.

Details of key dates regarding the dividend are:

- Ex-dividend date: Tuesday, 14 March 2017
- Record date: Wednesday, 15 March 2017
- Payment date: Wednesday, 10 May 2017

Shareholders may reinvest dividends in accordance with the dividend reinvestment plan established in February 2015. Further details are set out later in this announcement.

OUTLOOK

Austal expects FY2017 group underlying EBIT of $55-60 million (after removing one-off impacts of the arbitration matter) which is above the original guidance. Headline EBIT is expected to be $45 - 50 million and is therefore, in line with original guidance. The US shipbuilding margin is expected to remain unchanged at between 5-7 per cent.

Austal Chief Executive Officer David Singleton said Austal was pursuing its strongest ever pipeline of work which if successful would positively impact across all 3 of its shipyards. However, there is much to do over the next 2 to 3 years to make that a reality and the management understands the criticality of the phase we are in.

“We are in the midst of bidding multi-billion dollar defence and commercial vessel opportunities that can be designed, built, and sustained at our shipyards in the US, Australia, and the Philippines,“ Mr Singleton said.

“In the US, the new administration has a stated target for a 355-vessel Navy, a fleet expansion the US Navy has long argued for, which provides a major opportunity for Austal as a proven prime defence contractor to extend the current programmes out beyond 2021”

“The pipeline of work in Australia is significant. Austal is lodging its final bid for the 12 ship, $3 billion OPV program by the end of March, partnering with German shipbuilder Fassmer on the design. Longer term, the future frigate presents a major opportunity given our proven capabilities to design and construct complex, similar-sized vessels in the US.”

“Meanwhile the pipeline for commercial vessels which are designed in our Australian facilities and usually built in the Philippines shipyard is at its strongest level in seven years. In support of this we are working on plans to extend the facilities in the Philippines and are carrying out new R&D work in Australia to further entrench our reputation for building the finest fast ferries in the world.”

“Underpinning the construction programs is the ongoing opportunity for support work in sustaining Austal-built defence vessels as they are deployed around the world. As our capability grows in both the USA and Australia so does the opportunity.”
Conference Call

Austal Chief Executive Officer David Singleton and Chief Financial Officer Greg Jason will hold an analyst and investor conference call today to discuss the Company’s H1 FY2017 results at the time listed below.

Conference call details:

Date: Monday, 27 February 2017
Time: 6:30am Perth time (AWST) / 9:30am Sydney time (AEDT) – participants are requested to dial in 5 minutes prior to the start time

Dial-in details:

Domestic participants can dial either of the numbers below to join the call.

Toll free: 1800 123 296 or Toll: +61 2 8038 5221
Conference ID: 6700 8909

International toll-free numbers are listed below. For countries not listed below, the Australian Toll number can be dialled.

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Archived Call: An archived copy of the call will be available shortly after the conclusion of the call via http://www.openbriefing.com/OB/2441.aspx.

Dividend Reinvestment Plan (DRP)

Austal operates a DRP which allows eligible shareholders to elect to invest dividends in shares which rank equally with Austal ordinary shares. It provides a convenient and cost effective way for eligible investors to invest part or all dividends into new Austal ordinary shares, without incurring brokerage charges or commission. Participation in the DRP is open to all shareholders who have a registered address in Australia or New Zealand.

Ordinary shares will be issued to participants for the interim dividend to satisfy any ordinary shares to be allocated under the DRP. The allocation price for the shares to be issued under the DRP will be calculated as the volume weighted average market price of Austal shares traded on the ASX over a period of 5 business days from Monday 20 – Friday 24 March 2017. No discount shall apply to the
allocation price. Shares will be issued on Wednesday, 24 May 2017 following the payment of the dividend.

The last date for receipt of applications to participate or cease participation in the DRP is 5:00pm (WST) on Thursday, 16 March 2017.

Shareholders may obtain a Participation Notice by contacting Advanced Share Registry:
Advanced Share Registry Services

110 Stirling Highway
Nedlands, WA, Australia 6009
Enquiries: (618) 9389 8033

A summary of the DRP rules and the rules are available on Austal’s website at www.austal.com.

Key dates to note for the application of the DRP to the upcoming interim dividend are:

- Last date for receipt of elections to participation in DRP: Thursday, 16 March 2017.
- 5 trading day pricing period for DRP: Monday, 20 March 2017 to Friday, 24 March 2017.
- Date for issue of shares under DRP: Wednesday, 24 May 2017.

About Austal

Austal is a global defence prime contractor and a designer and manufacturer of defence and commercial ships. For more than 27 years Austal has been a leader in the design, construction and maintenance of revolutionary ships for governments, navies and ferry operators around the world. More than 255 vessels have been delivered in that time.

Ships

Defence vessels designed and built by Austal include multi-mission combatants, such as the Littoral Combat Ship (LCS) for the United States Navy, and military high speed vessels for transport and humanitarian relief, such as the Expeditionary Fast Transport (EPF) for the U.S. Navy and High Speed Support Vessel (HSSV) for the Royal Navy of Oman. Austal also designs, constructs, integrates, and maintains an extensive range of patrol and auxiliary vessels for government agencies globally, including the Cape Class Patrol Boat Program for Australian Border Force. Defence vessels are designed and constructed in Mobile, Alabama and in Henderson, Western Australia.

Austal has been at the forefront of the high speed ferry market since the early days of the industry. Our market leading designs of high performance aluminium vessels have long been at the heart of Austal’s research and development.

Systems

Austal has expertise in integrating complex systems into its ships, including ride control, ship management, and communication, sensors and weapon systems.

Support
Austal provides a wide range of support services, including through life support, integrated logistics support, vessel sustainment and systems support. These services are delivered through our global support network in the USA, Australia, Asia, and the Middle East together with partner shipyards worldwide.

**For further information contact:**

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