



HD Austin Engineering Limited (ASX:ANG) Acquisition of VR Steel South Africa and Trading Update

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Brisbane, Australia, May 21, 2014 - (ABN Newswire) - The Directors of Austin Engineering Limited (ASX:ANG) are pleased to announce the signing of a binding memorandum of understanding (MOU) to acquire 74.9% of the shares in South African **mining** attachment business, Van Reenen Steel Pty Ltd (VR Steel).

The minority shareholder is VR Steel's Black Economic Empowerment (BEE) partner, a trust known as the Building Exciting Education Trust, which is chaired by VR Steel principal, Mr John Van Reenen. It is a requirement of the **Mining** Charter of South Africa, issued under that country's **mining** development laws, that all suppliers to the South African **mining** and minerals industry, such as VR Steel, have a BEE partner which has minimum ownership in the supplier of 25% plus one share.

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Acquisition rationale

The proposed **acquisition** is consistent with the **Company's** long standing stated **acquisition** strategy and objective to have **operations** in every major **mining** region of the globe. This includes **China**.

It provides:

- a low risk entry into the African **mining** products market
- exposure to the **China** market and manufacturing capabilities
- exposure to the US/South American/Indonesian market for draglines, dippers and shovels
- potentially significant opportunities for Austin and VR Steel to cross sell their product to each other's customers in their traditional markets.

It also creates a significant IP rich business and positions the **company** to take advantage of increased in spending by its **mining** clients.

Managing Director Michael Buckland stated "the combination of Austin Engineering and VR Steel will see a clear market leader on a global basis delivering a range of non-EOM products second to none within the industry. VR Steel has been approached for **acquisition** in the past by significantly larger companies than Austin but has chosen Austin as its partner going forward due to the synergies and potential of the combined entity. The fact that the principal of VR Steel, Mr Van Reenen, has taken the consideration in shares highlights his and Austin's faith going forward.

About VR Steel

VR Steel started business in 1992 as a specialist steel distributor and service centre. It has since grown to be one of the world's largest non OEM **mining** attachment design and manufacturing companies, second to Austin Engineering.

VR Steel designs, manufactures and repairs all loading tools and truck bodies with its principal manufacturing and office facilities in Alrode, Gauteng, South Africa and representative sales offices in Australia, **China**, Chile and the USA.

VR Steel is also the exclusive marketing agent of Taiyuan Heavy Industry Co Ltd's range of heavy **mining** machinery into the South Africa/North American market. VR Steel also licences its truck body and bucket designs under a commercial arrangement with a **Chinese** manufacturer to supply one of the leading **coal** mines in **China**.

The **acquisition** offers Austin an ideal entry point principally into the South African **mining** products market where VR Steel is currently the only **mining** attachment business with their own design IP and manufacturing facilities. It also provides exposure to the **China** market for its truck body designs and to the US market for its buckets.

Design and manufacture of customised **mining** attachments

VR Steel has developed strong relationships with the major multinational **mining** companies in Southern Africa, which it leverages to sell its existing range of products and imported products and which creates a solid platform for new sales into new **mining** product markets in the north and west of the African continent.

Their experience in the custom design of **mining** attachments for open cast **mining** covers a broad range of commodities from **coal** to **iron ore**, **copper**, platinum and diamond **mining**.

Repair and maintenance

VR Steel's maintenance division leases a facility from one of its multi-national customers in the Middleburg **coal** fields region where it offers a unique maintenance contract. These maintenance contracts offer a regular flow of repair work through the facility as well as an opportunity for VR's engineering team to trial and monitor innovative new concepts and modifications to their bucket designs. The facility provides repair and maintenance services to a range of customer in the area for all open cast **mining** attachments including buckets and truck bodies.

Synergies and benefits of a combined product range

There are excellent global synergy opportunities between VR Steel and Austin.

Both Austin and VR Steel have successful truck body designs. Austin's Westech business has 45 years of experience since it first began designing off highway truck bodies in 1969. The VR Steel truck body design has also been very successful, particularly in hard rock environments in South Africa and Australia.

By adding the VR Steel truck body design to the product range Austin is now able to offer global customers a variety of body design options to best suit their individual requirements. Immediate opportunities also exist for VR Steel to introduce the Westech and JEC body designs into Africa, particularly in the expanding **coal** market where Westech's new flow control design is outperforming expectations and competition.

In addition, VR Steel provides Austin with experience in a wider range of buckets and shovel dippers and a new product line in equipment jewellery such as rigging chains and attachments manufactured from high strength steel plate. Its extensive knowledge and experience in dragline buckets, dippers and face shovels will complement Austin Engineering's current range of **mining** attachments and complete the full suite of **mining** attachment products for the business.

The additional product range acquired from VR Steel will enhance Austin Engineering's product offerings across its global **operations**. This will increase workflow through Austin's **operations** increasing recoveries and profits.

There are significant opportunities for VR Steel's products, in Australia, South America, Indonesia and USA in particular, where larger digging tools are more common. A number of Austin facilities across the world already manufacture larger equipment for others and with the introduction of the VR Steel designs; Austin will now be able to sell a more competitive product direct to the end user on the back of VR Steel's knowledge and experience as a world leader in this product category.

Benefits of VR Steel designs

VR Steel's equipment offer a unique design in that they are fully fabricated from plate materials and do not require large castings which are typical of most OEM designs. The fabricated designs reduce overall weight offering improved digging performance as well as significantly improved manufacturing **lead** times and reduced cost.

VR Steel's innovative tapered bucket design also improves filling time and reduces weight by eliminating the need for a spreader bar and associated rigging. The industry feedback on the tapered bucket design has been very positive.

Engineering capability

Both Austin and VR Steel differentiate themselves in the **mining** attachment market through their custom engineering capabilities. VR Steel has a highly qualified and experienced engineering team using the latest software for engineering design and analysis. Their software is compatible with Austin's software which allows for seamless sharing and integration of engineering IP and the opportunity to share engineering resources.

Exposure to **China** market and manufacturing capability

VR Steel has an exclusive license to sell TZ heavy equipment into the South African market which gives significant cost benefits to the end user. To date they have been successful with orders for a major African miner and expect a further order shortly. VR Steel will also provide accessory equipment for each of the machines sold as well as maintenance services. This form of revenue contributes excellent returns and is expected to increase over the years.

VR Steel also licences its truck body and bucket designs to a **Chinese** manufacturer under a commercial arrangement to supply one of the leading **coal** mines in **China** that has a fleet of over 250 trucks and numerous digging equipment. The agreement with the manufacturing partner is based on VR providing design packages and technical support in return for a share of the net profits earned on all equipment manufactured through the facility. The manufacturing partner owns the workshop facility and provides all of the labour, management, administration, materials and consumables.

There is potential for additional sales of VR Steel products to new customers in the **Chinese** domestic **mining** product market and also for sales of the existing Austin product range.

The manufacturing facility of VR Steel's manufacturing partner could potentially also manufacture truck bodies for supply into the Australian market.

Exposure to US market for draglines, dippers and face shovels

VR Steel LLC is a relatively new entity which has been established to grow the dragline, dipper and face shovel business in the US and Canada. The US business has had some excellent success in a fairly short space of time with the receipt of 5 new dragline bucket orders to be completed in FY15.

Proposed **acquisition** terms

- Completion conditional on Austin shareholder approval, due diligence satisfactory to Austin, South African regulatory approvals and shareholders agreement with minority BEE partner
- Forecast FY15 EBITDA of \$5.8 **million** (see Note 1) and immediately EPS accretive (excluding synergy benefits)
- Written down value of total assets of AUD\$21m (see Note 1)
- Agreed **purchase** price of AUD\$21.8m for 74.9 % of VR Steel and controlled entities, based on multiple of 5.0 times forecast FY15 EBITDA of 2AUD\$5.8m. The forecast FY15 EBITDA is attributable to VR Steels existing ordinary business revenue, together with incremental revenue from the distribution of **Chinese** equipment into Southern Africa and US dragline sales. A large part of the forecasted earnings is supported by existing orders.
- Funded by issue of 12,663,876 Austin Engineering Ltd shares at issue price of \$1.70, plus A\$300,000 cash
- Consideration shares to be escrowed
- Austin has the right to place/buyback shares becoming available for **sale**
- The Managing Director of VR Steel, Mr John Van Reenen, will continue in his current capacity for a minimum of 3 years and in each financial year from FY15 - FY17, will be entitled to receive a bonus equal to the amount by which VR Steel EBIT exceeds 1 \$5.3 **million**. Austin will receive and retain the benefit of revenue synergies from the **sale** of VR Steel equipment or products in existing Austin markets.
- Land and buildings are not included and will be leased. An option to acquire the land is being negotiated
- Completion is expected by the end of July

Industry Consolidation

In addition to VR Steel, the **company** can confirm that it has been in discussions with two other companies that operate in the **mining** equipment market.

Commenting on the discussions Managing Director Michael Buckland stated:

"We have seen the need/opportunity for consolidation of the **mining** equipment/services industry over the last 12 months during a time in which the **mining** companies have been delaying significant amounts of expenditure, despite increases in production levels.

We consider the current cycle to be at the bottom, and the right time to make strategic acquisitions/mergers, to position Austin as the dominant global player as the market picks up. The companies that we are in discussions with are very highly respected companies in the **mining** equipment/services market and have specialised IP and products which, when added to Austin's existing range, provides the market with an unparalleled range/choice of customised equipment.

The principal aim of these acquisitions will be to achieve significant synergies and efficiencies."

Due diligence is underway on the other two potential targets. The **Company** expects that if discussions prove to be successful, further announcements will be made over the next two months. Investors and shareholders should be aware however that there is no assurance that any discussions will be successful or that any transaction will eventuate from the current or any future discussions. Conjecture about the outcome of these discussions or a resulting transaction is premature.

Revised earnings guidance

The earnings guidance provided by the **Company** was based on expected orders. These have not been received in the expected timeframes due to continued deferred procurement by major miners and longer than expected contract administration **lead** times,

As a result, the Directors have been required to review their assumptions and, based on the revised assumptions, the **Company** provides revised guidance for FY14 of \$15 - 18 **million** EBITDA.

While there can be no denying that this is a very disappointing and unexpected result, the Board continues to believe that the overall strategy remains fundamentally correct. We are established in the major **mining** centres of the world, with a reliable and trusted product range and have not seen a diminution of our market share. We continue to see increasing use of customised design equipment over standard OEM equipment. This encourages Austin to believe that the current downturn is due to cyclical factors. It is about timing; while the miners continue to dig they require our product. That the experienced owners of VR Steel are willing to take almost all scrip consideration represents some independent validation of the **Company's** view.

Many of Austin's **operations** are based on 2 - 4 week turnover of orders i.e. Cor Cooling (6 **operations**), Austbore, Pilbara Hire, Calama maintenance and the two crane **operations** in Chile. Orders of this nature can contribute \$2 - 3 **million** of EBITDA per month. The larger Austin **operations** generally need 4 - 6 weeks for order processing and orders of this type can contribute \$5 **million** of EBITDA per month. The **company** was of the view that if the expected combination of smaller and major orders were received, the **Company** was capable of producing a result not materially lower than earlier guidance.

Amongst the major projects that the **company** anticipated, but are still delayed, are the following:

- Vale - The **Company** has been waiting on the Vale corporate office to complete registration of part numbers against Austin products in Vale purchasing systems. The delay has been caused by changes within the Vale organisation handling the Austin contract and a major transition to a new enterprise management system. Vale has assured Austin that the first order will be issued before the end of June as the new system begins processing.

The Vale contract is a 3 year supply agreement and although the precise value of this contract is not predetermined, Vale has informed the **company** that the previous contract was for a total of USD 200 **million** and that the current contract will be split between two companies, with Austin receiving the larger part of the contract. Vale has confirmed that no orders have been placed with either Austin or the other supplier due to the above issues.

- Collahuasi - A very significant contract for the supply of all new and replacement truck bodies and the maintenance of the entire truck body fleet. Site services will also be included. Collahuasi is Chile's second largest **Copper** mine and is planning a doubling of the mine over the next 2-5 years. The **Company** believes it will be awarded this contract soon but planning and administrative issues are delaying the finalisation of the agreement. The length of the contract will be a minimum of 3 to a maximum of 9 years

- Codelco -Chile's major client deferred all tray replacement in March (usually 30-50 trays) until 14/15 financial year

- East Coast - Two major tenders have been submitted and subsequently negotiated over the last 6 months. Contract awards are expected in the next month

- Indonesia - Awaiting a major contract for a new mine. Austin believes it is likely to be the preferred supplier of over 20 trays

- Colombia - Awaiting awards of equipment for the Cobre Panama project (\$5 billion mine)

- West Coast - Major clients of our operations had initially deferred scheduled production for one year, this has now been deferred a further 6 months. The West Australian operations have seen the biggest decline to prior periods

A number of new 3 year contracts have been announced but these will have minimal impact on second half FY14 numbers as contributions will only impact 2 - 3 months in FY14. These contracts will have a full 12 month impact on FY15 and beyond.

Commenting on the results Managing Director Michael Buckland stated "despite a good start to the second half and expectations of some major contracts the miners have continued to delay purchases of all equipment. This has now continued for 12 months despite maintaining or increasing production levels. Whilst equipment can be maintained for a period beyond its normal life, the costs increase rapidly making it uneconomical to keep persevering with repairs. We have seen an increase in the number of enquiries but as yet these have not been converted into orders.

Based on its recently announced multi-year contracts and the expected award of new contracts, Austin is expecting to see a significant turnaround in FY15 compared with the forecast FY14 result, especially from January 15 onwards (excluding the contribution from VR Steel and other potential acquisitions).

Bank facilities

The reduced earnings may potentially result in technical breaches of Austin's banking facilities. Austin is working constructively with its senior lenders to address these issues proactively and the senior lenders are supportive of the Company.

The Company believes that it will not need to raise additional capital to meet its debt service requirements.

Note: 1. Based ZAR / AUD\$ exchange rate of R9.67 to \$1.00

About Austin Engineering Limited

Austin Engineering is a leading designer and manufacturer of customised dump truck bodies, buckets and ancillary products used in the mining industry. We are also a complete service provider, offering on and off-site repair and maintenance and heavy equipment lifting services to customers including miners, mining contractors and original equipment manufacturers. With a presence in some of the world's principal mining regions, Austin Engineering provides high quality, cost effective solutions, delivered on-time and backed by through-life product support.

To view the release, please visit:

<http://media.abnnewswire.net/media/en/docs/77206-ASX-ANG-798077.pdf>

Contact:

Managing Director

Michael Buckland
Tel: +61-7-3271-2622

Scott Richardson
Chief Financial Officer
Tel: +61-7-3271-2622
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