



# A STABLE PLATFORM FOR FUTURE PROGRESS

This year's performance has been underpinned by our leading market positions. We have delivered increased profits and our order books are at record levels. With changing market conditions, it is important we remain fit and healthy for future growth. We have therefore launched the Future Proofing Kier programme which is focused on improving our ways of working.

## **We have market-leading positions supported by specialist capabilities, enabling us to deliver for our clients.**

### **How would you summarise the Group's performance in 2018?**

Overall it was a good year for Kier and I am pleased with our underlying performance. This performance is particularly noteworthy given the challenges that the contracting sector has had to address during the year.

We have made progress on our key financial and non-financial targets and are on track to deliver on our Vision 2020 goals. We increased profit by 10%, delivering full-year underlying operating profit of £160m in line with our expectations and market consensus. We also maintained our market-leading positions in the infrastructure services and buildings markets, and our top-three position in the affordable housing and maintenance market.

With greater investor attention on debt following the demise of Carillion, our net debt position remains under focus. Net debt increased in the year, as expected, following the acquisition of McNicholas in July 2017.

It is anticipated that our decision to stabilise investment in the Property and Residential businesses and the Future Proofing Kier programme will significantly reduce net debt over the next two to three years.

Following the acquisition of McNicholas in July 2017, we have successfully completed the integration of that business, making us one of the largest providers of services in utilities with specialisms in the energy and power, telecoms and water sectors.

We have also performed well against our Vision 2020 non-financial targets covering safety, customer experience, employee engagement and retention, and sustainability. These targets are intrinsically linked to our strategic priorities and business model, creating value for our customers and other stakeholders.

### **Record order book**

# £10.2bn

(2017: £8.9bn)

### **Revenue<sup>1,2</sup>**

# £4.5bn

(2017: £4.3bn)

<sup>1</sup> Continuing operations. Group and share of joint ventures.

<sup>2</sup> Continuing operations. Stated before non-underlying items. See note 4 to the consolidated financial statements.

# “OUR CLIENTS’ PRIMARY OBJECTIVES ARE TO SERVICE THEIR END-USERS AND WE NEED TO SUPPORT THAT GOAL”

Turning to safety, which is at the heart of our licence to operate and remains a priority for clients when procuring work, I am delighted to say that our safety performance in 2018 was encouraging. We achieved an accident incidence rate (AIR) of 96, which is UK-leading for the Group as a whole and reflected a 26% improvement on the previous year.

I am pleased with our overall performance for the year.

## Can you explain the rationale for the move to the three market positions?

The transition to the three market positions of Infrastructure Services, Buildings, and Developments & Housing, reflects the increasing demand in these markets from customers as well as our specialist capabilities.

In adopting this approach, we also aim to address the main challenges facing the UK today. All three of these markets have robust long-term fundamentals which are driven by changing demographics and the increasing use of technology. As part of Future Proofing Kier programme, a re-aligned business model focuses the efforts of our teams and makes it easier for us to deliver for our clients.

Whatever sector they operate in, our clients’ primary objectives are: to service their end-users – be they water consumers, road users, housing tenants or rail passengers – as best they can. Through our three market positions, we aim to leverage our skills, knowledge and innovation to provide solutions which make this happen as efficiently and effectively as possible. We also want to build closer relationships with clients, so we can better understand the challenges they face and find solutions with them.

## How will the new Future Proofing Kier programme help to drive efficiency across the Group?

Following the launch in June of Future Proofing Kier, our efficiency and streamlining programme, we are currently focused on improving our productivity, removing duplication of processes and non-value activities, and disposing of non-core operations. It is anticipated that the actions taken during FY19 will deliver annual profit and cash flow improvements of 10% of profit from operations, c.£20m from July 2019, with targeted proceeds of £30m-£50m from the disposal of non-core businesses. This programme will help the Group achieve its target of year-end net cash and average net debt of £250m for FY21. The programme activity undertaken in the current financial year will be cash and earnings neutral and I expect the programme to deliver material improvements in operating margins and cash generation in the financial year ending 30 June 2020 and beyond.

Our alignment to three market positions and our significant investment in new systems provides the opportunity to optimise how we operate. We want to be resilient to accommodate changes in the marketplace; our markets continue to evolve, which requires us to be flexible and front-footed to ensure we meet the changing needs of our clients and the markets in which they operate.

Streamlining and transforming the Group in this way will make us more agile and give greater responsibility and accountability to our operations. In procurement, for example, we have created a powerful back-of-house shared services function. The Future Proofing Kier programme will ensure this and other similar back-of-office functions link seamlessly to the operations.

Overall, the programme will improve the resilience of the Group in a changing market and help us to better leverage the system investments we have made while strongly positioning the Group for 2020 and beyond.

## What is your balance sheet strategy?

Our debt position remains a key area of focus for us and our investors. Historically we have used our asset-backed debt strategy to fund our Property and Residential activities. We have now taken action to accelerate the reduction of our net debt position and stabilise the Group’s investment in our Property and Residential divisions through the use of joint ventures with our clients. Our current average net debt position of £375m is backed by assets at a cost of £500m, which provides significant cover for our net debt position.

The average net debt figure for this year increased on the previous year as a result of the acquisition of McNicholas and the reduced Construction revenues over the winter due to bad weather, which have since returned to levels in line with our expectations. I believe our efforts to reduce net debt will yield results, and these will now be further strengthened by the results of the Future Proofing Kier programme.

## Pension surplus

Looking more broadly at the balance sheet, our pension schemes are now in surplus. Our current pension scheme is fully funded and we therefore expect our tri-annual valuation discussions in March 2019 to be positive. At the same time, our working capital performance is strong, with operating cash conversion for 2018 at more than 100%, which shows we continue to maintain very good financial discipline. Having reached the end of our major systems investment, we also expect our capital expenditure to return to normalised levels of around £30m per annum, having been around £90m per annum for the last few years.

# “WE WANT TO USE OUR POSITIONING TO BUILD CLOSER RELATIONSHIPS WITH CLIENTS, SO WE CAN BETTER UNDERSTAND THE CHALLENGES THEY FACE”

## How did market developments impact Kier in 2018?

There has been a significant level of turbulence in our markets over the past 12 months. Unsurprisingly, this has led to increased scrutiny of the performance and financials of companies in our sectors and the ways in which we operate – for example, how we work with the supply chain and SMEs with particular reference to payment terms.

We are confident that Kier has always had and will continue to have strong financial and operational disciplines particularly in its commercial and risk processes.

For example, in Construction our focus is on high-volume, modest-value contracts, primarily pursuing new work under frameworks or lower risk contract models. We operate over 400 projects at any one time, with an average value of about £7-8m. This helps us spread our operational risk and means we are more agile to respond to market developments.

We are a key supplier to government in the markets in which it is investing in e.g. affordable housing, social and economic infrastructure. Many of our businesses operate through government frameworks and five-year funding periods, which gives us access to more visible pipelines of work.

More specifically, as a result of market developments in the year including the liquidation of Carillion, Kier acquired a greater share of the HS2 project and the Highways England's Smart Motorways portfolio. We transferred over 150 people into the company to help deliver these increased project requirements and worked closely and collaboratively with our clients during these challenging periods.

## Collaboration

We are known for our strong relationships with clients, working collaboratively with them, anticipating issues they face, providing problem-solving solutions and innovation.

A good example of working collaboratively is our work with Highways England, who have long-term, stable budgets and visible future investment plans. As a key supplier to Highways England, we work with them as they develop solutions such as their Routes to Market strategy and are helping them with the transition to this model. Closer working with our clients provides the best outcomes and is critical to securing new work, such as the recently announced extensions to Highways England Areas 3, 6, 8 and 9 contracts.

## Sector opportunities

More generally in transport, a market sector where Kier has established credentials, there are considerable opportunities arising in local authority roads, and in the rail sector with the launch of its next investment period, CP6. Our credentials in rail have been significantly enhanced following the acquisition of McNicholas and we expect to play an active role in the next review period, CP6.

In infrastructure we anticipate the increase in demand for UK power generation will present opportunities in the nuclear, renewables and gas sectors over the next five-to-ten years. We will continue to monitor these markets closely and we are also in discussion with many of our water company clients as the water cycle, AMP7, starts its procurement phase.

In Buildings, we remain the UK market leader with a focus on key sectors such as education and health. In education, expenditure is driven by a growing population and the need to continually invest in the existing estate.

In health, the Government has recently announced an increase in NHS funding of 3.4% pa. Whilst it is expected that much of this investment will go into front-line services, we expect this will create an additional pipeline of opportunities in related sectors such as bioscience where we have also successfully established a strong presence over the last few years.

In addition, the UK's investment in aviation, with the approval for expansion at Heathrow airport, will provide a major, multi-year boost to a sector which is seeing growth across in the UK. Meanwhile, public policy is increasingly supporting modern methods of construction (MMC) and we have already delivered over £2bn of projects that include MMC over the past five years.

In our Residential division, we are set to benefit from the UK Government's Help to Buy scheme that has been extended to 2021, supporting the increase in the building of affordable housing. With a national shortfall of a least one million homes, this is a market with significant growth potential and one we are actively targeting. Our innovative approach to using joint ventures, such as the Homes England joint venture launched in May, is enabling us to accelerate the development of our residential land bank through a capital efficient model. The creation of the Homes England joint venture has created an opportunity for Kier to increase the scale of its affordable house building activities by c.500 units per annum from 2020.

## Strong progress against Vision 2020

Since 2014 we have made good progress on our Vision 2020 targets.

Key metrics	2020 target	June 2018
Annual average operating profit growth	> 10%	On target
Property – ROCE	> 15%	Ahead
Residential – ROCE	to 15%	On track and improving
Construction – EBITA	to 2.5%	On track
Services – EBITA	to 5.0%	On track
Net debt: EBITDA	1:1	Achieved
Dividend cover	2x	On track and improving

### How is Brexit affecting your markets and business?

We have seen no material impact of Brexit to date. However, the Kier internal Brexit Taskforce team monitors our supply chain-labour mobility and materials availability. With continued uncertainty, we are scenario-planning and working with our clients and others in the industry to ensure we are able to respond to future developments.

We are particularly focused on monitoring the issue of labour mobility. The strength of many of our supply chain partners is directly linked to the flow of people and skills into the UK, particularly in London and the South East, where a larger proportion of our supply chain workforce is made up of non-domestic individuals.

Our regional presence will therefore significantly mitigate any Brexit labour mobility risk that arises, as will our sector diversification. Our property development business has experienced limited change in occupier demand and investment, but it continues to closely monitor the market and the phasing of property transactions.

### How did Kier perform from a non-financial perspective this year?

#### Safety

Our safety performance in 2018 was encouraging, although improvements can always continue to be made. Our safety focus is a key element of how we operate as a business. We achieved an accident incidence rate (AIR) of 96, reflecting a 26% improvement on the previous year. As a recognised measure of safety performance, our AIR not only reflects how we do business but is a key differentiator in the market. Indeed, safety is becoming increasingly important for our clients at the selection stage.

During the year, we maintained our focus on promoting a good safety culture. As the majority of our safety incidents are slips, trips and minor falls, our priority is to improve behaviour rather than overhaul working policies and practices.

To this end, in 2018 we engaged and partnered with external safety consultants to address the issue of minor incidents, particularly in our Highways and Buildings businesses. Looking ahead, we will continue to progress with our current efforts, focus more on every day behaviours, and drive improvements in areas such as health and wellbeing.

#### Health and wellbeing

The health and wellbeing of our teams, both Kier employees and the supply chain, is key as it directly impacts on operational safety. We have approximately 100 health champions across the Group who are trained to monitor and assess employees' mental and physical wellbeing. They are supported by a team of qualified on-site healthcare professionals. We provide fitness-for-work health screening for Kier employees as well as ongoing care through the occupational health team.

## Chief Executive’s strategic review continued

### Diversity

Diversity and inclusion is a key priority and one where we are taking meaningful action as a business. Our business and industry already employs people with very diverse socio-economic backgrounds, but we acknowledge we have considerable scope for improvement in the areas relating to ethnic and gender diversity. We have established several internal forums, such as our Balanced Business Network and the LGBT+ and Allies Network. In addition, we have created a Gender Strategy Steering Group which is responsible for driving leadership action on gender. We have a particular focus on gender pay, where our median pay gap reported this year was 20.2%, higher than the national average. We have fewer women in senior roles which means we have proportionately more men earning higher salaries. We are focused on tackling this gap to increase the number of women coming into Kier and progressing to senior roles.

In addition to Group initiatives, our operational businesses support a number of key topics which are of particular importance to their clients. For example, in our Highways business, we have made good progress around disability, and in 2018 we achieved the Disability Confident accreditation for our work, supporting Highways England’s focus on this topic.

We also continued our strong focus on our graduate and apprenticeship programme, where we have maintained more than 5% of our workforce on approved training schemes. As a member of the UK’s 5% Club, we have approximately 1,200 graduates and apprentices currently engaged in training across the business. As a responsible business, it is vital we are in a position to develop the necessary UK skills and expertise to support industry growth in the future. We are actively seeking to encourage the Government and the public sector to make this level of commitment a pre-requisite for tenders. We are continuing to promote our Shaping Your World campaign, launched in September 2017, which encourages 11-15 year olds to consider careers in construction and the built environment. We are proud to report that we have exceeded the targets we put in place for the first year of the campaign with over 350 Shaping Your World ambassadors across the Company who regularly visit schools to explain the industry and to talk about the many and varied career opportunities available. This campaign reached more than 15,000 students in its first year.

### Environment

In 2018 we launched the first three environmental initiatives as part of our 30 by 30 strategy, which aims to reduce our energy usage by 30% by 2030. The strategy covers a broad range of activities, from the reduction of construction waste to water consumption and use of plastics. It should begin to deliver financial savings over the next 12 to 18 months, and over time will enable us to make a greater contribution to environmental protection and sustainability.

### What sets Kier apart from the competition?

The Kier business model is at the heart of our competitive differentiation. Through our three market positions, we aim to leverage our skills, knowledge and innovation to provide solutions which make this happen as efficiently and effectively as possible. Our business model provides stability and certainty when individual markets fluctuate.

In Construction, our high-volume, low-value approach offers a lower risk model which protects us from profit and cash flow volatility. It provides us with long-term visibility, with projects often delivered in framework arrangements, many with five-year terms.

The breadth of our Services business also provides both job interest and career opportunities for our employees, and stable financial performance. We have chosen to work in markets where we provide critical services, such as repairing roads or fixing leaks in water networks – essential everyday maintenance that has to be undertaken, and where future investment is more certain.

We are increasingly using joint ventures across our Property and Residential operations to make more efficient use of our capital. This is evidenced through the Cross Keys and Homes England joint ventures announced over the last year, and the use of joint ventures on many of our property development schemes, such as those with Network Rail and Watford Borough Council.

We provide specialist services to a broad range of sectors, and we have a track record of problem-solving and providing fresh thinking to our clients. For example, we regularly use off-site construction and modern methods of construction on projects. As part of this process, we offer our clients a unique breadth of complementary capabilities to help meet their project requirements.

### Supply chain

Our focus is truly local, using local resources and talent to benefit the local community. It’s what I call a national footprint with a local flavour. Our regional network of over 80 offices enables us to deliver projects and services anywhere in the UK. Another key differentiator is the fact that, as a result of our average project size and the every day services we provide, we use very local SME supply chains. Around the business, we have a strong regional focus, unique among our peers, having developed robust supplier relationships built on local knowledge and trust over many years. These relationships have helped us establish powerful market positions outside of London and the South East.

Collaboration with our supply chain is also critical, and each year our businesses spend time with our suppliers, working to understand how we can better partner and innovate alongside them. Keen to deepen these relationships and ensure continuity of supply, we offer a variety of contract types and payment mechanisms, including early payments schemes for the supply chain. These are popular, often helping them with their working capital challenges, a typical feature of the sector.

### Shaping Your World campaign

**350+**

Kier ambassadors

**15,000+**

Students engaged

### Safety: Group Accident Incidence Rate (AIR)

**96**

Improved by 26%  
(2017: 130)

# “THROUGH OUR THREE MARKET POSITIONS, WE AIM TO LEVERAGE OUR SKILLS, KNOWLEDGE AND INNOVATION TO PROVIDE SOLUTIONS WHICH ARE EFFICIENT AND EFFECTIVE”



Watch Haydn Mursell's interview online – [www.kier.co.uk](http://www.kier.co.uk)



These activities are clear recognition of the importance of our suppliers to our long-term business success and sustainability.

In our Highways business, we have brought new technology into the sector. For example, the Kier Highways team has transferred the concept of Roadrake, which is used to clean beaches in Australia, to the UK to clear litter on the Highways England network. This technology is now being rolled out on to other parts of the Highways England network. Working in collaboration with our supply chain, we are responsible for introducing a range of new technology into the highways market which Highways England and other members of their supply chain have adopted. We are proud of our track record in this field.

## What are your future priorities?

The UK's demographic trends support our three market positions while our balance sheet will continue to strengthen and benefit further from the implementation of our Future Proofing Kier programme.

We are focused on reducing our net debt, which will also benefit further from the Future Proofing Kier programme. We will continue to pursue growth in our core operations, streamlining the Group's portfolio of businesses as necessary, and we will increase the operational efficiency of the business, ensuring we continue to deliver for our clients and be their trusted partner. In light of market challenges, we will continue to closely monitor the risk profile of the Group.

We are on track to deliver on our Vision 2020 goals. We have a record order book of c.£10.2bn, and our Construction and Services divisions are 90% secured, with improved visibility of the work they need to undertake in the 2019 financial year. We also have a pipeline of work of £3.5bn in our property and residential businesses. These developments will provide the Group with greater resilience as we progress to 2020 and beyond.

I believe our core businesses are performing well and we have leading positions in our chosen markets. Kier is very well placed for the future.

**Haydn Mursell**  
Chief Executive

19 September 2018