Austal Limited Half-Year Report

31 December **2019**

AUSTAL

Company Overview

Austal (ASX:ASB) is an Australian shipbuilder, global defence prime contractor and marine technology partner of choice, designing, constructing and supporting revolutionary commercial and defence vessels for the world's leading operators.

Specialising in high-speed aluminium monohull, catamaran and trimaran hull vessels, Austal now offers (and is producing) steel vessel solutions for clients including the Commonwealth of Australia.

An export award-winning company, 80% of Austal's global vessel production has been delivered to overseas customers, from shipyards located in Australia, the United States of America, The Philippines and Vietnam.

The company also has a joint venture operation in China called Aulong that is designing and constructing commercial ferries for the domestic Chinese mainland market.

Austal has designed and constructed some of the world's most innovative defence vessels that are redefining naval capability; including the 127 metre trimaran-hull Independence-class Littoral Combat Ship (LCS) and the 103 metre Spearhead-class Expeditionary Fast Transport (EPF) catamaran for the United States Navy.

Austal USA, in Mobile Alabama is the only foreign owned prime contractor designing, constructing and supporting ships for the United States Navy.

Austal's success in high-speed commercial vessel design and construction is demonstrated by an impressive portfolio that includes more than 180 passenger ferries, vehicle passenger ferries, offshore crew transfer vessels, wind farm vessels, cruise, live aboard and private motor yachts delivered since 1988.

2020 H1 Key Facts

$1.04B
Revenue

$4.3B
Order Book

3
New ships ordered

41
Ships scheduled or under construction

6
Ships delivered

27
Vessels under sustainment

7 shipyards in **5** countries

6 Service Centres

6,000 Employees

Contents

Directors' report

It is my pleasure to present the financial report for the half-year ended 31 December 2019 to you on behalf of the Board of Austal Limited.

Directors

The Directors in office during the half-year and until the date of this report were:

- John Rothwell (Chairman)
- David Singleton (Chief Executive Officer)
- Giles Everist (Non-Executive Director)
- Sarah Adam-Gedge (Non-Executive Director)
- Chris Indermaur (Non-Executive Director)

Principal Activities

The principal activities of entities within the consolidated entity during the reporting period were the design, manufacture and support of high performance vessels. These activities are unchanged from the previous reporting period.

Results

Austal reported key financial results as follows:

- FY2020 H1 revenue was $1,038.762 million which is higher than the prior corresponding period (PCP) (FY2019 H1: $851.253 million).
- Earnings Before Interest and Tax (EBIT) was $59.929 million (FY2019 H1: $40.374 million).
- Profit Before Tax (PBT) was $57.060 million (FY2019 H1: $36.304 million).
- Net Profit After Tax (NPAT) was $40.752 million (FY2019 H1: $23.667 million).

Reconciliation of EBIT and EBITDA (unaudited)

		2020 H1 $'000		2019 H1 $'000
Profit Before Tax	$	57,060	$	36,304
Finance costs	$	4,014	$	4,321
Finance income		(1,145)		(251)
EBIT	$	59,929	$	40,374
Depreciation	$	23,116	$	19,152
Amortisation		1,333		1,138
EBITDA	$	84,378	$	60,664

Austal uses a number of non-AASB measures to assess performance which are defined as follows:

- EBIT – earnings before interest and tax.
- EBITDA – earnings before interest, tax, depreciation and amortisation.

The information is unaudited but is extracted from the financial statements which have been reviewed by the auditors of the Group. EBIT and EBITDA are used to understand operating performance of the Group.

Review of Operations

USA Operations

USA segment revenue was $804.612 million (FY2019 H1: $686.823 million), and EBIT was $65.564 million (FY2019 H1: $49.137 million). The segment result is a combination of shipbuilding and sustainment activities.

Revenue and earnings in FY2020 H1 were higher than the prior corresponding period, principally due to:

- Expanded throughput on the Expeditionary Fast Transport (EPF) and Littoral Combat Ship (LCS) programs following the $3.1 billion of new vessel awards received during FY2019.
- Growth of the sustainment business.

The Independence-class LCS program is at full rate production with six ships currently being commissioned or under construction. USS Kansas City (LCS 22) successfully completed acceptance trials in the Gulf of Mexico during November 2019 and is scheduled for delivery in FY2020 H2. The future USS Oakland (LCS 24) was launched recently and is being prepared for trials, whilst final assembly is well underway on the future USS Mobile (LCS 26) and USS Savannah (LCS 28). Modules for the future USS Canberra (LCS 30) are under construction in the module manufacturing facility, and construction of the future USS Santa Barbara (LCS 32) began in October 2019.

Two Spearhead-class EPF are under construction, USNS Newport (EPF 12) is in final assembly, whilst construction recently began on the future USNS Apalachicola (EPF 13) in the module manufacturing facility. Manufacturing of the future USNS Cody (EPF 14) will commence in FY2020 H2.

Delivery of EPF 11 USNS Puerto Rico occurred in December 2019.

Sustainment revenue continues to expand providing a significant increased source of recurring earnings from the San Diego, Singapore and Mobile service centres.

Australasia Operations

Australasia segment revenue was $240.711 million (FY2019 H1: $169.677 million), and EBIT was $8.226 million (FY2019 H1: $4.148 million).

Revenue and earnings in FY2020 H1 were higher than the prior corresponding period, principally due to:

- The Guardian Class Patrol Boat (GCPB) 21-ship program operating at full production capacity.
- Higher sustainment activity including the continuation of servicing and support for the Cape Class Patrol Boat (CCPB) fleet of 8 vessels operated by the Australian Border Force, CCPB fleet of 2 vessels operated by the Royal Australian Navy (RAN) and sustainment for the GCPB delivered vessels.
- Significant throughput on the 94 metre $98 million catamaran ferry being manufactured in Vietnam for the Government of the Republic of Trinidad and Tobago (GORTT) (awarded in December 2018).
- Progress on a $126 million contract to construct two 58 metre aluminium monohull CCPB for the GORTT which was awarded in August 2019. The Commonwealth of Australia has supported the GORTT with a financing package through Export Finance Australia.

The remaining vessels currently being manufactured in Australasia were progressed including the 109 metre $108 million Fjord Line ferry (awarded in August 2017), two 117 metre Fred Olsen trimaran ferries in the $190 million total contract (awarded in October 2017) and the 83 metre $68 million trimaran ferry for JR Kyushu of Japan (awarded in March 2018).

GCPB 4 and 5 were delivered on time to the Government of Australia during the period. GCPB 4 was then gifted to the Government of Samoa and GCPB 5 to the Government of the Solomon Islands. Austal have now delivered 5 vessels during the last 12 months. Twelve Pacific Island nations including Papua New Guinea, Fiji, the Federated States of Micronesia, Tonga, Solomon Islands, Cook Islands, Kiribati, Marshall Islands, Palau, Samoa, Tuvalu, Vanuatu and Timor Leste will receive the 21 vessels through to 2023.

A $136m contract to construct a 115 metre catamaran ferry for Molslinjen was awarded in October 2019 following the delivery of a 109 metre catamaran to Molslinjen in January 2019. The vessel will feature Austal's signature raked-bow and optimised hull form, and an LNG-capable medium speed engine that offers a powerful yet economical and environmentally-friendly solution.

Austal Philippines delivered a $30 million, 49 metre, high speed catamaran to SNC Aremiti in August 2019.

Cash management & dividends

The net cash position as per the balance sheet was $107.622 million at 31 December 2019 (30 June 2019: $101.911 million).

The Group's net cash position is supressed by the CCPB 9 & 10 leasing program where the accounting treatment of the residual value guarantee increased debt by $(44.763) million at 31 December 2019 (30 June 2019: $(48.798) million). The net cash position was $152.385 million at 31 December 2019 excluding this impact (30 June 2019: $150.709 million).

Importantly, Austal has maintained a strong cash balance of $274.584 million at 31 December 2019 (30 June 2019: $275.665 million), demonstrating the ongoing cash generating strength of the business and ability to distribute dividends. An unfranked interim dividend of 3 cents per share was declared post 31 December 2019.

$10.335 million cash was returned to shareholders via an unfranked dividend following the declaration by the Board of a 3 cents per share dividend on 30 August 2019. The dividend was paid to shareholders on 15 October 2019.

Rounding of Amounts

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars ($'000) unless otherwise stated under the option available to the Group under ASIC Corporations (Rounding in Financial / Directors' Reports) Instrument 2016 / 191. The Company is an entity to which the instrument applies.

Auditor's Declaration of Independence

Austal has obtained an independence declaration from its auditors, Deloitte Touche Tohmatsu, which is on page 8 and forms part of the Directors' Report.

This report has been made in accordance with a resolution of Directors.

John Rothwell

Chairman

19 February 2020

Auditor independence

Deloitte.

Deloitte Touche Tohmatsu
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The Board of Directors
Austal Limited
100 Clarence Beach Rd
Henderson, WA
6166, Australia

19 February 2020

Dear Board Members,

Austal Limited

In accordance with section 307C of the Corporations Act 2001, I am pleased to provide the following declaration of independence to the Directors of Austal Limited.

As lead audit partner for the review of the financial statements of Austal Limited for the half-year ended 31 December 2019, I declare that to the best of my knowledge and belief, there have been no contraventions of:

(i) the auditor independence requirements of the Corporations Act 2001 in relation to the review; and

(ii) any applicable code of professional conduct in relation to the review.

Yours sincerely,

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

A T Richards
Partner
Chartered Accountants

Consolidated statement of profit and loss and other comprehensive income for the half-year ended 31 December 2019

	Notes	2020 H1 '000		2019 H1 '000	
Continuing operations					
Revenue [1]	4	$	1,038,762	$	851,253
Cost of sales	4		(929,578)		(774,145)
Gross Profit		$	109,184	$	77,108
Other income and expenses		$	7,875	$	5,983
Administration expenses			(44,599)		(34,019)
Marketing expenses			(12,531)		(8,698)
Finance costs			(4,014)		(4,321)
Finance income [1]			1,145		251
Profit / (loss) before income tax		$	57,060	$	36,304
Income tax benefit / (expense)	9	$	(16,308)	$	(12,637)
Profit / (loss) after tax		$	40,752	$	23,667
Profit attributable to:					
Owners of the parent		$	40,752	$	23,667
Total		$	40,752	$	23,667
Other comprehensive income					
Amounts that may subsequently be reclassified to profit and loss:					
Cash flow hedges					
- Fair value gain / (loss)		$	6,496	$	(2,682)
- Income tax benefit / (expense)	9		(1,778)		1,277
- Net		$	4,718	$	(1,405)
Foreign currency translations					
- Fair value gain / (loss)		$	(603)	$	24,929
- Net		$	(603)	$	24,929
Amounts not to be reclassified to profit and loss in subsequent periods					
Asset revaluations					
- Fair value gain / (loss)		$	-	$	2,103
- Income tax benefit / (expense)	9		182		(637)
- Net		$	182	$	1,466
Other comprehensive income net of tax for the period		$	4,297	$	24,990
Total comprehensive income for the period		$	45,049	$	48,657
Total comprehensive income attributable to:					
Owners of the parent		$	45,049	$	48,657
Total		$	45,049	$	48,657

Earnings per share (cents per share)	cents / share	cents / share
- basic for profit for the period attributable to ordinary equity holders of the parent	11.5	6.7
- diluted for profit for the period attributable to ordinary equity holders of the parent	11.3	6.6

1. Finance income was previously included within Revenue and has been reclassified below Gross Profit for the current and comparative period.

Consolidated statement of financial position as at 31 December 2019

	Notes	31 December 2019 '000	30 June 2019 '000
Assets			
Current			
Cash and cash equivalents		$ 274,584	$ 275,665
Inventories and work in progress		230,368	167,042
Trade and other receivables		109,798	225,268
Prepayments		11,074	9,480
Derivatives	6	3,114	1,932
Income tax refundable		-	1,701
Total		$ 628,938	$ 681,088
Non - Current			
Property, plant and equipment		$ 574,018	$ 588,384
Intangible assets and goodwill		19,842	20,743
Investment in joint venture		1,729	1,729
Derivatives	6	1,716	258
Right of use lease assets	2	12,464	-
Other financial assets		13,172	11,859
Other non-current assets		6,584	14,838
Deferred tax assets		6,713	8,402
Total		$ 636,238	$ 646,213
Total		$ 1,265,176	$ 1,327,301
Liabilities			
Current			
Interest bearing loans and borrowings	7	$ (8,160)	$ (51,211)
Progress payments received in advance		(81,403)	(120,402)
Trade and other payables		(159,269)	(202,308)
Provisions		(70,269)	(85,305)
Derivatives	6	(4,467)	(8,992)
Deferred grant income		(3,378)	(6,445)
Lease liabilities	2	(3,355)	-
Income tax payable		(1,531)	-
Total		$ (331,832)	$ (474,663)
Non - Current			
Interest bearing loans and borrowings	7	$ (158,802)	$ (122,543)
Provisions		(1,880)	(1,707)
Derivatives	6	(7,176)	(7,552)
Deferred grant income		(54,717)	(56,214)
Lease liabilities	2	(9,313)	-
Deferred tax liabilities		(33,762)	(33,839)
Total		$ (265,650)	$ (221,855)
Total		$ (597,482)	$ (696,518)
Net Assets		$ 667,694	$ 630,783
Equity			
Equity attributable to owners of the parent			
Contributed equity	8	$ 135,119	$ 130,570
Reserves		191,825	189,520
Retained earnings		340,750	310,693
Total		$ 667,694	$ 630,783
Total		$ 667,694	$ 630,783

Consolidated statement of changes in equity for the half-year ended 31 December 2019

	Issued Capital '000	Reserved Shares [1] '000	Retained Earnings '000	Foreign Currency Transl'n Reserve '000	Employee Benefits Reserve '000	Cash Flow Hedge Reserve '000	Common Control Reserve '000	Asset Reval'n Reserve '000	Total Equity '000
Equity at 1 July 2018	**$ 130,165**	**$ (11,836)**	**$ 270,530**	**$ 82,190**	**$ 3,977**	**$ (5,789)**	**$ (17,594)**	**$ 93,935**	**$ 545,578**
Comprehensive Income									
Profit for the period	$ -	$ -	$ 23,667	$ -	$ -	$ -	$ -	$ -	$ 23,667
Other Comprehensive Income	-	-	-	24,929	-	(1,405)	-	1,466	24,990
Total	$ -	$ -	$ 23,667	$ 24,929	$ -	$ (1,405)	$ -	$ 1,466	$ 48,657
Other equity transactions									
Shares issued for dividend reinvestment plan	$ 589	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 589
Dividends	-	-	(10,550)	-	-	-	-	-	(10,550)
Shares issued to employee share trust	202	(202)	-	-	-	-	-	-	-
Shares issued for vested performance rights	313	-	-	-	(313)	-	-	-	-
Dividend retained in relation to AGMSP [2]	9	95	-	-	-	-	-	-	104
Share based payments expense	-	-	-	-	808	-	-	-	808
Total	$ 1,113	$ (107)	$ (10,550)	$ -	$ 495	$ -	$ -	$ -	$ (9,049)
Equity at 31 December 2018	**$ 131,278**	**$ (11,943)**	**$ 283,647**	**$ 107,119**	**$ 4,472**	**$ (7,194)**	**$ (17,594)**	**$ 95,401**	**$ 585,186**

	Issued Capital '000	Reserved Shares [1] '000	Retained Earnings '000	Foreign Currency Transl'n Reserve '000	Employee Benefits Reserve '000	Cash Flow Hedge Reserve '000	Common Control Reserve '000	Asset Reval'n Reserve '000	Total Equity '000
Equity at 1 July 2019	**$ 131,836**	**$ (1,266)**	**$ 310,693**	**$ 110,102**	**$ 8,574**	**$ (7,022)**	**$ (17,594)**	**$ 95,460**	**$ 630,783**
Comprehensive Income									
Profit for the period	$ -	$ -	$ 40,752	$ -	$ -	$ -	$ -	$ -	$ 40,752
Other Comprehensive Income	-	-	-	(603)	-	4,718	-	182	4,297
Total	$ -	$ -	$ 40,752	$ (603)	$ -	$ 4,718	$ -	$ 182	$ 45,049
Other equity transactions									
Shares issued for dividend reinvestment plan	$ 360	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 360
Dividends	-	-	(10,695)	-	-	-	-	-	(10,695)
Shares issued to employee share trust	241	(241)	-	-	-	-	-	-	-
Shares issued for vested performance rights	3,794	-	-	-	(3,794)	-	-	-	-
Shares transferred to beneficiaries	-	395	-	-	(395)	-	-	-	-
Share based payments expense	-	-	-	-	2,197	-	-	-	2,197
Total	$ 4,395	$ 154	$ (10,695)	$ -	$ (1,992)	$ -	$ -	$ -	$ (8,138)
Equity at 31 December 2019	**$ 136,231**	**$ (1,112)**	**$ 340,750**	**$ 109,499**	**$ 6,582**	**$ (2,304)**	**$ (17,594)**	**$ 95,642**	**$ 667,694**

1. Reserved Shares are held in relation to employee share trusts.
2. The Trustee sold all of the shares within the Austal Group Management Share Plan (AGMSP) during FY2019.

Consolidated statement of cash flows for the half-year ended 31 December 2019

		2020 H1 '000		2019 H1 '000
Cash flows from operating activities				
Receipts from customers	$	1,049,647	$	954,525
Payments to suppliers and employees		(1,020,396)		(848,131)
Borrowing costs paid		(3,494)		(2,149)
Interest received		1,145		251
Income tax refunded / (paid)		(4,827)		(2,602)
Net cash from / (used in) operating activities	$	22,075	$	101,894
Cash flows from investing activities				
Purchase of property, plant and equipment	$	(9,060)	$	(19,732)
Proceeds from sale of property, plant and equipment		-		1,153
Purchase of intangible assets		(420)		(1,057)
Net cash from / (used in) investing activities	$	(9,480)	$	(19,636)
Cash flows from financing activities				
Repayment of borrowings	$	-	$	(8,486)
Dividends paid (net of dividend reinvestment program)		(10,335)		(9,961)
Principal component of lease payments		(2,686)		-
Net cash from / (used in) financing activities	$	(13,021)	$	(18,447)
Net increase / (decrease) in cash and cash equivalents	$	(426)	$	63,811
Cash and cash equivalents				
Cash and cash equivalents at beginning of period	$	275,665	$	162,024
Net foreign exchange differences		(655)		7,445
Net increase / (decrease) in cash and cash equivalents		(426)		63,811
Cash and cash equivalents at end of period	$	274,584	$	233,280

Notes to the financial statements for the half-year ended 31 December 2019

Note 1 Corporate information

The half-year Financial Report of Austal Limited and its controlled entities (the Company, Group or consolidated entity) for the period ended 31 December 2019 was authorised for issue in accordance with a resolution of the Directors on 19 February 2020.

Austal Limited is a company limited by shares, incorporated and domiciled in Australia whose shares are publicly traded on the Australian Securities Exchange.

Note 2 Basis of preparation

The half-year Financial Report is a general purpose condensed financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001 and AASB 134 Interim Financial Reporting.

The half-year Financial Report does not include all of the notes normally included within the Annual Financial Report and therefore cannot be expected to provide as full an understanding of the financial performance and financial position of the consolidated entity as the Annual Financial Report.

The half-year Financial Report should be read in conjunction with the 2019 Annual Financial Report and considered together with any public announcements made by Austal Limited and its controlled entities up to the release date of this report in accordance with the continuous disclosure obligations arising under the Corporations Act 2001 and Australian Securities Exchange Listing Rules.

The half-year Financial Report has been prepared using the same accounting policies as used in the Annual Financial Report for the year ended 30 June 2019, except for the implementation of the Standards and Interpretations described below. These accounting policies are consistent with Australian Accounting Standards and with International Financial Reporting Standards.

i Change in accounting policies

AASB 16 Leases became applicable for the current reporting period and the Group has changed its accounting policies and made adjustments as a result of adopting the new accounting standard.
The impact of the adoption of AASB 16 Leases is disclosed below:

1. AASB 16 Leases

This note explains the impact of the adoption of AASB 16 Leases on the Group's financial statements and discloses the new accounting policies.

The Group has adopted AASB 16 retrospectively with a cumulative effect applied from 1 July 2019, but has not restated the prior corresponding period, as is permitted under the specific transitional provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 July 2019.

Adjustments recognised on adoption of AASB 16

The Group recognised lease liabilities in relation to the adoption of AASB 16 which had been previously classified as 'operating leases' under the principles of AASB 117 Leases. These lease liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rates as of 1 July 2019. The weighted average incremental borrowing rate applied to the lease liabilities on 1 July 2019 was 3.31%.

For leases previously classified as finance leases the Group recognised the carrying amount of the lease asset and lease liability immediately before transition as the carrying amount of the Right of Use Lease Asset and the Lease Liability at the date of initial application, 1 July 2019. The measurement principles of AASB 16 Leases are only applied after that date. The re-measurements to the lease liabilities were recognised as adjustments to the related right of use assets immediately after the date of initial application.

The table below reconciles the operating lease commitments disclosed at 30 June 2019 and the opening lease liability position under AASB 16 Leases:

	Total '000
Operating Lease Commitments disclosed at 30 June 2019	$ (11,661)
Discounted at 1 July 2019	$ (10,070)
Add: finance lease liabilities recognised as at 30 June 2019	(2,670)
Excluded: short-term leases recognised as expense	1,059
Lease liability recognised as at 1 July 2019	$ (11,681)

The table below shows the split of the lease liability between current and non-current:

	Total '000
Lease liability at 1 July 2019	
Current lease liability	$ (4,852)
Non-current lease liability	(6,829)
Total	$ (11,681)

The associated right of use lease assets for property leases were measured on a retrospective basis as if the new rules had always been applied. Other right of use assets were measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the balance sheet as at 30 June 2019. There were no onerous lease contracts.

The table below shows the right of use lease asset composition:

	31 December 2019 '000		1 July 2019 '000	
Right of Use Lease Assets				
Properties	$	10,856	$	9,011
Equipment		1,473		2,670
Motor Vehicles		135		-
Total	$	12,464	$	11,681

The table below depicts the impacts to the Profit and Loss and Balance Sheet split by reporting segment:

	Australasia '000		USA '000		Total '000	
2020 H1						
EBITDA	$	1,333	$	445	$	1,778
Balance at 31 December 2019						
Segment Assets	$	8,752	$	3,712	$	12,464
Segment Liabilities		(8,839)		(3,829)		(12,668)

Practical expedients applied

The Group has used the following practical expedients permitted by the standard in applying AASB 16 Leases for the first time:

- The accounting for operating leases with a remaining lease term of less than 12 months as at 1 July 2019 are classified as short-term leases and excluded from the disclosure.
- The exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application, and
- The use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

Accounting treatment of the Group's leasing activities

The Group leases various offices, shipbuilding facilities and vehicles. Lease contracts range from fixed periods of 1 to 40 years and may contain extension options. Lease terms are negotiated on an individual basis and contain a range of different terms and conditions. Lease agreements do not impose financial covenants and leased assets are excluded from security for borrowing purposes.

The lease of property, plant and equipment were classified as either finance or operating leases until 30 June 2019. Operating leases were off-balance sheet with payments made expensed to the Profit and Loss on a straight-line basis over the period of the lease. Finance leases were disclosed on balance sheet within property, plant and equipment and interest bearing loans and borrowings.

Leases are recognised as a right of use asset and a corresponding liability at the date at which the leased asset becomes available for use by the Group from 1 July 2019. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to the Profit and Loss over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right of use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Assets and liabilities arising from a lease are initially measured on a present value basis.
Lease liabilities include the net present value of fixed payments and variable lease payments that are based on an index or a rate.

The lease payments are discounted using the interest rate implicit in the lease or the incremental borrowing rate is used if that rate cannot be determined. The incremental borrowing rate reflects the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions. The weighted average incremental borrowing rate applied to the lease liabilities on 1 July 2019 was 3.31%.

Right of use assets are measured at cost comprising the following:

- The amount of the initial measurement of lease liability.
- Any lease payments made at or before the commencement date.
- Any initial direct costs, and
- Restoration costs.

Payments associated with leases with a lease term of 12 months and leases of low-value assets are recognised on a straight-line basis as an expense in the Profit and Loss.

Note 3 Reporting segments

	USA '000	Australasia '000	Unallocated '000	Elimination / Adjustments '000	Total '000
2020 H1					
Revenue					
External customers	$ 804,612	$ 233,479	$ -	$ 671	$ 1,038,762
Inter-segment	-	7,232	-	(7,232)	-
Total	$ 804,612	$ 240,711	$ -	$ (6,561)	$ 1,038,762
Profit / (loss) before tax					
EBIT	$ 65,564	$ 8,226	$ (13,576)	$ (285)	$ 59,929
Finance income	-	-	1,145	-	1,145
Finance expenses	-	-	(4,014)	-	(4,014)
Total	$ 65,564	$ 8,226	$ (16,445)	$ (285)	$ 57,060
Balance at 31 December 2019					
Segment Assets	$ 908,290	$ 333,276	$ 32,736	$ (9,126)	$ 1,265,176
Segment Liabilities	(349,341)	(203,469)	(44,672)	-	(597,482)

	USA '000	Australasia '000	Unallocated '000	Elimination / Adjustments '000	Total '000
2019 H1					
Revenue					
External customers	$ 686,823	$ 163,498	$ 908	$ 24	$ 851,253
Inter-segment	-	6,179	-	(6,179)	-
Total	$ 686,823	$ 169,677	$ 908	$ (6,155)	$ 851,253
Profit / (loss) before tax					
EBIT	$ 49,137	$ 4,148	$ (12,937)	$ 26	$ 40,374
Finance income	-	-	251	-	251
Finance expenses	-	-	(4,321)	-	(4,321)
Total	$ 49,137	$ 4,148	$ (17,007)	$ 26	$ 36,304
Balance at 30 June 2019					
Segment Assets	$ 913,301	$ 320,408	$ 103,200	$ (9,608)	$ 1,327,301
Segment Liabilities	(411,658)	(242,372)	(42,488)	-	(696,518)

Inter-segment revenues, investments, receivables and payables are eliminated on consolidation.

i Identification of reportable segments

The Group is organised into two business segments for management purposes based on the location of the production facilities, related sales regions and types of activity.

The Chief Executive Officer, who is the Chief Operating Decision Maker (CODM), monitors the performance of the business segments separately for the purpose of making decisions about resources to be allocated and of assessing performance. Segment performance is evaluated based on operating profit or loss.
Finance income, finance costs and income tax are managed on a Group basis.

ii Reportable segments

The reportable segments are USA and Australasia.

1. USA

The USA manufactures high performance aluminium defence vessels for the US Navy and provides training and on-going support and maintenance of these performance vessels for the US Navy.

2. Australasia

Reporting of the Australia, Philippines and Vietnam shipbuilding operations is combined into a single Australasia segment. These locations act as a single business unit for tendering, scheduling, resource planning and management accountability.

The Australasia business manufactures high performance vessels for markets worldwide, excluding the USA and provides training and on-going support and maintenance for high performance vessels.

iii Accounting policies, inter-segment transactions and unallocated items

The accounting policies used for reporting segments internally are the same as those utilised for reporting the accounts of the Group. Inter-segment sales are recognised based on an arm's length pricing structure. Certain unallocated items are not considered to be part of the core operations of any segment.

Note 4 Revenue and expenses

Profit before income tax expense includes the following revenues and expenses whose disclosure is relevant in explaining the performance of the entity:

	2020 H1 '000	2019 H1 '000
Revenue and expenses disclosure		
Revenue		
Vessel construction and support	$ 1,033,939	$ 846,127
Charter vessels income (CCPB 9 & 10)	4,823	5,126
Total	$ 1,038,762	$ 851,253
Cost of sales		
Vessel construction and support	$ (929,578)	$ (774,145)
Total	$ (929,578)	$ (774,145)

i Recognition and measurement

1. Vessel construction and support revenue

Revenue from contracts with customers is recognised in the Profit and Loss statement when the performance obligations are considered met. Revenue is recognised at an amount that reflects the consideration the Group expects to be entitled to receive, net of goods and services tax or similar tax.

Full disclosure of the Group's approach to AASB 15 Revenue from Contracts with Customers can be found in Note 2 of the 2019 Annual Financial Report.

ii Significant accounting judgements and estimates

1. Contract revenue and expected construction profits at completion

The assessment of contract revenue in accordance with the Group's accounting policies requires certain estimates to be made of total contract revenues, total contract costs and the current percentage of completion, which if ultimately inaccurate will impact the level of revenue recognised in the Profit and Loss of FY2020 H1 and future reporting periods.

Estimates were made by management with respect to total contract revenues, and total contract costs, which had a resulting impact on the percentage of completion, in line with the Group's accounting policy for contract revenue.

Note 5 Dividends paid and proposed

		2020 H1 '000		2019 H1 '000
Dividends paid on Ordinary Shares				
Unfranked final dividend for the prior year, 3 cps (FY2019 H1: 3 cps)	$	10,695	$	10,550
Dividend declared subsequent to the reporting period end (not recorded as liability)				
Unfranked interim dividend for the current year 3 cps (FY2019 H1: 3 cps)	$	10,696	$	10,584

Note 6 Financial instruments

A comparison of the carrying amounts and fair values of financial instruments other than cash and short-term deposits held by the Group at 31 December 2019 is set out below:

	31 December 2019		30 June 2019	
	Carrying amount '000	Fair value '000	Carrying amount '000	Fair value '000
Financial assets				
Loans and receivables				
Trade and other receivables	$ 109,798	$ 109,798	$ 225,268	$ 225,268
Other financial assets	13,172	13,172	11,859	11,859
Total	$ 122,970	$ 122,970	$ 237,127	$ 237,127
Fair value in other comprehensive income				
Derivatives	$ 4,830	$ 4,830	$ 2,190	$ 2,190
Total	$ 4,830	$ 4,830	$ 2,190	$ 2,190
Total	$ 127,800	$ 127,800	$ 239,317	$ 239,317
Financial liabilities				
Loans and receivables				
Go Zone Bonds	$ (122,199)	$ (122,199)	$ (122,286)	$ (122,286)
Trade and other payables	(159,269)	(159,269)	(202,308)	(202,308)
Vessel finance for Cape Class Patrol Boats 9 & 10	(44,763)	(44,763)	(48,798)	(48,798)
Finance leases [1]	-	-	(2,670)	(2,670)
Total	$ (326,231)	$ (326,231)	$ (376,062)	$ (376,062)
Fair value in other comprehensive income				
Derivatives	$ (11,643)	$ (11,643)	$ (16,544)	$ (16,544)
Total	$ (11,643)	$ (11,643)	$ (16,544)	$ (16,544)
Total	$ (337,874)	$ (337,874)	$ (392,606)	$ (392,606)

1. Finance leases were reclassified to Lease Liabilities at 1 July 2019 in accordance with AASB 16 Leases. Refer to Note 2.

Note 7 Interest bearing loans and borrowings

		31 December 2019 '000		30 June 2019 '000
Current				
Vessel finance for CCPB 9 & 10	$	(8,160)	$	(48,798)
Finance Leases [1]		-		(2,413)
Total	$	(8,160)	$	(51,211)
Non - Current				
Go Zone Bonds	$	(122,199)	$	(122,286)
Vessel finance for CCPB 9 & 10		(36,603)		-
Finance Leases [1]		-		(257)
Total	$	(158,802)	$	(122,543)
Total	$	(166,962)	$	(173,754)

1. Finance leases were reclassified to Lease Liabilities at 1 July 2019 in accordance with AASB 16 Leases. Refer to Note 2.

i Go Zone Bonds

Go Zone Bonds (GZB) are tax-exempt municipal bonds in the United States and attracted an average coupon rate of 1.34% in FY2020 H1. GZB holders are secured by letters of credit issued by Austal's banking syndicate.

The Bank of America letter of credit securing 50% of GZB debt was extended to November 2022 during the reporting period. Société Générale (SG) did not extend their participation in the letter of credit securing 50% of GZB debt. Austal received a commitment from Citibank in December 2019 to replace SG in the facility. Preparations for the GZB substitution process are underway and are forecast to be completed in FY2020 H2. The average cost of the letters of credit in FY2020 H1 was 1.54%.

Austal has repaid a cumulative amount of ~ US$137 million and owed US $87.500 million ($122.199 million) at 31 December 2019. Austal has the option of redeeming the outstanding GZB balance, in whole or in part, at any time during the term of the indebtedness with a 30 day notice to bondholders.

ii Vessel finance for Cape Class Patrol Boats (CCPB) 9 & 10

Austal entered into a finance arrangement with National Australia Bank (NAB) and the Royal Australian Navy (RAN) for the construction of CCPB 9 & 10 in December 2015. NAB financed the purchase of the vessels and is leasing them to the RAN for an initial 3 year term. RAN, NAB and Austal executed agreements in August 2019 to extend the vessel finance contracts to April 2022 and May 2022. The contract extension reduces the total residual value to $24.335 million at the end of the extension period.

This arrangement results in non-cash entries being recorded in Austal's statutory reporting during the charter period for notional revenue, notional depreciation and notional interest. Notional revenue of $4.823 million was reported in FY2020 H1 (FY2019 H1: $5.126 million).

Note 8 Contributed equity

	Shares		'000	
	2020 H1	2019 H2	2020 H1	2019 H2
Ordinary Shares on Issue				
Opening	353,357,283	350,857,529	$ 131,836	$ 130,165
Shares issued for performance rights vested	3,032,442	-	$ 3,794	$ -
Shares issued to Employee Share Trust	57,718	212,998	241	454
Shares issued for dividend reinvestment plan	85,667	912,560	360	1,922
Options exercised	-	1,374,196	-	2,110
AGMSP shares sold [1]	-	-	-	(2,763)
Dividend retained in relation to AGMSP[1]	-	-	-	13
Tax expense on AGMSP [1]	-	-	-	(65)
Closing	356,533,110	353,357,283	$ 136,231	$ 131,836
Reserved Shares				
Opening	(676,695)	(4,165,697)	$ (1,266)	$ (11,836)
Shares issued to employee share trust	(57,718)	(212,998)	$ (241)	$ (454)
Shares transferred to beneficiaries	125,765	-	395	-
Dividend retained in relation to AGMSP[1]	-	-	-	95
AGMSP shares sold [1]	-	3,702,000	-	10,929
Closing	(608,648)	(676,695)	$ (1,112)	$ (1,266)
Net	355,924,462	352,680,588	$ 135,119	$ 130,570

1. The Trustee sold all of the shares within the Austal Group Management Share Plan (AGMSP) during FY2019.

Note 9 Income tax

Major components of income tax expense were:

	2020 H1 '000		2019 H1 '000	
Profit and Loss				
Current Income Tax				
Current income tax charge	$	(6,221)	$	(3,632)
Adjustments in respect of current income tax of the previous year		(1,584)		(610)
Total	$	(7,805)	$	(4,242)
Deferred Income Tax				
Relating to origination and reversal of temporary differences	$	(9,078)	$	(8,669)
Adjustments in respect of deferred income tax of the previous year		575		274
Total	$	(8,503)	$	(8,395)
Total income tax (expense) / benefit charged to Profit and Loss	$	(16,308)	$	(12,637)
Other Comprehensive Income (OCI)				
Current and deferred income tax related items charged or credited directly to OCI				
Current and deferred gains and losses on foreign currency contracts	$	(1,778)	$	1,277
Deferred gains on revaluation of property, plant and equipment		182		(637)
Total income tax (expense) / benefit charged to OCI	$	(1,596)	$	640

A reconciliation between tax expense and the product of accounting profit before income tax multiplied by the Group's applicable income tax rate is as follows:

	2020 H1 '000		2019 H1 '000	
Income tax reconciliation				
Accounting profit / (loss) before income tax expense	$	57,060	$	36,304
Income tax at the Group's statutory income tax rate of 30% (2019 H1: 30%)	$	(17,118)	$	(10,891)
Adjustment for USA statutory income tax rate of 25.3% (FY2019 H1: 25.3%)	$	2,409	$	1,766
USA revalue deferred balances for change in average state tax rate		(74)		(421)
Other foreign tax rate differences (primarily Philippines)		1,142		1,735
Adjustments in respect of current and deferred income tax of the previous year		(1,009)		(336)
Transfer pricing adjustments in respect of intercompany royalties		(815)		(1,729)
Non-deductible share based payments expense		(506)		(178)
Revenue losses not recognised		(139)		(1,589)
Other non-assessable or non-deductible items		(198)		(404)
USA withholding tax leakage due to losses in Australia		-		(590)
Total adjustments	$	810	$	(1,746)
Income tax (expense) / benefit reported in the Profit and Loss	$	(16,308)	$	(12,637)

i Revenue authority audits

The Group establishes a provision based on reasonable estimates, for possible consequences of audits by the tax authorities of the respective countries in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences in interpretation may arise for a wide variety of issues depending on the conditions prevailing in the respective domicile of the Group companies.

An Australian Taxation Office (ATO) audit of Austal Limited that was concluded in CY2017, has resulted in differing interpretations of inter-company royalties associated with intellectual property deployed from Australia to the USA. The ATO's position creates double taxation for Austal because the ATO requires that a higher level of royalty income be recognised in the Australian taxable income than may be taken as a deduction in the USA.

Austal has been admitted into Mutual Agreement Procedures (MAP) between the Competent Authorities of Australia (ATO) and the United States of America (Internal Revenue Service) in order to seek relief from the double taxation.

Austal has accounted for and paid tax in Australia based on the ATO's position and may receive tax refunds in Australia or the USA if the outcome of the MAP process results in the removal of economic double taxation. Austal is currently unable to determine what the outcome of this process may be and the timeline to resolution.

Note 10 Corporate investigations

In January 2019, ASIC advised the Company that it had opened a preliminary investigation into certain market disclosures in late CY2015 and mid CY2016. US Regulatory authorities, including the Securities Exchange Commission, have also commenced separate but apparently related investigations. The Company provided an update on the state of these investigations in Note 29 to the financial statements in its 2019 Annual Financial Report (August Update).

Since the August Update, the progress of the investigation has centred on resolving disagreements as to the application of legal privilege to documents, with ASIC contesting Austal's assertions of legal privilege over a large number of documents. Despite efforts to agree on these matters, the application of legal privilege over a large number of documents remains unresolved and the matter has been brought before the Federal Court in Victoria for determination. This determination is expected to occur in March 2020.

In relation to the substantive investigation, Austal continues its efforts to cooperate with regulators in Australia and the USA. Other than the legal privilege matters discussed above, the matters being investigated have not substantively changed since the August Update.

The Group had to apply significant judgement when considering whether and how much to provide for costs. The provision could change over time as new facts emerge and the investigations progress as a result of the level of estimation uncertainty.

The Group is not aware of any wrongdoing or all of the specific matters currently being investigated and accordingly no provision has been made for any penalties or damages that may arise from the investigations.

The provision is recorded based on the best estimate of the probable incremental professional services costs relating to this matter. The movement in the period is set out below:

		2020 H1 '000		2019 H2 '000
Opening Balance	$	(11,031)	$	-
Arising during the year	$	(2,300)	$	(12,000)
Utilised		4,227		969
Movement	$	1,927	$	(11,031)
Closing Balance	$	(9,104)	$	(11,031)

Note 11 Events after the reporting date

Austal was awarded a $15.5 million contract to build a 41 metre high-speed catamaran ferry for SGTM Mauritius in January 2020. The new vessel is based on an existing and proven Austal design with specific customer modifications to be undertaken by Austal Vietnam. The construction will commence in Vietnam in March 2020 with delivery approximately one year later.

The Directors declared an unfranked interim dividend for FY2020 H1 of 3 cents per ordinary share on 19 February 2020. The dividend has not been provided for in the half-year financial report.

Directors’ declaration

In accordance with a resolution of the Directors of Austal Limited, I state that in the opinion of the Directors:

- The financial statements and notes of the consolidated entity are in accordance with the Corporations Act 2001, including:
  - Giving a true and fair view of the financial position as at 31 December 2019 and the performance for the half-year ended on that date of the consolidated entity.
  - Complying with Accounting Standard AASB 134 Interim Financial Reporting and the Corporation Regulations 2001.
- There are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

On behalf of the Board

John Rothwell

Chairman

19 February 2020

Independent Auditor's review report

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Independent Auditor's Review Report to the members of Austal Limited

Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Austal Limited, which comprises the consolidated statement of financial position as at 31 December 2019, consolidated statement of profit and loss and comprehensive income, the consolidated statement of cash flows and the consolidated statement of changes in equity for the half-year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the Directors' declaration of the consolidated entity comprising the company and the entities it controlled at the end of the half-year or from time to time during the half-year as set out on pages 9 to 25.

Directors' Responsibility for the Half-Year Financial Report

The Directors of the company are responsible for the preparation of the half-year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors determine is necessary to enable the preparation of the half-year financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the half-year financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at 31 December 2019 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Austal Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Auditor's Independence Declaration

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the Directors of Austal Limited, would be in the same terms if given to the Directors as at the time of this auditor's review report.

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Austal Limited is not in accordance with the *Corporations Act 2001*, including:

(a) giving a true and fair view of the consolidated entity's financial position as at 31 December 2019 and of its performance for the half-year ended on that date; and

(b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

A T Richards

Partner

Chartered Accountants

Perth

19 February 2020

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