# RESPONSE TO QUERIES RAISED BY SECURITES INVESTORS ASSOCIATION (SINGAPORE) REGARDING THE GROUP'S ANNUAL REPORT FOR THE FINANCIAL YEAR ENDED 30 SEPTEMBER 2021

The Board of Directors of BRC Asia Limited (the "Company", or the "Group") refers to the following queries raised by Securities Investors Association (Singapore) ("SIAS") regarding the Group's annual report for the financial year ended 30 September 2021 and would like to provide the following response:

## Question 1

(i) The company has carried out three placements and the proceeds have been used to pay down the group's outstanding bank borrowings. At the end of the financial year, loans and borrowings amounted to $435.8 million and the group's net debt was $352.8 million. With $300.9 million in equity attributable to owners of the company, the net debt to equity ratio is 1.17 times. Gearing (defined by net debt divided by capital plus net debt) is at 54%, an increase from 43% a year ago (page 119). Can the board/management confirm that it is comfortable with the current gearing of the group? Has the board set an internal limit on the group's gearing? Does the group have the appropriate capital structure to support its growth? Have the banks expressed concern over the group's leverage? Will the company be looking to deleverage further in the next 12-18 months?

Company's response

**We refer to note 23 on page 96 of our FY2021 Annual Report ("AR"). Out of the S$358.1 million current loans and borrowings as of financial year end, S$343.8 million relates to bills payable to banks (unsecured) for inventories, which stood at S$466.2 million (AR page 90, note 17). The higher gearing arose from increases in inventory costs which was in tandem with escalating steel prices during the financial year.**

**The trade facilities available are sufficient to finance the procurement of steel raw materials to hedge and fulfil the existing sales order book. The Board/Management is comfortable with the current gearing of the Group. We are not aware of any bank which has expressed concern over the Group's leverage.**

(ii) In view of the constant fundraising and the deleveraging, is the company able to maintain/increase its dividends? Is it efficient to be carrying out both fundraising and declaring high dividends? Is management spending considerable time and attention in carrying out private placements which takes them away from focusing on the core business?

Company's response

**Our dividend pay-outs have increased in line with improved profitability. Managing the capital markets is an important part of Management's responsibilities. The Group has sufficient resources to carry out private placement exercises without compromising focus on other core activities.**

(iii) What are the potential areas of collaboration with HLA in the near term?

<u>Company's response</u>

**As and when necessary and in accordance with SGX listing rules, appropriate announcement/s will be released on a timely basis to update shareholders on any material/significant information on any collaboration with Hong Leong Asia ("HLA").**

(iv) It is noted that the outlook for the constructions sector remains to be supported by healthy pipelines of housing projects and strong demand for general construction. Given the group's market positioning, how confident is management in tendering and building up the group's order book while at the same time maintaining a commensurate level of profit margin (see question 2)?

<u>Company's response</u>

**Management is cautiously optimistic about being able to maintain a fair level of profit margin whilst continuing to build up our sales order book, *ceteris paribus*.**

(v) With HLA as a new substantial shareholder with a 20% stake, has there been any engagement with HLA over the group's strategies and long-term growth plans?

<u>Company's response</u>

**Please see response in Q1 (iii) above.**

(vi) Has the company received any director nomination from HLA (which was provided for in the subscription agreement)?

<u>Company's response</u>

**HLA will make its recommendations to the Company in due course.**

(vii) In addition, given that the majority shareholder, Esteel, has actively reduced its stake, what assurance do minority shareholders have over Esteel's long term commitment to the group?

<u>Company's response</u>

**We understand that Esteel is fully committed to its investment in the Group, and any reduction in its stake is done with the long-term objective of bringing onboard strategic and institutional partners to strengthen the Group. Esteel's continued presence as the majority shareholder is further testimony to its commitment.**

## Question 2

(i) Can management help shareholders understand the extenuating circumstances that led the group to recognise $46.1 million in provision for onerous contracts?

**Company's response**

**During the course of the financial year, international steel prices increased significantly, neatly encapsulated in an article by S&P Global Platts titled "Historical global steel price rally sweeps iron ore to all-time high" on 27 April 2021.**

(https://www.spglobal.com/platts/en/market-insights/blogs/metals/042721-global-steel-price-rally-iron-ore-iodex-all-time-high-china-stimulus)

**In the situation of increasing steel prices, provision for onerous contracts are made when the steel raw material costs plus conversion costs to fulfil the obligations of certain contracts (which were secured when steel prices were lower) are estimated to exceed the revenue generated from them.**

**It is Management's practice to timely hedge its steel raw material exposure of the sales order book on an overall tonnage basis, subject to viable purchase shipment quantities. However, as steel raw materials drawn down could not be earmarked to specific projects, they are utilised as a pool (for both fixed price and provisional pricing projects) and accounted for on a weighted average costs basis.**

**The duration of the projects in the sales order book could range up to 5 years, and the actual deliveries of the contracts may not be in the same chronological sequence as the contracts were entered into. In addition, when steel prices are rising, sales contracts delivered at provisional prices (current market prices) utilising weighted average inventory costs would result in excessively high margins in the current period; on the other hand, as weighted average inventory costs increase in tandem with rising steel prices, there may be potential loss when certain fixed price contracts are actually delivered in the periods going forward. Provision for onerous contracts are made for such foreseeable losses and these provisions are reversed when contractual obligations are met or no longer exist or when the costs to meet the obligations no longer exceed the sales value (mostly when steel prices soften).**

(ii) What percentage of the group's contracts is on a fixed price basis? Is it the group's practice to hedge its exposure once contracts are signed?

Company's response

**On average over time, the proportion of fixed and provisional price contracts in our sales order book is about balanced on a 50-50 basis. Please see Q2 (i) for explanations on managing steel raw material exposure of the sales order book.**

(iii) Has the board identified steel price as a key material risk factor for the group? If so, can management elaborate further on the group's strategy in managing the volatility in steel price? What is management's view on the price of steel going forward?

Company's response

**The Board is satisfied that the hedging of steel raw material exposure of the sales order book is in place to mitigate the risks associated with the volatility in steel prices. On the price of steel going forward, we would like to refer you to reports such as the one found at the following link:**

https://www.hellenicshippingnews.com/global-steel-prices-forecast-to-remain-elevated-in-2022/

(iv) Given the increased scale of the group's operations, are there opportunities for management to further finetune its inventory stocking policy?

Company's response

**Management is of the opinion that the existing inventory stocking policy is in line with the hedging of steel raw material exposure.**

(v) What are the reasons for the disproportionally large increase in allowance for inventory obsolescence?

Company's response

**Management is of the opinion that the quantum of allowance for inventory obsolescence, which constitutes 0.85% of the inventory, is not material to be of concern.**

(vi) Can management also elaborate further on the provisional pricing contracts?

Company's response

**Provisional pricing contracts include a fluctuation clause that allows for selling price adjustments to be in line with current market prices, based on the monthly material price index published by the Building & Construction Authority.**

## Question 3

(i) Can the board help shareholders understand if it is the usual practice for non-board committee members (i.e., the executive directors) to attend board committee meetings?

**Company's response**

**It is the usual practice for non-Board committee members to attend Board committee meetings to better enhance the contributions of the Board as a whole, as well as that of each individual Director, given the diversity of thought, experience, background and job scope (for the Executive Directors). The process of decision-making by the Board is independent with no concentration of power. No individual director is involved in any decision-making in matters involving himself/herself, and may be asked to be excused from the meeting should the need arises. No directors is to be involved in fixing his/her remuneration. The Audit Committee, for example, met with the external and internal auditors without the presence of the Executive Directors.**

(ii) What is the group dynamics at the board committee meetings when the independent directors on the board committee may be reviewing and discussing matters that are related to or affect the executive directors? Such board committee meetings would have included agenda items on interested party transactions, performance assessment, remuneration of the executive directors and on the audit/financial reporting/internal controls of the group.

**Company's response**

**Please see response in Q3 (i) above.**

(iii) Do the executive directors also actively participate in the discussions during the board committee meetings? If so, how are board committee meetings different from board meetings?

**Company's response**

**As the Executive Directors are involved in the day-to-day operations, they are able to clarify or update matters as and when such information is requested by Board committee members during the meeting. The agenda items for the respective Board committee meetings also differ, and each meeting is led by a different chairperson.**

(iv) Are the committees able to make decisions objectively and independently?

**Company's response**

**Please see response in Q3 (i) above.**

**BY ORDER OF THE BOARD**

**Seah Kiin Peng**

**Executive Director and Chief Executive Officer**

**21 January 2022**