Presentation transcript

29 March 2022

PRE-CLOSE TRADING UPDATE

Operator
Good day ladies and gentlemen and welcome to the Barloworld pre-close trading update. All participants will be in listen only mode. There will be an opportunity to ask questions later during the conference. If you should need assistance during the call, please signal an operator by pressing * then 0. Please note that this call is being recorded. I would now like to hand the conference over to Dominic Sewela. Please go ahead, sir.

Dominic Sewela
Thank you very much. Good afternoon everybody on the line. I hope wherever you are, you are safe. And joining me on this call on my side I've got Chris Wierenga, the CEO of the consumer business, as well as Quinton. Quinton is here physically with us this time around. We also have Ramasela on the line, the CEO of Avis, and we also have Andronicca, Chief Operating Officer of Equipment. I've got with me Nopasika, who is the FD, and Nwabisa, our Investor Relations Executive. I guess most of you have had an opportunity to look at the voluntary trading update for the five months to the 28th February 2022. I would like to say it has been a great five months up until the 24th February when we had challenges coming out of Ukraine and Russia. But notwithstanding that I think the business overall has done very well for this last five months.

I think more importantly in Equipment Southern Africa we've seen a turnaround particularly in the DRC. The order book is almost at an all-time high in Equipment Southern Africa. I will give Andronicca a turn to highlight some areas. And when we come to Equipment Eurasia, I think, Quinton, by all accounts this could have been one of the greatest years if you look at the five months. But I guess given the challenges of sanctions things will evolve and over time we will see that it might be a challenging six months from here on. But I guess having said so it's still good to see that the order book is solid in Eurasia as well. You will talk probably more around Mongolia as well.

I think on Chris' side as well we've seen good volume pick-ups. So I think overall the business has done well. But the bigger turnaround has really been in car rental, the Avis fleet. Ramasela's teams have done well there. I will give her an opportunity to also give us a highlight. Maybe let's give over to Andronicca. Just key highlights given that most of the people on the call have already seen the statement.

Andronicca Masemola
Thanks, Dominic, and good afternoon everyone. Just a quick highlight from Equipment Southern Africa. We have seen in the trading update that one of the highlights is the recovery of rest of Africa. In the past we had noted that we were operating at a split of about 70/30 with 70% being SA operations. Where we are now rest of Africa is moving towards the 60/40 split that we have enjoyed in the past. From a South Africa perspective we had a bit of a slow start mainly influenced by supply chain constraints but also as a result of the type of market that we're

serving, quite a number of contractors. Some of the finalisation of the contract miners with the mining houses was delayed, but we are starting to pick up and deliver on those.

Operating profit was up. We committed to delivering the operating margin that we have always shared with you in terms of what it looks like. I know for the five months we are slightly below the 10%, but we are seeing activity picking up in the second quarter of our year as the supply chain constraints ease up and we expect the margins to improve closer to 10% by half year when we report. On the positive side, as Dominic alluded, DRC is doing well. The turnaround plan is delivering results and since the beginning of the financial year DRC has been reporting positive results. Thanks, Dom.

Dominic Sewela
Thank you. Quinton, over to you.

Quinton McGeer
Thank you, Dominic. Good afternoon to everyone. I think from a Eurasia perspective up until February it's fair to say that in the Russian environment it was a record result for the first five months both at the revenue side as well as at the operating level. We managed to grow our firm order book from a good, solid $224 million to $314 million and a very well balanced, diversified firm order book with all commodities represented: gold, coal, diamond, copper, nickel and then also very strong construction and power firm order book. I think also to highlight that even from a cash perspective up until February results were exceptionally good and we had a very clean book in Russia.

I think Mongolia on the other side the trading has been not as expected, but largely due to China with China closing its borders firstly due to the winter Olympics. China has got a no COVID policy so they are very strict on the border, and those border closures hit us quite severely in the first five months. But irrespective of that, the business still generated a very solid, good quality operating margin. I think it's fair to say that during February the conflict arose between Russia and Ukraine and there were quite a number of sanctions that were implemented. The business is now focussed on understanding, interpreting and then complying. I think Dominic has alluded to it. I think the next few months will be challenging, but I'm sure we'll work through it. We've been through this before, and we will focus on what we can control for now.

Dominic Sewela
Thanks for the summary. Chris.

Chris Wierenga
Thank you Dominic. Good afternoon everyone. I think just touching on the Consumer Industries vertical, and specifically Ingrain, we've had a very good performance of the business bearing in mind that now we're looking at five months included in our actual results versus four months in the prior year. So you would see an up drift because of the additional months of trading in the business. Despite that we've seen very strong volume and price improvements across most of the business with all sectors performing very well.

We've seen a strong recovery in the alcoholic beverages sector. I think that has boded well because of the lockdowns and restrictions on sales of alcohol in the prior reporting period. Obviously the contribution from that sector is slightly lower than what we see overall in the business, so the mix in volumes has reduced contribution margins in the business. But Rand for Rand, EBITDA between the two reporting periods is up quite strongly.

More pleasingly for the business though is we had higher plant availability on the back of a rollout of BBS across the business. And we've seen a much better peak coming into October, November and December this year with plants performing ahead of the prior year and an improving maize grind as well. Within the business at the moment we are seeing rising maize prices, and these are being dealt with in line with our hedging strategy, so we are investing in [unclear] the margin on the SAFEX account where necessary. That will obviously unwind as those customer contracts are priced going forward.

But more importantly, the business in the short-term we have secured maize until mid-2023 and are obviously continuously monitoring maize prices and availability in the current situation. But we're sitting with good crops that have been harvested. We are expecting a good harvest coming through despite some of the crop damage that we've seen. Our experts on the ground are telling us we should see a crop in excess of 15,000 tonnes this year.

And I think if I look in the business over the period we've continued to invest in the maintenance capex that we'd seen pre-acquisition and also investing in the critical skills required to maintain the plant availability and improve maintenance practises in the business. So I think overall in the period under review things are going well. We're obviously monitoring the external environment very closely. Domestic volumes are strong, pricing is coming through nicely, and we're seeing opportunities going forward in the organic growth of the business as well.

Dominic Sewela
Thanks Chris. Ramasela.

Ramasela Ganda
Thank you very much, Dominic. Good afternoon everyone. I think it is fair to say that we have learned over the period to weather the COVID storm. If you just think back that the five months was when Omicron started, and we have traded ourselves very well out of that Omicron phase. Looking at our operating profit from a car rental point of view, one of the key things was when you look at the volume of 2019 we're still operating at 65% of 2019, mainly because as we know inbound was not yet back. We are trading still on average between 11% and 12% of the 2019.

But our operating profit, which is what we've highlighted when we really get into the deep dive of COVID to say how are we going to work our way out of this, looking at our strategy of moving from the airport, looking at the subscription model, we still get surprised every day with the amount of subscription that we get out of the market, how the market is moving to taking up the subscription model. I think in South Africa when you see rain you can already factor some good business for car rentals, and we had a couple of good rains in the couple of months.

Our efficiencies are key as everybody knows about the constraint of the fleet in the market. Our efficiencies really are showing off when you start looking at the fleet utilisation. You get to a point where there is this average throughout Southern Africa in all our operations, but you get to a point where Gauteng will run at an average of 83% and Cape Town at 81% a car. And it's all about the turnaround, the time that a fleet is available for utilisation. We have mastered that process and it's something that we will continue working to improve. As I keep on referring to this utilisation you will find it difficult to compare anything close to 75% in the standard, and that's something that we're really working hard to keep.

The used car market remained buoyant. With the shortage of fleet, margins no doubt have really become even stronger than it has been in the previous years. And we will continue making sure that we sell at the right time based on kilometres and the time that we have the fleet so that we balance our business very well. We are happy to start seeing domestic market picking up. December was one good period where we saw a lot of domestic travel. Looking at the leasing business we're seeing corporate coming on board in a strong way. One of the things that corporate is starting to do is really funding through the financing lease. That book of ours is growing. The challenge is just delivering them on time purely because of the delay in the supply.

But other than that a very good, solid business for both leasing and car rental with very strong EBITDA levels. When you compare ourselves with 2019 now when you look at the operating profit we've already surpassed the February 2019 level. So that's something. And if you think about it in South Africa, COVID only hit us for real in March. So that five months is pre-COVID in South Africa and we've managed to surpass it. So we are well geared with where we're sitting to continuously grow based on our strategy and our cost containment that we've done over the period, bearing in mind that the used car market doesn't look like it's slowing down any time. That's one thing that we will always manage and monitor when we look at our total fleet from both the leasing and the car rental operations. Thank you very much, Dominic.

Dominic Sewela
Thanks Ramasela. I think you get a sense from all the trading activities overall, notwithstanding the challenges we're still operating under, we still have COVID in this country but all the businesses are doing well. On the logistics front in terms of us pivoting out of auto and logistics we've seen progress. We have basically finalised the bulk of the transport business, being Manline Energy, Manline Freight and Timber which was concluded. As of February the money is in the bank in terms of the transaction. We've sold the 51% of Aspen Logistics. I think that was announced in November last year. And currently we are in the throes of concluding the supply chain business and by the end of this month we should have signed the SPA regarding that transaction.

And I think overall the other action I just wanted to update is around the de-risking of the pension fund. To that extend we have invested some capital to de-risk that. And that will give us the flexibility to move the money in between the UK and South Africa, and we are currently looking at insurance companies that could actually buy that liability from us. I think by the time we release the results in May we will give you further update on that front. I guess all of you have received your dividend in January. The reason I'm highlighting this is when you look at the cash generation we did utilise cash over this period, largely because of the order book that you're seeing in both Russia and South Africa as well as in Asia, and therefore this will unwind in the second half. I will pause there and see whether there are questions that we can take.

Operator
Thank you. Ladies and gentlemen, if anyone would like to ask a question, you are welcome to press * then 1 on your touchtone phone or on the keypad on your screen. If you however wish to withdraw the question, you may press * then 2 to remove yourself from the question queue. We have a question from Paul Steegers of Bank of America. Please go ahead.

Paul Steegers
Hello everyone. Can you hear me?

Dominic Sewela
Yes we can hear you very well, Paul.

Paul Steegers
Thank you. Hi Dominic. A question for Quinton and maybe Dominic on Eurasia. On Russia the next few months are going to be obviously difficult. We get that. I'm just wondering with Caterpillar I believe suspending operations they haven't fully pulled out yet. Is that correct? That's the first part of the question. And how are you going to manage this business? Will it potentially become loss-making, or will you look to wind it down and potentially sell it? I'm just wondering what the outlook is for the Russian services business in light of what Caterpillar is doing and what you're seeing on the ground going forward. Thank you.

Dominic Sewela
Thanks, Paul, for the question. I think just so that we outline the areas where we operate, I've said previously that as Barloworld our focus is in emerging markets. And these areas irrespective of where you look, whether it's Mongolia, the DRC, Angola and now Russia, these are very challenging environments that we operate in. As Barloworld we have operated in those environments, making sure that we stick to the laws of the countries where we operate in and also not playing politics and making sure that our business is to look after our customers.

So with respect to Caterpillar, they spoke about the suspension of their Tosno base actually. And to that extent that's what they're speaking about. Remember Caterpillar only manufactures in Russia in Tosno and Novosibirsk as well. Those are the suspensions that they have spoken about. But you have several dealers. We are one of the dealers. So around the world they distribute that equipment to the dealer network. I guess what's constraining us, Paul, is that we have to comply with sanctions not only from the US but the UK, EU, as well as Russian counter-sanctions. And that creates a lot of challenge. Quinton and the team are on the ground making sure that we comply with the sanctions. That makes it difficult.

Our view at this point is that we're going to hunker down and continue to support our customers in Russia, and hopefully the conflict gets resolved earlier. But my view is that given the past experience this is worse than we anticipated. We are likely to be in this situation for the long haul. So the mandate to Quinton and the team is to do their level best to service our customers where they can. But I can't tell you today what things are going to be tomorrow. As long as we are able to trade, we will trade. But if we can't trade it's a different story.

I think that's why we're saying there's a likelihood that we will have to look at impairment in this situation. The longer the process lasts in terms of the conflict and the sanctions stay, it makes it even more difficult for us to trade. Therefore it's difficult to predict what six months and 12 months is going to look like. That's why we're saying at the time of finalising the results in May we would know the impact of what type of impairment we might be taking. I don't know, Quinton, if you want to give a better…

Quinton McGeer
No, I think you've summarised it. Paul, just to add, I think our mantra with the team is just to focus on what we can control, focus on our customers, focus on assisting and supporting one another in Russia. I think that's all that we can do at this point in time. Obviously, as Dom has alluded, compliance is a very important part of our business. So things will get slower as the time passes until there is a full grasp exactly what you can do and what you can't do. I think then the other thing that's also impacting us is that things keep on changing. What is allowed today might not be relevant tomorrow. So for us it's managing the business day to day and focussing on what we can control and our customers. I think that's all I wanted to add.

Paul Steegers
I appreciate that sentiment. Just coming back to the question, do you think that in the next six months…? There is a big fixed cost base here. Things are going to slow, and it is obviously nobody's fault. Do you think that business will be loss-making in the next six month period? Ironically you've had record results. It's really frustrating for you obviously. But I'm just wondering now going forward what you can control and the costs that you have there. How quickly does this business move down in terms of profitability and will it become loss-making? I guess that's the question. Thank you.

Dominic Sewela
I guess it's very difficult, Paul, currently particularly if you look at the trading for the last five months. And there is still trading taking place in territory. But if you look at that business overall in terms of the cost structure it's one of our leanest businesses. But having said that, the challenge you have is things are fluid. But currently customers are also anticipating the challenges. They are ordering. The issue is going to be to what extent from a supply chain point of view we will be able to get parts into the territory whilst we comply with the sanctions that are in place. That's going to be something that determines whether or not we're going to be profitable or not.

Key for us – because we're going to take a long-term view here – is that 50% of the stuff there is after market. It is people who are looking after service. It's to make sure that we don't lose the skills. And my view is that come the 20th March when we release the results we will be able to give you better insights, Paul. I know it's frustrating for all of us in terms of wanting to get certainty, but unfortunately that's what it is in terms of the challenge we have. But at the moment we haven't taken a view that we're going to be loss-making, but we do believe that if we don't have clear visibility come the time we put out the numbers, we'll have to take an impairment.

Paul Steegers

Thank you. I appreciate the insight. And while I have the mic, one last question from me. Apologies. You've mentioned looking to unbundle or sell Avis, both fleet and car rental. We can all make our view on how much those businesses are worth. The question is how much debt is in those businesses broadly speaking? Secondly, if you manage to unbundle or sell it, whatever happens, by the end of the year, what would you do with any proceeds from that sale? Thank you very much.

Dominic Sewela

Thanks. As I've said, the commitment in terms of the capital allocation strategy is that whenever we sell and we get the proceeds first and foremost we say is there an opportunity to buy back. At this level clearly there is a huge opportunity for us to buy back. Alternatively, like we've done, we will repatriate the capital back to the shareholders. And if there is an opportunity to further strengthen the Consumer Industries or Equipment, we will look at that in that order. And that's what we will do with the capital.

Operator

Our next question is from James Twyman of Prescient Securities. Please go ahead.

James Twyman

Yes. Thank you very much. I've got two questions. The first one is as far as Russia is concerned can you actually say whether you're still getting supplies from Caterpillar into Russia, or has the train of product basically stopped, and therefore you're already yin the process of running down your inventory? Just to get an idea of the timing of that. Secondly, how is Mongolia affected by this? Are they still able to continue? I know you said business is slow, but are they still able to get product from Caterpillar presumably via China? That's it from me. Thanks.

Quinton McGeer

Okay. I think let's maybe just first deal with the Mongolian question. I think from a Mongolian perspective, Mongolia was never reliant on Russia. In fact no product except the product that was manufactured in Russia came from Russia to Mongolia. So the events in Russia Ukraine don't impact Mongolia directly. What impacts Mongolia is China. Anything that happens in China impacts Mongolia automatically. I think for us we've also got to look at China. When China shuts down for a COVID outbreak or whatever the case might be, that impacts the supply chain through to Mongolia because it means the Chinese border is closed. That is something that we're managing separately. Then I think the question on Russia, what was the question on Russia again?

Dominic Sewela

Whether you're able to trade with Caterpillar.

Quinton McGeer

Caterpillar like all suppliers in the world are busy interpreting and understanding what you are allowed to do and what you're not allowed to do. And it sounds like it's relatively easy to interpret, but it's not. From a product perspective that's easy. We've got clear guidance what and how product can flow. The customs in all the various countries, products flow through customs. And customs first need to understand if this is allowed to go through to Russia or not. Caterpillar is still in that process, working through the process to see what is being sanctioned, what types of products is allowed, because there are certain products like dual use parts or whatever the case might be that are not allowed to be sold to Russia.

So that process is quite complicated. It's comprehensive. It's not just Caterpillar that's in this. Customs needs to make sure that they cover all suppliers in the world. So that's where the hold-up is. Caterpillar hasn't stopped shipping to Russia. They haven't withdrawn. But they need to work through the process and customs needs to work through the process in terms of what is allowed through customs to Russia. And that process because it's so big will take time. But I'm pretty sure that over the next month or two there will be a lot more clarity in terms of this exactly. And customs will know that when they allow this shipment to pass that it's actually in terms of complying with all legislation.

James Twyman
If I could ask one more quick question if I may on the unbundling. It was going to be a sale of the Avis business and now you've mentioned unbundling. Does that mean we should be a little concerned that you're not so confident on pricing? Or does it more likely mean that unbundling is an additional option to speed the process up?

Dominic Sewela
I think it's to speed the process up because we've received bids from potential buyers. But I guess a lot of people tend to want to take advantage, thinking because of COVID we will take any price. But the business has done phenomenally well. To that extent we are running dual processes to say we will look at sale if it is warranted. Remember when we sell the business we will actually have to get approval from Avis. And unbundling similarly we will have to get a clearance. But I think we get to a point where we say what's in the best interests of the shareholders in terms of these two processes to get the right value.

James Twyman
Okay. Thank you.

Dominic Sewela
Thanks James.

Operator
Thank you. Our next question is from Mark Ter Mors of SBG Securities. Please go ahead.

Mark Ter Mors
Thank you for the presentation. More of a philosophical question relating to ESG and the ESG assessment of possibly remaining in Russia. Since the invasion of Russia into a democratic country, Ukraine, we've seen several global companies exiting Russia completely. I would just like to know how management looks at the ESG considerations relating to possibly remaining in Russia.

Dominic Sewela

Thanks, Mark, for that question. It's a fairly difficult scenario which you find yourself in. The point I was trying to make is once we've chosen a strategy to invest in certain emerging markets these countries are politically challenging because there could be political instability. There could be all sorts of other challenges. And hence if you look at currently as we speak there is a war in Mozambique. And in the DRC we've lived in that type of an environment. I guess what's regrettable in any war, Mark, is the loss of life on either side. For us we are business people.

One of the key issues is to make sure that we operate in an environment where it's peaceful. Whenever there is going to be conflict it is very important for the dealers to engage in trying to find resolutions of problems. It's not for us as business people to do that. I guess it depends from one company to another what they choose to do. But our view is we get into those countries long term, and we understand the vicissitudes of the political challenges that come up with investing in these countries.

And therefore our view is that we are likely to stay as long as it makes sense in terms of the safety of our employees. Also what we hope is that various leaders are able to enter into discussions and resolve problems accordingly. But I can't speak for them. I'm not a politician. But from the point of view of the social impact that we make, we make impact in creating jobs in Siberia, the same thing in Mozambique. And we hope that whatever challenges we face could be resolved by the politicians. If it makes business sense for us to stay, we will continually look at those options.

Mark Ter Mors
Thank you for the well-considered answer. I appreciate it.

Operator
Thank you. Our next question is from Brent Nadel of Absa CIB. Please go ahead.

Brent Nadel
Good afternoon. Thanks for taking my question. I'm sorry to push on this issue a little bit. I guess my first question I was going to ask is just some level of clarity on how the sanctions are impacting the Russian business. I think you have clarified that to a large extent. Can I ask, if there is an order that is due to be delivered to Russia, is that sitting at the port in which it's being exported, in other words it cannot be delivered to the customer? Or are you getting some products into Russia?

Two, if you can't get products into Russia, if my understanding is correct there are quite onerous penalty charges that Caterpillar or yourselves could face if deliveries are done. Do those still apply? And three, if you cannot deliver is there a potential that that order could shift across to manufacturers, for argument's sake, in China who could possibly take that order themselves and deliver on that order?

Dominic Sewela
Quinton, do you want to comment?

Quinton McGeer

I think maybe to answer on the first question first obviously there are some ports where the supply chain is still operational and running. And then if product is manufactured in that region and there was an order, and you are allowed to sell that product, then it's relatively easy. But obviously Caterpillar manufactures all over the world and product comes from all over the world on different supply chains and routes through to Russia. So the first thing we need to do when you do receive an order or if we've got a contract is to establish are we allowed to sell that product. Firstly, can we sell the product? Secondly, are we allowed to sell the product to the customer? So we go through those processes.

The next question is can we deliver, because the supplier route might not be operational at this point in time, as I've explained before, because the customs also need to go through this process. And they don't just have to deal with Caterpillar. They've got to deal with every single manufacturer in the world. So it is a massive process, and it is human beings sitting there that need to go through this process. So what we will do is we will go through that process. We will then be in contact with the customer. We will give the customer various options.

Obviously delay the shipment would be one option. The customer might be happy to delay without penalties. Another option is to cancel. The customer might say I'll rather wait because we are in a mining boom. So many customers are prepared to wait and say let's take a breather and wait until there is more clarity. Or we decide we cannot deliver, it gets cancelled, and then we need to find a different home for that product. Luckily we are in a world mining boom where it should not be too problematic for us to reroute or redirect our product.

In terms of finding ways to go through different routes, that's always an option. But you've got to look at cost. That's the one thing. Then the other thing is you've also got to make sure that you don't circumvent the law. So to try and make a plan to say, well, we're not going to comply to do this, then we circumvent that. So we're also very careful from that perspective. So it is a complicated process, and as we said a little bit earlier, that's why things are going to slow down because there are a lot of things that need to be taken into account before you make a decision to either continue or whatever the circumstances might be. I hope that answers all the questions. I don't know if I forgot some.

Brent Nadel
If I can just clarify one issue. Say there is a late delivery and there is a penalty that's applied, or if there is no delivery and there is a penalty that's applied, who pays that? Is it Barloworld or is it Caterpillar?

Quinton McGeer
Well, the first thing is we need to get to the penalty. We are in negotiations with our customers and obviously it's our customer's choice if they would want to continue. And then you've also got force majeure. When there are force majeure circumstances then those penalties will not apply. So it's a whole process. I think Dominic has just alluded to it just now. There is a political side to what's happening and then there is the business side. All our customers are businessmen. All they are interested in is trying to do the best for their stakeholders, employees etc. So they all understand the situation. They are not throwing their toys out of the cot and demanding things. They're all looking to see how we work together for them to eventually receive that product. So as we sit today or at the end of February I would say there has been no talk even of penalties at that point in time.

Brent Nadel
Just my last question if I can, just on the strategy. If the worst case scenario plays out where the Barloworld Russian business unfortunately just cannot survive, would you be rethinking the strategy of selling car rental and leasing? From a strategic perspective are you guys happy to go ahead with that process no matter what happens on the Russian front?

Dominic Sewela
So, Brent, we regard our Caterpillar distribution business as very core to our being. And therefore this event would not stop us from distributing Caterpillar. I'm talking about worst case scenario. We've had worst case scenarios in countries in like Zimbabwe. We held the license. We had to basically sell a portion of our license to Zimplow. And we were stuck in Zimbabwe for many years. You know the challenges in Zimbabwe. But eventually we believe that Zimbabwe will come out. I don't know when.

And therefore in that worst case scenario we will still be able to stay holding the license in Russia. So when you look at the strategy, the strategy was informed by the basis of the fact that fundamentally we believe that automotive and logistics fit in line with our long-term strategy. So the issue for us was the timing of when we can realise good value for either exiting through a sale or unbundling for Avis. Therefore that will go ahead irrespective.

Brent Nadel
Many thanks.

Dominic Sewela
Okay. Who is next?

Operator
Thanks. Our next question is from Roy Campbell of RMB Morgan Stanley. Please go ahead.

Roy Campbell
Good afternoon. Thanks very much. Just a couple of questions please. I know we are harping on Russia a little bit, but just your view in terms of Caterpillar suspending production in Russia. Is that a function of their supply chain that Quinton has been talking about, or do you think that they for now don't want to be exposed to Russia – what Mark was talking about from an ESG perspective – in which case, is remaining in Russia a Barloworld management decision or can that be influenced by Caterpillar and its exposure in Russia? That's the first question.

The second is I struggled to hear the South Africa Equipment spiel just now. If you can just give us a bit more background to the supply chain challenges that you've had in that business. Is the increase in the order book a function of that? And when and how do those supply chain challenges alleviate, and do we see that all coming through in the second half? Thank you.

Dominic Sewela

Okay. I guess on the issue in Russia I cannot speak for Caterpillar because they are a separate legal entity and so are we. I can only quote what they have said. They are suspending manufacturing in those two operations in Tosno as well as Novosibirsk. That's as far as I can say on that. We are given a license by Caterpillar in terms of the territory where we operate in. So if Caterpillar decides tomorrow that they're not going to manufacture completely for whatever reason, and we can source product elsewhere whilst we comply with sanctions, we will continue to trade.

So that link is independent, unless we then decide on our own to say quite frankly, Caterpillar, thank you very much for the license. We don't want to hold this license in Russia. That's a different story. It's ultimately the decision like we did in Spain. We said to Caterpillar we don't think it makes sense for us to remain in Spain. We would like to actually sell the business. And we exited Spain. But we then pursued another jurisdiction, being Mongolia. That's basically how that will pan out in the end. Andronicca, did you hear the question?

Andronicca Masemola

I did. Thanks Roy. In terms of the supply chain the impact is twofold. The machine lead time has increased particularly in the mining space. The lead times are much longer. On average we are looking at lead times of eight weeks. For some mining machines we are looking at lead times of close to 40 weeks. On the positive side our firm order book started growing even before we closed September. So some of these orders we anticipated and we started placing orders with Cat. And we are expecting that we will convert those into sales in the second half of the year.

The second part of the constraint has to do with part availability. It is taking us much longer to close the job where we have to either repair equipment or the trucks that are in for service and require parts. It is taking much longer to close those jobs, and it is having an impact on our working capital. You would have noted that we have reflected on cash. You know the equipment business is a business that is slow to generate cash. But given these challenges that we're dealing with, working capital had to increase to cater for these challenges while we try to ensure that at the right time when supply resumes we are able to convert [unclear]. Thank you.

Roy Campbell

Thanks. Maybe if I can have a quick follow-up. Given the lead times going out to 40 weeks, what does that mean for your cash flows in the second half? Are you going to be investing or building up inventories quite significantly as a result? That's all. Thank you.

Andronicca Masemola

Thanks for that. We have started already building inventory. And in the second half we're expecting to convert that inventory into cash. December/Jan was the worst period in terms of order fulfilment from Cat, but now we are starting to see those bottlenecks easing and we are anticipating that in the second half the inventory that we've built up will be converted. So in a nutshell we expect the second half to be better than the first half from a cash generation point of view.

Dominic Sewela

Thanks Roy.

Operator
We have a follow-up question from James Twyman from Prescient Securities. Please go ahead.

James Twyman
Yes. Thank you. Just one more quick one from me. Would it be possible for you to say how much of your product in Russia comes from Russia? How much comes from the US and how much comes from elsewhere?

Quinton McGeer
I would say it depends on the cycle and what orders you've received. The Russian plant manufactures 777s, assembles some engines and some excavators. But the 777s it is not the only factory in the world. There are other factories in the world that also manufacture 777s. So a 777 is an important product, but you would only sell maybe per annum on average over a five year cycle you will sell 15 777s per annum.

Then some of the large mining trucks, that all gets manufactured in America. The dozers get manufactured in America. This is our bread and butter products. The dozers are America. The graders are South America. The underground machines are in Thailand. The articulated trucks are in the UK. The backhoe loaders are in India and the UK. So you have manufacturing plants all over the world, so it's a very small part that is actually in Russia. That's basically your question.

Dominic Sewela
Thanks James.

James Twyman
Thank you very much.

Operator
Thank you. Our next question is from Kgosi Rahube of Citi. Please go ahead.

Kgosi Rahube
Thank you very much for this opportunity. I was trying to move away from Russia, but I just have one question. In terms of the competitive landscape are you seeing any sort of movement especially around your competitors? Are they pulling out of Russia at this stage?

Quinton McGeer
I think some competitors have suspended. Nobody has pulled out. They have suspended certain operations. Some competitors are still doing business as per normal but within the law. Obviously China has always been very big, because if you look at the Russian market it's a big market but dominated by Chinese and Russian equipment. So the western equipment, let's call it the premium brands, play in a very small segment anyway from that perspective, and specifically in hard rock mining. So I think everyone is more or less in a similar boat,

so nobody has really said they are withdrawing completely from Russia. They have just suspended operations with some manufacturers still continuing to deliver.

Kgosi Rahube

Okay. Thanks. That's clear. Just maybe two last questions for Chris. In terms of Ingrain I'm trying to get a sense of maize prices. You mentioned that you secured maize until mid-2023. Can you perhaps just talk about pricing and also what you think of where the prices are today? That's the first question. And the second question is around the comment in the announcement indicates that margins will be lower as a result of normalised sales mix. Can you perhaps give us more detail around that? Thank you.

Chris Wierenga

Kgosi, thanks for the question. Maize prices are still fluctuating around R4,200 to about R4,400 depending on deliveries up to July. And when I say we've secured physical maize up until mid-next year that means we have contracted with farmers for delivery and we've obviously taken a corresponding position on SAFEX to hedge against that exposure. So we do have some unpriced maize that as soon as we're able to price with customers for physical delivery of starch, we price that maize accordingly. So effectively we don't have an exposure to the maize price. We shift that risk to customers, and as soon as we contract for pricing with customers in line with that exposure we lock in the position.

Obviously it's important to secure maize supply into the business. But I think at this point in time we're monitoring the situation very carefully and it is business as usual on procuring maize and making sure that we stay in close contact with customers on pricing. Customers are quite keen, seeing volatility, to be discussing pricing at this point in time and locking in positions on physical delivery of finished product from us.

If I then turn our attention to the mix, I said the contribution percentage will be down slightly because in this period we will be selling more product at a normalised level to the alcoholic beverages sector, which last year we had some short supplies into that sector, therefore lack of demand because of the alcohol curtailment as a result of lockdowns during the festive season.

So what you're seeing this year is a normalisation of that, but we are still expecting to see very healthy double digit EBITDA margins coming out of the business and probably more of a normalisation to EBITDA margin that you would have seen pre-acquisition in 2019 under the old Tongaat reported results. I think that's just the guidance that we were providing in that particular space to show that we're seeing a mix change that has been more normal with our standard domestic customer distribution that we're used to in the business.

Kgosi Rahube

Thank you so much.

Dominic Sewela

Thanks Kgosi. This brings us to the closure. I think we've taken all the questions. If there are any further questions you could email those to Nwabisa. Most of you have her details. And we will try and reply as quickly as we could. And we will be getting into a closed period as of 1st April. I guess we will give you a further update around May when we release the interim results. Thank you very much, everybody, and you all have a great afternoon. Thanks.

Operator

Ladies and gentlemen, that concludes this conference. Thank you for joining us. You may now disconnect your lines.

END OF TRANSCRIPT