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Costain Group PLC
(“Costain” or the “Group” or the “Company”)

Fully Underwritten Capital Raising of up to £100 million

Costain today announces:

- A proposed new equity capital raising of up to £100 million (the "Capital Raising") in the coming weeks;
- The Capital Raising has been fully underwritten by HSBC, Investec and Liberum on a standby basis;
- An agreement with the Company’s lenders to extend its existing bank facilities from June 2022 to September 2023, conditional on the completion of the Capital Raising;
- Agreement with the Costain Pension Trustee on an updated recovery plan; and
- An update on the Group’s dividend policy.

Update on Costain’s performance

Costain has today separately announced its full year results for the year ended 31 December 2019. In summary:

- **Underlying operating profit of £17.9 million** (2018: £52.5 million): in line with its revised expectations as set out in the trading update on 12 December 2019; the reduction in the year reflecting previously announced contract delays, a contract cancellation and the impact of the A465 contract arbitration outcome.
- **Continued strong momentum in securing new work**: £1.7 billion of new contract awards and extensions to existing contracts secured during the year, with the order book, as at 31 December 2019, standing at £4.2 billion.
- **New Leading Edge strategy in place**: accelerating the Group’s deployment of higher margin services through leveraging its strong client relationships and reputation for complex programme delivery.
- **Significant market opportunities**: Costain’s markets have significant long-term committed investment programmes in place, with a focus on addressing the UK’s strategic infrastructure needs and providing the Group with an annual £23 billion addressable market

Background to and reasons for the Capital Raising

Costain's markets have changed significantly over the last five years which has led to a change in the nature of the relationship between Costain, its clients and its suppliers.

Costain has successfully positioned itself to compete effectively for new business and work in strong partnerships with its clients, resulting in a transition to a structurally increased working capital requirement.

Specifically:

- Costain's major clients are continuing to consolidate their supply chains as they seek to derive business improvement and transformation by working in more strategic and collaborative relationships with key suppliers – as a consequence, Costain's clients are highly focused on appointing financially strong and stable partners as their reliance on those partners has increased;

- There has been an increase in the use of joint operation delivery structures and project bank accounts, as clients and partners respond to the impact of the well-documented failure of certain contractors in the sector by requiring increased direct control over their financial risk profiles – this has resulted in an increase in the level of Costain's balance sheet cash being held in such joint operation structures and project bank accounts, rather than being freely available for the Group to use for general working capital purposes; and

- The introduction of the Prompt Payment Code whereby contractors are required to pay their suppliers earlier has also resulted in higher working capital requirements – in response, Costain has implemented revised processes to ensure that suppliers are paid promptly, with the average time taken to pay invoices reduced to 34 days from 58 days.

The Board believes there is a significant opportunity for the Group to capitalise on the growing infrastructure market opportunities available to Costain, in line with its strategy. Also, having a strong balance sheet has become increasingly important to Costain's clients and other stakeholders. For these reasons and to provide additional headroom in the current environment to effectively manage working capital flows in the business, the Board has concluded that it is in the best interests of the Group to raise up to £100 million of new equity to strengthen the Group's balance sheet.

Capital structure and cash position

A key element in the successful implementation of the Group's Leading Edge strategy is the efficient allocation of capital. The Board regularly reviews the appropriate capital structure for the Group and capital allocation with regard to ensuring that the Group can deliver on its ongoing obligations, including addressing the legacy pension contribution commitments and making regular returns to shareholders, and effectively exploit available growth opportunities.

In addition, maintaining a strong and flexible balance sheet is a key requirement of clients in tendering large long term contracts, is necessary to manage the increasing move in the sector to delivery through joint operations and use of project bank accounts, and supports the investment needed to deliver Costain's Leading Edge strategy.

The Group continues to have a positive net cash position, which as at 31 December 2019 was £64.9 million (2018: £118.8 million). Of this, approximately £35.0 million (2018: £30.0 million) reflects positive timing receipts at the year end which reversed in the early part of 2020. Included within the Group's net cash position is £83.5 million of cash in joint operations (2018: £84.5 million). The average month-end net cash was £41.2 million for the period (2018: £77.1 million), of which £78.3 million was the average month-end net cash in joint operations (2018: £83.4 million). Before taking the Capital Raising into account, the Group expects to maintain a positive average month-end net cash balance (including cash in joint operations) in 2020, increasing going forward.

The Group has total banking facilities in place of £187.0 million (which were £116.0 million drawn as at 31 December 2019, with month-end average drawings during the year of £93.7 million), and £320.0 million of committed and uncommitted bonding facilities.

In 2019, the Group's net cash position was impacted by a number of market factors and performance on certain contracts:

- Market dynamics:
  - The Group has implemented revised processes to ensure that suppliers are paid promptly, with the average time taken to pay invoices reduced to 34 days, moving into line with sector best practice, from 58 days in the same period in 2018, reducing cash held by £15.0 million; and
  - Structural market changes, including the level of cash held in joint operations and project bank accounts, have increased the Group's general working capital requirement.
- Contract performance:
  - A465 contract: £37.0 million cash outflow in the year;
  - Diamond arbitration: cash cost of £9.7 million in the year; and
  - Delays to the start of new contracts and a contract cancellation, reducing the level of profit in the year by approximately £16.0 million.

In addition, with regard to the National Grid Peterborough and Huntingdon contract, the timing of the increased forecast costs and contract receipts is expected to have a temporary working capital impact during the period of the contract, which is anticipated to complete in October 2021.

The Capital Raising will leave Costain with a combination of a demonstrably strong cash balance and committed, available long-term bank facilities to take advantage of the significant growth opportunities and to manage the working capital requirements of the business.

Costain has also agreed with its banks that the maturity date of its existing £187.0 million facilities will be extended from June 2022 to September 2023, conditional on completion of the Capital Raising by a long stop date of 30 June 2020.

The Capital Raising has been fully underwritten by HSBC, Investec and Liberum on a standby basis. The standby agreement contains customary representations and warranties, undertakings, termination rights and conditions.

Rothschild & Co is acting as financial adviser to Costain on the Capital Raising.

Pension Recovery Plan

In accordance with the pension regulations, a triennial actuarial review of the Costain defined benefit pension scheme was carried out as at 31 March 2019 and an updated deficit recovery plan has been agreed with the Scheme Trustee. Under the terms of the plan, from 1 April 2020 to 31 January 2029, the Group is required to make: (i) cash contributions of £10.2 million per annum (increasing annually with the Consumer Price

Index) (the “Shortfall Correction Contribution”); and (ii) if, in any year, the total dividend amount paid by Costain exceeds the Shortfall Correction Contribution, an additional contribution equal to such excess. Any additional payments in this regard would have the effect of reducing the recovery period in the agreed plan.

Dividend policy

Recognising the importance to Costain of maintaining a strong and growing capital base, following the proposed Capital Raising, Costain will target a dividend cover of around three times underlying earnings, taking into account the free cash flow generated in the period. The first dividend to be paid under the new policy is expected to be an interim dividend for the six months ending 30 June 2020, payable in October 2020.

- End -

This announcement contains inside information for the purposes of article 7 of EU Regulation 596/2014. The person who arranged the release of this announcement on behalf of Costain was Tracey Wood, General Counsel and Company Secretary.

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