MANAGING DIRECTOR’S STATEMENT

FINANCIAL PERFORMANCE

During the financial year under review, the Group continued to be impacted by cost escalations in its commercial shipbuilding projects, which affected the Group’s earnings. BHIC recorded a loss after tax of RM112 million compared with the profit after tax of RM18 million in 2011. Nevertheless, it is important to note that despite the difficulties faced on the commercial shipbuilding front, BHIC has fulfilled its obligations and delivered the vessels to the agreed quality and standards.

On the other hand, the share of profit from associates was higher in line with the progress achieved on the Littoral Combat Ship project.
Dear Shareholders,

While we continue to grow our businesses, BHIC has never lost sight of the need to redefine and strengthen the pillars that provide the foundation for our organisation. The year under review proved to be another busy period for the Group in which we strived to build a sustainable entity through good governance, sound infrastructure development and a committed workforce equipped with the relevant competencies and expertise.
Over the past five years, we have constructed various commercial vessels

- Double-hulled chemical tankers
- A well testing and servicing vessel
- Tugboats
- AHTS with DP2 setups
- A floating hotel
- Accommodation barges
Throughout 2012, the project involving the construction of six littoral combat ships (LCS) by our associate, Boustead Naval Shipyard Sdn Bhd (BN Shipyard) focused on engaging its primary stakeholders to determine the requirements of the project and to establish contractual deliverables for the vessels that are bigger, faster and more sophisticated than the first generation of patrol vessels. Following consultations with the Royal Malaysian Navy (RMN), the contract build specifications for the LCS were agreed during the year. This resulted in the finalisation of the concept design stage in November 2012.

As it stands, the design fulfils the LCS’s primary mission of detecting, identifying, and neutralizing air, surface and subsurface threats. It also provides support to land, air and sea operations and acts as a platform for intelligence gathering.

At the same time, the preparation work to gear the company for the implementation of the project is underway. BN Shipyard design engineers have participated in the concept design which was intended as an avenue for capability building. Another group of personnel involved in material management has attended workshops on the material management system in order to learn from our partner shipyard (DCNS S.A.) practices for adoption in BN Shipyard. Capability audits have also been carried out by DCNS S.A. to assess the gaps in BN Shipyard’s yard infrastructure and resources.

Contract negotiations were undertaken throughout 2012 with many major original equipment manufacturers (OEMs) for the supply of systems and equipment. In addition, verification and validation process with all potential suppliers has been ongoing in order to finalise the technical procurement specifications. Thus, not only will this project generate a positive multiplier effect in terms of equipping our staff with new expertise and knowledge, the local business community can enjoy the benefits of technology transfer and vendor participation.
Boustead Penang Shipyard Sdn Bhd in 2012 delivered another 67.8-metre anchor handling tug supply vessel, following the successful completion of our first ship developed with DP2 requirements in the previous year. Subsequently, the shipyard completed two American Bureau of Shipping class 111-metre accommodation barges. Equipped with a helicopter deck and 236 cabins, these barges were built to perform mid- to long-term offshore activities. With the delivery of the second accommodation barge, the last major vessel under the commercial shipbuilding projects, Boustead Penang Shipyard will not incur further cost implications of this nature in the current financial year. Moving forward, efforts are underway to transform the yard in Jerejak island into an efficient and profitable yard to support our shipbuilding and ship maintenance, repair & overhaul (MRO) businesses.
In Kedah, Boustead Langkawi Shipyard Sdn Bhd has started construction of two 16-metre general purpose harbour tugs. With a 20-tonne Bollard Pull (pulling capability), the vessels will be utilised by BN Shipyard for harbour support duties that include towing, mooring and assisting sea trials of other ships. The design, created in collaboration with Macduff Ship Design, a UK-based company, received the stamp of approval from Ships Classification Malaysia, the only local authorised body to undertake classification of ships registered in the country.

In line with the strategy review in 2011, the Group has moved forward to become less reliant on large commercial projects, and instead, is developing a portfolio of smaller commercial craft that will afford us a share of control over design and which can lead to multiple units or repeat orders.

Our collaboration with Macduff Ship Design, which provides BHIC with access to their portfolio of tugs and workboats, is the crucial first step that will enable us to enhance our own ship design capability, especially in the offshore support vessel (OSV) category. OSVs are vessels designed and built to cater to the needs of the oil and gas upstream industry, and its demand is anticipated to grow in tandem with the healthy level of capital expenditure planned by PETRONAS in the next several years.

Large new capex for Malaysian offshore oil fields gives impetus needed for the local O&G industry. We aim to take advantage of this opportunity.
MANAGING DIRECTOR’S STATEMENT
The Group is proud to partner with the Government in protecting national sovereignty. The LCS and FICs incorporate state of the art technologies to help defend our waters.
During the year, the Group handled various ILS projects. In-service support of the two RMN submarines, KD TUNKU ABDUL RAHMAN and KD TUN RAZAK, continued to progress smoothly under Boustead DCNS Naval Corporation Sdn Bhd (BDNC). BDNC’s scope of work included management of all maintenance and industrial activities related to the submarines including technical and logistics engineering aspects, management and supply of spare parts, as well as provision and maintenance of yard facilities and equipment.

Scheduled maintenance for the submarines is integral to maintaining their optimal capability and availability. Through this process, there is a tangible transfer of technology and technical know-how to our Malaysian personnel and subcontractors involved. The Group is on-track to be in a position to undertake the maintenance of the submarines with a completely local team of technicians by the end of the in-service support contract in 2015.

During 2012, BDNC successfully completed three scheduled maintenance cycles for both the RMN submarines.
BHIC Navaltech Sdn Bhd continued to provide services for various classes of the RMN fleet throughout 2012. The year also saw the company increasing its presence in Kuantan where it carried out preventive and corrective maintenance, modification work and other related services.

A RM70 million three-year contract for the supply and delivery of spare parts, maintenance services and training for the 23rd Frigate Squadron of the RMN was secured by BN Shipyard in September 2012. The ILS contract for the 17th Patrol Vessel Squadron, which commenced in mid-2011, is still on-going. In addition to this, the company also performed repairs on several luxury yachts in Lumut in the year under review.
BHIC MRO activities range from ships, submarines and helicopters, to combat management systems, defence electronics, electrical equipment and internal combustion engines. There is a focus on strategically important assets.
In 2012, Atlas Defence Technology Sdn Bhd, a BHIC subsidiary, successfully renewed its LRQA's QMS ISO 9001:2008 certificate, an internationally recognised quality management system standard, for another three years. During the year, the company provided maintenance services and spare parts for the Bridge Shiphandling Simulator at RMN's training centre, KD PELANDOK, as well as the Action Speed Tactical Trainer for RMN's Maritime Tactical Centre, PUSTAKMAR. In addition, technicians undertook various repair and maintenance work for RMN's New Generation Patrol Vessels' combat management system, navigation radar, electrical and degaussing systems. RMN also received other specialised work such as hydrographic/oceanographic sub-system equipment servicing for its hydrographical ships.

Both BHIC Defence Techservices Sdn Bhd and BHIC Bofors Asia Sdn Bhd (BHIC Bofors) are involved in providing gun repair solutions. In 2012, BHIC Defence Techservices secured a contract from the MMEA for the repair and overhaul of 20mm Oerlikon guns whereas BHIC Bofors obtained a three-year RM6.0 million contract renewal for the supply, maintenance and training for its 40mm BOFORS gun and a two-year RM5 million contract for the maintenance and training for its 57mm BOFORS gun. To accommodate equipment testing and maintenance work of these guns, BHIC Bofors' Kota Kinabalu workshop facilities were expanded in 2012.
Additionally, Dominion Defence & Industries Sdn Bhd, a BHIC subsidiary based in Lumut, continued with its principal activity of supplying marine, defence and general products to the BHIC Group, as well as government defence agencies and the commercial sector in 2012.

We are pleased to report that a joint venture company within the Group, BHIC MSM Sdn Bhd’s MRO work on MTU Friedrichshafen GmbH’s engines progressed according to plan during the year. Although BHIC MSM is currently concentrating on the maintenance of MTU engines below 3000KW, there are plans to diversify the MRO work to other models in the MTU Series in 2013.

Since setting up a temporary facility at Terminal 3, Sultan Abdul Aziz Shah Airport, BHIC AeroServices Sdn Bhd (BHICAS) has started servicing MMEA’s Dauphin AS365N3 helicopters. BHICAS also sent its technicians to the Eurocopter Training Services in Marignane, France, for helicopter training services in preparation to service eC725 tactical transport helicopters.

The Royal Malaysian Air Force took delivery of the first two of 12 eC725 helicopters in December 2012. As part of the offset arrangement, Eurocopter has set-up a regional EC225/725 Full Flight Simulator Center (R-FFS Center) to become a training centre for helicopter pilots and crew members covering military and civil (off-shore oil & gas) customers in the South East Asia region. BHIC has a minority stake in this enterprise.

In Lumut, Kuantan and Kota Kinabalu, BN Shipyards’s ship repair division carried out a multitude of services on RMN ships. These included underwater repair work, refit and the Service Life Extension Programme. Two more ships, KD HANG TUAH and KD TUN ABDUL JAMIL, were delivered to RMN in July and November respectively after refit work was successfully completed. In January 2013, we secured the refit work for KD SRI INDERA SAKTI, and with the renewal of the right to provide all scheduled maintenance on RMN vessels obtained in mid-2012, the company expects more vessels to be sent for MRO work in 2013.

Boustead Langkawi Shipyards Sdn Bhd remained focused on luxury yacht repairs in addition to its tugboat construction contract. The company also performed MRO work on ferries and other commercial vessels.

In Lumut, BHIC Electronics & Technologies Sdn Bhd’s (BEAT) technicians carried out various MRO jobs on electronic equipment and systems onboard RMN ships, including KD LAKSAMANA TUN ABDUL JAMIL and KD HANG TUAH in 2012. As for KD JEBAT, the team carried out third level maintenance on the MM40 missile prior to a firing exercise. The company’s other major client is the Malaysian Army, where it provided maintenance services and supplied spare parts for tactical radio equipment during the year.
The global economic slowdown has affected this segment. We are expanding on other activities and providing value-added services to mitigate its impact.
The year marked the successful delivery of all of the fast interceptor crafts (FIC) to the Malaysian Maritime Enforcement Agency (MMEA) by BYO Marine Sdn Bhd (BYO Marine). Categorised as MRTP 16 or Multi-Role Tactical Platforms, the FIC comply with stringent international standards including Det Norske Veritas (DNV) and High Speed Light Craft (HSLC) Rules. A proud moment for BHIC, this project was a successful collaboration with our Turkish partner, Yonca-Onuk Savunma Sanayii A.S. The effective transfer of technology to BYO Marine by our Turkish partner enabled the local workforce to master the construction of advanced composite boats of up to 44 metres, which resulted in the 2011 award of ISO 9001-2008 certification award by Lloyd’s Register Quality Assurance Ltd.

Aimed at enhancing the effectiveness of maritime law enforcement, the FIC are well-suited for interceptor roles, anti-smuggling and anti-piracy activities. They can also serve as sea ambulances and be utilised for search and rescue missions, among other activities.
After obtaining a manufacturing licensing agreement in 2011 with American-based Raytheon, the company has now qualified our Group’s manufacturing arm, Contraves Advanced Devices Sdn Bhd (CAD) as a participant in its Strategic Enterprise Aligned Commodities provider programme and a Raytheon preferred supplier.

CAD was subsequently awarded a contract by Raytheon in early 2012 for the production and supply of components for its Evolved Sea Sparrow Missile. However, reflecting the slowdown in many developed economies in 2012, CAD’s commercial electronics manufacturing arm experienced slower export sales to Europe and the US.

During the year, CAD and its subsidiary were given the opportunity to undertake a RM2.0 billion procurement, engineering and integration works for the LCS’s combat management, fire control and communication systems. As a result, CAD will be expanding its Melaka factory as well as establishing a new centre in Cyberjaya. In partnership with established OEMs, the company is committed to delivering a sustainable vendor programme as the ten-year contract will require local vendor selection and development of small to medium sized enterprises to support CAD’s supply chain requirements.
BHIC has agreed with the Government to form Pyrotechnical Ordance Malaysia Sdn Bhd (POM) in response to the need for national self-reliance for artillery propellants. The new plant in Bentong will be operational in 2013, and POM will be a 49% associate of the Group.

The second half of the year saw a significant improvement in our chemical tanker charter operations. MT CHULAN 1, which successfully completed its first year time charter with Asahi Tankers Co. Ltd. in November, managed to secure a five month extension at a higher charter rate. After months of uncertainty in the open spot market, MT CHULAN 2 secured a thirteen months Contract of Affreightment with Vitol Asia Pte Ltd, in July 2012.

This was followed by MT CHULAN 3 which was also taken up by Vitol Asia Pte Ltd under a thirteen month Contract of Affreightment immediately upon its delivery in August. The acceptance of the vessels by the oil majors is undeniable proof of their high quality standard and performance capability.

Our Marine Technology Academy (MTA) continued to offer diploma level courses to Royal Navy of Oman (RNO) technicians. A new batch of RNO personnel enrolled in the Engineering Application Course and the Technician Application Course in February 2012. The training was carried out in two phases; the first was held in Universiti Teknologi Malaysia (UTM) and the second technical application phase was held primarily at MTA’s premises in Lumut. In addition, the students were enrolled into BN Shipyard’s Toastmasters Club to enhance their command of the English language.

During the year under review, a new programme called Technical Conversion Course was developed in collaboration with UTM. There are 14 RNO personnel attending the one-year programme which commenced in September 2012. The programme’s main objective is to facilitate the conversion and development of mechanical-based knowledge to technicians supporting the operation and equipment maintenance on RNO ships.
TRANSFORMATION INITIATIVES

The Group is committed to nurturing a high performance culture centered on work-life balance as this forms the crux of its transformation strategy. To this end, town hall meetings for employees were conducted in Lumut, Kuala Lumpur, Langkawi, Kota Kinabalu and Pulau Pinang to disseminate key messages and updates.

MANAGING DIRECTOR’S STATEMENT

Following the formalisation of the BHIC Group Policy Manual and Limits of Authority, engagement with all relevant staff was held to provide them with clarification and to obtain feedback. The Group Corporate Communications Department also launched its own Policy and Manual which will help guide our communications with external stakeholders as well as within the internal “BHIC community.” A rejuvenated corporate website was unveiled in early January 2013.

During the year under review, the BHIC Group focused on instilling the importance of workplace health and safety amongst employees. Towards this end, BHIC organised a Health, Safety & Environment Week in Kuala Lumpur in June 2012. In conjunction with this event, selected Continuous Improvement Representatives were exposed to the 5S, a workplace decision-making process in a “train the trainers” programme. In turn, they were to guide colleagues on the processes involved. The week-long event culminated with a competition to award the most organised and most creative & innovative departments. Additionally, a safety logo and the slogan ‘Safety First’ were formally adopted for the Group’s use.

After the successful roll-out of the Group’s Performance Development Review Form, the Group’s compensation structure was revamped as a first step to achieving the objective of aligning our compensation to the market. The performance-based compensation structure follows the balanced scorecard approach which also rewards effective learning. During the year, employees at all levels participated in a wide variety of training programmes and seminars.

In addition, to ensure each business and support unit is operating in alignment with the Group’s vision and mission, the operating plan and budget of the units are subjected to review by the BHIC Group Corporate Planning Committee. Selected steps and measures were taken to address the identified gaps and to realise the benefit of synergies.

In 2012, the BHIC Group Information System Department implemented and expanded the coverage of its flagship
MANAGING DIRECTOR’S STATEMENT

application and enterprise resource planning software, the SAP System. It successfully rolled out the financial, human resources and project management systems to Boustead Penang Shipyard Sdn Bhd. In addition, the SAP Business Consolidation System (BCS) is being developed to improve the Group’s financial consolidation process.

Emphasis was also placed on data security in order to safeguard data and information via encryption technologies. Initiatives are now in place to maintain operational excellence through the adoption of Information Technology Infrastructure Library (ITIL) practices and information technology standards, augment efficiency and effectiveness of its related infrastructure, and improve staff competency through continuous learning and professional development.

Another key initiative in 2012 was the establishment of BHIC’s Intranet portal as a common platform for knowledge-sharing among employees. The platform will allow content collaboration and support integration of commonly used MS Office suite programmes. The first phase of the Intranet went live in January 2013.

MOVING FORWARD

The prospects for the maritime sector remain challenging amid surplus capacity. However, in certain segments, such as OSVs, demand for new vessels is expected to grow in tandem with a robust oil and gas sector.

As part of its Entry Point Project, BHIC is investing resources in developing new designs to cater for new industry trends and environmental regulations. Over the long term, we plan to train more than one hundred local ship designers and systems engineers and, by doing so, move up the value chain.

We are optimistic about this segment of the market as the OSVs require various MRO services which the Group is more than capable of providing. Moreover, our facilities and extensive vendor pool is being expanded and enhanced to ensure a captive market. There are ongoing efforts to secure selected oil & gas fabrication work for our Jerejak shipyard, due to the physical limitation imposed by the Second Penang Bridge. At the same time, efforts to secure a new site for this important activity are underway.

On the LCS project, we are expecting 2013 to move forward on a positive note, with all contracts with the government, partnering shipyards and major OEMs being finalised according to plan.

For specialised vessels such as FIC, there is great potential for repeat business in the near future given our good track record. Furthermore, there is a large volume of available work in servicing naval ships and equipment. Thus, the Group’s subsidiaries are regularly expanding their scope of services to ensure that the needs of our clients are well taken care of.

The Group’s venture into aviation has a bright outlook with BHICAS’s permanent MRO Centre at the Subang Helicopter Centre on track to begin operations in 2014. The MRO Centre will be equipped and qualified for the maintenance needs of various military helicopters.

APPRECIATION

I would like to take this opportunity to express my sincere gratitude to all Warga BHIC for your dedication and perseverance, as well as for upholding our ethics and values during the course of our business activities in the year under review, in spite of the challenges we faced.

Our shareholders have again shown their unwavering loyalty to the Group and we thank you for this. We also acknowledge the support of the Government of Malaysia, its agencies and regulatory bodies, as well as our customers and business partners. With your continued support in 2013, we will move BHIC into a new era of growth.

Terima kasih.

TAN SRI DATO’ SERI AHMAD RAMLI BIN HAJI MOHD NOR