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## **SNC-Lavalin First Quarter 2020 Earnings Conference Call Transcript**

**Date:** Thursday, May 7, 2020

**Time:** 9:30 AM ET

**Speakers:** **Ian Edwards**  
President and Chief Executive Officer

**Jeff Bell**  
Executive Vice-President and Chief Financial Officer

**Denis Jasmin**  
Vice-President, Investor Relations



**Operator:**

Good morning, and welcome to SNC-Lavalin's First Quarter 2020 Earnings Conference Call.

As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be opportunity to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an operator by pressing star and zero.

I would now like to turn the conference over to Denis Jasmin, Vice President, Investor Relations. Please go ahead.

**Denis Jasmin:**

Thank you. Good morning everyone, and thank you for joining the call.

These are very difficult and uncertain times for all of us and I very much hope that you and your family are safe and well. I do appreciate you taking the time to listen in today.

Our Q1 earnings announcement was released this morning, and we have posted a corresponding slide presentation on the Investors section of our website. The recording of today's call and webcast will also be available on our website within 24 hours.

With me today are Ian Edwards, President and Chief Executive Officer, and Jeff Bell, Executive Vice President and Chief Financial Officer.

Before we begin, I would like to ask everyone to limit themselves to one or two questions to ensure that all analysts have an opportunity to touch base. You are welcome to return to the queue for any follow-up questions.

I would like to draw your attention to Slide 2. Comments made on today's call may contain forward-



looking information. This information by its nature is subject to risks and uncertainties and, as such, actual results may differ materially from the views expressed today. For further information on these risks and uncertainties, please consult the Company's relevant filings on SEDAR. These documents are also available on our website.

Now, I'll pass the call over to Ian Edwards. Ian?

**Ian Edwards:**

Thanks, Denis. Thank you all for joining us and I hope you are all managing well through the current situation and working safely.

Please turn to Slide 4.

Before we walk through the first quarter, I want to make two points considering the unprecedented nature of the current situation and the Company's evolution over the course of the last year. Firstly, the pandemic. We have moved quickly to safeguard our people, business and financial flexibility. Secondly, solid results today for Q1 demonstrate that our new strategic direction is proving effective, even in the current backdrop. The reshaping of our organization remains on track. We have a diversified business across engineering services in essential sectors such as infrastructure, transport and nuclear, with key skills that are in demand. Most of all, our employees have shared the same mindset and approach. I like to thank all our employees for this and their continued resilience, and the innovation shown on a daily basis. I'm very proud to lead this organization.

If you would turn to Slide 5, I'd like to outline the COVID-19 impacts on our business and the actions taken.

Our number one priority remains the health and wellbeing of all our employees. In the main, our physical projects are deemed essential services, so our Infrastructure Services, Operations and Maintenance and Nuclear work continues. Our LSTK projects continue with a couple of exceptions.



More than 30,000 people in our Professional Services moved to fully working remotely very quickly and we've retained all our capabilities.

In a very short space of time, we've moved from dealing with the immediate effects of safety and business resilience factors to being able to offer innovative and value expertise directly to government in tackling COVID-19. We've won contracts to support governments, managing projects related to COVID-19, and we're using logistics, field and project management expertise to help deliver responsive health facilities in both Canada and the U.K.

We were a first mover in taking actions to secure our financial standing. Our liquidity remains strong and we believe we have financial flexibility to deal with the impacts of COVID-19.

With our role as the economy restarts already beginning, we will be at the forefront of this alongside our government clients. Infrastructure planning and engineering will be key to stimulating economies and adjusting to new ways of living, and we have key capabilities here.

I'll walk you through how this looks for each sector in more detail, but first, if you turn to Slide 6, we've delivered a solid Q1. Revenue is up for Engineering Services excluding capital. This business remains the future of the organization and continues to deliver a strong EBIT.

The projects backlog is progressing well and it's reassuring that the Infrastructure EPC contributed a small segment EBIT and resources projects are now only 10% of the LSTK backlog left.

Crucially, we enter Q2 with a strong financial position. I'll let Jeff talk in more detail later on the full Q1 and our liquidity and financial flexibility.

I'll now talk about each part of the business, starting with EDPM on Slide 7. In Q1, the core EDPM business in the U.K., the U.S. and Canada continued to perform well. We did experience impacts in Asia Pacific and the Middle East as COVID hit these regions earlier. Business winning in Q1 remained



active with a number of transportation and infrastructure wins across the world.

As a key part of our future growth in Engineering Services, EDPM is driving our Digital Future strategy. Across the organization, our investment in digital technologies and ways of working has proven valuable through the current situation, and the insights we can provide clients by harnessing data will form the next generation of our projects.

If you turn, please, to Slide 8, for EDPM in Q2, remote working was swift and included nearly all employees, so our productivity rates are stable, although we do expect to see revenue reduce in Q2 due to the current uncertainties.

We are actively supporting governments in our core geographies and we are winning business in every region. Our government and client relationships are key as COVID-19 restrictions are gradually lifted and we are ready and we'll be there to support governments as crucial projects and infrastructure are put in place to ensure a positive recovery.

Nothing changes in our strategy for EDPM. Our focus is on having our capabilities active now and ready to grow as the recovery starts. We are seeing many opportunities for expansion in core services, including cybersecurity, defence, innovative housing solutions across the regions.

On Slide 9, we'll look at Nuclear. This is a great business and our position is enviable. In Nuclear, we have a strong global position and our work here proves to be resilient. In Q1, we won a number of diversified contracts across decommissioning, clean-up, and a framework agreement to support an existing nuclear fleet. We are focused on partnerships and being a leader in technology for our clients alongside enhancing our own operational excellence to ensure we grow and build on a strong market position.

Let's go to Slide 10 and I'll talk more on opportunities in COVID.



Nuclear has generally been deemed an essential service in our key geographies and where there is some natural slowdown with COVID, the demand for nuclear services remains strong. Already in Q2 we have delivered the Darlington Unit 2 refurbishment and this is part of our refurbishment work running through to 2026.

We have a number of new opportunities across our diversified nuclear business, and in our core geographies of the U.S., the U.K. and Canada, we are seeing multiple small-medium reactor projects requiring ongoing support.

Our Nuclear business is resilient, continues to deliver and is positioned for growth.

Please turn to Slide 11.

Infrastructure Services continues to be successful and gives an important presence in the North American infrastructure and transportation markets. Such services in these markets are key to the ongoing transformation of our company and the contracts in this area can often run for multiple decades as we operate and maintain facilities.

Additionally, our Infrastructure Services business has a number of differentiated offerings in niche markets around the world. Linxon has expanded its geographic reach and our leading district cooling business alongside facility and program management services continues to grow organically in the MENA region.

We are developing our Project Integrator model and this is where we will take our major project expertise and bring them to our clients as an integrated project and portfolio management service.

Moving to Slide 12 and how we are able to react quickly to the current climate with Infrastructure Services.



Our Infrastructure Services business has already seen new business in directly supporting the efforts to tackle COVID-19. We have a JV that is providing mobile health facilities to the Canadian government, and we are working in the pharmaceutical space to adjust production facilities towards testing kits.

As with our Nuclear business, the physical sites that we provide services on are primarily deemed essential. We are continuing our provision of services to hospitals, transit, power plants, defence, and civil administration.

Linxon has seen delays in contracts awards, however, we expect demand for power distribution to remain strong. This is simply a matter of timing. This is also the case for those projects where we are providing services to civil construction projects.

We are standing with governments, and across Canada and globally we will be a champion of infrastructure, contributing our project integrator, project management, engineering services and helping shape the social and transportation infrastructure solutions for the recovery.

Finally, in Engineering Services on Slide 13, we have capital. First off, the temporary dip in 407 traffic has some fairly obvious impacts on both 407 dividend and the contingent sales fund.

On our other concessions, we are not seeing a similar impact, with the different contract types based on availability rather than end user demand.

Our expertise in capital and the financing structure of major projects remains of value, particularly as governments may look to quickly finance and push through large projects in the recovery.

Let's look at Slide 14 and the Infrastructure LSTK projects.

The controlled management of the Infrastructure projects continues to progress well, and as noted earlier, these actually contributed a small positive EBIT in the quarter. Most of these projects continued



and where projects experienced temporary suspensions, we have worked with our clients to minimize cost of both demobilizing and returning to work safely. It's worth also noting that on the REM project, engineering and planning work continued.

In relation to COVID-19, we are well protected by contract clauses such as change in law and force majeure, and while there are obviously slower rates of progress on these projects that remain open, we currently have not foreseen forecast completion dates move significantly and we continue to assess these with our clients.

On Slide 15, we will take a look at Resources. We are now down to \$300 million of backlog remaining for LSTKs in Resources, and these projects are largely scheduled to complete this year. A swift action in the restructuring was to initiate withdrawal from the Valerus business, and we successfully completed that closure within Q1.

Services within Resources are under pressure and we are taking further actions to reduce cost.

Please turn to Slide 16.

As you've seen, the backlog of LSTK projects has been reduced by 20% to this time last year, and we have additional project control measures in place which further de-risk the remaining backlog. Of the remaining \$2.9 billion, only \$300 million remains in Resources and the majority of the Infrastructure projects relate to light rail transit systems. If we move to Slide 17, then we can see the phase-out of these projects.

From July '19 to the end of March 2020 we progressed \$0.5 billion of LSTK backlog. The Resources element is now a minimal portion and we are working with all our clients to maintain good visibility of the phasing out of each project. Nigel White's team remains very active in all these projects and he's working closely with sector presidents and the project teams directly in ensuring tight management of schedule and delivery.





Please turn to Slide 18. The Company is well positioned. We have moved rapidly to protect our employees, our business, and we have financial flexibility. We're able to maintain our services capability through this period and we're already seeing new demand for our expertise as governments and clients address the pandemic itself and transition to the phase beyond.

Our strategic direction remains on track and unchanged, and today's solid Q1 demonstrates our continued progress down this path.

The fact that we have already been tested over the past year has played to our favour of we have been able to demonstrate our ability to be agile and responsive in changing circumstances.

I'd like again to thank our employees for their resilience, collaboration, and positivity through this time.

I'll now pass to Jeff for more detail on the Q1 financials. Thanks, Jeff.

**Jeff Bell:**

Thank you, Ian, and good morning everyone.

Before I begin, I'd like to draw your attention to a change that we have made in our terminology. To better reflect the Company's new strategic direction and activities, we are now calling Engineering and Construction, or E&C, Professional Services and Project Management or PS & PM.

If you could turn to Slide 20, I will firstly summarize the first quarter results.

While total revenues fell 6% to \$2.2 billion from the prior year, driven primarily by reduced revenue from SNCL projects as the LSTK backlog runs down, segment EBIT of \$99 million was in line with the prior year as growth in Engineering Services from strong Nuclear and Infrastructure performance and reduced losses in SNCL projects offset the reduction in capital from lower Highway 407 dividends. In



Engineering Services, EBIT margins rose slightly to 7.3%.

Adjusted net income after including higher SG&A costs compared to Q1 2019 as a result of additional provisions and one-time reversals in the prior year was \$25.7 million or \$0.15 per share. On an IFRS basis, which included a fair value revaluation of the Highway 407 ETR contingent consideration receivable of \$50 million post tax, the Company had a net loss of \$66 million or \$0.38 per share.

Turning to Slide 21, we saw SNCL Engineering Services, excluding Capital, grow revenues, EBIT and EBITDA year-over-year. Revenue totalled \$1.5 billion, an increase of 6.4%. EDPM segment revenue fell 3.9% mainly due to shortfalls in the Middle East and the impact of COVID-19 in Asia Pacific. This is more than offset by a 5.9% increase in Nuclear segment revenues which had a strong performance across its key markets and a 49.8% increase in Infrastructure Services segment revenue, where our Linxon joint venture continued to expand its activities.

Segment EBIT results year-over-year showed the resilience of the Engineering Services portfolio. EDPM segment EBIT margin fell to 6.1% compared to 8.2% in Quarter 1 2019, primarily due to lower gross margin from the fall in revenues just mentioned. However, the Nuclear and Infrastructure Services segment EBIT increased in the first quarter to \$37 million and \$17 million, respectively, with EBIT margins of 15.5% and 4.9%. These were driven by underlying growth in Services and a nonrepeat of a one-off charge in Nuclear taken in Quarter 1 2019.

Engineering Services EBITDA increased 7% to \$143 million.

Capital segment EBIT fell \$23 million from Quarter 1 2019 to \$42 million as a result of lower dividends received from our reduced stake in the Highway 407 ETR.

Turning now to SNCL Projects on Slide 22, revenues for Q1 2020 decreased by 24% to \$648 million, mainly due to the continuing backlog runoff of certain major LSTK construction projects and a reduction in Services revenue and Resources as business win rates have slowed. Infrastructure EPC



projects delivered a segment EBIT of \$3.8 million compared to a loss of \$6 million in Quarter 1 2019 following solid delivery in the first quarter on key projects and limited impact of COVID-19. Resources recorded a negative segment EBIT of \$58 million due to unfavourable LSTK project reforecasts and a cost base misaligned to the reduction in Services revenue in backlog. Acceleration of cost reduction measures and business closures and/or sales are underway.

Turning to Slide 23, cash flows from operating activities have significantly improved in the quarter, totalling \$23 million in Quarter 1 2020 compared to a use of \$249 million in the same period last year. SNCL Engineering Services excluding Capital generated cash flow from operations of \$142 million, an increase of 27% from strong EBIT conversion and working capital efficiencies and timing initiatives. SNCL Projects continue to consume cash with a cash outflow from operations of \$152 million, although this was an improvement on the first quarter last year.

On Slide 24, the Company's focus on improving financial flexibility and liquidity can be seen. At the end of the first quarter, the Company had \$2.1 billion of cash on-hand and an additional billion dollars available to be drawn on the revolver credit facility. The Company's debt profile and maturities are spread over the next four years with \$300 million maturing later this year.

The net recourse debt to EBITDA ratio on the revolver credit facility calculated in accordance with the terms of the Company's credit agreement was 2.3 times at the end of March, well below the required covenant level of 3.75 times.

Finally, on Slide 25, as previously communicated, the 2020 financial outlook that was provided in the 2019 Q4 financial results press release is no longer valid due to the uncertainty created by the ongoing COVID-19 pandemic and the Company does not intend to provide any further outlook for 2020 at this time.

This concludes my presentation. We can now open the line for questions. Thank you.

**Operator:**

Certainly. We will now begin the question and answer session. To join the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. To join the question queue, please press star, then one now.

Our first question comes from Chris Murray of AltaCorp Capital. Please go ahead.

**Chris Murray:**

Thank you, gentlemen. Good morning. Just starting maybe thinking about the resources group and how to manage some of these losses on a go-forward basis. I guess the question, you talked a little bit in your script about accelerating some cost reductions and maybe some changes of business. Could you elaborate a little bit on the pace of what you think you're going to be able to do and the magnitude of getting that to at least stop being as much of a drag as it has been for the last few quarters?

**Ian Edwards:**

Yes, thanks for the question on that. I mean we said in our strategy going back that we look at all options with the Resources business and clearly the resources sector is under pressure. I mean there's volatility in the oil prices, we know, and there's COVID, and that brings also regional stress within the Middle East. So, yes, we're absolutely thinking at how we accelerate or take measures to ensure that we minimize any losses within the whole of this business. It is in two components. We have the LSTK, which we're working our way through. We always said that the LSTK portion didn't have any major kind of elements in there of risk such as we experienced on the Codelco, but it's not without risk and as you've seen, there's been some project reforecasts, not of large magnitude, over the last three quarters, but we are getting through the backlog and we're down to \$300 million there, and by the end of this calendar year the backlog in the LSTK will be done.

The remaining is a billion dollars of backlog in the services sector and clearly we have to fulfill the obligations there. Much lower risk activity and we don't see any issues in running down that backlog



and running through that backlog. But the key issue for us is cost and making sure that we get cost out and in line with the activity levels that we see, and we're working on that.

**Chris Murray:**

What about—it might be a bit challenging but I mean you have talked previously about even divesting of the group. Is there any opportunity to look at something like that?

**Ian Edwards:**

I think if—for sure, we were looking hard at that. I think to be realistic in the current climate it would be unlikely that we would be able to divest the whole business. There may be opportunities to divest parts of the business that have specific benefit to other potential purchasers, and clearly we're looking at that and clearly we are looking at those opportunities.

**Chris Murray:**

Okay, fair enough.

Interesting commentary around your free cash flow and operating cash flow, the fact that the Engineering Services business seemed to be a pretty positive contributor, but then the whole projects business has been a bit of a drag, offsetting a lot of that. The thought, though, I thought always was on that the—on the whole, the LSTK projects should, as they wind down, contribute some cash flow, so it's a bit of a project cycle thing. As these wind down, do you think that the cash flow drag from projects will either slow or reverse through the back half of the year?

**Ian Edwards:**

Let me pass this on to Jeff, but you're right in saying that what we expect is positive cash flow through the life of the project, and I think in the last quarter we were clear in saying that we would expect during the course of this calendar year to have a negative drag from projects, but over the life of the project to be positive. But let Jeff just expand on that, if you would, Jeff.

**Jeff Bell:**

Yes, happy to, and Ian, you've hit it right on the head. We absolutely said that over the life of these projects we would expect them to be cash flow neutral to positive, but that they would be a drag on operating cash flow here in 2020.

I think the other element you referred to was we made the observation back at the end of February that in terms of our view pre COVID-19 and withdrawing our outlook that we saw operating cash flow overall for the group, so obviously with Engineering Services and Projects being weighted to the back half of the year. Clearly, in the current environment we're in it's extremely difficult to quantify or estimate how exactly that's now going to shake out over the next two or three quarters, hence our withdrawing of the outlook. But certainly before that, on an overall basis, weighted to the second half, absolutely, as you said.

**Chris Murray:**

Okay, so the expectation is that, again, we'll have to see how the performance of the business actually goes but at this point no real change in your thoughts around the shape of cash flows, then.

**Jeff Bell:**

I think it's fair to say we'll have to see how it goes. I think that shape and its absolute amount will clearly be impacted by what happens as a result of COVID.

**Chris Murray:**

All right, fair enough. Thank you.

**Ian Edwards:**

Thank you.

**Operator:**

Our next question comes from Yuri Lynk of Canaccord Genuity. Please go ahead.



**Yuri Lynk:**

Hey, good morning.

**Ian Edwards:**

Good morning.

**Yuri Lynk:**

I'm wondering if you can provide a little more colour on EDPM and the performance in the quarter. I was a bit surprised by the decline in EBITDA and EBIT. I understand there was less FEMA work. Maybe you can quantify what that was and just your expectations for how that business should perform in the current quarter.

**Ian Edwards:**

I think we'll, myself and Jeff, we'll give this some colour. Let me go first.

Our EDPM business does go through a cycle during the year and for sure the first half of the year, and specifically the first quarter, has always showed less performance than the back half of the year, and there's a few reasons for that. One of the primary reasons for that is our business is obviously quite strong in the U.K. and is obviously also located in other jurisdictions where the end of the financial year is our first quarter, so the way that the work is awarded in that the first quarter is like a bidding cycle, and then those get awarded in Q2; the work is executed in Q3 and Q4. You'll have probably seen that historically through the numbers. That's one issue, so our expectation was much lower for this quarter than it would have been for Q4, for example.

Then the second component is really actually around the Middle East and Asia. I mean Asia Pacific, our downturn in business there hit at the Chinese New Year, so basically we had an impact through February and March, and for sure we saw an impact in business in March in the Middle East, and obviously clients have also held back awards in the Middle East because of the whole volatility around



the oil price. Primarily, the impact that you see in Q1 is there.

Going forward, we're not concerned about the business other than our overall concern on COVID.

Jeff, I mean I don't know if you want to add a little bit more to that, or?

**Jeff Bell:**

Yes. I think I'd make two observations. I think you're absolutely right, Ian. The decrease in revenue is in Asia Pacific and the Middle East, for sure, and we've talked about the impact of COVID. I think there's no question that the fall-off we've seen and the challenging environment in the oil and gas world, and obviously in that end of the world, does tend to have a knock-on impact to some of the infrastructure projects and civil engineering projects that EDPM does out there as well. And we saw some of that. There was, as you pointed out and we talk about in the MD&A, a fall in our revenue from FEMA in the U.S. It wasn't a massive number but it's more the absence of that in the first quarter this year versus last year where we had some work related to Hurricane Maria.

**Yuri Lynk:**

The Middle East and Asia would be what percentage of your EDPM revenue?

**Jeff Bell:**

It would—it's clearly it's a minority of our business. We can have a quick look. I don't have the percentage right to hand, but it would be a minority, but it was definitely the part that was impacted most dramatically. As you imagine, although it's a—if I think of Asia Pacific overall for the group, between our Hong Kong and Chinese offices, it's around 1%, 1.5%, but of course when you shut the offices down for a period of time, then it has a more dramatic effect, at least on the EDPM segment.

**Ian Edwards:**

I would also add on the Asia Pacific business, it's bounced back very quickly. I mean, our business is getting back to normal in Asia Pacific. As you can see, we've been awarded a fairly significant new





contract in Macau, so we're actually seeing a recovery through our business there quickly as well.

**Yuri Lynk:**

So, do you—should we expect maybe a but muted but still the same seasonal uptick in EBIT in EDPM for Q2?

**Ian Edwards:**

Progressively it has an uptick through the course of the year, so for sure. I mean, you should see that being repeated. The only caveat I would put on that is the impact of COVID. Whilst we feel our business, particularly our EDPM business, which is primarily in the public sector, 75% of our business comes out of the governments that primarily we work for in Canada, the U.S. and the U.K., we're not making any kind of definitive statement about what we think the impact of COVID is through the rest of this year.

**Yuri Lynk:**

Okay.

**Jeff Bell:**

I think we talked about the fact that—and you can see that in the press release as well—we are seeing through the first month here of Q2 some fall-off in revenue in the EDPM segment and in the Engineering segment; even though a lot of it is government-backed, we are seeing some reduction.

**Yuri Lynk:**

Okay. Thanks, guys.

**Operator:**

Our next question comes from Frederic Bastien of Raymond James. Please go ahead.

**Frederic Bastien:**



Thank you. I was just wondering on the resources sector, how are you approaching services opportunities? I appreciate right now there might not be a lot of opportunities to bid on but is your strategy to still pursue service opportunities in that particular sector?

**Ian Edwards:**

For sure, and we were having success, pre COVID, developing our services offering to the major clients and government sponsored clients in the Middle East and North America, but there has absolutely been a drop-off that we've seen during this crisis. It's a double impact, obviously, from oil price volatility and COVID. For us, our concentration here is making sure that we adjust our cost base to match and accommodate revenue fluctuations that we see within that sector. And obviously, burn off the LSTK as effectively and efficiently as possible. That's the current focus right now.

**Frederic Bastien:**

Right, but are discussions around margins, going-in margins and all that stuff, does that mean that—are they adequate for you to say, 'Okay, let's go with it,' and it's worth pursuing?

**Ian Edwards:**

Well, what we saw for sure pre COVID was, yes, at adequate margins in the services sector for that business, the Engineering and the Professional Services part of it. We saw good opportunity, but like I say, I mean that landscape is definitely changing now.

**Frederic Bastien:**

Okay. Thanks for that colour.

Then on the Infrastructure Services with the addition of Linxon, we get better revenue, better margins. Is the performance that you delivered in Q1 sort of a good run rate to use on a go-forward basis?

**Ian Edwards:**

Yes, I think so. Yes. I mean, yes. Linxon and the O&M part of the business and the project



management part that we're trying to grow within Infrastructure Services, I think what you see is pretty much representative, yes.

**Frederic Bastien:**

Okay.

**Jeff Bell:**

I'd add to that, Ian, that it's a repeatable type of product that they sell and install, but I'd make the observation they do that in a fair number of different geographies and some of their sites as part of local government restrictions have had to be suspended here into the second quarter because of that. Again, I think in a non-COVID world where there's no restrictions, I think what you saw in the first quarter is good representation. We're going to see some impact here in Q2 for the fact that some of their sites have been suspended for a period of time.

**Frederic Bastien:**

Okay, thank you. That's helpful.

**Operator:**

Our next question comes from Maxim Sytchev of National Bank Financial. Please go ahead.

**Maxim Sytchev:**

Hi. Good morning, gentlemen.

**Ian Edwards:**

Hi.

**Maxim Sytchev:**

A quick question in terms of oil and gas business. Is it fair to assume that the Services part of the business right now is also generating a negative EBIT?



**Jeff Bell:**

Why don't I take that one, Ian?

**Ian Edwards:**

Sure.

**Jeff Bell:**

Yes, it is. As Ian said, it's primarily related to the cost base that we're carrying which is why we're taking accelerating action on reducing that and realigning that. To the extent we're bidding on new business, we are bidding on business with growth margin thresholds that we're comfortable with but it's taking the associated operating costs and overhead out as a part of that. But if you looked at Resources overall in the first quarter, about half of that EBIT loss was related to Services, effectively because of the misalignment of the cost base—there is a bit of Valerus in there—and then the other half is related to projects.

**Maxim Sytchev:**

Right. In your opinion, how long do you think it's going to take to see the revenue and kind of on costs get to the point where, I mean like at least it's breakeven? Is this a number of quarters? Years? How should we think about this?

**Ian Edwards:**

Sorry, I thought Jeff was going to answer that one. We think we need—we're acting quickly. I mean we certainly undertook to act quickly around the Valerus and we've now closed that out. There are other components of the business that we are looking at very closely now. I mean it's an ongoing effort to make sure that we balance the backlog that we have and the revenues that flow through from the Services side of this to the cost base, but we're going at this really, really actively, and we'll be adjusting through Q2. We'll certainly be making further adjustments through Q2 to get to a place as quick as we possibly can so that the cost base matches the revenues that we've got in the Services



business to get it at least to breakeven perspective.

I think Jeff has been dropped off the line, but that's okay.

**Maxim Sytchev:**

Okay, then maybe because my next question was really around the noncash working capital, I don't know Ian if you are comfortable to kind of comment on that, the fact that we had positive operating cash flow in Q1, which is historically—I mean it hasn't happened in years.

**Ian Edwards:**

Yes.

**Maxim Sytchev:**

Just trying to get better understanding in terms of the moving parts there, if there is some unusual items that help you out. Is this dynamic going to unwind in Q2? Just, again, trying to get a better sense in terms of how we should be thinking about this.

**Ian Edwards:**

Yes, okay. Obviously everything we've tried—everything we're doing is to produce cash, operating cash flow and free cash flow. The whole strategy, the way that we set the company up in the middle of last year and the exit of the LSTK is because we know that our Services business that now are in SNCL Engineering Services have historically produced good cash flows, and we also know that the LSTK has been very, very volatile.

I think what you see is, as we're working through some of the LSTK, is a gradual stabilizing of that but not a complete elimination of it. There are some timing issues within Q1 that you'll see from the positive cash flow there, but in the main it's an improved cash flow performance through the LSTK and some timing issues.



I think Jeff is back on the line there. I don't know, Jeff, if you got that question. It's really about the cash flow positive—operating cash flow positivity that we saw, which is significantly better than in the past in Q1.

**Jeff Bell:**

Yes, and my apologies. My line cut off there.

Yes, year-on-year, it's a combination both in projects—so projects, although still a cash drain on an operating cash flow level in the first quarter, is better than last year, and that's partly a function of the fact that we have fewer ongoing projects, which helps from that perspective, and also we've been taking very proactive measures, particularly in Resources, to ensure that we're more closely matching revenue receipts from customers with payments that are going out related to those projects. That has helped, although clearly not complete eliminated the operating cash flow drain on projects.

Then on the Engineering Services business, which is a more naturally cash flow, operating cash flow generative business, again, we've been closely monitoring that, closely managing that so that we would expect to hold on to some of the efficiencies there, but we are benefitting from some timing as well through the end of the quarter, so we will see some reversal in the second quarter as a natural result of that.

**Maxim Sytchev:**

Okay. Clearly, you're making a reference specifically to the noncash working capital, I presume, when you're talking...

**Jeff Bell:**

Yes.

**Maxim Sytchev:**

... about the timing of things.



**Jeff Bell:**

Yes, exactly. Exactly.

**Maxim Sytchev:**

Okay.

**Jeff Bell:**

The other thing I should say is that there's a small amount in there around things like FX and those sorts of things, but that's the general story.

**Maxim Sytchev:**

Okay, and we still have not received anything on the Champlain, right?

**Jeff Bell:**

No.

**Maxim Sytchev:**

No, okay.

Last question, I just want to go back to EDPM because revenue declined 3% year-on-year, but EBITDA is down 23% year-on-year, so there is a pronounced negative margin dynamic, so I'm just curious to see exactly was there an execution issue that arose? Because again, I mean obviously I appreciate the seasonality, but I mean people look at these things year-on-year, so I'm just a big confused about that mismatch between revenue and EBITDA drop-off.

**Ian Edwards:**

I'm glad you asked another question on EDPM because the one thing I think that we—clearly, this business, it's very similar in its nature to other peers in the business, and we feel that our particular



EDPM is robust. There is absolutely—there is nothing underlying within the business other than its seasonality that has changed from the performance that we've seen in the past years, apart from COVID, and we particularly feel that our blend of customers and work, primarily being from the government sector or government clients public sector at 75% will ensure that our business is robust. I would further say that the majority of the revenues from this business is in Canada, the U.S. and the U.K. Clearly, we've got North American revenues, Middle East and Asia Pacific, but by far the majority comes out of the three geographies. So, there's nothing underlying here.

Now, what we have to do as we enter this crisis and we see revenues adjust, is we've got to be really agile in adjusting the cost base of the business to match the adjustments in revenue and we've taken numerous measures that we announced in our press release to undertake a menu, if you like, of how we would go about those cost measures. They're from general pay cuts, reduction of hours, furloughs, and where we don't see any business coming back, redundancies.

Now, when we hit this crisis in Asia Pacific, and to some extent in the Middle East, we were probably slower than we would like to have been to make those adjustments, and you'll have seen certainly the profitability downside from that. I think that kind of gives you the whole story and where we're feeling about where we're moving from here into the year. But I'd have to caveat everything by saying we don't really know what the impacts on revenues will be in Q2 and Q3. We're seeing we're winning work going forward, we're able to still win work. The scenarios that we planned, we're ahead of that, so we're feeling pretty good, but I would just put an override on that that it's still yet to be seen.

**Maxim Sytchev:**

I guess the bottom line, so is it fair to say that as you're making these adjustments on the cost side that we should be still kind of in a typical engineering type margin even with—obviously, I mean everybody is projecting revenue compressions. Is this still something that's what you're targeting?

**Jeff Bell:**

Yes. I mean I think there's—the other element I'd add to this obviously is that in the short term





obviously our operating costs are broadly fixed and what you then see, where you get a slowdown like in Asia Pacific or in the Middle East, is that you lose the gross margin, and broadly the gross margins we're realizing and targeting are in line with our long-term guidance and aspirations there, but of course you get a multiplying effect as that sort of moves down the P&L.

**Maxim Sytchev:**

Right. Okay, that's it for me. Thank you very much.

**Ian Edwards:**

Thank you

**Operator:**

Our next question comes from Mona Nazir of Laurentian Bank. Please go ahead.

**Mona Nazir:**

Good morning and thank you for taking my questions.

First of all, Jeff, congrats on your appointment. I'm just wondering or I'm interested in hearing your view when it comes to the story from a fresh perspective. I understand that there's significant uncertainty on the back of COVID, but I'm just wondering where do your priorities lie and if you could give a pecking order, what's your goal, or what would you like to see occur within SNC, whether that's for 2020 and beyond?

**Jeff Bell:**

First of all, thank you. That's definitely a wide-ranging question, but I'll boil it down to something fairly short.

I would have the following observations, having come in. The first is that I think the strategy and our capability—and I've only been here just under three months—I think are very well aligned, and we're



clearly going through, as everyone is, the current pandemic crisis, but my observation is one of the reasons I joined SNC is that I thought the excellent capability that the business has is well aligned to the strategy going forward.

I think my second observation is clearly there is a lot of transformation to be done, including I think as a high priority transforming the Resources business and with a slightly longer burn rate, obviously, running off the LSTK projects, both in Resources and in Canada, which are mostly transit, rail lines and we have a lot of experience in all of that.

I think my third observation is that—and you will continue to see us do that—a real focus on cash flow going forward in addition to some of the other metrics we have, but a real focus on cash going forward, and therefore, ultimately, as we transform the business and move forward with effectively the Engineering Services business, putting an appropriate capital allocation framework around that in terms of how we see the ability to invest free cash flow across investing in the business, returns to shareholders and what's required for the balance sheet, but all that will come down the road.

**Mona Nazir:**

Perfect. That's very helpful.

Just lastly, in your prepared remarks you touched on your heavily weighted public exposure and we've seen some decline there. I'm just wondering if you could give some insight in regard to the discussions that you're having with your end customers, whether that be on the government side or the private side. Thank you.

**Ian Edwards:**

Yes. Well, actually, we see being weighted in our EDPM business as an advantage. The reason we think that is because we believe, as in post crisis, post kind of 2008 crisis, that the stimulus will come through investment in infrastructure. The services that we offer, both in Infrastructure Services and in EDPM are front-end services. The design, the inception, the working through the planning, the whole



front end of development of infrastructure is what we do, and whilst it takes time to get that investment into physical construction—shovel-ready so to speak—actually exiting the construction part of our business as we have, we don't see that—we'll have a greater impact because of that and actually, we think we're really well placed in those businesses.

What we're actually doing is trying to be really proactive here through our clients and to governments, and actually thinking through how do we help be a partner to get these projects so-called shovel-ready as soon as possible to gets jobs into the marketplace and dollars into the economy. We think we're a good partner to do that because of our range of capabilities.

**Mona Nazir:**

Perfect. That's very helpful. Thank you. That's it from me.

**Ian Edwards:**

Thank you.

**Operator:**

Our next question comes from Mark Neville of Scotiabank. Please go ahead.

**Mark Neville:**

Hey, good morning.

**Ian Edwards:**

Hey, Mark.

**Mark Neville:**

Maybe if I can start with the EDPM and maybe just—I appreciate the comments around the business longer term, but maybe just thinking shorter term, again, I understand there's typically a seasonal uptick from Q1, but now you're layering on sort of COVID, you're talking about some declines I think in Q2. I'm



just—again, appreciate you're not providing guidance, so maybe just order—ballpark order of magnitude sort of what to maybe expect for the next couple of quarters, just so we're sort of all not without base on that.

**Ian Edwards:**

Really difficult to be that precise. Really difficult. What I can say is that we are continuing to win work. We're continuing to make adjustments to the cost base of the business if and where we see revenues decline, wherein the majority of our markets are where we will see the type of work that we do strong, which is North Europe, the U.S., Canada and the U.K.

There will be some softening around the Middle East, but the Middle East is not a significant part of our EDPM business, and what's really encouraging is what we've seen in Asia Pacific and Australia in that it's back to business pretty quickly there, and the stimulus is coming through. In Hong Kong, they're making a real effort to get projects started and to get the business going again.

We're trying to be almost deliberately open-minded as to—and agile, as to how this thing evolves because I don't know how we could say it's going to be like this or like that. I mean it's—the business is not back—the economy is not back to normal. It's a pretty big impact and I think it would be wrong for us to sort of be misleading and say it's going to be 10%, 20%, 30% because we don't know. What I do know is that we're resilient and having lived through a crisis for the past 18 months, I think it puts us in a good position to actually bolster the Company, ready for adjustments in a crisis and being agile.

**Mark Neville:**

Okay. Again, I'll ask a similar type question but I might get a similar type answer. Just around the margin, you had 6% in Q1. If I'm understanding it correctly, maybe you were a little slower to react on the cost side when the revenue dropped, but you've taken pretty swift action across the business now, so just, again, sort of would the anticipation be—again, sort of near-term from here, there's more margin degradation in the near term, or, again, confident that you can always offset and maybe keep it flattish, or you can grow it from here, near term?

**Jeff Bell:**

Why don't I—Ian, why don't I make an observation? I mean I think what Ian has been rightly signalling is that what we're seeing is a slowdown, in a sense, volumetrically. In terms of the gross margin percentages that we're realizing on projects, that's continuing to be strong, but I think if you then look at the operating costs, the actions we took early on at the end of March to try and rightsize and build some flexibility into our cost base in order to ensure that we had flexibility around varying levels of business, that helps.

Now, as you do that, you're always running a bit behind, but I think we've generally tried to get to a good point on that, but clearly the operating cost base is always a bit more fixed than the gross margin delivery, so you can end up with a bit of leakage that way.

**Mark Neville:**

Okay. Maybe onto the Resources, the actions to read on the cost structure, is this really just come down to people? I'm just curious if there was any significant costs that you might incur to bring down that, to rightsize that?

**Ian Edwards:**

Yes. I think primarily it's people, but it's also geography and business lines. I mean, we're looking at all the separate geographies that we've got business in and we're looking at discrete businesses within the overall business because there's mining businesses, there's oil and gas businesses, there's engineering businesses, there's operations, maintenance, support, sustaining capital, so we're looking across the whole business and we're looking at what is the backlog on-hand? What is the ability to win good work in this environment? Where we don't see that coming back at all, we will take very decisive action. Where we see there's an imbalance between the amount of revenue and the cost, we will take action. The intent is obviously to get this business into at least a breakeven position as soon as we possibly can outside of the LSTK, and the LSTK is all about running those off, managing the risk and fulfilling our obligations to the customers.

**Mark Neville:**

Okay. Then maybe just on the Resource Service business, appreciate it could be a good business, and again, I understand that you're still bidding work. I guess maybe the naïve question would be why, if it's such at this point? Would the ultimate objective—if you're still bidding work and if you rightsize it, presumably it would be fairly small. Would the ultimate objective be to eventually divest it, or potentially if you do rightsize it, keep it?

**Ian Edwards:**

Well, I think all of that. I know that's not a helpful answer but the overriding objective is to have a business which operates at a complementary performance level to the rest of our business from a profitability and a cash flow perspective, but that's the objective. If we can't get there, if we can't get there it doesn't belong as part of our future, and that's how we're looking at it.

**Mark Neville:**

Okay. Then maybe just one last question. Jeff, you made some comments, I think in response to Max's question, just around working capital. I missed it. I wasn't sure if you were giving sort of colour on what the working capital looks like in the next couple of quarters. I just sort of missed what you said. Maybe just if you could repeat it?

**Jeff Bell:**

Yes, happy to. The comments that we made was when you look at operating cash flow that we said the projects part of the business would be a cash drain through 2020 at an operating cash flow level, although over the life of the projects would be neutral to positive, but we did see a cash drain here in 2020. We had originally said back at the end of February that for the overall company we saw that being weighted to the back end of the year with a use of cash in the first half of the year, so I think our observation is the initiatives and the actions we took in Q1 have been positive overall.

I think my additional colour to that thought is it's hard to predict in the current environment as we're still seeing what level of business we're receiving and how COVID is impacting that, and while a number



of—while a lot of the working capital improvement or the operating cash flow improvement was related to working capital and nonworking capital elements on the balance sheet, some of which we'll retain, some of it is also timing and we'll naturally expect to reverse over the next quarter or two.

**Mark Neville:**

Negative for the year, or is it—because you're already, I think it's was negative \$150 million in Q1, so I'm just—I'm not sure. It's negative for the year, or sort of negative for the remainder of the year?

**Jeff Bell:**

Sorry, for projects.

**Mark Neville:**

Yes.

**Jeff Bell:**

Yes, in a sense I don't think our view has changed.

**Mark Neville:**

Okay.

**Jeff Bell:**

We had indicated that we would be negative over the year for projects, so I don't expect that to change.

**Mark Neville:**

Okay, great. Thank you. I'll get back in queue. Thanks, guys.

**Jeff Bell:**

No worries.

**Operator:**

This concludes time allocated for the question-and-answer session. I would like to turn the conference back over to Denis Jasmin for any closing remarks.

**Denis Jasmin:**

Thank you very much everyone for joining us today. I know there's some that were still in the queue but we actually have to move to our virtual AGM right away, but I'm always available to answer any questions, so don't hesitate to call me if you have any further questions.

Thank you very much everyone. Have a good day and stay safe. Bye bye.

**Ian Edwards:**

Thank you. Thank you. Stay safe, thank you.

**Operator:**

This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.