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SNC Lavalin Second Quarter 2020 Earnings Conference Call Transcript

Date: Friday, July 31st, 2020

Time: 8:30 AM ET

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

Jeff Bell
Executive Vice-President and Chief Financial Officer

Denis Jasmin
Vice-President, Investor Relations



Operator:

Thank you for standing by. This is the conference operator. Good morning, and welcome to SNC-Lavalin's Second 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 an 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.

I hope you have all been keeping safe over the past few months. We appreciate you taking the time to listen in today.

Our Q2 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 its transcript 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.



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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 participate. 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.

Also during the call, we may refer to certain non-IFRS measures. These measures are defined and reconciled with comparable IFRS measures in our MD&A, which can be found on SEDAR and our website. Management believes that these non-IFRS measures provide additional insight into the Company's financial results and certain investors may use this information to evaluate the Company's performance from period to period.

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're well and managing safely through the current situation.

Please turn to Slide 5.

You'll have seen this morning we announced a transformation plan for the Resources Services. I'm pleased to say we have concluded both the review of all options and finalized the business plan for its transformation and restructure. We've already moved to enter the implementation of this plan but I expect to see the Resources as a profitable services offering complementing our Engineering Service capabilities in primary markets. I'll cover more about this later.



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SNCL Engineering Services has been resilient through COVID-19 and delivered strong results and cash flow from operations; however, SNCL projects has been impacted by COVID-19, resulting in losses. While no one quite knows what to expect as lockdown started, we quickly took action to transition to remote working and adjust our cost base. Our decisive actions underpinned by the strategic direction we launched a year ago, have seen the business we're taking forward well positioned both for resilience in the pandemic and for growth in the future. Our SNCL Engineering Services business has a broad business mix and the essential nature of our long-term contracts, particularly with governments, make this business resilient.

For SNCL projects, we continue to reduce our LSTK backlog and the Resources LSTKs remain on track to be largely completed by the end of the year. This gives us great visibility as we enter the final phases of the projects. COVID-19 did impact negatively on our SNCL projects with resulting project reforecast. In addition, we adjusted for approximately \$70 million on our Resources LSTK project, where we've had ongoing warranty and claims disputes that have escalated in the quarter and COVID has impacted our ability to mobilize resources to site, rectify issues and negotiate a satisfactory conclusion. We do not consider this to be representative of the general performance of the LSTK rundown. Our financial position is strong, generating \$130 million of operating cash flow in the quarter, with total cash on the balance sheet of \$1.6 billion, and a low debt level.

Turning to Slide 6 and our plan for the transformation of the Resources business. This has been a priority since I took over as CEO a year ago. At the time I said we would explore all options with regard to this business and, as such, we undertook a strategic review to thoroughly assess the most effective path to deal with this underperforming business. This review was extensive and took into account both the shift in the oil industry and COVID-19. We now have a comprehensive plan in place to transform and restructure the Resources business.

Our conclusion is that the best return for the long-term shareholders is to transform and reposition Resources as a services offering that complements our engineering capabilities in primary markets with clients where we have a track record of executing profitable work. This means we will focus on markets in the Americas and Middle East, where we can work together with our other Professional Services and



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Project Management businesses. We will wind down all of the geographies through closures and sales. We have recently agreed to the sale of South Africa Resources business with 1,800 employees and a divestment of our European fertilizer business. This follows the closure in March of Valerus in the U.S. Revenues for the transformed services business are expected to represent circa 10% of the overall Company's 2021 revenues. This contrasts 23% in 2019.

Turning to Slide 7, you can see some of the projections for transitioning the Resources Services offering to profitability. We expect the business to breakeven in the first half of '21 and turn to a profit for that year. This forecast is based on a number of elements, including a rigorous approach to project selection with strong opportunities for new business wins, a significant reduction in overhead costs and deep relationship with specific international oil companies and national oil companies in our primary markets.

On Slide 8, we'll look at our progress on the LSTK backlog, a key milestone in our future success. Firstly, on backlog, we are on track to complete most of the Resources LSTKs by the end of the year. On the right-hand graph, you can see a significant increase in Q2 losses over recent quarters. This was due to taking a \$70 million charge on a completed project in the Middle East, as noted earlier. We don't see this representative of current performance and we have much clearer line of sight on all outstanding completion risk. We would highlight, however, there are still uncertainties around COVID impacts.

Turning to Slide 9, we've recorded a \$19 million loss in Infrastructure as projects have been affected by postponement, suspension and productivity losses. Even with the impacts of COVID-19 in the last quarter, you can see over a 12-month period we've actually achieved a slight positive segment EBIT on these projects. For the Infrastructure projects, we expect that these will be cash flow positive over the remaining project life, as these continue to phase out. We remain on track to complete this infrastructure backlog in 2024.

Turning to Slide 10, the performance of SNCL Engineering Services was strong, with a solid segment adjusted EBIT margin compared to Q2 2019, and only a modest revenue decrease in what was an



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unprecedented quarter. The resilience in Engineering Services is seen through Nuclear, EDPM and Infrastructure Services. It's largely due to the strong weighting to government work, long-term contracts and uninterrupted services for essential operation and maintenance activities.

Please turn to Slide 11.

The resilience of EDPM and COVID-19 is a key element in this quarter's results. COVID impact is primary in the Middle East and specific business lines, such as aviation and commercial buildings; however, through quick mitigation actions, EDPM has performed well. In March, we were able to quickly transition to remote working with little impact on productivity. We've continued to invest in our digital future, which is driven by EDPM, but central to the whole Company as we transform. Business winning has continued across all geographies and we have a clear line of sight through 2020. Strong relationships with governments have seen supporting efforts around COVID-19 and we're seeing opportunities in the U.K., U.S. and Canada for innovative and digital solutions as countries make investment plans for COVID-19 recovery.

Please turn to Slide 12.

The portfolio of nuclear services that we offer, combined with cost controls, has delivered target EBIT margins despite some projects being slowed by COVID-19. The level of new contracts and long-term nuclear contracts gives us firm belief and visibility in Nuclear's continued strength. Our Nuclear business has been strong and winning business in all core geographies and across a breadth of markets, such as nuclear technology and decontamination and decommissioning.

Moving to Slide 13, our Infrastructure Services business also proved resilient through COVID-19, with many essential O&M and services contracts operating as normal. The Government of Canada awarded us the scope to provide 100-bed mobile care units to be deployed across the country to our Flexibility to Healthcare System. We've won an award to provide services to refurbish and expand the hydrogenerating station in Ontario. And as an example of another innovative solution through collaboration with teams across the world, we identified and developed our ASRI concept, Accelerating



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Shovel-ready Infrastructure, to help governments expedite post-COVID infrastructure investments. We're in positive discussions with a number of governments on how we can bring our expertise as a project integrator and drive rapid, collaborative developments using ASRI.

Turning to Slide 14, 407 ETR announced earlier this month that it was seeing modest but steady improvements in traffic volumes. We continue to strongly believe in the long-term value of Highway 407 ETR. Our other concessions saw minimal impact from COVID-19.

On Slide 15, I want to take a minute and highlight the release of our 2019 Sustainability Report and our goals here. To align with our business strategy we're focused on three UN Sustainability Development Goals as priorities: affordable and clean energy; sustainable cities and communities; and climate action. I'd invite you to read more on these in our Sustainability Report on our website. Across environmental, social and governance elements, we have plans aligned to the UN goals and good performance in terms of ESG. Safety and integrity are our core values and we have active programs addressing diversity and inclusion across our business.

So I'd like to move to Slide 16 and conclude my remarks before Jeff takes you through more detail on the Q2 numbers.

We are a year into our transformation journey and I'm extremely proud of the achievements we have made as a company through this period. As a leading global professional services and project management company, SNC Lavalin is strongly positioned to meet and deliver growing demands for engineering services in the post-COVID stimulus, particularly in innovative solutions for infrastructure. In Q2 we performed well on Engineering Services, continue to strengthen our position and announce our plans for the Resources business. I'm disappointed to have the loss in LSTK, but we have continued to progress the backlog down and the Resource LSTKs are in the final quarters. I'm really excited about our future.

And with that, I'll pass to Jeff. Thank you.



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Jeff Bell:

Thank you, Ian, and good morning everyone.

Before I begin, just a quick note on our financial presentation. As you may have seen, effective from the second quarter, we are now presenting the financial results of capital outside of SNCL Engineering Services. Capital is a core part of our business and this is only a reclassification and does not require any restatements. We believe that presenting it this way makes it simpler and clearer.

Now let's turn to Slide 18, where I will summarize the second quarter results.

The Company reported an IFRS net loss attributable to SNC Lavalin shareholders of \$112 million, or \$0.64 per diluted share in Q2 2020, compared with a net loss of \$2.1 billion, or \$12.07 per diluted share for the corresponding period in 2019. Q2 2019 included significant non-cash goodwill impairment charges related to the Company's Resources segment and unfavourable reforecast on certain LSTK construction projects.

The Q2 2020 net loss includes restructuring costs of \$47 million after taxes, mainly related to the Resources Services transformation and EDPM. Resizing the Resources business will result in expected one-time restructuring costs in 2020 of \$50 million to \$60 million, with \$30 million of this restructuring charge incurred in the second quarter.

The adjusted net loss from PS & PM in Q2 2020 amounted to \$38 million, or \$0.22 per diluted share, compared with an adjusted net loss of \$300 million, or \$1.71 per diluted share in the corresponding period in 2019.

The Company continues to have a strong financial position. At the end of June, we had \$1.6 billion of cash on hand, and an additional \$1.5 billion available to be drawn on the revolver credit facility.



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At the end of June, 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 1 times, well below the required covenant level of 3.75 times.

At a sector level, if you turn to Slide 19, you will see a breakdown of SNCL Engineering Services. As I've indicated, the SNCL Engineering Services business has been resilient through COVID-19, with \$1.5 billion of revenues in the quarter, a 2% revenue decrease compared to the prior period, and segment adjusted EBIT up 7.4% to \$133 million. The EDPM segment revenue decreased by 4%, mainly due to the combined impact of the COVID-19 pandemic across our region as clients deferred or cancelled projects in sectors such as aviation, education and commercial property, together with the impact of reduced infrastructure investment in the Middle East, driven by the fall in the oil price.

In North America, we had a continuation of the first quarter position where we saw lower FEMA related revenue in the U.S. compared with the prior period. EDPM segment adjusted EBIT was strong at \$79 million, an 8.4% margin, in line with our long-term target range and underpinned by long-term client relationships and a strong public sector focus, as well as early cost mitigation measures.

In Nuclear, segment revenues decreased by 8.5, mainly due to projects in Canada in 2019, which are now completed, and lower volume in the U.S., partially offset by higher activity in Europe. Infrastructure Services saw a 10.1% increase in segment revenue, which had increased scopes of work and additional services on existing operations within maintenance contracts. The Nuclear and Infrastructure Services segment, adjusted EBIT margins were also strong in the second quarter at 14% and 7.3%, respectively. These were mainly driven by cost control and lower overhead.

Now turning to Slide 20. The SNCL Engineering Services backlog is also demonstrating resilience through the unprecedented COVID-19 situation. Awards for the second quarter amounted to \$1.5 billion, representing a booking to revenue ratio of 1.01, demonstrating the Company's strength in winning work, even while working remotely. Backlog at the end of June totalled \$11 billion and was in line with the end of March 2020 and December 2019. EDPM had a backlog of \$2.7 billion at the end of



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June, up 2.8% compared to the end of March 2020, while the Nuclear backlog was at \$1 billion, and Infrastructure Services at \$7.3 billion.

Turning now to SNCL projects on Slide 21. In line with our LSTK exit strategy, revenues for Q2 2020 continued to decrease. Revenues fell by 35% to \$462 million, mainly due to the continuing backlog run-off of our major LSTK construction projects. Infrastructure EPC projects delivered a negative segment adjusted EBIT of \$19 million, compared to a loss of \$126 million in Q2 2019. This quarter loss was mainly due to forecast adjustment on some LSTK projects to reflect lower productivity caused by COVID-19. Resources recorded a negative segment adjusted EBIT of \$122 million, which was also due to lower productivity caused by COVID-19, but also due to the current underperforming Services business as cost reduction and restructuring activity driven by the new strategic direction announced this morning was still in an early stage during the quarter and by the \$70 million charge on an LSTK project I've described earlier.

Turning to Slide 22, the decrease in the Capital segment adjusted EBIT was due to our investment Highway 407ETR, which did not pay any dividends in the second quarter as toll revenues have significantly decreased since the beginning of the COVID-19 pandemic. We're seeing improvements in traffic volume as Ontario continues to progress with reopening businesses and easing restrictions across the GTA. For example, the traffic level during the recent July week was 47% lower compared to the same week last year, compared to a decrease of 67% during the second quarter when compared to Q2 2019. We believe these are exceptional circumstances and with 78 years remaining on the concession, continue to strongly believe in its long-term value.

Moving on to Slide 23. Cash flows from operating activities have significantly improved in the quarter totalling \$130 million in Q2 2020, compared to a use of cash of \$368 million in the same period last year. It should be noted that Q2 2020 benefited from temporary positive working capital from certain projects and also included about \$100 million of benefit from COVID-19 government payment terms and sales tax deferrals, which will reverse in the coming quarters. Taking this into account as well as the announced restructuring charges, second half operating cash flow is unlikely to be as strong as the first half. SNCL Engineering Services generated cash flow from operations of \$222 million, a \$177



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million increase compared to the prior year from strong EBIT conversion in working capital positions. SNCL projects had a significant improvement compared to Q2 2019, but continued to consume cash with a cash outflow from operations of \$51 million.

And finally, on Slide 24, as the scale and economic impact of the business from COVID-19 becomes clear and the resiliency of the Company's businesses are supplemented by management actions, it gives us confidence to give a level of outlook for SNCL Engineering Services for the remainder of 2020. The Company expects that SNCL Engineering Services revenue for the second half of 2020 should decrease by a low to mid single-digit percentage compared to the second half of 2019 and that its segment adjusted EBIT margin should be between 8% and 10%. We are also keeping our long-term EBIT margin targets for each segment composing this business line.

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

Operator:

Thank you. 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. We will pause for a moment as callers join the queue.

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

Yuri Lynk:

Hey, good morning guys.

Ian Edwards:

Good morning.

Yuri Lynk:



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I'm wondering if you could put a little more colour on the back half of the year guidance for the Engineering Services business. At the midpoint it kind of points to a 15% to 20% decline in H2 EBIT versus 2019, so what's driving that after a pretty good start to the year?

Ian Edwards:

Yes, thanks for the question. So, overall, on the year, as we said in our guidance, in our outlook, we're already, for SNCL Engineering Services, is down about—between low single-digit, mid single-digits, and on the whole year, we felt that the—we feel that the business is actually performing very well. Now, the overview to kind of the fact that we have is mainly driven from the Middle East and specific aviation and commercial property impact, and we're seeing that occur through Q2 and we've taken the appropriate kind of cost-out measures to ensure that that reduction in revenue in our specific lines of business are out permanently as we go through H2.

So, we maintained our EBIT percentage profitability in certainly all of the business lines that we've got in Engineering Services. And can I just ask, your question was specifically around Engineering Services, right?

Yuri Lynk:

Yes, because the margin guidance is materially lower than what you had in the back half of '19 for that segment.

Jeff Bell:

And maybe, Ian, might I comment to that? It's Jeff. So what I'd say, as you heard in my remarks, obviously quarter-on-quarter the percentage EBIT margin does move around. As we indicated at the end of February and we've re-indicated today, our long-term EBIT percentage margins in SNCL Engineering Services overall we've said is 8% to 10%, and in fact that was also what we said with respect to EDPM, and therefore, what we're giving as outlook today is that EDPM would remain in the back half of the year in that 8% to 10% range. Now sort of quarter-on-quarter, that may move around in that range, obviously. And you're right, in 2019 it was a particularly strong EBIT percentage margin in the back half of the year. I think as you've heard from me and in some of my remarks, the impact on



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EDPM going forward where we've seen reductions in revenue in the Middle East and in some of those business lines, like aviation or commercial development, will continue and expect to continue to see that in the second half of the year.

So even with the cost actions we've taken, we'll see some reduction in overall gross margin but we've taken, we think, the right actions to adjust the cost base to be able preserve the EBIT margin percentage on the bottom line.

Yuri Lynk:

Okay, that makes sense. Just want to switch to the new services business within Resources, how you're planning on moving ahead with that. Ian, can you give us a flavour of the exposure to that business between mining and oil and gas on the Services side. And not that long ago SNC was a top three player in mining engineering. I mean, how much of that platform is left and do you think you'll be able to participate in the current gold tape (phonetic 26:27) that we're seeing recover here.

Ian Edwards:

Yes. I mean, I think—so what we're transitioning to here is something that is complementary to the rest of the businesses that we're taking forward into the future. So, under SNCL Engineering Services, clearly, what we're taking into the future is Professional Services and Project Management. So, we looked hard at the Resources business that we have and the geographies that we're present in and we obviously looked for where have we got a long-term track record of profitability in Services work, and in the end the plan really revolves around clients, specific clients, both national government clients and international clients, private clients.

So, I mean, to your specific comment on mining, we've really centred it around specific clients in Peru, Brazil, Canada and those are really forming part of the basis moving forward, and the oil and gas part of this business is, again, it's centred around clients in the Middle East, the kind of national clients in the Middle East that we've worked with for a long time that has been profitable and specific clients in the U.S. and Canada.



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So, and what we expect from this business as we move it forward is a reduced exposure to the sector. I mean, it wasn't that long ago that Resources formed 30% of the revenues of the Company and we're targeting 21%, for this to be about 10% of business, but obviously, no LSTK in the business, Professional Services, longer term kind of projects and frame agreements with specific clients.

Does that...

Yuri Lynk:

Yes, no, that's...

Ian Edwards:

Does that help the question?

Yuri Lynk:

Yes. Thanks. I'd better turn it over there. Thank you.

Jeff Bell:

Thank you.

Operator:

Our next question comes from Jacob Bout of CIBC. Please go ahead.

Jacob Bout:

Good morning.

Ian Edwards:

Good morning.

Jacob Bout:



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First question here just going back to the Resource business. So you announced the sale of the South Africa Resources business. Any other parts of the business could actually be sold or should we just be thinking about this as a winddown?

Ian Edwards:

Yes. So the key here, I think, is that we want to—obviously, we want to transition to profitability quickly and we want to get a—maintaining control of destiny, so to speak. So, we have over the year been looking at divesting parts and successfully, as you rightly referenced, divested the South Africa business. We also recently divested a fertilizer business from Europe. It's likely as we move forward that the majority of the exit will be closures and exits from countries, but if on the journey through the rest of this year and into the very early part of next year, if we can divest more, then we will. The important thing for us is to simplify the business, get the overhead down, concentrate on these clients that we've got a long track record with and get the business back to profitability.

Jacob Bout:

In your mind, what's the potential for future write-downs as you move through this process?

Ian Edwards:

In the Services business, I think we've been pretty specific in the presentation and the press release of what we expect the range of losses going through the rest of this year and the restructuring charges.

Jeff, if you just want to recap on those, perhaps?

Jeff Bell:

Yes. I mean, we indicated that as we transform and restructure the business on the services part of the Resources segment we'd expect losses, quarterly losses of \$15 million to \$25 million, but as we've indicated, by the time we get into the beginning of next year we'd expect to be at a breakeven level to begin with and then moving into profitability.

Jacob Bout:



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Okay. On the Highway 407 you talked about some of the improvements in volumes. What is the messaging from the 407 been around the dividend?

Jeff Bell:

Yes. I mean, I think what we'd say, and 407 talked to this I think yesterday or recently in their announcement, traffic volumes are still down but clearly improving from where they were in the second quarter, but I think the 407 decisions around dividends in the future will undoubtedly be related to how they see traffic volumes continuing to improve or not. I think we'll all just have to wait and see. It's clearly an asset that has 78 years to go, a concession with 78 years to go and we continue to think over that period it's a highly valuable and attractive asset. So we take that view but clearly in the short term we'll have to see what happens with traffic volumes, I think.

Jacob Bout:

But no talk around minimum baseload levels or anything like that?

Jeff Bell:

I don't think we could comment on any of that now.

Jacob Bout:

All right, I'll leave it there. Thank you.

Jeff Bell:

Thank you.

Operator:

Our next question comes from Devin Dodge of BMO Capital Markets. Please go ahead.

Devin Dodge:

Thanks. Good morning guys.



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Ian Edwards:

Good morning.

Devin Dodge:

Maybe just coming back to the Resources Services business, there's been a lot of good colour on the turnaround plan and when you expect to become profitable. I'm just wondering when you think about this business, what margins do you think this business should be able to achieve once all these actions are completed and over what kind of timeframe should we be expecting?

Ian Edwards:

So, I mean, clearly, our first priority is to get this business to profitability and that the key to getting it to profitability is, as I said, it's a reduction of overhead, which I think we've kind of articulated through the presentation, that that's absolutely one key. The second is to simplify the business and get it focused on specific clients and specific geographies and exit other geographies and close down other parts of the business.

So that's our focus, and that's our focus through the rest of this year and into '21. We're not going to give kind of guidance beyond '21 yet, but clearly at the right time we will do.

Devin Dodge:

Okay, fair enough. Maybe switching to EDPM. The backlog looked like it held up I'd say quite a while in Q2. Just trying to get a sense, what are you seeing in terms of RFP or bid activity in EDPM and how did it progress in the quarter? (Multiple speakers)...

Ian Edwards:

Yes.

Devin Dodge:

... trends, either positive or negative that are standing right now?



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Ian Edwards:

Yes, that's a good question. I mean, obviously, when we entered into the COVID crisis, we did a lot of simulation and covid analysis and in actual fact we were obviously really concerned about how strong the backlog would hold up and as we went into Q2 and worked our way through Q2 a pattern emerged that was really centred around the Middle East and we took the relevant kind of adjustment to the cost base in the Middle East because we felt that was permanent. And we saw the business lines globally, such as aviation and to some extent commercial property, get adjusted and we also took some permanent adjustments where we felt that the revenues wouldn't come back. But apart from that, and I think what's strong about our EDPM business is that it really is centred around transport and specifically the transport with governments where we've not seen revenue adjustments so much from the transport sector and government.

So we feel pretty strong about this year and we feel pretty strong about our revenues going through to the end of the year based on what we see now and based on kind of what we have experienced through COVID and would expect to experience in the next couple of quarters. Beyond that, I think it's a bit early to say. I mean, what might be the effects beyond that I think we need to observe and monitor pretty closely.

Devin Dodge:

That's good colour. I'll leave it there. Thank you.

Ian Edwards:

Okay. Thank you.

Operator:

Our next question comes from Michael Tupholme of TD Newcrest. Please go ahead.

Michael Tupholme:

Thank you very much. Just in terms of the outlook, the suggestion that in the second half of the year you expect low to mid single-digit percentage revenue declines for all of SNCL Engineering Services.



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Are you able to be a little bit more specific just in terms of the various, the three segments that make up that business line? Are those declines expected to be across all three or is it more concentrated in one or two areas?

Ian Edwards:

Yes. Jeff, do you want to pick that up?

Jeff Bell:

Yes. I mean, I think we'll leave—clearly, we've made the guidance at an SNC Engineering Services level. There will clearly be movement and differences within the areas underneath it. I think our observation is that in areas like infra services where it has large operations and maintenance and nuclear where there's a lot of essential services, we'd probably see revenue there potentially towards the low end of the range, probably see an EDPM where it's more of a consulting service, engineering services business, maybe towards the higher end of that range. But to be perfectly frank, there's a lot of road still to run on this and while we have good visibility into the backlog, which gives us the confidence to give the guidance that we are, clearly, quarter-on-quarter, month-on-month we may see a bit of movement around that, but we don't expect it to be materially different.

Michael Tupholme:

Okay. And just...

Ian Edwards:

Probably just...

Michael Tupholme:

Sorry, go ahead.

Ian Edwards:

Sorry. Go ahead. No, no, you go ahead. What I was going to add, sorry, is just, I mean, our Engineering Services business hasn't really got like a comparable peer and because it's got EDPM



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Nuclear and Infra Services within it, so it's somewhat different because there's a lot of long-term contracts, reimbursable services contracts embedded in Nuclear and the Infra Services business. So, we felt that as a combination of the businesses that we're taking forward that they've been actually quite robust because it's got this mix of short-term and long-term contracts and primarily centred around government.

Michael Tupholme:

Okay, that's helpful. Thank you. Just in terms of the Resource Services transformation, are you able to provide a little bit more detail on what that ultimately looks like in terms of a business mix? I think you were asked earlier about oil and gas versus mining, but just from a mix perspective, either from an end market or a geographic perspective how you sort of envision that business looking once the transformation is complete. And then when you talked about an expectation of margins in that business that are consistent with other engineering services businesses, should we be thinking about this 8% to 10% range you've talked about for your SNCL Engineering Services business as an ultimate sort of objective or is there something different about what services and resources will look like at the end of the day?

Ian Edwards:

So, we're focused around the Middle East and the Americas, and you could say that there's a balance there between the Americas and the Middle East. And it really is about clients. I mean, the reason for that is clients' track record, performance in the past and relationships. So, if you think about the Middle East, I would say weighted towards kind of Saudi Arabia, the Emirates, with some kind of relationships in Qatar, Oman, Kuwait. And then in the Americas, we're really talking about specific clients in the U.S., specific clients in Canada, and specific clients in Brazil and Peru. I mean, that's basically it. It's very, very focused. It's very targeted around clients. And so the margin question—I think we kind of answered that that we're really, really focused on getting this business to profitability. Of course, we will drive this business to profitability equal to the peers in similar kind of business lines and space.

Michael Tupholme:



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Okay, that's helpful. And then as far as Infrastructure EPC, that segment had been generating profitability line for several quarters. It turned negative this quarter. Is that seen as sort of a one-off that's related to COVID, and if so, I mean, how do we think about this business sort of in the back half and into next year?

Ian Edwards:

So let me give you some specifics around that, because I think that is based around specifics. In Q2, we saw—I mean, we've got basically four live contracts in the main—one in Newfoundland, one in Montreal, and two in Ontario. What we saw in the quarter, as you probably have heard, is that certainly our projects in Newfoundland was suspended for a year. So the job is being postponed, so all the revenues and margins that were expected out of that have been deferred for a year. In Québec, the projects were suspended for seven weeks and restarted, but on the restart and through to the current situation, we're seeing productivity losses. And in Ontario, the projects continued, but we saw productivity losses.

So we assessed that these kind of productivity losses are between 10% and 15% and the reason for them is because on the physical work on site, you've got to implement social distancing and that has its effect in being able to kind of move materials around and move construction activities around. And in addition to that, there's considerably more hygiene breaks. So the way that we have executed those, and actually the way that the requirements are, is that we've got to provide more breaks for hygiene.

So the effects of all of that has obviously had an impact. Now, the contracts are not without some ability to recovery. So, the losses and all of that, the loss is our assessment of what we think is the outcome for Q2, Q3, of all of this kind of productivity and suspension impact, and we thought that it was prudent to take a charge on that as we understand how this develops past Q3 and beyond.

Michael Tupholme:

Okay, that's helpful. I'll turn it over. Thank you.

Operator:



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Our next question comes from Margo Tefanovic (phonetic 43:50) of Capital Markets. Please go ahead.

Mark Tuchonic:

Good morning folks. Mark Tuchonic (phonetic 43:55) here filling in for Chris Murray with ATB.

Ian Edwards:

Hey Mark. Good morning.

Mark Tuchonic:

Good morning guys. My question is around your cash balance. Is there cash that you show on the balance sheet right now that's actually tied up in joint ventures? In other words, cash that is not at your discretion to employ?

Jeff Bell:

Yes. So we do have cash on our balance sheet that's tied up. I mean, it's a natural part of running the projects. So there's about \$400 million of cash across our joint ventures and projects; about half of that is in the projects that Ian was just talking about. Our main ones are underway. But we naturally account for that and our share of that appropriately and it's included in, obviously, sort of how we think about our working capital movements as well.

Mark Tuchonic:

Okay, thanks. And should we expect that cash to go away somewhat once the lump sum turnkey projects are run off?

Jeff Bell:

Yes, I mean, to my point, about half of it's tied up in those four main infrastructure projects, so obviously as those wind down over the coming months and years, you would expect that sort of cash amount and that investment in cash in joint ventures to reduce as well. There will always be some element of that with our businesses there, but I would expect to be reduced over time.



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Mark Tuchonic:

Okay. Thanks a lot. That's it for me guys. Thanks.

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. So as you continue to focus on profitability there is a number of changes, restructuring, and I'm just wondering with the Resources transformation do you think you've kind of turned over every rock, or if there's a second or third wave from COVID are there any additional steps or levers that you may look to pull within the overall business?

Ian Edwards:

Yes, it's a good overall question. So I think the way we look at this is that we're trying to permanently transform the Company and when we set about this permanent transformation we obviously didn't factor in the COVID impact. But what we found is that the business that we are taking forward, which is SNCL Engineering Services, which currently has the EDPM Nuclear and Infra within it, being really robust in terms of COVID, and obviously, we feel that we made the right decisions a year ago. Now, we've finalized what we will do with the Resources business and that will ultimately join the family of Services business that create the future of the Company, which we believe will complement each other, and again, be reasonably robust to the environment that we see through COVID. And I don't—providing COVID today somewhat as it is now, which is clearly variable globally, then I think the performance of the three businesses will be pretty much in line with what we've talked about today. Now, obviously, if the world goes backwards to a complete lockdown again, ultimately, there may be some long-term impact from that, which we haven't predicted and not sure we could predict right now.



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And then the next job for us is to burn off our LSTK backlog. And we're very confident of our Canadian backlog, say for the comments that we made in the last question about the short-term impacts that we're experiencing on those projects, and then we have to get through the remaining Resources backlog, which has clearly been impacted in the Middle East as well as through COVID.

Mona Nazir:

Okay, that's very helpful. And just secondly, I'm wondering if you could speak specifically about Atkins. When you first purchased Atkins it was double-digit margins, there was over \$100 million of synergies. I know there's been some re-segmentation in combination with some legacy projects. I'm just wondering if you could speak about Atkins or should I take your overall EDPM commentary as that to Atkins as well?

Ian Edwards:

Yes, I think so. I mean, obviously, there were other business lines in Atkins that we redistributed into our Nuclear and our Resources, but in the main I think what you've described is correct. I mean, the body of Atkins is EDPM and that's continued to perform in line with and slightly even an improvement to the pre-acquisition phase.

Mona Nazir:

Okay, perfect. And just lastly for me, I'm just wondering if you're expecting any government aids, either further tax deferrals or any room on payment terms or even the emergency wage subsidy?

Ian Edwards:

Jeff, do you...

Jeff Bell:

Yes. Yes, no, I mean, I think, obviously, and I referenced this in some of our cash flow comments that we obviously will experience some timing benefit with respect to, for instance, deferral of U.K. VAT payments that U.K. government has put in place for businesses in the U.K. or some employment tax deferrals that the U.S. government has indicated in the second quarter that amounted to about \$100



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million against our operating cash flow, and obviously that will reverse in the coming quarters. To the extent that there's additional programs put in place, then we'll look to see if we qualify and if that helps us from—our business from a cash perspective we'll do that as well. From a government grant perspective, we have seen and been able to qualify for some of that in Canada and the U.S. as well. Although in reality, those payments have largely simply offset our ability to hold on to productive capacity within the organization that otherwise we would have had to put on temporary layoff or permanent layoff.

Mona Nazir:

Thank you. That's it for me.

Ian Edwards:

Thank you.

Operator:

Our next question comes from Sabahat Khan of RBC. Please go ahead.

Sabahat Khan:

Thanks and good morning. You provided some colour on your EDPM segment around some headwinds or some deferred projects in aviation, education and commercial. Can you maybe talk a little bit about geography, maybe what across Canada, the Americas whether these segments are also impacted or maybe the end market trends you're seeing across some of your larger markets outside of the Middle East?

Ian Edwards:

Yes. Yes, for sure. I mean, I think most things are holding up pretty well. Most geographies are holding up pretty well. As you know, we had some impact in Asia in Q1, which came back pretty strong, and we've got some new wins in Asia. So that came back quite quickly. We have about 20% of the revenues coming out of the U.S. That's actually holding up pretty well. The U.K. is doing okay. That's held up well. And Canada.



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So I think outside of the Middle East, and say for those kind of specific business lines that we've identified as aviation, commercial property, which are not kind of significant portions to our core geographies. I think it's all holding up quite well. And I would say, again, I think one of the key for us in EDPM is it's weighted towards government, so 75% of the work is with government, and a lot of it is in transport that we've seen continued commitment to transport from governments. So I think that's probably helping us. And our main kind of impact has been the Middle East, where, really projects have been cancelled and postponed and we've taken some permanent measures to readjust further in the year the scale of our business in the Middle East.

Sabahat Khan:

Great, thanks. And then on the Nuclear segment, I think it was mentioned earlier that the margins there could be a little bit on the lower end. I know there's obviously some headwinds in Ontario projects on the Nuclear side. But can you maybe comment around whether you're seeing any of these COVID related impacts on Nuclear projects outside of Canada? And then has there been any major pushed out projects or deferrals of the Nuclear pipeline that you're pursuing around the world? I just want to get an idea of how that business, kind of the outlook...

Ian Edwards:

Okay. Let me—let's do this together with Jeff. I mean, I want to give you kind of a bit of an overview first and I'll let Jeff go into some—maybe some more granular.

So, our core geographies for Nuclear are the U.S., Canada, the U.K., pretty much the same as the general business that we're kind of focused on. So in Canada, you're right. I mean, there was initially some deferment, particularly on our Darlington, and actually, that deferment was talked about going through to the end of the year, but it's come back again. So it's imminent. The restart there is imminent. So the impact too is kind of now defined.



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In the U.S., our businesses is a lot focused around decommissioning and remediation of nuclear waste, cleanup from nuclear waste. So we have seen some kind of suspension of some of those projects in the U.S., but the impact overall is not so great.

And then in the U.K., we're involved in a newbuild in Hinckley and we've also got services contracts to ongoing both waste and ongoing power generation. And the impact there is very, very small.

Now on top of all of that, we do have a services and technologies offering which is global and we've seen that pretty much continue and pretty much revenue's pretty flat.

So, I mean, with that, Jeff, I don't know if there's anything you want to add to that sort of specifics.

Jeff Bell:

Yes. Just wanted to clarify one element in there. You may have been referring where I said to the lower end of the range with respect to our revenue expectations within Engineering Services for the remainder of the year where we talked about low to mid single-digit. But that was a revenue comment. I don't think I made any comment about or we've made any comment about specifically Nuclear being at the lower end of the range of it, long-term target margins of 13% to 15%, and obviously in Q2 we were well within that. We were 14.5%, 14.6% in terms of the EBIT range. And as we indicated we'd expect the components of Engineering Services going forward to be within their ranges as well.

Sabahat Khan:

Good. Thanks for clarification. If I could just squeeze in one more. When we look at the transformation you announced this morning of the Resources segment, the nine markets that you're choosing to stay in, was this really, I guess, client driven or was it the type of work you're doing in some of them? When we look at markets like the Middle East, you're still looking to maintain a presence there. Just want to get an idea of the thought process around how you chose those nine...

Ian Edwards:



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Yes. Yes, very, very much around Professional Services and Project Management to specific clients. And that is in the business that we—you know, we've always had it in Resources is this—the frame agreements, long-term project management, design, consultancy, that we've offered for the kind of national oil companies in the Middle East, some of the international oil companies and also some of the national mining companies in South America. So it's actually profitable and it's a profitable part of the business and the gross margins are good, the work is consistent because it's based on long-term frame agreements, it's based on relationships. So the real core and essence of the strategy going forward is to focus on that in countries that are complementary to the overall SNCL Engineering Services business that we want to take forward.

And then also, it focuses back from a generic capability offering, if you like, to complementary skills and design and project management and consultancy, which is what we're driving out of all of the rest of the business - in EDPM, Infra Services and Nuclear. So it's all highly complementary and when we transition everything to the future offering in the Company and work our way through our LSTK backlog, all of these sectors - Nuclear, Infrastructure And Resources - will work together to offer our capabilities.

So it is very much around Project Management and Professional Services and specific clients.

Sabahat Khan:

Thank you.

Operator:

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

Frederic Bastien:

Thanks. My first question is on Infrastructure Services. We saw significant gains in Q2 with EBIT more than doubling. Can you provide a bit more colour on the performance, and I'm wondering is this all Linxon or was there other moving parts here?

Jeff Bell:



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Yes, why don't I take a—some initial comment on that. Part of it was Linxon. We're seeing, particularly compared to last year, we're seeing revenue growth, we're seeing growth in profit falling through as that business sort of gains scale and continues to leverage the pipeline that it has. I'd say also at the same time, as you heard Ian say, we've continued over the last year to supplement the operations and maintenance business with new contracts and the performance on those, which is primarily related to availability, has held up really well in terms of COVID-19 and the backdrop of the environment that we see there.

So, we've seen improved profitability on both sides there, which has been good to see.

Frederic Bastien:

Okay, thanks. And then I don't want to beat a dead horse, but can I ask why it took you a year to arrive at what seems to be a very—probably wasn't a straightforward conclusion on the Resources side. But just wondering if anything changed from the moment you started looking at it or did COVID have a big impact on your overall decision?

Ian Edwards:

No, I don't think COVID has. I mean, I think the challenge if we go back a year is that we were—at that time obviously we had \$600 million of LSTK to work our way through. We had other geographies and businesses even in services that were not profitable that we had to work our way through and embedded in the midst of all of this were some profitable long-term relationships. I think we also spent quite a lot of time looking at what the options were from part divestment, whole divestment, closure of the whole business to concluding what is the best long-term plan for value creation within this business and we felt that now is the right time to conclude on that. We've got an end in sight to the LSTK. We've been existing non-profitable business and geographies through the last year. We're well on with the plan and we can see an end in sight to the transition to profitability. I think if we kind of concluded earlier than this, I think the task in getting to the end point would have been less definable, should I say. I mean, we're feeling really comfortable that we can actually get to where we've said we're going to get to and we've got our arms around this business and we can see the Resources LSTK burning off.



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Because it's not—some of the overhead embedded in this business also supports the LSTK, which obviously by the early part of next year we're out of and all of that comes out as well.

So, I think it's the right time to define our commitment for the future and I'm really pleased with the plan that we've come up with and I think it's the right thing to complement the rest of the business going forward.

Frederic Bastien:

Thanks, Ian, that's great colour. Thank you.

Operator:

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

Denis Jasmin:

Thank you everyone for joining the call. I know there's many of you still in the queue but unfortunately we're running out of time. We'd be more than pleased to answer any of your questions. Please don't hesitate to contact me.

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

Ian Edwards:

Yes, thank you all.

Jeff Bell:

Thank you.

Operator:

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



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