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SNC-Lavalin Second Quarter 2021 Earnings Conference Call Transcript

Date: **Friday, July 30th, 2021**

Time: **8:30 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 Second Quarter 2021 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.

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

Denis Jasmin:
Good morning, everyone, and we appreciate you joining the call.

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.

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:
Thank you, Denis, and good morning, everyone.

Starting on Slide 4, we're pleased to have delivered a strong second quarter, and, combined with the first quarter's performance, have reported solid results for the first half of 2021, and we remain on track to meet our 2021 outlook.

SNCL Engineering Services delivered another robust performance, with Segment Adjusted EBIT growth and strong profitability across all three segments. Our LSTK projects continued to progress well, and discussions with our clients on compensation for the additional costs related to COVID-19 impacts have been constructive.

Also, to date, we've announced the substantial close of the sale of our oil and gas business. This represents an important strategic milestone for the Company.

Quarterly performance was driven primarily by Engineering Services, which generated revenues of $1.5 billion, an increase of 2.4% on Q2 last year. Excluding the impacts of foreign currency, we saw robust organic growth of 6.8%. Segment Adjusted EBIT increased 9.5%, resulting in an Adjusted EBIT margin of 9.6%.

Backlog also remains robust at $11.1 billion, with $1.5 billion in new bookings in the quarter, up 1.1% over the prior year. In SNCL Projects, the LSTK contracts backlog reduced by approximately $200 million, bringing the remaining backlog down to $1.4 billion.

In summary, having delivered a solid second quarter, our first half ’21 performance shows that our strategic initiatives to transform this Company are generating results.

Now, let me share with you the progress we’ve been making in each of our strategic initiatives, and I’m on Slide 5.

First, as I mentioned before, we’ve achieved the substantial close of the oil and gas business, a significant step forward in our transformation. The transaction has received all regulatory approvals, except for one jurisdiction, Saudi Arabia, which is expected towards the end of Q3.

Secondly, we have been successfully running off the LSTK projects, where the backlog has fallen from $3.4 billion in June ’19 to just $1.4 billion in June ’21, over 58%, since we launched our transformation plan.

Third is driving consistent financial performance within Engineering Services. In the first half of this year, revenue has grown year-on-year, EBIT margins are in the upper half of our target levels, operating cash flow was $275 million, and we see a robust pipeline that gives us confidence in the continued performance going forward.

Fourth, we are focused on building a connected, collaborative organization. We see significant opportunity to leverage our capabilities and product offerings more broadly across our core markets. Our world-class Global Technology Centre in India and growing digital capabilities allow us to deliver for our customers across all time zones and geographies, while providing an attractive set of professional development opportunities to retain our employees and attract new talent.

Finally, we continue to transform and align SNC-Lavalin with two fundamental growth trends, where we have clear capabilities and a compelling value proposition. One is climate change and the other is digital transformation.

On climate change, governments around the world, including Canada, are increasingly enacting regulations around achieving net zero carbon. We are well positioned to be a leader in engineering a sustainable society with our Engineering Net Zero initiative and providing clean and affordable solutions to our clients. As governments in our core geographies continue to prioritize infrastructure spending, we see significant opportunity for SNC-Lavalin in the months and years ahead.

With respect to our digital transformation, we continue to leverage our digital expertise and invest in further fortifying our capabilities in this space. Digital is an enabler for all we do and a way to differentiate our core services, and it focuses on design transformation, program management, digital twinning, and provides the infrastructure and services required for a globally connected and data-driven engineering business.

Turning to Slide 6, and an update on our sustainability strategy, we have proactively positioned ourselves to be a leader in engineering a sustainable society and we have been growing our portfolio work in this area. A great example of this is our recent award from the U.K. government, where we will be ensuring that over 4 million square feet of public sector office space meets enhanced sustainability standards, as part of a U.K. government investment to accelerate its net zero agenda. In May, we also communicated our goal of being net zero carbon by 2030.

Next, I'd like to move on to our business lines, starting with Slide 7, and the results for EDPM. EDPM generated revenues of $935 million, broadly flat to the same quarter last year. However, excluding the impact of foreign exchange, revenue growth was up 5.3%, driven by strength in our U.K., Middle East and U.S. businesses. Segment Adjusted EBIT of $85 million increased 8.5%, resulting in a 9.1% EBIT margin. Backlog grew 12% to just over $3 billion, a record high for EDPM, driven by major wins in the U.K., Middle East and Australia, where we recently logged a major award supporting the Sydney Metro

Project. We see this as a key step to realizing our growth ambitions in Australia. Additional awards included rail, road, transportation and solar projects, and looking ahead, the pipeline remains strong at $27 billion.

Turning to Slide 8, the Nuclear segment increased 6.1% on a reported basis, and 9.6% on a constant currency basis. Growth was driven by increased support of assets for North American and European clients. Canada showed particular strength, as we saw increased demand for our Engineering and Field Services. Segment Adjusted EBIT of $33 million increased 7.5% over the prior year, resulting in 14.2% margin. Profit improvement was driven primarily across the U.S., Canada and Europe, partially offset by a reduction in Asia-Pacific.

We continue to see several significant opportunities and growth catalysts on the horizon. These include continued demand for reactor support, CANDU refurbishments and decommissioning, intensified tendering by the U.S. Department of Energy for environmental management work, as well as continued momentum in the U.K. We also see opportunities for new build work and decommissioning activities within Canada, the U.S. and the U.K. A key component to our continued success is our nuclear products and technology, which is a portfolio of physical, software and licensing rights for the nuclear reactor designs and operational support licences, as well as waste management reduction and process technologies. Our capabilities are differentiated and, in many cases, unique, enabling us to secure contracts, like the expansion for medical isotope extraction at our Oakridge facility.

Moving to Slide 9, and Infrastructure Services, this segment had a solid quarter, with revenues of $334 million, representing growth of 6.3%, compared to Q2 2020. On a constant currency basis, revenue increased by 9.2%, driven by increased levels of activity in Linxon, because of significant new orders in the U.S. and the EMERA region. Segment Adjusted EBIT of $26 million increased 15.8% and resulted in an EBIT margin of 7.9%.

We remain very optimistic about the numerous opportunities ahead, including growth in renewables, such as wind, solar, and hydro, as well as data centres, rail and transit, and social infrastructures in the Americas and Europe.

Turning to Slide 10, and Capital, this segment continued to be impacted by COVID restrictions in Ontario, which has resulted in reduced traffic volume on Highway 407 ETR. As a result, there was no dividend payment in the quarter. However, we do see increased volumes as a result of easing restrictions, that really started in earnest at the end of June, and we remain optimistic for increasing traffic volumes over the short to medium term, as more people return to offices. Our other concessions continue to perform well, and looking ahead, we are building a pipeline of new public/private partnership opportunities, where we can leverage our engineering and O&M capabilities. These include several PPPs in Canada and the U.K. in the sewage water treatment and hospital space.

Moving to Slide 11, and the Infrastructure EPC Projects, we continue to make good progress reducing the LSTK construction backlog. Comprising three Canadian LRT projects, this portfolio's backlog is down 45% versus a year ago and down 13% since the end of Q1. This segment recorded an Adjusted Segment EBIT loss for the quarter of $22 million, compared to a loss of $19 million a year ago.

We are also proactively monitoring potential macroeconomic challenges, including potential inflationary pressures on labour and materials, supply chain issues and labour constraints. While we have not seen any material impact on our LSTK projects so far, we are tracking these very closely.

Turning to Slide 12, and the Resources segment, we continue to target full completion of the sale of our oil and gas business by the end of Q3. Our Mining and Metal Services business is performing well. We are seeing growth in revenue and profitability, driven primarily by increased demand for the materials used in clean energy storage, including electric vehicles.

With that, I'll now turn the call over to Jeff.

Jeff Bell:
Thank you, Ian, and good morning, everyone.

Turning to Slide 14, total revenues for the quarter increased by 8% to $1.8 billion, compared to Q2 2020. SNCL Engineering Services revenue was higher by 2.4%, in line with our outlook range for the year. SNCL Projects revenue was higher by 62%, as the comparative period in 2020 was impacted by a temporary shutdown of some projects due to the initial wave of the COVID-19 pandemic and a client dispute in Resources.

Segment Adjusted EBIT for the quarter was $140 million, which was comprised of $145 million for SNCL Engineering Services, $16 million for Capital, and negative $21 million for SNCL Projects. This latter negative EBIT was mainly due to the Infrastructure EPC Projects segment, which had a loss in the quarter due to reduced gross margin, including the ongoing impacts of COVID-19 and close-out costs on certain projects.

Corporate SG&A expenses totaled $27 million in the quarter, in line with our expectations. On a year-to-date basis, corporate SG&A expenses totaled $43 million, lower than we expected, mainly due to a slower phase-in of our digital spending program, which we now expect to be weighted to the second half of the year.
The adjusted net income from PS&PMwas $54 million, or $0.31 per diluted share, representing a significant improvement compared with Q2 2020. Note that the effective income tax rate related to the adjusted PS and PM net income was higher this quarter at about 33%, compared to our normal range of 20% to 25%. This was mainly due to one-time adjustments related to the revised estimate on certain income tax liabilities and the impact of the enacted U.K. tax rate changes on deferred income tax balances.

Backlog ended the quarter at $13 billion, compared to $13.8 billion last year, primarily due to the continued run-off of the LSTK construction contracts backlog, which totaled $1.2 billion over that period.

SNCL Engineering Services backlog, on the other hand, increased by 1% during the same period, with an increase of 12% in the EDPM segment, totaling a record-high of $3 billion at the end of June 2021. In Nuclear, backlog decreased by 17% over the last 12 months, mainly due to the progress on the Company's long-term refurbishment contracts in Canada. As for Infrastructure Services, the backlog remains solid at $7.2 billion, in line with the end of June 2020, and continued client deliveries and strong contract wins over the last 12 months, particularly in Linxon.

Turning to Slide 15, and the balance sheet, our days sales outstanding continued to improve, reaching 58 days at the end of the quarter for EDPM, a 13-day improvement, as compared to Q2 2020. This improvement is mainly the result of our continued focus on cash collection and early government payment programs related to COVID-19. The strong operating cash flow attributes of SNCL Engineering Services are expected to be partially offset by a return to a more normalized DSO level in the second half of the year.

At the end of June 2021, the Company had $663 million in cash. The Company's net recourse debt to EBITDA ratio on the revolver credit facility, calculated in accordance with the terms of the Company's credit agreement, was 1.8 times, well below the required covenant level of 3.75 times.

Moving on to Slide 16, net cash generated from operating activities was $78 million in Q2 2021, compared to $130 million in Q2 2020.

SNCL Engineering Services continued to generate strong cash flow from operations, with $157 million in the quarter, due to strong EBIT conversion and a low DSO in the EDPM segment, while Capital generated $4 million. After cash taxes, interest and corporate items, you can see that we generated $102 million of operating cash flow in the quarter. SNCL Projects had an operating cash flow usage of $27 million, while discontinued operations contributed $3 million.

For 2021, we continue to expect the Company's operating cash flow to be largely breakeven as a result of a return to a more normal DSO profile in Engineering Services by the end of the year and the usage of cash in SNCL Projects.

Regarding capital allocation priorities, we are primarily focused on reinvesting in our core portfolio and we look forward to communicating more details on our capital allocation plans at the upcoming Investor Day.

Finally, turning to Slide 17, and our 2021 outlook, as it pertains to 2021 outlook, we are reaffirming our SNCL Engineering Services revenue expectation of low-single-digit percentage growth year-on-year, including the impact of a weaker U.S. dollar, and we are maintaining our SNCL Engineering Services Segment Adjusted EBIT margin outlook of 8% to 10%. We also continue to target the same long-term EBIT margin percentages for each segment.

This concludes my presentation, and I'll now hand back Ian.

Ian Edwards:
Thanks, Jeff.

Turning to Slide 19, I'd like to conclude my remarks with a few key takeaways.

We continue to execute on our transformation strategy, with a focus on two main priorities: to de-risk our portfolio and accelerate growth in Engineering Services. On our first priority, we continue to make consistent progress on unwinding the LSTK backlog, while the substantial close of the oil and business represents a significant strategic milestone in our transformation. On our second priority, we are seeing a strong pipeline of new business opportunities across all our core markets, as governments invest in new infrastructure and sustainability initiatives.

We are pleased with the strong performance of the first half of the year and we remain focused on executing our strategy. We look forward to sharing more about our vision for the future and our growth opportunities at our upcoming Investor Day in September.

Lastly, I'd like to thank all our employees around the world for their ingenuity and their continued dedication to the Company.

Thank you. I'll now open the call for questions.

Operator:
Thank you. We will now begin the question-and-answer session. We will pause for a moment as callers join the queue.

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

Jacob Bout:
Good morning.

Ian Edwards:
Good morning.

Jacob Bout:
The first question is just on your 8% to 10% margin guidance. If we look at what happened in the first half of the year, over 9%, and considering the seasonality, where second half margins are stronger than first half, is it more likely going to be at the higher end of that, or how should we be thinking about that?

Ian Edwards:
Yes, I mean, clearly, it's been a good first half of the year, we're pleased with the first half of the year, and from a specific profitability perspective, I think that's a fair takeaway. We're not about to change the

range, as we've reaffirmed in this quarter, but I think that's a fair takeaway, and clearly we're pushing as hard as we can to make sure we stay at that level and push to the higher end of the range.

Jacob Bout:

Then, how about your thoughts on discretionary SG&A increase in expenses, as employees head back to work, and labour costs increase?

Jeff Bell:

Yes, it's Jeff, Jacob, maybe I'll take that one. I think, as you saw, from a corporate SG&A expense perspective, a bit of saving, particularly around our digital transformation and spend program, so we do expect a bit more of that in the second half of the year than the first half of the year, but I think that's just phasing and expect, overall, the year to be in line with our expectations.

I think so far, more generally, we haven't seen a lot of labour inflation. Attrition has started to come back up, I would say, to more kind of pre-COVID levels, but, as I think you heard Ian say, we continue to think we've got a really attractive business and opportunity for employees to be a part of, and I think at this point that's absolutely turning out to be true from an attraction and retention perspective. We'll keep our eye closely on labour inflation and materials inflation, but so far all that's been manageable.

Jacob Bout:

That's my two. Thank you.

Ian Edwards:

Thanks, Jacob.

Operator:

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

Yuri Lynk:

Hey, good morning, guys.

Ian Edwards:

Good morning, Yuri.

Jeff Bell:

Good morning.

Yuri Lynk:

Ian, were you surprised by the delay in getting approval in Saudi Arabia for the sale of the oil and gas business?

Ian Edwards:

No, I don’t think surprised. I mean, obviously, these things are a process. We went through a process which needs certain specific submissions, which we’ve completed, but through the process of those submissions, there’s always a bit of to-ing and fro-ing and clarification and update, further information, but we’re at a point now where they’ve confirmed they’ve got all they need, so it’s really a question now of just process and getting the response. It’s not something we can really influence, I mean, it’s regulatory, it’s government process. So, pretty confident now, having answered all the questions, that we will see that within Q3. So, pretty confident that’s going to come through soon.

Yuri Lynk:

Okay, and this is just—in this to and fro, it’s just clarification issues. Are the terms of the sale agreement changing in any way?

Ian Edwards:

No, not at all, not at all. It’s literally, you know, regulatory bureaucracy, more documents, more clarification, that kind of thing, but I think the key point that I would make is they have confirmed they’ve

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got everything they need and they're satisfied with what they've got. So, like I said, we're confident we're at the right place, just got to wait now to get the response back.

Yuri Lynk:

Okay, and for my second question, I'd just like to switch to the Projects segment. When you talk about …

Ian Edwards:

Sorry, would you just speak up a little bit? Sorry.

Yuri Lynk:

Okay. Can you hear me better now?

Ian Edwards:

Yes, yes, much better. Yes, thank you.

Yuri Lynk:

Okay. When you talk about operating cash flow being breakeven for the year, does that anticipate any recapture of additional costs that you're talking about with your clients on COVID?

Jeff Bell:

Yuri, it's Jeff, why don't I take that one? I think within it, and you will have seen in my statement, that we are expecting, just the way DSO is within Engineering Services, some of that to start to normalize in the second half of the year. We are expecting to see continued cash usage in SNCL Projects and, therefore, we're not anticipating much in terms of additional monies back related to COVID. We've got a bit in there, but not a lot, and all of that is just recognizing that the discussions, which are constructive and are ongoing, often take time. If we can close those out before the end of the year, great, but if that needs to sort of fall into the beginning of next year, we've stayed that way.

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Yuri Lynk:

Okay. I'll turn it over. Thanks.

Ian Edwards:

Thank you.

Operator:

Our next question comes from Benoit Poirier of Desjardins Capital Markets. Please go ahead.

Benoit Poirier:

Yes, good morning, everyone.

Ian Edwards:

Good morning.

Benoit Poirier:

With respect to the Segment EBIT loss for SNCL Projects in the quarter, could you maybe provide more colour about what drove the costs for closing out certain projects and whether this is something we might see as you wind down the three other infrastructure projects?

Ian Edwards:

Yes, thanks, Benoit, for sure. I think the first point I'd make is Projects are going well. We've got some strong execution on these last three jobs in Canada. I mean, as you saw, the backlog for the Canadian projects is down to $1.3 billion, so a $200 million reduction in the quarter. So, I think you can appreciate that COVID is still affecting these three jobs. We've said in the past that productivity is affected on different activities, anything in the range of 15% to 25%, and, unfortunately, as the pandemic is still evident, that's still the case. We might see some inflation through labour and materials, we're not seeing that yet, there could be some post-pandemic.

So, I think the message I'm trying to send here is we're not through the pandemic yet. Obviously, we're very hopeful that in the fall, as soon as we go through Q3, Q4, everything's going to get back to normal and we're going to execute back to normal productivity levels. That's what we're expecting.

Specifically, the loss is really a combination of COVID and overhead. Obviously, we're carrying overhead to execute the closure of these three jobs, and, indeed, just tidying up everything else from the exited business line of LSTK. So, that's really where that comes from, Benoit.

Benoit Poirier:
Okay, and for my second question, looking at operating cash flow, you, Jeff, provided some great colour about the expectation for the second half, the normalized DSOs and also the use of cash for certain LSTK projects, but beyond 2021, could you talk a bit about the use of cash, whether it will reverse into positive territory for the remaining LSTK projects, how we should be thinking beyond 2021, with respect to the use of cash for LSTK projects. Thank you.

Jeff Bell:
Yes, I'm happy to take that, Benoit. It's Jeff. I think what we'd say is, and we continue to be of the view, that over the life of Infrastructure Projects as a portfolio, for the remaining projects, we expect them to be cash flow neutral, maybe slightly positive. That'll clearly vary period to period and year by year, as we've talked about. So, I think we clearly would intend to see post-2021 a more normalization of that. I think it's, frankly, too early and we'll talk a bit more at the Investor Day about how we see cash flow post-2021, and our thoughts around that, but I think I'd leave our sort of outlook and statements largely the way we've talked about them previously.

Benoit Poirier:
Okay, thank you very much for the time.

Ian Edwards:
Thank you.

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Operator:

Our next question comes from Chris Murray of ATB Capital Markets. Please go ahead.

Chris Murray:

Thanks. Folks, good morning. Jeff, maybe you want to take this one. You did start calling out currency as a bit of an issue in terms of revenue growth just earlier, so just a couple questions on this, just to confirm, one, this is just really a translation impact, there's no real FX risk in this, and then, two, just trying to understand, and making sure I understand, the mix of currencies that impact you in the different segments, so we can maybe try to forecast this a little better on a go-forward basis.

Jeff Bell:

Sure, yes, Chris, happy to. I think my first observation would be it's absolutely been the difference between the strength of the Canadian and U.S. dollar that impacted Q2. We saw a fairly significant move in that, with the Canadian dollar strengthening, as I'm sure you're aware, back in sort of April, early May, and so it was just to call out the point. Effectively, our reported results are in line with our guidance around revenue outlook, low-single-digit, but the reality was that if currencies had stayed constant to the previous year from an underlying organic growth in local currency, the organic growth was stronger, it was more in the mid-single-digit range, so was just calling that out.

The two currencies, primarily, that affect us are the U.S. dollar to the Canadian dollar and the British pound to the dollar. Those are the two largest ones by far. The rest are fairly minor. It's really those two.

Chris Murray:

Okay. No, that's fair. It all really is just translation, there's no …

Jeff Bell:

Yes.

Chris Murray:

… material balance sheet impact.

Jeff Bell:

No, absolutely.

Chris Murray:

Okay, and then just my other question for you, just going back to the Capital business maybe for a second. In the quarter, saw a bit of a sizeable step-up in book value of the Capital business. I'm just wondering if there's any kind of additional colour you can give us on what actually resulted in what looks like about a $60 million plus increase in the net assets of the Capital portfolio.

Jeff Bell:

Yes, I think that's just related to a couple of things, Chris. One is around some investments that we make as part of some of our joint venture investments, and it really just has to do with the point at which we're moving capital into those investments, in terms of our cash flows. I wouldn't call anything out there, in particular, just a bit of the normal movement in terms of how we account for those investments.

Chris Murray:

Okay, fair enough. All right, folks, that's my questions. Thank you very much.

Ian Edward:

Thank you.

Operator:

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

Frederic Bastien:

Hi, good morning, everybody. A quick question on sort of your business development approach. The Metro Sydney award shows that you're still able to participate in very large-scale projects, but without taking on undue risk, so I was wondering what are you telling clients differently than you were perhaps two years ago that is convincing them to give you a shot at these projects and your ability to perhaps team up with local domestic contractors to pursue the work. So, how fundamentally have you changed your approach to bidding on these jobs?

Ian Edwards:

Yes, very fundamentally changed, and the first thing I'd say is we're very, very clear that we're out of LSTK contracting, and making that clear to our customers globally, and we're not alone. I mean, a lot of our peers have indicated similar strategies, maybe not as definitive as ours, but certainly indicated similar strategies. I think the laws of supply and demand are such that our customers are having to find new ways to develop and build their infrastructure, and we're seeing a change in the way that that procurement is being undertaken, and we're seeing a change significant enough, I think, to fuel the growth demands that we have, such that we can be selective. We're working on kind of numerous prospects in Canada and the U.K. and Australia, where we're seeing this type of collaborative, non-fixed price style of delivering major projects is evident. We're really optimistic about building our capability from the past, where we used to deliver LSTK projects, to delivering collaborative projects with our customers. So, very optimistic about that, that kind of part of our business future.

Frederic Bastien:

Thanks, Ian. Then, secondly, we're seeing good progress in the U.S. with respect to Congress potentially approving an infrastructure bill in some shape or form, so can you remind me how well positioned you are to potentially participate in any future work related to this stimulus bill?

Ian Edwards:

Yes, for sure. When we acquired Atkins, one of the very attractive parts of that acquisition was the start they'd made on growth in the U.S., and we've been able to continue the organic growth of that growth in the U.S. It's been very, very successful in very specific states, such as Florida, Georgia, North

Carolina, Texas, Colorado, Nevada, and recently in our strategic planning, we've identified the white space areas, which are primarily Northeast, Northwest, California, and we've started opening offices, and we have an organic approach to building more capacity and building more connectivity to the states. That's going well for us, and we would also clearly add to that through inorganic growth, and we'll give a bit more flavour around that in our Investor Day, but it's a very key part of our strategy for growth.

What we're seeing, obviously, even without the Biden trillion dollars, what we're seeing is good opportunities and a good pipeline, and strong growth areas, without the trillion dollars, because the trillion dollars is additional. I mean, once this bill is passed, that's additional funding that we're going to see flow through in '22 and '23, and beyond. So, very, very key to our future, and I think we're really well positioned for it.

Frederic Bastien:
Thank you very much.

Ian Edwards:
Thank you.

Operator:
Our next question comes from Sabahat Khan of RBC Capital Markets. Please go ahead.

Sabahat Khan:
Great, thanks, and good morning. I want to talk a little bit about the Infrastructure Services segment. It's a bit smaller, I won't talk about it a lot, but it's done quite well through H1. Can you maybe about just the opportunity set there, the kind of work you're doing, and is it just a lot of opportunity out there in that segment? Just some commentary there, please.

Ian Edwards:

Yes, for sure, for sure. I mean, it's really—you could think about the segment in three parts. There's the Linxon part, which is this joint venture with ABB, that does some station and transmission distribution work; it has the O&M business in it, which has very, very long-term Canadian O&M contracts, primarily won through the PPP market; and we have the services part of really what is legacy SNC-Lavalin, such as hydro and clean energy and industrial. So, when you think about those three components, they're pretty buoyant in markets all around, and the key, and our growth strategy going forward, is really to take those beyond Canada and think about where we can position those capabilities in the U.S. and the U.K. So, very strong growth specifically in the first half of the year out of Linxon, we've seen some good wins in the Linxon business, and we're seeing from the services side, in certainly the hydro market and the clean energy side of power, quite strong demand there, too. So, good capabilities that gives us this platform for growth in the future.

Sabahat Khan:

Great, and then just a second one, I want to talk a little bit about the backlog, particularly, the Nuclear backlog. Maybe a two-parter there, I guess. Can you maybe comment on the opportunities out there as you kind of wind down the existing work, what kind of work you're looking at? Then, just the second part. We've talked a little bit in the past about how Nuclear fits into kind of the future of clean energy. Should we expect that, until that debate is settled, more of the work in your backlog will come from cleanup and remediation, just as kind of an outlook on that segment, please?

Ian Edwards:

Yes, okay, and I think the answer is basically yes. Very many components to our Nuclear business, and that's obviously the key strength, and the fact that we've got a diverse range of capabilities, but if we try to think about it probably in three parts, one is environmental, so cleaning up nuclear waste and decommissioning power plants, which is about 40% of the business, very, very strong pipeline ahead, both in the U.K. and the U.S., and to some extent in Canada, very strong Department of Energy in the U.S., lots of opportunity where we're already supplying our service, again, in the U.K., in Sellafield, and cleanup through there, so probably one of the key growth drivers in the short term.

Another component is basically life extension to reactors or new build reactors. Obviously, in Canada, with LPG and Bruce, we have successful business with them on the extension of their nuclear plants, and those contracts are going well. They're a bit lumpy, frankly, because they're big contracts. When they get awarded, they're big jobs, add to lots of the backlog, and then obviously it takes a long time to burn that backlog off.

The U.K. new market, very, very important to our future. We're very prevalent in Hinkley in a design and technical services capacity. We have almost 700 engineers on that job. Interesting so see what happens next. Sizewell is the next one. The government does have a Nuclear program there, they're fairly committed to it, for clean energy. Obviously, something we'd like to see across the globe, but other countries are kind of sitting on the fence at the moment with that.

Then, we've got all of the third leg to the business, which is really all of the reactor support, the technology. Even that little component I threw into the presentation, we actually have the technology to extract medical isotopes from nuclear waste, which are used in the medical sector. So, very interesting from a technical perspective and book-and-burn type work.

So, we're really bullish on the Nuclear sector, not all dependent on seeing new builds, but a lot of opportunity, even just what we see as Nuclear's status quo.

Sabahat Khan:
Great, thanks very much.

Ian Edwards:
Thank you.

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

Devin Dodge:

All right, thanks. Just maybe a couple questions on the EDPM segment. The MD&A mentioned selling a number of project final accounts in Q2. Just can you provide some colour there on how meaningful those close-outs were? I think we recognize that these can occur from time to time. I'm just trying to get a sense if the margin performance in the quarter was sustainable or if 12 months from now we'll be talking about EDPM having a difficult margin comp.

Jeff Bell:

Yes, it's Jeff, why don't I take that one, Devin. Yes, you're absolutely right, as part of EDPM, there are true-ups and settlements of different projects as they close-out, both on the positive and negative side. On the positive side, it was effectively something that was in the sort of $10 million range in and of itself, but I would say there were a couple going the other way. The net impact of the positive contract close-out versus a couple of small ones was kind of low-single-millions. So, I think, from a comp perspective as we move forward, I think it'll be fine, and I think the results themselves reflect well the underlying operating performance of the business, notwithstanding at the margin there's a few ups and downs.

Devin Dodge:

Okay, that's good colour. The second question on EDPM, look, I was a bit surprised to see some restructuring costs in the EDPM business in Q1. I think it was in the $9 million to $10 million range. Just can you provide some colour on the nature of those restructuring charges?

Jeff Bell:

Sure, yes. So, as a part of continuing to bring what was effectively the Atkins business and the SNCL business together, particularly in Canada, we've looked to streamline the organization, have it very focused, and redesign how it goes to market, so that it's well set up to drive growth, and as a result of that, we've also taken out some spends and layers and layers of management to streamline the organization that way, and so what you're seeing there are primarily severance costs related to doing that.

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Devin Dodge:

Okay, thanks for that. I'll turn it over.

Ian Edwards:

Okay, thank you.

Operator:

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

Michael Tupholme:

Thank you. A bit of a follow-up question on the Nuclear segment, further to some of the comments you made earlier in the call on that segment. So, another quarter with solid performance in Nuclear, and you sound quite positive on Nuclear's outlook. I'm just wondering, though, the backlog in Nuclear, it's been coming down for the last six quarters or so—and I know, Ian, you just mentioned a moment ago that it can be lumpy, particularly in the life extension work , but I'm just wondering, if we look at that segment, do we need to see the backlog start to turn higher relatively soon to sustain the kind of performance you've been delivering in Nuclear, or can you maintain what you've been doing without necessarily seeing any kind of a near-term uptick in backlog?

Ian Edwards:

I think the answer is both, really, because the parts of the business are quite different. There is a book-and-burn element to this, which is short cycle. We win those mandates, we execute them quite quickly, and you won't see a particular buildup of backlog, it's going to be fairly consistent. However, if you think, then, about the longer term contracts, which are both in clean-up and—in Canada, for example, in Bruce, the reactors there are issued one-by-one. I mean, we have an option, that is an optional bump both ways, for the client and ourselves, for Reactors 2, 3 and 4 in the series. We're working on the first reactor, but that's not in the backlog. We're currently negotiating the second one, we would hope to secure that, that'll go into the backlog and you'll see a bump. Similarly, these big jobs in the U.S., and

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they are multi-billion-dollar projects in the U.S. for clean-up, when we award one of those, again, you'll see a significant bump in the backlog.

I think the most important thing for me is the strength of the pipeline and the barriers to entry. There's limited competition here, because the barrier to entry, having the technical capability, is quite high, hence its profitability is high, and the pipeline is strong. So, I'm not worried, I'm really kind of optimistic about the future.

Michael Tupholme:

Okay, no, that's helpful, and just in terms of tracking this going forward and having these opportunities in the pipeline translate into awards and seeing an upturn in the backlog, do you have some visibility on that? Is that something we should look for over coming quarters, or are these longer term opportunities that could take longer to materialize?

Ian Edwards:

Yes, and if you think back to the specific Investor Day that we had in the nuclear facilities, we tried to give a bit more transparency in our pipeline, and we'll do that again in the Investor Day, we'll show a bit more of the pipeline and the different kind of components of this sector.

Michael Tupholme:

Okay, that's helpful, and then in terms of my second question, on the EDPM business, good reported year-over-year revenue growth, and even better on a constant currency basis. You've talked a fair bit about your views around, regionally, where you're seeing strength, but I'm wondering, from an end market or sector perspective, can you speak a little bit about that and which areas are driving that growth, and maybe which areas are lagging in terms of the sector and the end market?

Ian Edwards:

Yes, yes, and it is a varied picture. For ourselves, the U.S. is a key growth market for us. Our business in the U.S. is really road and bridge, rail and buildings, and all of those components are strong state by state. We're only in a handful of states. So, the growth for us there is let's keep doing the same thing, but let's take it to more states, expand our geography. We've seen very, very strong growth in the U.K., and a lot of that growth currently is coming from new business. Obviously, we're very—we're almost the market leader in terms of rail and transit and road.

We've been looking at digital work, we've been looking at how we sell our digital capability. We're bringing in new revenues from our digital capability, and we're bringing in revenues, such as the Government Property Agency work, which is using our knowledge of buildings, using our O&M knowledge, using our digital capability, to apply it to net zero. That's almost like a flagship project for us, because we're actually helping the U.K. government bring down the carbon footprint of the national government buildings, and that's by analysis, consultancy, it's by bringing our design and technical and operation capability all to the client to do that.

So, I think there's two things there, geographical growth in the U.S. and then bringing more digital and technology capability to the needs of our customers. That's probably a flavour.

I mean, markets that are not buoyant, they're pretty obvious, you know, like aviation, where we're obviously seeing a contraction in the aviation. Apart from that, we're focused on our core geographies, which is the U.K., Canada and the U.S.

Michael Tupholme:
Okay, that's helpful. Thank you.

Ian Edwards:
Thank you.

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

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Maxim Sytchev:
Hi, good morning.

Ian Edwards:
Good morning.

Maxim Sytchev:
Ian, I just wanted to start with a kind of high level question. You mentioned digital services as something that you are trying to grow. Do you mind maybe providing a bit more flavour in terms of how material this business is and the kind of go-to-market strategy, whether it's dramatically different versus kind of the typical RFP thing that you do? So, maybe any colour on that business, please.

Ian Edwards:
I think about it in two ways. The first way is complementing our capability with digital tools; in other words, being more efficient and effective in the services we offer our customers by bringing our design, our consultancy, our delivery, our commissioning and operation and maintenance expertise to a digital level, where we can differentiate how customers see our capability. That's an important part of our digital strategy, and digital twinning, as you might have heard me say before, is pretty key to that. So, we can actually simulate everything for a customer before he actually sees it being built, or before he sees it being developed. That's an important part. Our Global Technology Centre in India, with 3,000 really smart people in it, that's supporting our businesses globally, is also a key part. That, for us, is not a back office, it's a very, very advanced technology centre with great capability on the digital side. That's one half of it.

The other half, it really plays to what I was just talking about, which is new business. It's actually offering our customers something, which is untraditional for ourselves, in digital technology. An example would be the modeling of the buildings to bring their carbon footprint back down. Another example of that would be we've been a preferred supplier to Heathrow for quite a long time now, helping them install biometrics across the whole airport, and digital tracing of people within the airport to reduce queuing times, and we worked alongside the client to actually, with a technology provider, to project manage that, implement it, understand.

So, it’s really—the whole thing really is getting ahead of what our customers want and being able to offer what our customers are looking for ahead of our peer group. That’s the way I’d see it.

Maxim Sytchev:
Right. Is it high margin business, Ian, or is it similar?

Ian Edwards:
Currently, I think it complements the margin range that we’ve put out for EDPM. I think, over a period of time, if we truly differentiate ourselves, I think we’d have to keep observing that, but we’re not about to change the range right now.

Maxim Sytchev:
Okay, fair enough, and then I have a couple of quick ones for Jeff, if I may. The tax rate was pretty high in Q2, I think it was 41%. How should we think about the rest of the year and for the entirety of the year in terms of the tax rate?

Jeff Bell:
Yes, as I said, there were a couple of one-off items in there, which increased the effective tax rate in Q2. I wouldn’t expect that to continue in the second half of the year. I’d expect this to be back more in our normal range of 20% to 25%. I think, if you then look at it from a full-year basis, Max, it may be towards the top end of our normal 20% to 25% range, but wouldn’t expect Q2 to continue. It was a one-off related to kind of one-time items.

Maxim Sytchev:
Okay, that’s helpful, and then maybe in terms of—you collected a government grant in Q2. In Q3, we should expect nothing. Is that a fair assessment?

Jeff Bell:

The government grants that we disclosed are global, and there is a bit outside of Canada, as well. The majority of it is in Canada. We would expect, as you say, to see very little of that, either in Canada or globally, in Q3 and going forward. Most countries are winding down those programs.

Maxim Sytchev:

Okay, that's great. Thank you so much for clarifying.

Ian Edwards:

Thank you.

Jeff Bell:

Thank you.

Operator:

Our next question comes from Troy Sun from LBS. Please go ahead.

Troy Sun:

Good morning, gentlemen. Thanks for taking my questions. I'm just wondering—I wanted to go back to the Nuclear segment here for a little bit. I'm very intrigued by some of the technology offerings that Ian discussed early on in the call. I'm just wondering if you can provide some more specific applications on those programs, and any early feedbacks on the client side. I'm just trying to understand whether these offerings are specific to individual reactors or they can potentially become transferrable to other sites, as well.

Ian Edwards:

Yes, thank you, and maybe the easiest way for me here is to give you an example. We own the technology and developed technology for vitrifying nuclear waste, and in simple terms, it's a process to

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put large volumes of nuclear waste into glass, into small glass volumes. I wouldn't pretend to understand the technology myself, but in simple terms, that's what it is. Now, we currently offer that to the Department of Energy in the U.S., and we actually have facilities that we've installed in old nuclear facilities to do that, and those, you know, small glass, they go into long-term storage. We currently are in advanced conversations in the U.K. for the nuclear storage facility in the U.K., in Sellafield, to do just that. So, it's to transfer that capability and technology to another customer, and that's obviously a key kind of strand to the Nuclear business, and as I said, it's in three components: technology, reactor, vendor support, and having the CANDU technology is one strand; the life extension and new build is another strand; and then the decommissioning and nuclear environmental management and clean-up is another strand. The basis of all of these is our capability and our Nuclear capability that we've developed over many, many years, both in SNC-Lavalin and Atkins. So, for me, it's a key capability that we have, that we're really proud of.

Troy Sun:

Thank you, that's super-helpful. Maybe just quick ones for Jeff here. Just given where the balance sheet is right now, as well as potentially operating cash flow coming back in the near future, what's, I guess, the comparable level of leverage that you'd be targeting, and are there any thoughts around potentially putting in an NCIB in place in the near future?

Jeff Bell:

I think what I'd say is that we'll talk more about that at the Investor Day. I think, as you've heard me say before, having a strong balance sheet, we think is important to the Company and important in executing on our strategy, and, therefore, we continue to have the view that we will move ourselves back towards having financial metrics consistent with investment grade. We were pleased to see in Q1 that both rating agencies took off their negative outlook, so to speak, so we are at BB high or BB plus, and we think that continues to be the trajectory that we're on, but we'll definitely come back more at the Investor Day and give more clarity on that.

Troy Sun:

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Okay, great, thank you. That's it for me.

Ian Edwards:

Thank you.

Operator:

This concludes 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. If you have any additional questions, please don't hesitate to contact me directly. Thank you very much and have a beautiful day, everyone. Bye-bye.

Ian Edwards:

Thank you.

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.