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First Quarter 2023 Results

Conference Call and Webcast Transcript

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

Ian Edwards
President and Chief Executive Officer

Jeff Bell
Executive Vice-President and Chief Financial Officer



Operator:

Good morning, and welcome to SNC-Lavalin's First Quarter 2023 Results 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. (Operator instructions).

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

Denis Jasmin:

Thank you, Cherise. Bonjour tout le monde. Good morning everyone, and thank you for joining us today. For those dialing in, we invite you to view the slide presentation that we have posted in the "Investors" section of our website, which we will refer to during this call. Today's call is also webcast.

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 financial measures. Reconciliation of these amounts to the corresponding IFRS financial measures are reflected in our earnings release and MD&A, which can be found on SEDAR and on our website.

And now, I'll turn the call over to Ian Edwards. Ian?





Ian Edwards:

Thank you, Denis. Good morning everyone, and thank you for joining us today.

We began the year on a strong footing as Q1 results were solid across our SNCL Services businesses. Our core purpose is “engineering a better future for the planet and its people”, and we’re only able to do so through the hard work and dedication of our employees, whose contributions help us achieve our long-term growth aspirations. I’m very proud of this growing team.

On Slide 3, we outline our accomplishments in relation to our Pivoting to Growth strategy as we have become a professional services and project management company. As a reminder, our goal was to wind down our LSTK projects and grow our SNCL Services businesses in our chosen geographies to drive long-term value creation. Our results in Q1 further emphasize that our plan is now working.

SNCL Services continue to grow, expanding its revenue by 10.8% year-over-year, while segment Adjusted EBIT grew 23.4% as we were able to deliver strong margin percentages.

We achieved another record backlog this quarter, totalling \$12.1 billion at March 31, as demand for our services remains very strong in our core end markets and geographies.

We purposely pivoted into these geographies when we developed our strategy, and we are excited by the progress we have made in these markets.

We continue to be recognized as leaders in the nuclear sector. During the first quarter our backlog grew 23% year-over-year to just under a billion dollars. This quarter’s growth represents the largest backlog growth since 2016 and highlights the long-term potential of this business.

As we indicated last quarter, our two Ontario LSTK projects are largely physically complete. Testing and commissioning is proceeding as planned, and they remain on track to be handed over to our clients later this year. We recognized a \$9 million loss in this quarter, in line with the expectations we provided on the fourth quarter call, and as anticipated, the robust cash flow generated from our SNCL Services business offset the cash used on our LSTK projects.



Our success this past quarter further emphasizes that the strengths of our new strategy, the resilience of the business through times of economic uncertainty, and our growth opportunities are unfolding as planned. We continue to have great confidence in our forward trajectory, and we are well on track to deliver our stated goals for 2023.

On Slide 4, we highlight our backlog growth across SNCL Services. Our 8% growth in the first quarter of 2023 versus the first quarter of last year was mainly driven by wins across our Engineering Services and Nuclear businesses. The public sector focus on converting to a greener grid for baseload power, for greener infrastructure, has resulted in continued key wins across our core geographies, as well in as in other markets such as Saudi Arabia.

Turning to Slide 5, our Engineering Services business continues to drive robust growth for SNC-Lavalin, and outperformed year-over-year during the first quarter. Acceleration across our core geographies led to a 17.5% organic revenue growth versus the first quarter of 2022. Our year-over-year progression highlights our ability to capture market share and provides a clear roadmap for near-term and long-term growth prospects for sustainable infrastructure demand. Segment Adjusted EBIT margin and segment Adjusted EBITDA over net revenue margin were 8.4% and 14%, respectively, during the quarter.

We continue to achieve record backlog results with another quarter of growth. It now stands at approximately \$4.8 billion, which represents 25% growth versus our backlog as at March 31, 2022.

On Slide 6, we provide further insight into each of our core geographies of the U.K., the U.S., and Canada. In addition to organic revenue growth, we also earned several key wins across these markets that touch all of the engineering services that SNC-Lavalin provides.

In the U.K. and Europe, we saw continued revenue growth, which speaks to the focus of governments to spend on defence and energy. Performance this quarter emphasizes the resilience of our business as market dynamics appear positive despite underlying uncertainty in global economies. Our key wins this quarter include a contract to upgrade railways in the south of England over the next five years and leading the design of the new Dublin MetroLink in Ireland.



In the U.S., we continue to achieve record high backlog in this growing market. Our positioning in the U.S. is a key pillar of our Pivoting to Growth strategy. Our robust pipeline and long-term commitment by the governments to expand infrastructure spending as evidenced by wins this quarter sets us up well to maintain and accelerate our recent revenue and margin performance.

At home in Canada, we are also seeing increased government spending on infrastructure. Growth end markets include the focus on energy transition, energy storage and mining operations. We secured a number of key wins in Canada across the industrial, power and EV battery markets, as well as road improvements.

Looking out, demand remains robust for our services, driven by generational investments in infrastructure and climate resiliency, reshoring of manufacturing, and the energy transition. Here in Canada, for example, the \$180 billion Infrastructure Investment Program spread over 12 years and established in 2016 by the Government of Canada still has more than half of the budget left to spend.

In the U.S., the Infrastructure Investment and Jobs Act and the Inflation Reduction Act provide a strong tailwind for future growth opportunities.

Our robust pipeline sets us up well to top line and bottom-line growth in our Engineering Services business across each of the geographies for the foreseeable future.

I'd now like to move to Slide 7 and the results of our Nuclear business.

Our positioning in the expanding nuclear marketplace continues to bear fruit as we achieved approximately 5% organic revenue growth versus the first quarter of 2022 and sees strong demand trends across each of our core geographies with particularly noteworthy growth in Europe. Our Nuclear backlog now stands at \$986 million, which represents a 23% growth versus our backlog at March 31, 2022. This backlog growth further confirms SNC-Lavalin's position as a leader in the nuclear services marketplace.

Results this quarter highlight the long-term growth trajectory of this business as public entities continue to seek alternative energy sources for a cleaner planet. Commitments to Net Zero carbon by 2050 will significantly increase demand for low-carbon sources of reliable baseload power where nuclear facilities are poised to meet that demand.



On Slide 8, we highlight achievements in each of our Nuclear services business that we provide.

Nuclear new builds represent a significant potential opportunity for SNC-Lavalin. Across the globe, nuclear facilities are being seen as low-carbon energy source alternatives. We are underway on small modular reactor projects in the U.K. and Canada, while we are well positioned for upcoming major new build projects in Romania and the U.K.

We remain active in reactor support and life extension projects as indicated by our work across many of our core geographies. In Ontario, we continue to be actively supporting CANDU life extension work at Darlington and the Bruce Power sites where we are making excellent progress. In Romania, we signed our second pre-engineering contract for the Cernavoda I CANDU reactor life extension program, the primary contributor to the increased nuclear backlog this quarter. While in U.K., we are providing support to the EDF fleet reactors. Furthermore, we see opportunity for continued work on life extensions in the coming years.

On waste management and decommissioning, we're seeing continued progress in the U.K. and the UAE on two major projects. In the U.S., our subsidiary Isotek continues to remediate nuclear waste and produce critical medical isotopes. The pipeline in the U.S. for our decommissioning and waste management services remains robust.

And now, moving to Slide 9, and our O&M and Linxon business.

Our O&M segment generated \$126 million in revenue during the first quarter, a 9% organic revenue decrease due to lower additional services year-over-year on existing contracts. Segment Adjusted EBIT margin was 7.5%, above our long-term target of 5% to 7%. And we are well prepared for our Eglinton, Trillium and REM South Shore branch projects moving into operation this year.

We continue to see opportunity for growth and expansion in the U.K. through building and road infrastructure improvements, and we're also utilizing our strategic partnerships with key industry players and leveraging our capital group to maximize bidding opportunities for future growth in our core markets.

Our Linxon business saw growth in new orders across the U.S. and the Middle East, which added to the backlog in Q1 which now stands at just under a billion dollars at March 31. However, revenue was lower



compared to the same period last year due to lower backlog generated in '22 and equipment supply chain delays in Q1. Our strategic review to optimize our portfolio of businesses, including Linxon, remains ongoing and we will provide an update when applicable.

Moving to Slide 10 and our LSTK projects and Capital business.

As we announced in March our two Ontario projects, Eglinton and Trillium, are largely physically complete. Our last project ramp continues to progress really well and is more than 75% complete at the end of March '23. The quarterly loss is in line with our outlook. We believe a significant portion of the additional costs related to the pandemic, supply disruption, inflation and labour strike action should be recoverable under the contracts we have with our customers, and discussions remain ongoing as we vigorously pursue recovery of these losses.

Turning to our Capital business, first quarter revenues and segment Adjusted EBIT were flat as we did not receive any dividend from our holding interest in the Highway 407 ETR. However, in April '23, we received \$10.2 million in dividend payments. Traffic volumes continue to accelerate, albeit at levels lower than pre-pandemic, as traffic volume grew 28% compared to the first quarter 2022.

With that, I'll now turn it over to Jeff to discuss the financial highlights.

Jeff Bell:

Thank you, Ian, and good morning everyone.

Turning to Slide 12, as Ian said we had a strong start of year with total revenues for the quarter increasing 7% to \$2 billion compared to Q1 2022. SNCL Services revenue totalled \$1.8 billion, 10.8% higher than 2022 or 10.1% on an organic revenue growth basis.

Total segment Adjusted EBIT for the quarter was \$159 million, a 46% increase compared to Q1 2022, and was comprised of \$156 million for SNCL Services, \$12 million for Capital, and negative \$9 million for LSTK Projects. SNCL Services Adjusted EBIT margin was 8.5%, in line with our target range of 8% to 10%.



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Corporate SG&A expenses from PS&PM for the quarter was \$29 million, and restructuring and transformation costs were \$15 million. We continue to expect that these expenses should be about \$100 million and \$30 million, respectively, for the full year 2023, as the first quarter had a slightly higher phasing of the total expected full-year costs.

Net financial expenses for the quarter were \$47 million, higher than Q1 2022 due to a higher level of gross debt and higher interest rates on variable rate debt. We expect a similar level of quarterly expense to continue for the rest of the year.

The IFRS net income from continuing operations this quarter was \$28 million, compared to \$25 million in Q1 2022, and was composed of a net income from PS&PM of \$26 million and a net income from Capital of \$2 million. Adjusted net income from PS&PM for the quarter increased by 41% to \$55 million, representing \$0.32 per diluted share.

Backlog ended the quarter totalled \$12.6 billion, an increase of 4% compared to March 31, 2022, as the significant increase in SNCL Services backlog was largely offset by a decrease in the LSTK projects backlog. SNCL Services backlog increased to \$12.1 billion at the end of the quarter, which included a 25% increase in the Engineering Services segment backlog. This segment was awarded \$1.5 billion of work in the quarter, representing a 1.13 book-to-bill ratio.

It is also noteworthy to mention that the Nuclear backlog had another solid quarter with a book-to-bill ratio of 1.21, ending the quarter at \$986 million.

If we now turn to Slide 13, at the end of March 2023, the Company's net limited recourse and recourse debt was \$1.4 billion and the net limited recourse and recourse debt to Adjusted EBITDA ratio was 2.9 times, the same level as at the end of 2022. This ratio is above the Company's target range of 1.5 to 2 times at the end of 2024, but we remain confident that we will be meeting the target at that time. Note that under our credit agreement the net debt to EBITDA ratio is calculated differently and at the end of March 2023 was approximately 2.5 times.

Due to continuing efforts on cash collection, our day sales outstanding for Engineering Services remains strong and stood at 62 days at the end of the quarter.



If we now move on to Slide 14 and free cash flow.

As expected, net cash generated from operating activities was negative in the first quarter due to the cash out flows from the LSTK projects. We expect slightly higher cash out flows for the LSTK projects in the second quarter. These cash out flows should then reduce in the second half of 2023 as the supply chain is paid out and testing and commissioning activities wrap up. We also continue to actively pursue claims associated with the increased costs we've experienced on the LSTK projects.

SNCL Services had another strong quarter, generating cash flows of \$94 million. After cash taxes, interest, corporate items and capital, you can see that we generated \$46 million of operating cash flow.

We continue to expect the total operating cash flows should be negative in the first half of the year, while they should be positive in the second half of the year.

With that, I'll now hand the presentation back to Ian.

Ian Edwards:

Thank you, Jeff.

So, we began the year on a high note with robust results in Engineering Services showcasing the strength of our businesses. Our LSTK projects are progressing in line with our expectations, and we continue to pursue recoveries relating to outstanding payments due on these projects.

We remain focused on executing our Pivoting to Growth strategy with the objective to deliver consistent earnings and cash flow to fuel value creation and the long-term success of the Company.

We are winning through our unique competitive differentiators and our ability to fully service the entire lifecycle of an asset – from design to decommissioning. A generational effort will continue to be taken to offset the negative impacts of climate change, and we are well positioned to utilize our capabilities to enhance our footprint in the new infrastructure for low-carbon future.



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We strongly are positioned with a leading presence across our core markets of Canada, the U.S. and the U.K., and we continue to see several opportunities for long-term value creation for SNC-Lavalin across these core geographies and our end markets.

With that, let's open it up for your questions. Thank you.

Operator:

We will now begin the question-answer session. (Operator instructions).

The first question comes from Chris Murray with ATB Capital Markets. Please go ahead.

Chris Murray:

Yes, thanks folks. Ian, I guess thinking about some of the stuff you've talked about and where you want to go in terms of the Pivoting to Growth strategy, one part you didn't touch on was M&A. As we get closer, I think, to the end of LSTK, can you just talk about where you're feeling in terms of accelerating growth? It sounds like it looks like organic growth has certainly been very, very strong, probably stronger than we thought it was going to be. Can you just maybe give us an idea if organic growth is where you're going to stay for now, given the rate of growth? Or is that as we get past Q2 we could be looking for more—for you folks to become more acquisitive?

Ian Edwards:

Thanks for the question. Good morning.

We're obviously really pleased with where we've positioned the Company. I mean we've deliberately positioned ourselves in fast growing markets, and we see those markets continuing to be sustainable and fast growing, fuelled by infrastructure investments and fuelled by the energy transition. You're seeing the fruits of that come through from the organic growth, as you correctly kind of identified, that we've executed on.

I mean, clearly, in the transformation of the Company from what it was to this professional services and project management organization, we will ultimately be producing positive free cash flows and we're looking forward to that, towards the back half of this year as Jeff articulated.



But we also are very, very fixed on our capital allocation strategy that we articulated in the Investor Day, going back to the end of '21. In that we offer a process to, first, strength the balance sheet; second, look at how we create value through potential M&A; and third, look how we might return value to shareholders. That's still the case. And clearly, when we get to the right point, we want to accelerate our growth through M&A, and that would be for sure part of our land and expand strategy in the U.S., and we talked about that previously as well.

So, yes, we're definitely on that journey, but it's still a work in progress, so to speak.

Chris Murray:

All right, fair enough. Then I know you're probably going to kick this down the road a little bit, but you did talk about your strategic review a little bit. I guess a couple of questions on this. I mean first of all, the book-to-bill in Linxon was remarkably strong and you did allude to some new contract wins, but revenue was down. So I'm just trying to maybe square how you guys are treating that business, where it is today—you've got a little volatility in it—and where you are maybe in the strategic review process in terms of timing.

Ian Edwards:

Let's perhaps pick apart particularly on the Linxon part of the strategic review.

Linxon, we've been holding this share in this business now for four year, and three years, the first three years were positive, positive on cash flow, positive in getting the profitability in the range that we want. But 2022 was disappointing. We are looking at why that was disappointing. We are looking at if we can get this business to a consistent place of profitability and cash flow and growth. And we are also looking at its suitability for our portfolio going forward, which would mean all options are on the table for the Linxon business.

It has improved. The performance has improved. Backlog has grown. It's still under review. We're doing quite a lot of work to look at that and we'll communicate when we come to a rounding on that. We expect to actually get to a position fairly shortly in the early part of the second half of this year and communicate that out.



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Chris Murray:

All right. That's helpful. Thank you. I'll leave it there.

Ian Edwards:

Thank you.

Operator:

The next question comes from Yuri Lynk with Canaccord Genuity. Please go ahead.

Yuri Lynk:

Good morning, guys. Nice quarter.

Ian Edwards:

Thank you.

Yuri Lynk:

Ian, 17.5% organic growth in Engineering Services, quite strong. Wondering if there was any particularly lumpy award in there or one end market. Just any more colour on the strength that you saw there because it was on a very tough comp too. I think 10% in the same quarter last year. And related to that, how does pricing play into your ability to outgrow the market on organic growth? How aggressive are you being on price? Thanks.

Ian Edwards:

I think in some ways it goes back to what I said about the markets. Where we've deliberately positioned ourselves, the markets are fast growing markets and across the board, U.K, U.S., and Canada, we're seeing very strong investment in infrastructure. We're seeing significant opportunities in the energy transition, which is also bringing in the private sector investment into energy transition. And there's no—to your question, there is no single project which has fuelled the growth. It's just very good work winning across a range of size of business, from very small projects to medium sized Engineering Service type projects.

We have also been pretty successful in the Middle East over the last sort of couple of quarters, which has fuelled some of the growth, but most of it is in our core regions where we stay at 8% of the business.



Profitability is on an improving trend. So we are not being aggressive in our bidding. We are still on a margin improvement process in parts of the business, so we're not putting that at risk at all in order to win this backlog. So, it's really about market strength and where we've positioned ourselves.

Yuri Lynk:

Okay. I mean a lot of your competitors or peers are also in the U.K., the U.S., Canada and they're not growing 17.5%, but you're obviously in some pretty good niches there.

How do you feel about the full year? I mean, you did leave organic growth guidance in the 5% to 7% range. How should we square that with the first quarter performance?

Ian Edwards:

Yes. Obviously it is Q1, right? So it's still early in the year. We're very pleased at the start to the year, and we're very pleased with obviously the growth that we've achieved.

What I want to see and what we want to see before we kind of move that guidance is more development of the pipeline through the year. So, we have certain visibility of work ahead of us from a defined perspective. We're confident in the markets. We see strong markets, but we need to see our own pipeline be developed a little bit further into the year before we start looking at the full year outlook there.

Clearly, if we continue the trajectory that we've got and it looks for sure that that is going to be the case, as we move into Q2 we'll have to look at the book.

Jeff, would you add anything to that?

Jeff Bell:

No, I think that's very fair and the second quarter has got off to a good start. Similar to Q1, but as you say Ian, you know, we want a bit more visibility on future contract awards, the filling out of the pipeline for the rest of the year, and then I think we'll have a chance to kind of revisit where we are.





Ian Edwards:

Good. Thanks.

Yuri Lynk:

Okay, guys. That's my two. I'll hop back in the queue. Thanks.

Ian Edwards:

Thank you.

Jeff Bell:

Thank you.

Operator:

The next question comes from Benoit Poirier with Desjardins Capital Markets. Please go ahead.

Benoit Poirier:

Good morning everyone and congrats ...

Ian Edwards:

Good morning.

Benoit Poirier:

... on the first quarter results. Just in terms of free cash flow, could you maybe provide some colour about what we should be looking for in terms of free cash flow for Q2, the magnitude of the loss versus Q1. And maybe DSOs, still remain very low at 62 days; I'm just wondering how sustainable it is.

Jeff Bell:

Thanks, Benoit. It's Jeff. Maybe I'll take that one.

I think in terms of the second quarter, as I was talking about in my presentation and we've talked about before, we really see the first half of the year from an operating cash flow perspective being negative, driven by the LSTK projects. And as we said at Q4, we see that cash flow drag from LSTK in the first half of this



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year being similar to the first half of 2022 where in the first half it was a cash flow usage of \$250 million, \$260 million. We still think that's true for the first half this year, so that definitely implies that Q2 will be a bit more of a drag in terms of LSTK in the second quarter as we pay out supply chain and really begin to finish off testing and commissioning and those sorts of things.

But as we've said, as we move into the second half, that LSTK drag will come down and the natural cash generative ability of the go-forward business as we get later in the year I think will become much more apparent.

Benoit Poirier:

Okay. That's great. Just which ...

Jeff Bell:

Sorry, Benoit. I think I didn't talk to the DSO. Sorry, I apologize for that.

It is at a strong level. We've done a lot, actually, within the business to really focus on cash flow generation and the conversion of EBITDA into operating cash flow, and we're seeing the fruits of that. So we remain very focused on it. There's always some pressure on that, as you say in terms of it moving a bit higher, but so far we've been successful and we expect to continue to be successful and in that range in the near future.

Benoit Poirier:

Okay, perfect. Just with respect to Capital, net book value was up sequentially. Could you maybe provide some colour on what drove the increase and whether the timing to revisit your stake in the Highway 407 is still a second half story?

Jeff Bell:

Yes, I think that increase is really related to the building of Trillium and how we kind of built that asset in the build phase before it's handed over to the customer. Nothing out of the normal there, Benoit. That's really what's driving it from a book value perspective.

I think in terms of the 407 more generally, we saw traffic year-over-year improve. It's up about 28%. Still below pre-pandemic levels, but as 407 management has said, they expect revenue and traffic to improve



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over the course of 2023. Obviously we consider it a great asset; it has a lot of life left in it. We're a happy holder of the asset here in the short to medium term. As we've said previously, in the longer term we'll consider how it fits within the portfolio more broadly. But in the near term, pleased to see traffic improving.

Benoit Poirier:

Thank you very much. Congrats again.

Ian Edwards:

Thank you.

Jeff Bell:

Thanks.

Operator:

The next question comes from Devin Dodge with BMO Capital Markets. Please go ahead.

Devin Dodge:

Thanks. Good morning. I wanted to start by picking up on one of Yuri's earlier questions on organic growth in Engineering Services. I think clearly you guys have made a lot of progress in expanding the workforce in 2022. Just wondering how you're thinking about, or should we be expecting, like, a similar pace of hiring in 2023, or do you think this will maybe moderate a little bit?

Ian Edwards:

Yes, you should see that. We're very, very pleased with our ability to increase the net level of people in the business from an organic perspective. I mean, obviously, we are a people a business and people drive growth. The ability to attract good people to the Company is key to fuelling that growth.

We've done several things in the last few years to re-create the culture in the Company and to be an employer of choice. I mean, our purpose, to engineer a better future for the planet and the people, really resonate with our employees and it is really a point of being able to attract employees.



Our ED&I programs, our development programs, our collaborative approach to doing business and to working together internally have all helped in being an employer of choice. And we've now been able to get our attrition levels down to pre-pandemic levels after a spike after the pandemic, which is great news.

In Q1, we actually increased our headcount by over 1,000 employees in Q1, so that's a great run rate and a great fuelling of our organic growth. So, you know, very, very pleased. Our company is people and we value, obviously, all our employees very much.

Devin Dodge:

Okay. Good colour there. Thanks for that.

Then, Ian, you mentioned that the prospects with the U.S. Department of Energy remain strong for nuclear cleanup work. Yet I think we continue to see projects get awarded to others, including a large project award in the quarter where SNC was one of the incumbents. Can you elaborate a bit on what's driving the optimism there?

Ian Edwards:

Yes. Yes, for sure. It's a very, very big market. That's the first thing I'd say. Generally these projects are bid and undertaken in joint venture. We are in joint ventures for other projects. You're right to say there was a big cleanup project at Hanford that we didn't win in the quarter. That was disappointing. I guess you can't win them all. There are other prospects out there. I mean that win in itself—and it was a fairly large project—but because these things are done through joint ventures each loss is not material to the whole. We do upgrade expertise in the sector. We have our own IP technology in terms of vitrifying nuclear waste into glass. We have a technology that brings out these medical isotopes from nuclear waste into medical isotopes. And the market is huge. I mean the DoE is spending a significant amount of money on cleaning up the historical nuclear waste, so we still see it as a good pillar to the business.

Devin Dodge:

Okay. Understood, okay. Then if we just sneak one last one in, I think this might be for Jeff. Just trying to understand or better understand some of the restructuring costs in the quarter, particularly in Engineering Services. It just seems to us that the business is performing well, so it isn't really clear to me why there is much restructuring or severance costs. That should be considered nonrecurring.



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Jeff Bell:

Yes, it was just as we've been looking at that business, those additional restructuring costs were in our Hong Kong and China business where we've repositioned and restructured the business in line with our work rate there. It was in a fairly small part of the business, but that was something that we needed to do in the first—the end of last year and the first quarter of this year. That's what drove the slightly higher amount in the first quarter.

Devin Dodge:

Okay, thank you. I'll turn it over.

Ian Edwards:

Thank you.

Operator:

The next question comes from Michael Tupholme with TD Securities. Please go ahead.

Michael Tupholme:

Thank you. Good morning.

Ian Edwards:

Good morning.

Michael Tupholme:

Just a quick question on Linxon. I realize—well, first of all, nice to see that segment return to positive EBITDA in the quarter, although it was still quite modest relative to I think what you would like to see that segment doing. Obviously it remains to be seen what happens with that business as you work through your strategic review, but as long as it's part of the results, just wondering how we should think about performance in that business over coming quarters.

Jeff Bell:

It's Jeff, Michael. Why don't I take that?



As you say, it was good to see it back into profitability in the first quarter. And as Ian said earlier, we've been doing lots to strengthen the operational capability within that business. I think we'll see Q2 improving on Q1, not at the level probably we'd like it ultimately to be, but in the second half of the year with the backlog growth that they've been growing and the win rate that they have, we would see it back into its target range in the second half of the year. That's how I think the profile will look like through the year.

Michael Tupholme:

Okay. Thank you. Then a couple of questions about Nuclear. First off, another quarter-over-quarter improvement in Nuclear backlog. I guess, can you just—I think there's some commentary about this but maybe you can just touch on the drivers to the improving backlog there.

Then the second part of the question is, when we look at the margins for the Nuclear segment, 13.4% in the quarter, that is within your 13% to 15% range that you've talked about in the past, but it's certainly lower than we've seen that segment do for quite some time. So, I guess, just wondering what's pushing the margins down a little bit versus what we've seen in the last few years, and how should we think about Nuclear margins going forward here?

Ian Edwards:

Yes, thanks. Obviously we are very excited about the market and the resurgence of new nuclear as part of the energy, clean energy transition solution. And you're right, backlog is up 23% year-over-year.

I think we've spoke a lot about the potential in the market and we've spoke a lot about how we see the medium term of this business growing significantly. What we're seeing now is actually real projects and real project wins. That's fuelling the start of what we will see as really good growth in this sector. Examples of that would be obviously the SMR OPG project here in Canada at Darlington, the CANDU life extension project for the Cernavoda, Romania project. That's the second pre-engineering contract which came into backlog. Sizewell, we're now seeing the second large nuclear power plant being built in the U.K. which we're heavily involved with, so we're seeing work flow through now from Sizewell and that will continue.

Going forward, just a range of opportunity in small modular reactors: a range of opportunities both domestically and overseas for the CANDU technology, a range of opportunity to support both the technologies such as GE Hitachi, Rolls-Royce, the French technology where they really need our project



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management and nuclear kind of engineering general capability that we have. So, we're going to see a lot more fuelled here.

I think the margins, because of the barriers to entry, will remain in the range that we've got. We're confident that this is a differentiated high barrier to entry business. The work is obviously done under contract conditions which are favorable to ourselves. And we're in this sort of transition of winning work and there's no real pressure on the margins here. It's really about winning work and catering to customers.

Michael Tupholme:

Okay. That's very helpful. Thank you.

Maybe if I can just clarify one thing from earlier for Jeff on the cash flow side. I know the expectation was always that you'd have negative cash out flows in the first half and then positive in the second, and obviously LSTK, I think the expectation was for that to continue to be a drag in the short term at least. But the comment about expecting a higher cash out flow in LSTK in the second quarter, was that always the expectation, or has something changed on that front?

Jeff Bell:

No. Well, nothing has really changed in terms of the first half. Of course it's largely dependent as we pay out the supply chain, so we just saw a little less of that than we expected in the first quarter. It will clearly sort of catch up in the second quarter, so it was just a bit of a phasing between the first and the second quarter, but no change to how we sort of saw the first half.

Michael Tupholme:

Okay, that's helpful. Thank you.

Operator:

The next question comes from Sabahat Khan with RBC Capital Markets. Please go ahead.

Sabahat Khan:

Great. Thanks and good morning. There was a bit of discussion about the U.S. business earlier. Just want to get an understanding, in terms of your positioning in that market, and given your current footprint—and



obviously M&A is a bit further out—do you think you are well positioned given a lot of the infrastructure spending that's coming? Do you see yourself doing maybe some smaller M&A in the interim to better position yourself for the IIJA or the IRA spending? Just some thoughts on that.

Ian Edwards:

Yes. I mean, the plan is going well. But our aspirations for growth in the U.S. is high. As you said, the market, and as I said previously, the market is very, very strong in infrastructure and energy transition, fuelled by the IIJA, the IRA and the CHIP bills that have been put in place.

We've got our land and expand strategy, which is really state to state, which is beginning to yield results and we're seeing work wins come through in our new entry states in Northeast, Northwest and California. So that's working and that's an organic play, and that's bringing results.

But there are other parts of the market that we have recently reviewed and developed a plan to execute on, basically fuelled by the energy transition and the IRA, in clean power and the industrial kind of processes and manufacturing units that need to be built to support that clean power, particularly EV, battery manufacturing and processing plants which we are in discussion with customers and looking, hopefully, to get some wins through.

The resiliency work in the U.S. is strong, both in flood defence, disaster relief, but also in flood mapping and understanding where those areas of risk are, and we've been winning projects through that.

Ultimately, we will get to an M&A program. It will be a sensible step-by-step M&A program in the U.S. where we build on the business that we already have with tuck-in type acquisitions to give us a greater reach geographically and capability-wise, and relationships with customers to build on our aspirations. But we are 4,200 people in the U.S. and we want a lot more than that to be equal to our peers.

So, we have a plan that we're confident in and the market is there. The market is there to support that.

Sabahat Khan:

Great, thanks. Then, looking at the U.K. market, obviously Atkins has historically been a pretty large player there. I guess based on your read on the market, is it the kind of base level infrastructure spend that's driving



demand in that market? Or are you seeing contribution from some of the larger, sort of whether it's a levelling up agenda or kind of the larger one-time spend programs? Just want to understand how that market is doing and maybe any end markets that stand out to the positive or to the negative?

Ian Edwards:

Yes. We've got a very diverse business across the U.K., which is helping us in the resilience. In actual fact, our business is growing and we actually see it growing for the foreseeable future.

You'll have seen that the government in March through their budgeting process reconfirmed their £600 billion five-year infrastructure plan for the country, which is great to see and great to see that investment. But also, we're seeing very strong markets from the energy transition and the commitment to nuclear power. I mean, they've made a commitment in the U.K. for 25 gigawatts of nuclear power, which is obviously fuelling that part, which is good for us too.

Sectors that we're actually seeing good growth in are defence. We've had some good wins from the defence sector and the energy sector, generally. Levelling up is still going to invest in the north of the U.K. But we're still very confident that we've got this resilient, diverse business and still winning and growing the business, actually.

Sabahat Khan:

Great. Maybe just one last quick one. There used to be a project, the White Rose Project a while back. It used to be in LSTK. I think it got cancelled and it came back in under a different contract structure. Could you maybe just talk through sort of the new structure for that contract, or for that project and maybe how that project is progressing?

Ian Edwards:

The project is progressing well. It is under a new contract structure. That's not an LSTK structure. I won't get into the kind of details of it but it's a non-LSTK. It's a profitable project for us.

The project is going well. It was restarted. We're up in—we're doing what we call the slip forming of the principal part of the project, which is 24-hour operation, which is really going well. We've got a good



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relationship with our client there. Good partners on the project. So yes, no sort of new news really on that, other than the fact that we're pleased with the way that it's going.

Sabahat Khan:

Great. Thanks very much for that.

Ian Edwards:

Thank you.

Operator:

The next question comes from Dmitry Khmel'nitsky with Veritas. Please go ahead.

Dimitry Khmel'nitsky:

Hi and thanks a lot for taking my question. I wonder if you can disclose the amount of disputed receivables that are recorded on the balance sheet, if possible.

Jeff Bell:

Sorry, say that—the amount of which receivables, Dimitry?

Dimitry Khmel'nitsky:

The receivables that you'd like to recover (cross-talking 51:50).

Jeff Bell:

Yes. No, fair enough. We haven't disclosed that. As you can imagine, Dimitry, it's commercially sensitive as we look to negotiate and recover the costs that we think are due to us. But that process is going well, and as you've heard us say before, we think we are due a significant amount of those costs. Naturally, we're pretty prudent about what we would put on the balance sheet in terms of recovery, but we think we're owed a significant amount of money from the customers in terms of those additional costs that we've incurred.

Dimitry Khmel'nitsky:

Understood. Okay, thank you. I wonder if you can maybe talk a little bit about what gives you the confidence as to the ultimate outcome of the recovery. For example, are they under the force majeure provisions—and



COVID, and I guess the ensuing inflation, qualifies force majeure. So anything that could indicate what gives you the comfort that most of those will be recovered?

Ian Edwards:

Yes, yes. Thank you. Obviously we are confident and we undertake an incredible amount of work to pursue these recoveries from our customers. We have very, very large internal/external teams with external legal and quantum and entitlement analysis, and through those analyses and through those legal opinion, we develop a view as to what we believe is our entitlement to recover loss. And clearly, through the pandemic those losses were significant, as we posted them in real-time as they happened.

Many kind of contract provisions, many sort of areas of entitlement that we can recover ranging from changes in law to the specific provisions around force majeure and loss due to strikes or hyperinflation. So without, kind of, obviously going into too much specific project-by-project detail, we are confident and we will vigorously pursue recovery of those losses, either through negotiation or through litigation.

Dimitry Khmelnitsky:

Okay, understood. But you don't have a timeline yet of when you'd expect to make announcements related to recoveries?

Ian Edwards:

No. Obviously in a negotiation there are two parties and we can't speak for the other party. We're working at it hard. We are optimistic that we will get a outcome which is a win-win for ourselves and the customers, and negotiation is the best way to do that and we are optimistic that we will conclude it that way.

Dimitry Khmelnitsky:

Thanks, Ian. What are the key variables, or I guess moving parts related to full-year cash flow guidance that may swing the number significantly? Just trying to understand why are you a little hesitant in providing the annual number, obviously understanding there is a lot of moving parts; some of them are beyond your control. Just trying to see what are the key variables there.

Jeff Bell:

It's Jeff. Why don't I take that sort of last question, Dimitry?





I think there are a few moving parts. I mean it ranges within LSTK to the actual recovery of the holdbacks receivable that we have and paying out the supply chain that goes with that. There's the claims revenue, as Ian has talked about, in terms of our ability to negotiate some of those outcomes this year or not. There's dividends on the 407. So, there's a number of kind of operating elements within there that certainly at this point in the year we wouldn't get more specific in terms of our outcome around cash flow.

Dimitry Khmelnitsky:

Awesome. Thanks so much. Thanks for taking my questions.

Ian Edwards:

Thank you.

Jeff Bell:

Thanks.

Operator:

The next question comes from Yuri Lynk with Canaccord Genuity. Please go ahead.

Yuri, your line is now open.

Yuri Lynk:

Hey guys. Thanks. Just a quick one on the strategic review as it pertains to the capital assets excluding Highway 407. How active are you on that part of the strategic review? Do you envision divesting those assets in a package deal, or would they be piecemealed out? And any idea on timing? Is that something that can happen this year, or it's 2024?

Ian Edwards:

The strategic review in its essence really is about fine tuning. The whole concept here is about fine tuning the whole portfolio, whether that's capital or whether that's portfolio. It's not transformational. There's nothing in there that's going to be very, very significant and we're very happy with the company we've now built.





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Specifically on the capital assets, we do recycle, as you've seen. In 2022, we recycled John Hart and a fund that we had with Carlyle. We generally make sure that our assets get into smooth operation, so obviously we've got three assets that are going into smooth operation this year. Two of those have got a capital content in the Ontario projects. Once they're in—the defects are done, they're in a smooth operation, that's the point that we may recycle out.

There's nothing that comes to my mind immediately that we would look to recycle out this year, but it's an ongoing process. Obviously we're in the capital part of our business to win work and to fuel the growth of the Company, and we hold a small portion of some of them where we have an operation and maintenance obligation. So, nothing that comes to mind specifically.

But the strategic review, it's going well. I mean, it's all really about profitability and fine tuning, making sure that we push all parts of the business forward to the right place as we now are a professional services and project management company.

Yuri Lynk:

But Ian, I think collectively those assets have a book value of around \$600 million. Why not look to divest of them and you could immediately put the balance sheet in much stronger footing and potentially accelerate your capital allocation program?

Jeff Bell:

It's Jeff. Maybe I would just sort of build to that. We looked at all of them, and as Ian had said, some of them are at a nature that are on the balance sheet that aren't at a stage where they can be effectively recycled in terms of capital, and some are of a nature that our ability to sort of recycle those in the immediate near term is more constrained. I think the point is that we'll absolutely continue to look at every one, and if there is an opportunity to realize value, to your point, and as we've done in the past, we'll look to do that as a way of accelerating, particularly on the balance sheet, getting to where we want to be.

Yuri Lynk:

Okay. Thanks, guys.





Ian Edwards:

Thank you.

Jeff Bell:

Thank you.

Operator:

This concludes the question-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 in joining us today. If you have any further questions, please don't hesitate to contact me. Thank you and have a nice day. Bye-bye.

Ian Edwards:

Thank you.

Operator:

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

