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# Stantec, Inc. (STN)

Q2 2018 Earnings Call


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# MANAGEMENT DISCUSSION SECTION

**Operator**: Welcome to Stantec's Second Quarter 2018 Earnings Results Conference Call. Leading the call today are Gord Johnston, President and Chief Executive Officer; and Dan Lefaivre, Executive Vice President and Chief Financial Officer.

Today's call is webcast and those dialing in are invited to view the slideshow presentation which is available in the Investors section of stantec.com. All information provided during the conference call is subject to forward-looking statement qualification set out on slide 2 detailed in Stantec's Management Discussion and Analysis and incorporated in full for the purpose of today's call.

With that, I'm pleased to turn the call over to Mr. Gord Johnston. Please go ahead.

## Gordon Allan Johnston

*President and Chief Executive Officer, Stantec, Inc.*

Thank you, and thanks to all of you for joining today's call. I'm going to provide you with a brief overview of our second quarter, then Dan will get into the details of our results. After that I'll highlight some additional color and share our operational highlights. Then Dan and I will answer your questions.

For those of you following along with the slideshow, we're on slide 4. Our second quarter results highlight the strength of our Consulting Services business and demonstrate that we're headed in the right direction with our long-term strategy of focusing on revenue growth, operational efficiency and successfully executing our acquisition strategy. In Q2, we had solid growth in Consulting Services. In fact, this is our fifth consecutive quarter with gross [Technical Difficulty] (00:01:36-00:02:58)

**Operator**: Ladies and gentlemen, please stand by. We're just experiencing a momentary interruption in today's conference call. Thank you for your patience and please continue to hold.

[Technical Difficulty] (00:03:06-00:03:43)

**Operator**: Please go ahead.

## Gordon Allan Johnston

*President and Chief Executive Officer, Stantec, Inc.*

Thanks, Piena. Apparently, our line got dropped there. So I'll start up again on slide 4 which is just following the really introductory comments. So for those of you following along with the slide show we're on slide 4. Our second quarter results highlight the strength of our Consulting Services business and demonstrate that we're headed in the right direction with our long-term strategy of focusing on revenue growth, operational efficiency and successfully executing our acquisition strategy. In Q2, we had solid growth in Consulting Services. In fact, this is our fifth consecutive quarter with gross and net organic revenue growth. Each was strong at around 4.5%.

In the quarter, EBITDA as a percentage of net revenue reached 13.6% for Consulting Services, which is slightly above our annual targeted range. EPS for Consulting Services was a healthy CAD 0.58 per share. These results were offset by continuing issues with legacy projects in Construction Services. We had hoped the majority of


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negative impacts were behind us, but that wasn't the case this quarter. However, the core U.S. and UK business is strong and we're taking strides to reduce further impacts. This includes winding down exposure to the UK waste-to-energy market and continuing to put a hold on hard-bid projects outside our areas of expertise. We're also making positive progress in our strategic review.

And before I pass the call to Dan, at the end of July, we announced that we have maintained our status as a top 10 global design firm in two key industry rankings. For the second year in a row, Stantec ranked number 10 on Engineering News-Record's Top 150 Global Design Firms list. We also advanced to number 9 on Architectural Record's Top 300 Architecture Firms listing. Both of these lists are compiled based on 2017 revenue. We're proud of our position in the industry. These standings demonstrate the creativity of our staff, the diversity of our business and our growth in some of the world's best design markets.

I'll now hand things over to Dan to walk us through our Q2 2018 results.

## Daniel J. Lefaivre

*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

Thank you, Gord. Good morning everyone. As Gord mentioned, our Consulting Services business performed quite well this quarter, but that was offset by disappointing results from legacy projects in Construction Services.

Let's start with Consulting Services results on slide 7. Net revenue for Consulting Services was up. When comparing to Q2 2017, our net revenue increased 3.8% to CAD 863 million. Organic net revenue grew in all geographies with increases of 6.9% in Canada, 3.3% in the U.S., and 3.9% in our Global Consulting Services business.

Looking at our business operating units, we had organic net revenue growth in Water, Environmental Services and Energy & Resources. We're seeing a strong rebound in Energy & Resources with 32.4% net organic growth for the quarter. Organic net revenue retracted slightly in Buildings. Low private and public spending in the UK and the Middle East are driving the quarterly retraction, but we are reducing our exposure to those markets. Factoring in some of the recent project wins, we expect Buildings will improve over the remainder of the year.

In Infrastructure, organic net revenue retracted 2% in Q2 2018 and was flat year-to-date when compared to the same period in 2017. Our work on several new projects resulted in higher sub-consultant costs, which contributed to growth in gross revenue and retraction in net revenue.

And in our transportation business, projects wrapped up in Colorado and Texas and winter and spring weather conditions delayed work in some regions. Again we have some key project wins that add to our backlog in the U.S. transportation business such as our work on the Hampstead Bypass in North Carolina.

Looking at the income statement on slide 8, gross margin in Consulting Services decreased slightly to 54.5% in Q2 2018. This is primarily due to project mix, competitive pricing and increased revenues across all of our Energy & Resource sectors. Growth in these lower margin sectors impacts our overall gross margin.

In Consulting Services administrative and marketing expenses were lower as a percentage of net revenue. It was at 41.3% in Q2 2018 compared to 42.3% in Q2 2017. We can contribute this or attribute this improvement to our ongoing focus on operational efficiencies, higher utilization, lower integration costs and lower occupancy costs. Adjusted EBITDA increased 9.2% to CAD 117.9 million in Q 2018 (sic) [Q2 2018] (00:09:14) compared to the same quarter last year. This is because of acquisition growth, organic revenue growth, decreased admin and


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marketing expenses as I noted previously. When comparing Q2 2018 to Q2 2017, Consulting Services adjusted net income was up 5.8% to CAD 65.7 million and adjusted diluted EPS was up CAD 0.04.

Now, we'll move on to Construction Services on slide 9. During the quarter, we recorded an additional negative revenue and cost adjustments of CAD 16.3 million for UK based waste-to-energy projects, CAD 5.4 million on major design-build contracts in the U.S. and CAD 3 million on legacy U.S.-based hard-bid projects. These adjustments resulted from continued project delays and performance issues. Adjustments related to these projects negatively impacted consolidated gross margins, EBITDA and decreased earnings per share by approximately CAD 0.17 in the quarter.

The UK waste-to-energy projects or legacy projects are outside MWH's core area of water expertise. They were bid on about four years ago and at that time the waste-to-energy market benefited from government incentives and was set to be a lucrative opportunity. After the Brexit vote the incentives were no longer available and the market lost its appeal, so we are winding down our exposure. Settlement agreements in two of the three waste-to-energy projects have been agreed upon in principle and minimal additional costs are expected as these are 100% complete.

Further costs associated with the remaining project are related to additional estimated cost to complete; however, we are expecting to achieve project takeover to occur in the third quarter. The U.S. projects were also awarded several years ago when MWH was expanding its U.S. construction operation into new markets. The projects were outside MWH's core regional areas of expertise and we have placed additional oversight on bidding on work like this. In addition to impacts to margins, EBITDA and EPS, these project adjustments affected our effective annual income tax rate. It increased from 27% to 29% in Q2 2018. This is mainly due to losses incurred in our UK Construction Services operation. The loss attract a tax benefit at our UK expected tax rate of 17% which is much lower than our Q1 effective tax rate of 27%.

The relationship between the tax rates and the estimated earnings in jurisdictions where we operate increased the annual effective tax rate. The increase in the annual rate increased our Q2 tax rate to 30.8% and that had an impact of reducing EPS by about CAD 0.02 in the quarter.

And now on to slide 10 for a look at our results compared to our 2018 annual targets. You can see we're meeting all of our targets in Consulting Services but we're missing our targets in Construction Services and that's affecting the consolidated targets for gross margin as a percentage of net revenue and net income. Our consolidated administrative and marketing expenses is within the targeted range at 41.3% as is EBITDA as a percentage of net revenue, which sits at 10.3%. As previously noted, this is driven by strong performance in Consulting Services offset by disappointing results in Construction. Additionally, during the quarter we amended our syndicated credit facilities agreement, making all facilities unsecured.

The amendment extended the maturity date of our revolving credit facility and tranches B and C of our term loans. The accordion feature was also increased to CAD 400 million. This provides us with more flexibility and capacity to operate our business and drive future growth.

And yesterday, August 7, 2018, we declared a dividend of CAD 0.1375 per share payable on October 11, 2018 to shareholders of record on September 28.

Now back to Gord for a deeper dive into the operational highlights.


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## Gordon Allan Johnston

*President and Chief Executive Officer, Stantec, Inc.*

Thanks, Dan. We'll start by taking a look at Consulting Services Canada on slide 13. Gross revenue increased 9.7% and net revenue increased 7.9% in Q2 2018 compared to Q2 2017. These increases were mostly due to strong gross and net organic revenue growth of 8.8% and 6.9% respectively. We had organic net revenue growth in all business operating units with the exception of Environmental Services. We saw a slight retraction in Environmental Services mostly due to a slowdown in private sector work in Ontario.

We also had a late winter that extended into the early part of Q2. But this retraction was partially offset by growing public sector work elsewhere in the company. And we've had some good project wins and we've restarted some projects that were delayed or had been put on hold. Outside of Environmental Services, we saw growth in the private sector especially in Buildings, Energy & Resources and Infrastructure. In Buildings, we saw increased revenue in most regions. We're still seeing slow market conditions in the Prairies, but we're seeing an improving market in Atlantic Canada.

Our Energy & Resources business operating unit is doing very well in Canada. We're growing across all sectors and we're seeing increased activity from longstanding clients in all business lines. That speaks to our strong project delivery, focused account management and client relations. Increased urban development led to growth in our Community Development sector, and though we had a slight retraction in transportation, several key rail projects continued to boost that sector.

Moving on to Consulting Services in the United States on slide 14, gross revenue increased 3.9% and net revenue increased 1.9% when comparing Q2 2018 to Q2 2017. Organic gross revenue increased 4.7% and net organic revenue increased 3.3%. This organic revenue and acquisition growth was partially offset by the Canadian dollar strengthening against the U.S. dollar. Our Environmental Services business operating unit and the WaterPower & Dams and Mining sectors led organic revenue growth in the quarter. Our U.S. Water business performed well and had net organic revenue growth in the quarter. We also won several key projects which we expect to kick off in the second half of the year.

Growth in the U.S. was impacted by a retraction in our U.S. Buildings operation. This was partly due to large healthcare projects winding down. But looking at recent project wins we expect organic growth in Buildings in the second half of the year. We saw an increase in design-build projects for which we are very well positioned. Public sector work is also growing at both the state and federal levels. And although we had organic retraction in our transportation sector we have a solid strategic market position in transit, roadways and bridges and we've also begun design work on the Long Island Rail project which we won in Q1. And in Consulting Services Global gross revenue retracted 3.5%, but net revenue increased 1.9%. The retraction resulted from the impacts of foreign exchange and a decline in organic gross revenue, which retracted by 3.2%. This was mostly due to a major sub-consultant-heavy Environmental Services project slowing down in Italy. However, net organic revenue increased by 3.9%.

Water, our largest global business, is growing. And that's driven by new projects in Australia and New Zealand. We also saw a consistent revenue volume in the UK, thanks to our work on the AMP6 cycle. Mining markets continue to strengthen in the first half of 2018 and that translated into more work in Latin America and on Mining sector projects. As we said earlier, our Construction Services business continues to experience issues with legacy projects in the UK and U.S. and is detracting from our core Construction business, which is performing quite well. Again, we're looking to mitigate further issues at the project level. We're also making good progress in our strategic review which we announced in April. The goal is to evaluate a range of options to optimize the value of


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Construction Services business and provide the best prospects for our shareholders, our clients and our employees.

As of today, we're in discussion with a number of interested parties and we expect those discussions to continue through Q3. We hope to have the review finalized by the end of the year. Outside the issues we're experiencing with these legacy projects, the core UK and U.S. business is sound. When you take out the noise, Construction Services performing – Construction Services is performing to management's expectations and does have a healthy backlog. In fact backlog for Construction Services increased by approximately 11% when comparing Q1 to Q2 2018.

In the U.S. we generated CAD 180.3 million in gross revenue in the quarter and CAD 347.6 million year-to-date. We also have a steady stream of work on major water and waste water treatment plant construction projects in Florida, Texas and the western United States.

In the UK, we generated CAD 85.9 million in gross revenue in the quarter and CAD 179 million year-to-date. We are the number one water firm in the UK and revenue is driven by ongoing work for water utilities in the third year of AMP6.

Moving on to slide 17, our focus on top line growth is proving successful. Our backlog was CAD 5.3 billion at the end of the quarter; CAD 4 billion from Consulting Services, and CAD 1.3 billion is from Construction. We won a number of major projects in the quarter that I'm proud to share with you. The projects that you see on the slide are just a handful of the major wins we secured in Q2 and they highlight the diversity of our services from the offshore wind farm in Maryland to a major mine in Peru and a three-year framework with Melbourne Water.

Moving on to acquisitions on slide 18, we announced and closed our second global acquisition, this time in New Zealand. Our first is in the UK last quarter. Traffic Design Group or TDG is a transportation firm based out of – [ph] consulting (00:20:56) engineering firm based out of Wellington.

The addition of their talented team opens the door for us to bring our transportation expertise to New Zealand, where we're already a top-tier water design firm. Strengthening our North American operations are the acquisition of Norwest Corporation, an Alberta-based energy and resources firm; and Cegertec, a Québec-based top-tier engineering firm. These firms will add continued bench strength in the sectors and regions that they serve.

In total, we acquired five firms in the first half of 2018. This continues our long successful strategy of acquiring small to mid-sized firms and that allows us to grow where we need to grow and that they complement our culture and values.

Our approach is translating well into our new geographies and we look forward to more opportunities both in North America and also outside of North America in the UK, Australia and New Zealand through the remainder of 2018 and into 2019.

And finally, looking into the remainder of the year, our outlook slide on slide 19 really hasn't changed. We still believe we'll benefit from increased infrastructure spending in North America. We're still focused on expanding our global footprint and we're committed to our overall growth targets. Looking at our backlog, recent project wins, strategic acquisitions, and of course, our creative and inspired people, we're optimistic about Consulting Services and our core Construction Services business going forward. We're focused on the long term and I'm confident that we're well positioned to continue to win impactful work, execute projects with precision, grow our business and continue achieving positive results for our shareholders.


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With that, we'll turn it back to the operator to start the Q&A.

# QUESTION AND ANSWER SECTION

**Operator**: Thank you. [Operator Instructions] We will now take our first question. It comes from Jacob Bout from CIBC. Please go ahead. Your line is open.

Jacob Bout
*Analyst, CIBC World Markets, Inc.*

Q

Good morning.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Good morning.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Good morning.

Jacob Bout
*Analyst, CIBC World Markets, Inc.*

Q

Maybe just comment on the strategic review of Construction, what progress has been made to date and talk a bit about, has your thinking changed at all, are you thinking about selling part or all of the Construction business?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Great. Good question. And we were pretty sure that one was going to come up. When we announced our strategic review in April there since then we've had a lot of discussion with certainly our staff and clients, senior leadership and with investment community. So when we announced as well that we had hired a broker to help us through just to look at the value of the asset, so we started a very robust process there. Significant issue, some firms expressing issue in only the UK, some in only the U.S. But a number of firms looking at both assets, we have at this point received multiple indicative offers and based on the receipt of those offers we were pleased with both the number that we received and the indicative pricing. So right now we're in the middle of management presentations to those interested parties. So we're anticipating that we're going to – that we'll receive some letter of intent near the end of Q3, early Q4. Our preference is – would be if we did go forward with a divestiture, would be to divest the asset in one. We see a lot of synergy between the U.S. and the UK Construction business, but certainly as soon as we've made any material decisions we'll notify the market.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

That's kind of where I am. Maybe just a couple other additional notes for you, Jacob, once we complete the management meetings, the data rooms will be open for the participants to review all of our materials. We'll be


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looking for, as Gord said, indicative offers and then [ph] I'll (00:25:16) be going through their due diligence process. So it's still got a ways to go but it's progressing well certainly along the timelines that we'd expected.

Jacob Bout
*Analyst, CIBC World Markets, Inc.*

Q

In the organic growth that you saw in the Water portion of the Consulting Business, does the sale of Construction impact that outlook at all?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

No. We don't think so, Jacob. We've had a number of discussions with both the Consulting folks and the Construction folks. So, in the U.K. – sorry, in the U.S. in particular our Construction business is a construction firm that we would partner with, but we also partner with other construction firms. So, in the U.S. in particular we see limited opportunities forward to impact our revenue growth. In the U.K. we do as part of the AMP projects, there are some clients with which our Consulting and Construction groups are partnered. And there are others in which our Consulting group is a sub-consultant to Construction. So, in those cases in particular it would be important for us as we look at various parties to ensure that if we did divest in the U.K. the firm that we divested to didn't have a strong engineering group that would try to push our group out over time. But we truly – we haven't seen that to be a significant concern at this point in the process.

Jacob Bout
*Analyst, CIBC World Markets, Inc.*

Q

Last question here, just on the organic growth that we saw in the Infrastructure, so it's negative from a net revenue perspective. You made some comments there about some of the projects were coming to a close. Can you comment a bit on – it's just stage of projects or is there – they're just – win rates are a little lower here or maybe just comment a bit about backlog and bookings that you saw in the Infrastructure and Consulting group?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah. Sure. In Q2 2017, we were flat-out on a number of these design-build projects that we were working on in the southern United States. So, that was a particularly high quarter. As I look back, I see in Q2 2017, our net revenue growth was 7% over the previous year. So, we are coming off a pretty high comp as well because we are flat-out on those projects. So, I do think it's just a little bit of a blip there. As we mentioned we have – really are starting to engage on the Long Island Rail Road project in the U.S. and a number of other projects that we mentioned there in North Carolina and so on. So, I think it's just a blip. I think we'll see that come on again, strengthen into Q3.

Jacob Bout
*Analyst, CIBC World Markets, Inc.*

Q

Okay. Thank you very much.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Great. Thanks.


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**Operator**: Our next question comes from Sean Eastman from KeyBanc Capital Markets. Please go ahead. Your line is open.

Sean D. Eastman
*Analyst, KeyBanc Capital Markets, Inc.*

Q

Hi, gentlemen. Thanks for taking my questions. I'd just like to start on the top line, so really accelerated the [ph] Water (00:28:26) intake this quarter, you guys seem to be indicating some of the softness in Buildings and Infrastructure is set to reverse. So, I'm just wondering is it safe to assume some pretty healthy acceleration in organic growth through the back half of the year and how are you guys feeling about being able to hit the upper end of that low-to-mid single-digit organic growth target for the year?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Well, I think a couple of things. We are achieving that low-to-mid single-digit now and getting closer to the upper end of that. I think when you compare or look at some of the comparables that we have over 2017, I think we're still looking to achieve the same kind of growth as what we've seen in the first half. So, we haven't materially changed our outlooks for the remainder of the year. We've sat down with all of our leadership and are looking at our forecasts and they're coming in largely where we expected them to. So we're confident that we'll be able to still achieve some organic growth. It's always difficult to pin that write-down but...

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Right. But our guidance had been at low to mid single-digit and I think that's where we see the back half of the year as well.

Sean D. Eastman
*Analyst, KeyBanc Capital Markets, Inc.*

Q

Got it. Okay. That's helpful. And then really encouraging to see the EBITDA margin in Consulting Services well above the targeted range, and we're tracking ahead of the midpoint of that range in the first half here. I'm just wondering kind of what needs to happen in the back half for us to end the year toward the upper end of that range, maybe what the big swing factors would be and whether there's some seasonal aspects that we should be considering?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Sure, Sean. I think it's – again we talked about operational effectiveness. We talked about certainly maintaining our gross margin, but it also ties back to utilization and making sure our staff are utilized on direct projects. I think we'll probably see similar utilization in Q3 as we're in the summer months, but we always have that seasonality in Q4 which tends to drive down utilizations to some extent, and thus the EBITDA margin. So, I think over the year we'll see a bit of a normalization probably come down in Q4, at least I expect it to, that would be normal with what we've seen in prior years due to the – what happens in the fall with holidays, vacations and things of that such.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

And the other part of it of course is our ongoing cost control initiatives and we spoke about them a bit in the Q1 call and you see again that we're down 100 basis points over last year, quarter-over-quarter. So we're keeping


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our focus on the cost control side of things as well. So, working on continuing utilization to keep that higher, working on the cost side, so I think it's the balance of attracting additional revenue, executing it well and keeping the cost side under control and certainly we won't be removing our focus on any of those items.

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**Sean D. Eastman**
*Analyst, KeyBanc Capital Markets, Inc.*

Q

Got it. And just lastly, just a follow-up on the cost control side, would you kind of characterize this as just keeping cost under control at this point or are there still items you're targeting that could be more kind of chunky impacts in terms of cost takeouts?

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**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah, we don't see that there is material cost takeouts, it's about maintaining that control...

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**Sean D. Eastman**
*Analyst, KeyBanc Capital Markets, Inc.*

Q

Yeah.

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**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

...now that there are little pockets within the organization that we want to continue to pay attention to, but beyond that, it's about managing the business as tightly as possible.

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**Sean D. Eastman**
*Analyst, KeyBanc Capital Markets, Inc.*

Q

Got it. Okay, thanks so much. Thanks so much, gentlemen. I appreciate it.

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**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

Thanks, Sean.

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**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Thanks, Sean.

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

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**Devin Dodge**
*Analyst, BMO Capital Markets (Canada)*

Q

Hey. Good morning, guys.

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**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Good morning, Devin.

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Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good morning, Devin.

Devin Dodge
*Analyst, BMO Capital Markets (Canada)*
Q

Just wanted to come back on the margin kind of question here, but it seems like historically Q3 represented the high watermark for, I guess both net revenues and EBITDA margins for their Consulting business. I don't want to trap you guys into try to provide guidance here, but is there any reason that we should be thinking about why this pattern wouldn't hold in 2018?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

I would expect the pattern to be consistent in 2018. This is where our entire business gets busy especially areas like Environmental Services gets a lot busier. We had a late spring, pretty harsh winter and we can't get out into the field. We see some of that in transportation as well. So, I'd expect to see similar, assuming the weather holds, similar results to what you would have experienced in prior years.

Devin Dodge
*Analyst, BMO Capital Markets (Canada)*
Q

Okay. That's helpful. And I guess can you provide some color on the organic growth that you're experiencing in the Energy & Resources sector? Just trying to get a sense for how sustainable the stronger revenue performance is for this business given that your outlook suggests a modest recovery in the sector?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Yeah. We're seeing lots of activity in all of our business lines in Energy & Resources. We see it in Mining. After years of operational improvements a lot of our clients have strong balance sheets and so we're seeing them to begin to roll out some capital projects. Power is really strong for us. We're seeing a lot of conversion from hydrocarbons to renewables. We're working on that. We're seeing a lot of interest in storage of course. And that Power group is almost half of our Energy & Resources business. So a number of years ago, we were very, very heavy on Oil & Gas. Certainly, you saw the retraction of that over the last number of years; now Power is over half of that Energy & Resources business, but we are seeing that Oil & Gas is rebounding.

And I think we've talked in previous quarters about our strategy of staying with our clients during the downturn and that's really paying off now as we're starting to see some strengthening in the Oil & Gas market. So that's – I do see some continued growth and some continued strong tailwinds in Energy & Resources for the remainder of the year.

Devin Dodge
*Analyst, BMO Capital Markets (Canada)*
Q

Okay. That's helpful. Thank you.

**Operator**: Our next question comes from Mona Nazir from Laurentian Bank. Please go ahead. Your line is open.


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Mona Nazir
*Analyst, Laurentian Bank Securities*
Q

Good morning, and thank you for taking my questions.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Good morning.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good morning, Mona.

Mona Nazir
*Analyst, Laurentian Bank Securities*
Q

I was just wondering out of your current head count, how many individuals are currently in the constructors (sic) [Construction] (00:35:42) division?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good question. I think it's around 2,100 in total or something like that, Mona.

Mona Nazir
*Analyst, Laurentian Bank Securities*
Q

Okay.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

And it's roughly equivalent split between the U.S. and the UK but perhaps a touch heavier into the UK.

Mona Nazir
*Analyst, Laurentian Bank Securities*
Q

Okay. Okay. And then just your comments around the constructors (sic) [Construction] (00:36:09) division and you were saying that you were hoping to finalize a deal by year-end and that you could sell the entire constructor (sic) [Construction] (00:36:16) division to one party or break it up into the UK footprint and then the U.S. segment. But I'm also seeing wording that, we're looking at a number of strategic options to optimize the value and now you're putting on hold some of the fixed price work. I'm just wondering and really wanted to confirm that there are no other options being contemplated outside of an outright sale. Would that be correct?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Well, I think that we can't – given where we are in the process, we can't definitively say that we're going to accept an offer that comes in that would be too low or well below the value of the business. So to pin us in a corner like that and say we're absolutely going to sell the entire thing I don't think is the right thing to do for shareholders, for clients or our employees. So we believe the – as Gord mentioned in the opening comments, we believe that the indicative offers that we got are good, relative to what we were expecting. So, we just have to continue on to the


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process. So I don't think it's quite right to say it's absolutely 100% for sale, but certainly that's the direction we're headed if we get appropriate results through the process.

---

Mona Nazir
*Analyst, Laurentian Bank Securities*

Q

Okay. Perfect. Yeah. That's what I was referring to. That's your kind of top choice or what you would like to see from the division. And then just secondly, I have a confirmation question and sorry, Dan, if I missed this, but your comments were related to bidding on some of those waste-to-energy projects four years ago if I'm correct and was that related to the CAD 16 million UK charge and also is that legacy work?

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Yes and yes. It was 100% related to the waste-to-energy projects of which two are now finalized. As I mentioned, we have a signed lease indications of agreement and we're expecting to get those closed very shortly. And then the third project, we've actually made some significant progress in the quarter and since the quarter of getting what they call turnover where essentially we've got the plant up and running, it's functioning. We achieved a key milestone at the end of July. So that's moving forward as well. So we're expecting that we'll get that thing resolved in Q3 and so that's looking a lot more positive than it did, say, six months ago.

---

Mona Nazir
*Analyst, Laurentian Bank Securities*

Q

Okay. And so the CAD 16 million was legacy work from four years ago.

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

[ph] That's correct. (00:39:09)

---

Mona Nazir
*Analyst, Laurentian Bank Securities*

Q

And then the CAD 3 million in the U.S. hard-bid project, that was also legacy. Was the CAD 5.1 million U.S. design-build also legacy?

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

That – that's a comment that CAD 5 million is also obviously legacy coming from Construction. But it relates to a major manufacturer that we – if you recall, we had some project hits in Q4 and we made some recoveries in Q1 on the Consulting side. This is now that normalization of the combined project, as it has to be accounted for, achieving a normal margin over all of the Consulting and Construction. And so we've taken a very hard look at that, our estimates to complete and that is the remainder on that one. We don't expect any more significant breakdowns on that project, but yes it was started before Stantec had acquired MWH.

---

Mona Nazir
*Analyst, Laurentian Bank Securities*

Q

Okay. That's very helpful. Thank you.

---


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Thanks, Mona.

**Operator**: Our next question comes from Yuri Lynk from Canaccord Genuity. Please go ahead, your line is open.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*
Q

Hey, good morning.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good morning, Yuri.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*
Q

Good morning. In Q1, you had some execution issues in the Consulting Services Building (sic) [Buildings] (00:40:36) segment that negatively impacted the prior quarter. Can you just give us an update on those projects if they had any impact on Q2 in the Building (sic) [Buildings] (00:40:48) segment?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

We made some significant progress between Q1 and Q2 and in improving our execution in Buildings, we've put a lot of emphasis on that, some additional leadership and project management expertise to mitigate some of the issues. We certainly have taken a hard look at our estimates to complete on these projects. We're making what I would say a continued progress in the Buildings sectors as we said we were going to do at the end of Q1.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*
Q

So what would you say the odds are of – kind of what a – would sound like a surprise at this point. But further negative cost reforecast on some of those building projects, or you feel you're out of the woods on those and I'm talking obviously within the Consulting business?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Yeah. We think we're largely out of the woods, and always a key part of project management is always doing your earned value and looking forward on what your estimates to complete are. And that's where we're really focusing our attention on some of the projects that are nearing completion. But we think for the large part of it, we are through the worst of the execution issues there.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

And I think we made – we commented as well that we do see Buildings returning to positive organic growth in the second half of the year.


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Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*

Q

Okay.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

And I think it's also fair to note that some of those projects, a good number of those projects related to acquired projects, where the margins were not necessarily available to us post-closing the acquisition. So we're through the worst of that as well.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*

Q

Okay. Can you elaborate a little bit on the loss of architectural clients you're seeing in the U.S. from some of these acquired firms and how you can stem that within the Building (sic) [Buildings] (00:42:53) segment?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Sure. The way that works is, the architectural industry and the engineering industry collaborate and work together and generally the engineer is the sub-consultant to an architect on any project. As we acquire engineering firms, buildings engineering firms, the architectural firms that those firms would have worked for don't necessarily want to work with Stantec because we are an integrated architecture engineering firm. So what we're talking about is losing some of the external architecture clients but picking up Stantec architecture internally as a client which offsets some of that external revenue that we'd be losing. Hopefully, that's clear and not too circular.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*

Q

Clear as mud. No. I got it. A last one, just real quick, the three buckets of problem projects, the waste-to-energy, the U.S. design-build and the U.S. hard-bid, the waste-to-energy, can I assume this one is done in Q3 or is there a chance of a [ph] loss cost (00:44:07) reforecast if it's starting up and running? It's finished or...?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

We're – in our Q2 accounts, we had assumed that this would take us to the end of July in terms of our estimates to complete to get this thing up and running. We achieved that. I think, there are still some ongoing issues with the actual performance of the plant which will continue a little bit, but certainly we don't expect it to be anywhere near the cost impacts that we've seen to date on this project. So we figured that it's improving and then it will move over into O&M which we don't have any projected downside on at all.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*

Q

Okay. And then, the two other U.S. projects, are these finished now or?


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

The U.S. hard-bid projects are essentially complete. I'm just looking at my notes here and they're all in the 99% – 95%, 99% complete. So, not expecting any material impacts there again. We did talk about the Industrial project, it's really related to the last six months really of getting that sorted out between Construction and Consulting, so we think we're there as well. But you never know with Construction projects, they can always surprise you with change in environmental conditions, site conditions and so on.

Yuri Jonathan Peter Lynk
*Analyst, Canaccord Genuity Corp.*

Q

Yeah. Okay. Okay. I better turn it over. Thanks for the update.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Thanks, Yuri.

**Operator**: The next question comes from Benoit Poirier from Desjardins Bank Capital Markets. Please go ahead. Your line is open.

Benoit Poirier
*Analyst, Desjardins Securities, Inc.*

Q

Yeah. Good morning, gentlemen. And I just want to circle back a little bit on the Construction, you made some great comments, great color about what could turn wrong in the third quarter, but if you strip the potential impact with the waste-to-energy project, what type of margin we might see in the second half for Construction? Is it fair to say that it should be ranging between 7%-9% which is mostly in line with the guidance provided for the year?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah. I think that's what we should expect, stripping out any project execution as you see. As we've said the core business in the UK is operating well, we don't see a lot of organic growth there because it's tied into the AMP6 programs and we're now bidding AMP7. And the U.S. business, the core business is performing well as well, stripping out the legacy projects. So, yes, I think if without any project issues we expect a return to better EBITDA margins.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Yeah. Absolutely.

Benoit Poirier
*Analyst, Desjardins Securities, Inc.*

Q

Okay. And Oil & Gas you made also great comments about firing in all cylinder, Power, Oil & Gas, Mining, but would it – could you break down a little bit where we experienced the strongest growth? Would it be in Power? Or mostly Oil & Gas that bring the number high to close to 32%?


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**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*
A

No, I think we're actually seeing really strong activity and growth in all of our business lines. WaterPower & Dams is good. Power is good, Mining, Oil & Gas, we're seeing some great growth, great project opportunities, project wins in all of those groups. So we saw a 32% quarter-over-quarter, admittedly coming off of a low comp a year ago, but we're feeling pretty good about it.

**Benoit Poirier**
*Analyst, Desjardins Securities, Inc.*
Q

No, that's pretty good. And could you comment a little bit about the pricing in Environment, whether it should improve as the business becomes greater and if we could see a slight expansion on gross margin?

**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*
A

We've been in discussion with a number of our clients. When the oil and gas industry turned down, they were pretty quick to come at us with fee reductions, us and all of our competitors. Now that things are getting stronger, we're hiring significantly, we're going back to talk them about expanding, growing our fees, we're having some success, but certainly the fees came down faster than they're going up. That said, we are getting some movement in an upward movement of fees but it's certainly not as fast as they came down.

**Benoit Poirier**
*Analyst, Desjardins Securities, Inc.*
Q

No, okay. And in terms of M&A, you perform five acquisition year-to-date; however, given the strategic review of Construction, should we expect kind of a slowdown in the pace of M&A or not at all?

**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*
A

Yeah. No, we don't see any slowdown in our pace of M&A, Benoit. And in fact, we've been focusing significantly on refilling the M&A pipeline following the – following MWH we did from a plan perspective take a bit of a hiatus as we integrated that. But over the past six months to a year, we've been working hard to fill that pipeline both in North America but also in the UK and in Australia and New Zealand, sort of the three locations outside of North America where we stated that we're focusing. I do think you'll see some increased momentum through the last half of 2018 and into 2019.

**Benoit Poirier**
*Analyst, Desjardins Securities, Inc.*
Q

Okay. That's pretty good. And last one for me, for Consulting in the U.S. you mentioned that some key water project will kick off in the second half. Could you comment about those project, the size and what could be kind of the magnitude we might see in the second half?

**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*
A

Sure. We've achieved – we've won a lot of projects in our Water group over the past quarter, pretty broadly spread. I think we've press released a nice one that we won in Louisiana. We've press released I think, we've won some good work recently in the northeast with some of the large cities up in that area. So it's pretty broad-based, Benoit, in terms of the wins, some of the larger ones we have – we've press released but just a real solid growth


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and even though [ph] small- to mid-sized (00:50:52) projects. So it's pretty robust in the Water sector. We had a couple slower quarters in early Q4 of last year but we really feel like we've recovered well in [ph] Q1 and Q2. (00:51:06)

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Benoit Poirier
*Analyst, Desjardins Securities, Inc.*

Q

Okay. Thank you very much for the time, gentlemen.

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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Thanks.

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Thanks very much, Benoit.

---

**Operator**: Our next question comes from Mark Neville from Scotia Bank. Please go ahead. Your line is open.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Hi, good morning, guys. I just want to follow-up a few – a lot of questions actually, just first on the strategic review. I think you mentioned you've received some indicative offers. I'm just curious if you received offers for the entire asset, if that's the case?

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yes.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Okay.

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

For both U.S. and UK, yes.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Right. So obviously this has been a big drag in recent quarters, but you sound fairly positive on the core business. So I'm just trying to I guess, is there a scenario or can you envision a scenario where I mean, obviously everybody has to do due diligence. But again, you don't get maybe a price that you find attractive [ph] or (00:52:03) you actually end up keeping and running this business?

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A


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The core business is really solid and as you see from the provisions that we took in Q4 of last year, the provisions that we took this quarter, we're really cleaning up those legacy projects, putting a lot more certainty back into the business and I think that makes it more attractive for potential acquirers. So any – I guess there's a possibility of any scenario occurring but certainly based on the interest that we've seen to date, I don't think that's a significant possibility, but you can never say never, I guess.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Okay. And I guess in that scenario you – again you would just continue to run it, and again as opposed to winding it down, if that [indiscernible] (00:52:55).

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

So, the core business is solid, so I think you're right. If we did not proceed with the divestiture, the core business being solid now that we've kind of reined in from some of these projects they took on three or four years that got them in trouble, we think it is a very attractive asset. As we look at other firms that have experienced exposure to Construction, we think it's an attractive asset, perhaps more attractive to one of those firms. But should – we believe it's a good asset. And as Dan mentioned earlier, if – this isn't a fire sale, so if we got fire sale pricing, we might look at that and say on behalf of our clients and our shareholders a divestiture would not be the right thing. But to-date our indicative pricing hasn't led us to think that would be the case. But time will tell.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Okay. I understand that's all probably reasonable. I guess just on the

margin in Consulting, in Q2 very strong, I guess the G&A efficiencies that you've achieved, they seem sustainable, maybe a little more to come. Q3 again seasonally strong. So, just trying to get a sense for – maybe if you can handicap the 11% to 13% range, I guess your confidence in coming sort of above midpoint or closer to the high end at this point just given where we're trending?

[Technical Difficulty] (00:54:21-00:54:57)

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**Operator**: Ladies and gentlemen, please stand by. We're just experiencing momentary interruption in today's conference call. [Technical Difficulty] (00:55:06-00:55:48)

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Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Mark, are you there? We got cut off again.

---

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*

Q

Yeah. I'm here. Can you hear me?

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Sorry about that. We can hear you now. Yeah.


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Sorry. We don't know what's going on.

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*
Q

So, did you get that question?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

No.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

No. Could you repeat that, please?

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*
Q

Yeah. It's just on the margin in Consulting. Obviously Q2 is quite strong, the G&A, the efficiencies seem sustainable, maybe a little more to come, again gross margin has been fairly steady. So, just – again just trying to handicap sort of the 11% to 13% range for the year, sort of where you think you land at this point whether it's sort of closer to the high end. Again just given sort of where you've been at Q3 being seasonally strong and the efficiencies you've achieved.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Yeah. I think tied into a previous question that we had is again, we expect Q3 to be similar to Q2 in terms of margins, they generally operate around the same. And then lower at the end of the year. So the expectation is that we will fall in within that 11% to 13% by year-end. We could be at the top end, but I would suggest it would be from middle to top end, given our current performances, especially in Consulting.

Mark Neville
*Analyst, Scotia Capital, Inc. (Broker)*
Q

Perfect. Yeah. Thank you very much.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Thank you.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Thanks, Mark.

**Operator**: Our next question comes from Ben Cherniavsky from Raymond James. Please go ahead. Your line is open.


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Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Good morning, guys.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Good morning, Ben.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good morning, Ben. And we'll try to stay on the phone throughout your whole question.

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Yeah. It's a pretty simple question. I just – at least the first part of it. I'm just curious, in the disclosure around the drag like when you segment the Construction Services business down to the EPS and you say it lost CAD 0.17 per share and that the specific projects that you identified accounted for about CAD 0.17 a share of special costs. Is that the – am I reading that right first of all?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Yes. So, what we – certainly there is overhead costs and allocations and everything else in the numbers to get [indiscernible] (00:58:15) and certainly the tax impact, all of those things combined bring us down from EBITDA numbers down to a CAD 0.17 per share loss.

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

But – so if you didn't have – if these special projects or special costs hadn't transpired, Consulting would have been breakeven. And so I guess my question is, would that have been satisfactory for you in and of itself like that, I mean, you guys presumably would have expected this business to remain profitable without any kind of special costs or projects that went sideways. So is there anything else going on?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Absolutely.

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Yeah. So but it appears that it would have only been breakeven.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

No. We expect it would have achieved a profit, Ben, in the quarter without this, actually some of the core business actually did achieve a profit which offset the Construction losses, project losses.


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Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Right. But you said adjustments related to these projects negatively impacted EPS by CAD 0.17 and that you reported a CAD 0.17 loss. So, without the negative impact it would have been zero on a normalized basis?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Yeah. And perhaps that maybe isn't quite articulated correctly down in that. We would have achieved, I believe some earnings in Construction without these project losses.

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Okay. All right. I just wanted to clarify that.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Okay.

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

And then just you go back, what's it been, two years now since the MWH acquisition. If we'd had a conversation two years ago about what 2018 might look like, I assume these issues in Construction wouldn't have been part of what you expected. So, what is this – what are the lessons learned, and what does it say about the due diligence process you went through in acquiring MWH? And what are some of the takeaways and lessons learned now that you've gone through this experience, because I can't imagine this has gone according to plan?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

The Consulting business has more or less gone according to plan. We certainly have seen a lot of synergies and opportunities around the Consulting business. You're right, the Construction business absolutely has not gone according to plan and nobody anticipated these kind of losses from these legacy projects. Even the Construction folks didn't expect that for all three of these waste-to-energy projects, they were supposed to achieve – have achieved significant margins, but they were new projects. They were in an emerging business opportunity and they were very early in their stages as a couple of them hadn't even quite started when we were in discussions early in 2016.

So the – there's not much we could have done from a due diligence perspective, Ben, on those projects. The other projects around the legacy hard-bid projects, we did know about those and we did put appropriate provisions in based on what we knew at the time. Certainly again not enough based on what we've seen in the last couple of quarters, but now we believe we're through the worst of that for sure.

With respect to learning more about or doing more around due diligence, we've done a number of things not only with the MWH acquisition, but you're always learning as you do due diligence and where you need to place more emphasis. We're placing a lot more emphasis on projects, project margins, making sure that our due diligence process is really picking up weaknesses and in project execution looking at the margins that have been recognized to-date on the project, what's remaining from an estimate to complete perspective. We're doing a lot


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more due diligence there. We're being more conservative in terms of our opening balance sheet and if we do believe there are additional costs to incur, we're going to record that appropriately, as appropriately as we can on the opening balance sheets. And at the same time is really working hard on just uncovering everything we possibly can. But we've had a good track record on due diligence. The Buildings groups have been difficult for us in the U.S. over the last couple of years. We haven't seen other than these Construction projects any material weakness in our due diligence in the Consulting business and Water. It's actually performing exactly as we expected it to.

---

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Yeah, and – no, of course, I mean I guess there's a tendency to think you're only as good as your last game, but definitely you guys have had – this is more the exception than the rule with respect to due diligence. I wonder if it means anything about future acquisitions that might come with Construction. I mean, I don't want to box you in or – never say never, but would you be -would this make you more reluctant to go out – to pursue a similar kind of acquisition with the Construction Services business attached?

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Yeah, And Ben, I don't think that we had ever thought that we were going to pursue a firm that had Construction. It just happened that MWH was such an attractive firm in the Water space. But I think certainly, we've learned a lot about due diligence. We've learned a lot about Construction. But as we're going through our strategic review, I think we're seeing that this probably isn't something that fits into our long-term plans. So we certainly – this would be something we would look at going forward.

---

Ben Cherniavsky
*Analyst, Raymond James Ltd.*
Q

Okay. That's helpful. Thanks, guys.

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Thanks, Ben.

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*
A

Thanks, Ben.

---

**Operator**: The next question comes from Maxim Sytchev from National Bank Financial. Please go ahead. Your line is open.

---

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*
Q

Hi. Good morning.

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*
A

Good morning, Max.


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Hi, Max.

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

I was wondering if it will be possible to have Q3 and Q4 Construction EBITDA numbers for last year so that we can sort of properly stagger the progresses?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

I think we have that in our disclosures last year. I don't know the – I don't have it handy at my fingertips right now, Max, but certainly I can get that for you. I think we disclosed that.

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

Yeah. I would appreciate – Okay. No, well, I'll double-check. And then the other thing is while in your cash flow commentary you talk about the drain of [ph] CAD 62 million (01:05:21) in Construction Services. So how should we envision the cash flow dynamic post the sale, are you expecting a material free-up or how should we think about that?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Yeah. We expect to achieve some improved cash flows coming from a sale. We also expect to improve our cash flow from operations on the Consulting business. Our day sales aging has gone up and that's an area of focus for us going forward for the remainder of the year to improve that as well.

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

And the day sales have gone up exactly why?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

It's just that you get busier in the summer months. We've seen the WIP and the AR go up around CAD 60 million from year-end. Now, that's just the trajectory of the business. But the aging needs to come down and we'll be focusing on that in Q3.

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

Okay. In terms of, I know that right now you have broken out Consulting versus Construction but post the Construction hopefully divestiture how should we think about SG&A on a consolidated basis? Is there any potential sort of further pickup for you guys or how should we think about that?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A


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Again, an area of continued focus, but I don't think you're going to see material pickups as I mentioned again and third quarter should be similar to second and fourth will be lower similar to the first quarter.

---

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

Right. And then last quarter, correct me if I'm wrong, you were talking about some major midstream projects going and having you feeling better about Energy & Resources. So, can you maybe provide an update relative to your commentary in Q1 on that front?

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

One of the major projects is again we don't name these but it's still subject to I think a special license if you will.

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Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

[indiscernible] (01:07:30) Okay.

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

And so we are beginning – we've kind of slowed down and done minimal work on that. We're starting to see that progress with some changes in the macro environment there and so that should help us into the fourth quarter. There are other projects that we're waiting for FID on that if those proceed that should help us as well.

---

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

And how material the potential LNG go-ahead could be for you on a going forward basis?

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Really our exposure there is going to be in the transmission of product to the port and there may be some environmental work around the port facilities.

---

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Transportation...

---

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Transport – yeah, and, yeah, any other Infrastructure work. The real heavy lifting around the port I believe that an offer was Fluor, they got the early indication from LNG Canada, it was either Fluor or Jacobs.

---

Maxim Sytchev
*Analyst, National Bank Financial, Inc.*

Q

I think it was Fluor and JGC.

---


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**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah.

---

**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Yeah. On that one. So, but we wouldn't be involved in necessarily the terminal work per se from an engineering perspective, but we certainly could see some environmental work, Gord.

---

**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

Yes, absolutely. Yeah.

---

**Maxim Sytchev**
*Analyst, National Bank Financial, Inc.*

Q

And then maybe just the commentary around capital allocation, I mean obviously it looks like again big focus on M&A capital allocation. I mean, obviously, it looks like again big focus on M&A sort of share buybacks. Do you mind maybe qualifying where you want to be spending the improving free cash flow on a going forward basis?

---

**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Certainly, we're looking at the growth of the business, so reinvesting it back into the business and if we have surplus cash, we'll be paying down debt to drive down the debt levels.

---

**Maxim Sytchev**
*Analyst, National Bank Financial, Inc.*

Q

Okay, so no share buyback focus right now?

---

**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

At the appropriate price, Max. Again, we look at where we believe the shares are undervalued. I haven't looked at them yet today. I'm not sure I want to or I need to. But certainly, where it gets below a certain value, then we will buy back shares where we believe it's too low.

---

**Maxim Sytchev**
*Analyst, National Bank Financial, Inc.*

Q

Okay. All right. That's it for me. Thank you very much.

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**Daniel J. Lefaivre**
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Thank you.

---

**Gordon Allan Johnston**
*President and Chief Executive Officer, Stantec, Inc.*

A

Thanks, Max.


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**Operator**: Our final question comes from Chris Murray from AltaCorp Capital. Please go ahead. Your line is open.

Chris Murray
*Analyst, AltaCorp Capital, Inc.*

Q

Yeah. Thanks, guys. Good morning. Just quickly, Dan, on some of the cost reforecasts that you've booked right now, how much should we think that those have a reserve component into them and that – do you guys have any opportunity to go back to third parties and get any recovery for any of those costs?

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

The reserve – we always try to be conservative in the estimates to complete. So there is some contingency built into these reforecasts on the projects. A lot of these as I said before are virtually at completion. So there isn't going to be a lot more cost to incur. There are a few projects that still have some completion to do. So we want to be conservative there. That was the first part of your question. Second part was?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

[ph] Recoveries. (01:10:42)

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Recoveries, yeah, sorry. We have – we're tracking at about $20 million of potential recoveries on the projects that are remaining. So we haven't recognized the full amount of revenue or recovery on these projects, where there's potential of around $20 million in terms of recoveries. Now these are not certain. We're being fairly conservative in that regard. And still it results in either litigation settlements, having change orders that have not been accepted, et cetera, et cetera. So that's the process that you go through on these construction projects and certainly we're pursuing that if that will be certainly an area of discussion in the sales process and how those are treated. So it's certainly another area of focus for us.

Chris Murray
*Analyst, AltaCorp Capital, Inc.*

Q

Okay. Great. And along those lines you did mention you're talking a little bit about AMP7. Does your divestiture or your plan, your thinking around the strategic review of the Construction business, is that impacting your ability to bid AMP7 at all?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

No, we don't believe so and in fact we already with our Consulting group won the first and we press released this one a while ago, the first AMP7 award which was in Yorkshire, and that was completely a Consulting award. So we don't see that being an issue. A lot of the contracts that we have in fact are a five or a six, seven-year contract with the opportunity to roll it over and sort of re-up it. So we don't see a significant loss of opportunity in AMP7 should we divest of Construction.


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### Chris Murray
*Analyst, AltaCorp Capital, Inc.*

Q

Okay. Fair enough. And then the – just the last question for me, just – you kind – we kind of talked a little bit about M&A but I'm just wondering if there's been any change or any thought around what's going into your pipeline at this particular point, are we still thinking, you talked about the strategy and part of the MWH strategy when you acquired it was to be able to take what you've done in Canada and the U.S. and start leveraging it in other parts of the world. If you were to think about where your portfolio is right now in terms of potential M&A targets, is that still the case or is it starting to change a little bit your thinking around what you want to add to the portfolio just [ph] as we can see (01:13:20) some shift in certain of the segments?

### Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah, I know. A very good question, Chris, but very much so that is remains our strategy. For example in the UK, we're easily the number one water firm, but we're single-sector Water. Now we've added ESI. So we have a small environmental footprint as well. So when you look at all the service offerings of Stantec and the opportunities to bring in additional service offerings to our existing clients, we can expand there in transportation and Buildings and more Environmental Services and all of our – the service offerings that we have in North America. We see the opportunity to use Water as sort of the thin edge of the wedge to get us continued growth into the UK and a similar strategy in Australia and New Zealand.

So we certainly are not taking our foot off the gas from a North American acquisition perspective, but we are really focusing as well on those three locations, primarily the UK, Australia and New Zealand.

### Chris Murray
*Analyst, AltaCorp Capital, Inc.*

Q

Okay. And is Brexit changing – I mean, Brexit has been morphing but is it changing either the response from potential sellers in the UK or changing multiples or doing anything like that?

### Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

We're really looking at Brexit hard in terms of what it could do to overall industry there, you're starting to see of course in the papers the – some manufacturing clients are starting to be concerned about their supply chain and what that could look like. But really the work that we do, that core infrastructure work we see in the UK as an example, a lot of commitment from the government to continue to build housing. We're looking at high speed too, the rail, we're looking at a lot of school and hospital work that has been announced. So a lot of the core infrastructure work that we still do is will be strong, we believe there.

### Chris Murray
*Analyst, AltaCorp Capital, Inc.*

Q

All right. Thanks, folks. I'll leave it there.

### Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Great.


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Thanks.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Thanks, Chris.

**Operator**: We'll now take our next question from Derek Spronck from RBC Capital Markets. Please go ahead. Your line is open.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Okay, great. Thanks for taking my questions.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Good morning, Derek.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Good morning. Just quickly, I think you've largely answered it, but if you were to get a significant proceed from the sale of the Construction business, any particular plans for that proceed or as you mentioned it would just fall within your capital allocation priorities that [ph] you mentioned (01:15:57) previously.

Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

I think there's a couple of things I just – we don't know the exact details yet because we don't have any – we're not far enough along in the process but there will be a potential tax impact in the U.S. That business is not unlike [indiscernible] (01:16:18) but certainly not to the same extent where that business has been growing largely organically, so there's not a very high tax basis for the U.S. asset. So that could have a bit of a drain on the net cash received because we'll have to pay tax. But the remainder of whatever we earn or get from that sale would be going straight to paying down debt.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Okay. Yeah. Makes sense. And the acquisitions that you've completed year-to-date, how should we think of that run rate revenue lift in 2019 from currently completed acquisitions?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

The ones that we've completed to date have been near the smaller size of our range, 250 people, 300 people and smaller. So I don't know that it'll have, Dan, you could comment, but I don't know that it would have really at this point what we've done so far a material impact going forward. We're still as we look at the acquisitions, our sweet spot is really still in that 1,000 person or less range and that's where we'll continue to focus. So I think the ones


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that we've announced and closed on so far, Dan, unless you have any thoughts, we've probably added less than 1,000 people on our 22,000. So – yeah.

---

**Daniel J. Lefaivre** A
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

It's going to have a couple of percentage, I think...

---

**Gordon Allan Johnston** A
*President and Chief Executive Officer, Stantec, Inc.*

Yeah.

---

**Daniel J. Lefaivre** A
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

...on a full year run rate basis. Certainly, as we look at more acquisition opportunities we expect that to go up through the remainder of the year.

---

**Derek Spronck** Q
*Analyst, RBC Dominion Securities, Inc.*

Yeah. Okay. Okay. And just one last. Sorry, go ahead.

---

**Daniel J. Lefaivre** A
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

Go ahead. So I think it's going to be about 300, probably [ph] 300,000 (01:18:15) impact year-to-date or going forward.

---

**Derek Spronck** Q
*Analyst, RBC Dominion Securities, Inc.*

Okay.

---

**Daniel J. Lefaivre** A
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

[ph] Those are (01:18:22) 300 people.

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**Gordon Allan Johnston** A
*President and Chief Executive Officer, Stantec, Inc.*

That might be 300 people.

---

**Daniel J. Lefaivre** A
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

Sorry, 300 people is what we've added year-to-date. So, you do your metrics on that.

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**Gordon Allan Johnston** A
*President and Chief Executive Officer, Stantec, Inc.*

Yeah.

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Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Yeah. Yeah, okay. And just more generally, the public money flowing in the U.S. from a state and federal level. Is that coming down as expected and as quickly as expected, or how do you see that environment right now in the U.S. from a public infrastructure spending perspective?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah. We've all been talking for six months or more about the opportunity for a comprehensive infrastructure bill in the U.S., and we haven't really seen that come to fruition yet. That said, the market is still really robust even without that additional funding. So, if we do see a comprehensive infrastructure bill in the U.S., I think that will only add to an already fairly robust market. But we haven't really seen a lot of that coming yet.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Just in general, is the bidding environment more rational because of the amount of work both on the private and public sector side?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah. We're seeing actually a number of contractors beginning to talk about restricting the number of projects that they would bid on, because they're reaching capacity in the U.S., and we're seeing that from some engineering firms, us included, being more selective on what we can bid on. So, we're seeing less just people just chasing whatever they can find to stay busy and becoming a little bit more discerning.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

On the flip side, does that – any concerns around labor inflation in that sort of environment or...?

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Yeah. Absolutely. That's something we're monitoring on a daily basis. We're seeing poaching between firms becoming more and more common. So we're doing all we can to ensure that we stay competitive in these markets and ensure that we are – that we remain competitive. So there is some salary pressure. There is also just general pressure on ensuring that your staff are treated well and that they feel valued and give them interesting projects and geographic opportunities to move around. So we're seeing a lot of that in the first half of the year and I anticipate that that will be the same in the second half.

Derek Spronck
*Analyst, RBC Dominion Securities, Inc.*

Q

Okay. All right. All right. That's great. Thanks, thanks for taking my questions.

Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

A

Great. Thanks, Derek.


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Daniel J. Lefaivre
*Chief Financial Officer & Executive Vice President, Stantec, Inc.*

A

Thanks, Derek.

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**Operator**: As there are no further questions from the phone, I'll now turn the call back to your host for any additional or closing remarks.

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Gordon Allan Johnston
*President and Chief Executive Officer, Stantec, Inc.*

No, that's great. We certainly appreciate everyone's time this morning and we look forward to chatting with you through the quarter and then formally again in our Q3 call. So, thanks very much.

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**Operator**: That will conclude today's call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

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