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SNC-Lavalin Group Inc.
TSE: SNC

Publication Date:
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Price: C$24.29/share

Market capitalization: ~C$4.25B

SNCL Services: C$45 per share

Capital: C$10 per share

Corporate, LSTK Projects, Net Debt & Other:
(C$17.50) per share

SOTP: C$37.50 per share*

*SOTP may not add due to rounding; all figures in CAD unless otherwise noted

NOTE: This publication could be considered as advocating for corporate restructurings. Authors select companies for this report based on the potential for a future value-unlocking transaction. In many cases, these companies have or could come under activist investor pressure, media scrutiny, or general market speculation that a spin-off or asset sale is possible.

- SNC-Lavalin (TSE: SNC), a professional services and project management (PS&PM) company, operates five core business segments, including (1) Engineering Services, (2) Nuclear, (3) Operations & Maintenance (O&M), and (4) Linxon, which are collectively referred to as SNCL Services, as well as (5) Capital, which, in part, includes a portfolio of investments in infrastructure assets, most notably a 6.76% stake in Highway 407 ETR, a tollway connecting the greater Toronto area. The remaining (non-core) segment, Lump-Sum Turnkey (LSTK) Projects, has been in run-off since mid-2019 and is primarily comprised of three legacy construction projects, of which two will be completed in 2023 (with the bulk of the actual physical work being finished in late 2022) and the last in 2024.

- In our view, SNC shares are undervalued relative to the underlying value of the SNCL Services business and the Capital segment's portfolio of investments, most notably SNC's stake in the Highway 407 tollway. We think the ongoing wind-down and ultimate completion of the all company's legacy LSTK projects, which have been a significant drag on overall profitability in recent years (but where the incremental financial risk, excluding overhead costs, is estimated to be capped at ~$225 million), should precipitate a re-rating of SNC shares more in line with PS&PM peers, such as WSP Global (WSP CN) and Stantec Inc. (STN CN), which trade at ~11x 2024E EBITDA (compared with SNC's current valuation of less than 8.0x). Additionally, we estimate the value of its stake in the Highway 407 tollway could itself be conservatively worth ~$10 per share after-tax, based on recent transactions (including SNC's own sale of a ~10% stake in the project in August 2019 & the Chicago Skyway transaction in September 2022).

- Based on management guidance and commentary as well as peer and M&A valuations, SNC's SNCL Services business and the Capital segment's portfolio of investments could be valued at $45 per share and ~$10 per share, respectively. Accounting for projected future losses from LSTK Projects, corporate costs, projected net debt, and non-controlling interest of ~$17.50 per share yields a base case sum-of-the-parts fair value of $37.50 per share (with bull and bear cases of ~$47 and ~$27 per share, respectively).

- Potential catalysts include the roll-off/completion of unprofitable legacy LSTK contracts, the opportunistic monetization of capital investments, better than expected growth/margins at the core SNCL Services business, debt reduction, share repurchases and/or accretive M&A. Risks include management execution, raw material/cost inflation, leverage, competition, currency fluctuations, regulation, legal liability, labor issues, pandemics and/or a recession.

Institutional Research Group

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COMPANY BACKGROUND & FINANCIALS

SNC-Lavalin (TSE: SNC), which is headquartered in Montreal, Canada, was founded in 1911 by Arthur Surveyer to provide engineering services primarily for power projects, before expanding into the oil & gas, mining & metallurgy, and infrastructure sectors in the ensuing decades. In 1991, the company merged with Canadian engineering giant Lavalin and adopted the current corporate moniker. Subsequently, in 2014, SNC-Lavalin acquired Kentz Corp., a leading oil & gas services provider with a significant presence in Australia (as well as Asia and the Middle East). In July 2017, SNC purchased WS Atkins, a U.K.-based design, engineering and project management company that was founded in 1938 (and, at the time of the acquisition, generated ~£2 billion of sales, including its previous acquisitions of Faithful+Gould in the early-1990s and PBS&J Corp., which established a presence in the U.S., in 2010). In November 2017, the company added to its digital management capabilities as well as its scale in the U.S. infrastructure market with the purchase of Data Transfer Solutions (DTS).

In the early 2000s, the company was embroiled in several bribery, fraud, and corruption scandals, including, among others, its work in securing contracts for the construction of a hospital in Montreal as well as various projects in Libya under the Gaddafi regime. The former resulted in the resignation in 2012 of then chief executive Pierre Duhaime, who was subsequently arrested on corruption charges and pled guilty in February 2019 to charges alleging “willful blindness” to improper payments made to officials involved in the McGill University Health Centre construction project. (For its part, SNC itself also sued Mr. Duhaime personally for ~$40 million.) Mr. Duhaime was replaced by Robert Card, who was primarily tasked with repairing the company’s reputation and culture. In October 2015, Mr. Card passed the leadership to Neil Bruce, the company’s then chief operating officer. In June 2019, amid investor frustration surrounding perceived execution issues as well as the announcement that the company would face trial over alleged illicit activities related to its work in Libya during 2001-2011, SNC appointed Ian Edwards, who had joined SNC in 2014 and was promoted to chief operating officer in January 2019, as the company’s interim president and CEO. (Mr. Edwards’ position was made permanent in October 2019.) In December 2019, the company settled federal fraud charges brought by the Canadian government related to its activities in Libya in the years 2001-2011 by pleading guilty to a single charge and agreeing to pay a $280 million fine (payable over five years) as well as submitting to a three-year probation period during which it would be subject to an independent monitor. Importantly, the settlement allowed SNC to continue bidding on government contracts with both the Canadian and foreign governments (and for all intents and purposes marked the end of a difficult chapter in SNC’s history).

With SNC’s legal issues firmly behind it, Mr. Edwards articulated a strategy to “de-risk” the company with a focus on strengthening the balance sheet and delivering more consistent earnings and cash flow. To that end, in July 2019, the company announced that it would exit/wind-down its lump-sum turnkey (LSTK) construction/contracting business, which employs a model where contractors submit bids for a project and are solely responsible for the financial risk of any cost overages sustained during the work’s completion, to focus on more collaborative project management and engineering services activities (with more alliance-based contracting models where risks are shared among stakeholders), as well as explore options for its primarily oil & gas-focused Resources segment and exit underperforming/non-core geographies. In pursuit of those aims, the company has reduced its LSTK backlog from ~$3.4 billion in 2Q 2019 to ~$664 million at the end of 3Q 2022 (and capped potential future losses, excluding overhead costs, at an estimated ~$225 million), divested its European Fertilizer and South African Resources businesses in 2020 before completing the sale of its oil & gas business to private-equity-backed Kentech in August 2021, and exited at least 15 non-core geographies (i.e., currently ~80% of sales in Canada, the U.S. and the U.K). On the balance sheet front, in August 2019, the company sold 10.01% of its stake in Highway 407 ETR, a tollway connecting the various parts of the greater Toronto area, for $3 billion, with ~$250 million of potential additional payments over the next 10 years. (Currently, Highway 407 is ~50% owned by subsidiaries of the Canada Pension Plan Investment Board [CPPIB], while Cintra, a subsidiary of Ferrovial S.A., owns 43.23%, and SNC still controls the remaining 6.76%.)

On January 1, 2022, SNC realigned its business structure into six segments: (1) Engineering Services, which combined its engineering design & project management (EDPM), mining & metallurgy (previously included in the Resources segment) and infrastructure services, excluding operations & maintenance (O&M) and Linxon, businesses; (2) Nuclear; (3) Operations & Maintenance (O&M); (4) Linxon; (5) LSTK Projects; and (6) Capital (see Exhibit 1).

Exhibit 1 SNC-Lavalin: Consolidated Selected Financial Items, 2021–2024E
(C$ in millions)

	2021	9 mos. 2021	9 mos. 2022	2022E	2023E	2024E
Sales:						
Engineering services	$4,366.4	$3,150.1	$3,443.3	$4,720.5	$4,934.8	$5,134.1
Nuclear	$904.7	$684.2	$672.3	$892.7	$937.3	$975.2
O&M	$470.4	$355.8	$365.6	$488.2	$502.9	$515.4
Linxon	$588.4	$424.1	$427.3	$566.9	$578.3	$592.7
SNCL Services	**$6,329.9**	**$4,614.3**	**$4,908.5**	**$6,668.3**	**$6,953.3**	**$7,217.5**
LSTK Projects	$907.2	$743.2	$680.7	$881.7	$299.8	$174.6
Capital	$134.1	$68.9	$59.8	$125.0	$125.0	$125.0
Total	**$7,371.2**	**$5,426.3**	**$5,649.0**	**$7,675.0**	**$7,378.0**	**$7,517.1**
Adj. segment EBIT:						
Engineering services	$464.0	$274.4	$278.5	$387.1	$421.4	$464.1
Nuclear	$135.9	$101.1	$103.4	$134.3	$140.6	$146.3
O&M	$54.6	$43.1	$38.9	$48.7	$35.2	$36.1
Linxon	$18.2	$15.0	$4.4	$7.2	$17.3	$20.7
SNCL Services	**$672.7**	**$433.6**	**$425.2**	**$577.2**	**$614.6**	**$667.2**
LSTK projects	($302.6)	($69.6)	($111.1)	($262.9)	($121.5)	($62.1)
Capital	$119.3	$58.7	$48.1	$103.5	$103.0	$103.0
Total	**$489.4**	**$422.7**	**$362.2**	**$417.8**	**$596.1**	**$708.2**
Adj. segment EBITDA:						
Engineering services	$587.2	$367.1	$368.1	$508.6	$569.5	$618.1
Nuclear	$151.6	$112.8	$114.0	$148.4	$155.6	$161.9
O&M	$57.0	$44.9	$40.8	$53.9	$40.5	$41.3
Linxon	$22.1	$18.1	$7.4	$10.9	$21.4	$24.9
SNCL Services	**$817.9**	**$542.9**	**$530.3**	**$721.8**	**$786.9**	**$846.3**
LSTK projects	($277.8)	($51.2)	($91.5)	($238.9)	($111.0)	($54.2)
Capital	$119.4	$58.7	$48.1	$103.5	$103.0	$103.0
Total	**$659.5**	**$550.4**	**$486.9**	**$586.4**	**$778.9**	**$895.1**
Adjusted EBITDA (as reported)	$525.0	$466.5	$394.7	$456.4	$648.9	$765.1

Source: Company reports, Bloomberg and Institutional Research Group estimates.

For some context on the following discussion, at its 2021 Investor Day SNC management articulated several three-year (i.e., 2022-2024) financial targets for its core SNCL Services business, including annual organic revenue growth of 4%-6%, driven, in part, by global sustainability trends and infrastructure investments, segment adjusted operating (EBIT) margins of 8%-10%, and segment adjusted EBITDA margins of 14%-16% at the Engineering Services segment (see Exhibit 2). On a consolidated basis, the company is targeting 80%-90% free cash flow conversion (relative to adjusted net income) and a leverage ratio, excluding non-recourse debt, of 1.5x-2.0x (currently 3.3x at the end of 3Q 2022) with the goal of returning to an investment-grade credit rating (at which point the company will utilize its free cash flow to drive growth, including tuck-in acquisitions, or opportunistically return it to shareholders via share repurchases and/or dividend increases). Anecdotally, the company is targeting a "mid-teen" return on invested capital (ROIC) in 2024.

Exhibit 2 SNC-Lavalin: 2022-2024 Financial Targets, Core-SNCL Services and Consolidated

	2022E-2024E Targets
SNCL Services:	
Annual organic revenue growth	4% - 6%
Segment adj. EBIT margin	8% - 10%
Engineering Services	8% - 10%
Nuclear	13% - 15%
Linxon	4% - 6%
O&M	5% - 7%
Segment adj. EBITDA margin - Engineering Services	14% - 16%
Consolidated:	
Free cash flow (FCF) conversion (by end of 2024)	80% - 90%
Net leverage ratio, ex. non-recourse debt (by end of 2024)	1.5x - 2.0x

Source: Company reports.

The company has also articulated financial guidance specifically for full year 2022; in that regard, management projects SNCL Services organic revenue growth of 5%-7% (up from its initial 4%-6% forecast) with an SNCL Services EBIT margin of 8.5%-9.5% (compared with its initial 8%-10% projection) and an Engineering Services adjusted EBITDA margin of 14%-16%. Corporate selling, general & administrative (SG&A) costs are expected to be ~$130 million, while restructuring & transformation costs and acquisition-related amortization of intangible expenses are expected to be $35-$45 million and ~$90 million, respectively. Net cash used in operations is expected to be ~$300 million ($50-$150 million previously; initially flat to $100 million), with capital expenditures of $80-$100 million (see Exhibit 3).

Exhibit 3 SNC-Lavalin: 2022 Financial Guidance, Core-SNCL Services and Consolidated

	2022E Guidance		
	Initial	Previous	Current
SNCL Services:			
SNCL Services organic growth	4% - 6%	4% - 6%	5% - 7%
SNCL Services segment adj. EBIT margin	8% - 10%	8% - 10%	8.5% - 9.5%
Segment adj. EBITDA margin - Engineering Services	14% - 16%	14% - 16%	14% - 16%
Consolidated:			
Corporate SG&A	$130 million	$130 million	$130 million
From PS&PM	~$100 million	~$100 million	~$100 million
From Capital	~$30 million	~$30 million	~$30 million
Restructuring & transformation costs	$35 - $45 million	$35 - $45 million	$35 - $45 million
Amortization of intangible assets	~$90 million	~$90 million	~$90 million
Net cash generated from operating activities	$0 - $100 million	($50) - ($150) million	~($300) million
Capital spending	$80 - $100 million	$80 - $100 million	$80 - $100 million

Source: Company reports.

SNCL Services

The broader SNCL Services segment, which represented ~86% of consolidated sales in 2021 and 87% of adjusted segment EBITDA, ex-LSTK Projects, is comprised of four core business lines: (1) Engineering Services; (2) Nuclear; (3) Operations & Maintenance (O&M); and Linxon. (See Exhibit 4.) The SNCL Services segment, along with Capital, allows SNC to provide customers an end-to-end suite of solutions, from project consulting and design (including financing and procurement) through construction, into operations & maintenance, and, in nuclear cases, de-commissioning. (Anecdotally, management indicates its integrated capabilities are a differentiating factor in an industry that remains fragmented with many players offering services within a limited portion of an asset's lifecycle.) The company serves public (70%) and private sector (30%) customers, primarily in Canada (~30% of sales), the U.S. (~20% of sales), and the U.K. (~30% of sales), along with Europe (~5% of sales), the Middle East, Asia-Pacific (APAC), primarily Australia, and Latin America (LATAM), focusing on several key end-markets, including water and transportation infrastructure, power & renewables, as well as nuclear technology, waste management, and de-commissioning. From a contract composition perspective, with the exception of Linxon, which uses standardized engineering, procurement, and construction management (EPCM) contracts, the remainder of SNCL Services generates revenue primarily from reimbursable and engineering services contracts. (For context, under reimbursable contracts, SNC charges the customer for the actual costs incurred plus a mark-up that is generally based on a fixed fee per unit, a percentage of costs incurred, or an incentive fee based on the achievement of mutually agreed upon targets or milestones. EPCM contracts include time and material agreements based on hourly rates and fixed-price lump-sum contracts with limited procurement or construction risks.)

Exhibit 4 SNC-Lavalin: SNCL Services Segment, Selected Financial Items, 2021–2024E
(C$ in millions)

	2021	9 mos. 2021	9 mos. 2022	2022E	2023E	2024E
Sales:						
Engineering services	$4,366.4	$3,150.1	$3,443.3	$4,720.5	$4,934.8	$5,134.1
Nuclear	$904.7	$684.2	$672.3	$892.7	$937.3	$975.2
O&M	$470.4	$355.8	$365.6	$488.2	$502.9	$515.4
Linxon	$588.4	$424.1	$427.3	$566.9	$578.3	$592.7
SNCL Services	**$6,329.9**	**$4,614.3**	**$4,908.5**	**$6,668.3**	**$6,953.3**	**$7,217.5**
Adj. segment EBIT:						
Engineering services	$464.0	$274.4	$278.5	$387.1	$421.4	$464.1
Nuclear	$135.9	$101.1	$103.4	$134.3	$140.6	$146.3
O&M	$54.6	$43.1	$38.9	$48.7	$35.2	$36.1
Linxon	$18.2	$15.0	$4.4	$7.2	$17.3	$20.7
SNCL Services	**$672.7**	**$433.6**	**$425.2**	**$577.2**	**$614.6**	**$667.2**
Adj. segment EBITDA:						
Engineering services	$587.2	$367.1	$368.1	$508.6	$569.5	$618.1
Nuclear	$151.6	$112.8	$114.0	$148.4	$155.6	$161.9
O&M	$57.0	$44.9	$40.8	$53.9	$40.5	$41.3
Linxon	$22.1	$18.1	$7.4	$10.9	$21.4	$24.9
SNCL Services	**$817.9**	**$542.9**	**$530.3**	**$721.8**	**$786.9**	**$846.3**

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Engineering Services

The Engineering Services unit, which generated 59% of consolidated sales in 2021 and ~62.5% of adjusted segment EBITDA, ex-LSTK Projects, provides design (~40% of sales), consulting (~30%), project/program management (20%), and other (~10%) services to both public and private customers (with a ~70%/30% split). It operates primarily in six targeted end-markets, including: (1) Transportation (e.g., rail, road and aviation projects), which is SNC's largest vertical at ~40% of sales; (2) Buildings & Places (e.g., hotels, developments, sports arenas, and theme parks), which comprises ~20% of sales ; (3) Defense (e.g., cyber resilience and equipment/systems supply programs); (4) Water (e.g., wastewater treatment plants); (5) Industrial & Mining (e.g., production and processing facilities), with each representing ~10% of sales; and (6) Power & Renewable Energy (e.g., hydropower projects and battery gigafactories and lithium facilities), which makes up ~5% of sales.

In the first nine months of 2022, Engineering Services segment sales increased 9.3% to $3.4 billion, as organic growth of ~12% more than offset foreign currency headwinds, with a 1.5% increase in adjusted segment EBIT to $278.5 million and a ~0.5% increase in adjusted segment EBITDA to ~$368 million (see Exhibits 1 and 5). The Engineering services segment, which, again, derives its revenue primarily from reimbursable and engineering services contracts, ended 3Q 2022 with a backlog of $4.623 billion (compared with $3.843 billion at the end of 3Q 2021 and $3.745 billion at the end of 2021). (Anecdotally, the ~20% year over year increase in Engineering Service backlog was, in part, driven by contract wins for infrastructure development with the Departments of Transportation in Florida, Georgia, Colorado and Texas.) Based on its current outlook, management projects Engineering Services segment sales to grow 5%-7% (up from its initial expectation of 4%-6%), with an adjusted EBITDA margin of 14%-16% in 2022 (see Exhibit 3). [Note: SNC's recent decision to disclose the adj. EBITDA margin metric is, in part, an effort to facilitate easier comparisons with peers and ensure the business receives the valuation management believe it deserves.] In terms of the longer-term outlook (i.e., 2022-2024), SNC expects the Engineering Services segment will post annual organic revenue growth of 4%-6% with an adjusted segment EBIT margin of 8%-10% (see Exhibit 3). For our part, we expect compound annual top-line growth of ~4.5% in 2023-2024, with a relatively steady adjusted EBIT margin of 8.5%-9.0%, resulting in 2024E sales and adjusted EBITDA of $5.135 billion and ~$618 million, respectively (see Exhibit 5).

Exhibit 5 SNC-Lavalin: Engineering Services Business, Selected Financial Items, 2021–2024E
(C$ in millions)

	1Q 2021	2Q 2021	3Q 2021	4Q 2021	**2021**	1Q 2022	2Q 2022	3Q 2022	4Q 2022E	**2022E**	**2023E**	**2024E**
Sales	**$1,049.6**	**$1,061.2**	**$1,039.3**	**$1,216.3**	**$4,366.4**	**$1,138.2**	**$1,128.7**	**$1,176.5**	**$1,277.1**	**$4,720.5**	**$4,934.8**	**$5,134.1**
Adj. segment EBIT	$86.2	$95.2	$93.0	$189.5	$464.0	$85.2	$95.4	$97.9	$108.6	$387.1	$421.4	$464.1
Adj. segment EBITDA	**$118.5**	**$126.1**	**$122.5**	**$220.1**	**$587.2**	**$114.9**	**$125.7**	**$127.5**	**$140.5**	**$508.6**	**$569.5**	**$618.1**
Adj. operating margin	8.2%	9.0%	8.9%	15.6%	10.6%	7.5%	8.5%	8.3%	8.5%	8.2%	8.5%	9.0%
Adj. EBITDA margin	11.3%	11.9%	11.8%	18.1%	13.4%	10.1%	11.1%	10.8%	11.0%	10.8%	11.5%	12.0%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Nuclear

The Nuclear unit, which comprised ~11.5% of consolidated sales in 2021 and ~18% of adjusted segment EBITDA, ex-LSTK Projects, provides support and services across the entire nuclear life-cycle from new build design to reactor support, including field and technology services as well as spare parts, and life extensions/refurbishment, to waste management (and storage) and ultimately de-commissioning. The company is primarily focused on Canada (~45% of sales), where for over 60 years SNC has been the steward (and exclusive licensee) of CANDU technology, a unique heavy-water uranium reactor system developed by the Canadians with the U.S. representing ~30% of sales, and the U.K. & Europe (e.g., Romania) together accounting for ~25% of sales. The company see long-term growth opportunities in the global pursuit of a lower carbon future (where nuclear could provide the base load power generation as a compliment to "intermittent" renewable energy sources, such as wind or solar) that it estimates is likely to drive a 2x-3x increase in the demand for electricity (by 2050). As well, given the nuclear construction boom in the 1960s-1980s the pipeline of nuclear reactors that need to have their life extended, via refurbishment (e.g., current projects at Darlington in the UK and Bruce Power in Canada), or be retired/de-commissioned, is robust over the next decade.

In the first nine months of 2022, Nuclear segment sales fell 1.7% to ~$672.3 million, largely driven by currency fluctuations along with slightly reduced activity on major projects in the U.S. and Canada (partially offset by strength in Europe), with a nearly 2.5% increase in adjusted segment EBIT to ~$103.5 million and a better than 1.0% increase in adjusted segment EBITDA to $114.0 million (see Exhibits 1 and 6). The Nuclear segment, which generates sales from long-term (i.e., 5-15+ years), profitable, low-risk, high-cash-conversion contracts with tier 1 clients, both public and private, ended 3Q 2022 with a backlog of $859 million (compared with $802.5 million at the end of 3Q 2021 and $831 million at the end of 2021). With respect to the longer-term outlook for at the Nuclear segment, which is informed by SNC's insight into the new build (e.g., Sizewell), waste management, and decommission pipeline, where it has solid visibility out until at least the middle of the next decade, the company targets annual organic revenue growth of 4%-6% in 2022-2024, with a consistent adjusted segment EBIT margin of 13%-15%. For our part, we expect compound annual top-line growth of ~4.5% in 2023-2024 with a steady adjusted EBIT margin of 15%, resulting in 2024E sales and adjusted EBITDA of ~$975 million and $162 million, respectively (see Exhibit 6).

Exhibit 6 SNC-Lavalin: Nuclear Business, Selected Financial Items, 2021–2024E

	1Q 2021	2Q 2021	3Q 2021	4Q 2021	2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022	2022E	2023E	2024E
Sales	**$229.1**	**$234.7**	**$220.5**	**$220.4**	**$904.7**	**$232.1**	**$221.0**	**$219.2**	**$220.4**	**$892.7**	**$937.3**	**$975.2**
Adj. operating income	$31.8	$33.2	$36.0	$34.8	$135.9	$34.3	$32.5	$36.6	$30.9	$134.3	$140.6	$146.3
Adj. segment EBITDA	**$35.4**	**$37.8**	**$39.6**	**$38.7**	**$151.6**	**$38.0**	**$36.0**	**$40.0**	**$34.4**	**$148.4**	**$155.6**	**$161.9**
Adj. operating margin	13.9%	14.2%	16.3%	15.8%	15.0%	14.8%	14.7%	16.7%	14.0%	15.0%	15.0%	15.0%
Adj. EBITDA margin	15.5%	16.1%	18.0%	17.6%	16.8%	16.4%	16.3%	18.2%	15.6%	16.6%	16.6%	16.6%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Operations & Maintenance (O&M)

The Operations & Maintenance (O&M) business, which generated ~6.5% of consolidated sales in 2021 and 6.5% of adjusted segment EBITDA, ex-LSTK Projects, provides operations, maintenance, and asset management services for bridges, transit systems, highways, buildings, and industrial plants, including power plants, water supply & treatment systems, & desalination plants, as well as postal services and ships. To that end, the company operates three sub-segments, including (1) Transportation (25% of sales), (2) Facilities & Defense (~40%), and (3) Industrial (~35% of sales).

In the first nine months of 2022, O&M segment sales increased almost 3% to ~$365.5 million, driven by a higher level of services provided under existing contracts, with ~9% declines in adjusted segment EBIT and EBITDA to ~$39 million and ~$41 million, respectively, driven largely by higher bidding expenses in 3Q 2022 (see Exhibits 1 and 7). The O&M segment, where many contracts are fixed-price agreements with inflation-adjusted price adjustment mechanisms, ended 3Q 2022 with a backlog of ~$5.42 billion (compared with $5.78 billion at the end of 3Q 2021 and ~$5.85 billion at the end of 2021), which management indicates will drive consistent long-term sales and provides a high degree of visibility on its future revenue streams. [Note: SNC provides O&M services to more than a dozen of the projects within its portfolio of Capital investments, which will be described in greater detail on page #9 of this report.] For context, management indicates that the majority of its backlog stems from transportation projects (e.g., light rail systems) with the remainder focused on facilities and the industrial sector (e.g., McGill Hospital and the John Hart Power Station). Regarding its outlook, while management has not provided any specific top-line commentary, other than the broader growth projection for SNCL Services of 4%-6%, management expects the adjusted EBITDA margin profile at O&M to be in a range of 5%-7% through 2024 (see Exhibit 3). For our part, we project compound annual top-line growth of ~2.75% in 2023E-2024E with a margin profile of ~7%, implying 2024E sales and adjusted segment EBITDA of $515.5 million and ~$41.5 million, respectively (see Exhibit 7).

Exhibit 7 SNC-Lavalin: Operations & Maintenance (O&M) Business, Selected Financial Items, 2021–2024E

(C$ in millions)

	1Q 2021	2Q 2021	3Q 2021	4Q 2021	2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022E	2022E	2023E	2024E
Sales	**$141.6**	**$104.4**	**$109.8**	**$114.6**	**$470.4**	**$136.5**	**$104.8**	**$124.3**	**$122.6**	**$488.2**	**$502.9**	**$515.4**
Adj. operating income	$12.4	$13.4	$17.3	$11.5	$54.6	$11.7	$11.4	$15.8	$9.8	$48.7	$35.2	$36.1
Adj. segment EBITDA	**$13.0**	**$14.0**	**$17.9**	**$12.1**	**$57.0**	**$12.3**	**$13.7**	**$14.8**	**$13.1**	**$53.9**	**$40.5**	**$41.3**
Adj. operating margin	8.7%	12.8%	15.8%	10.0%	11.6%	8.6%	10.9%	12.7%	8.0%	10.0%	7.0%	7.0%
Adj. EBITDA margin	9.2%	13.4%	16.3%	10.6%	12.1%	9.0%	13.1%	11.9%	10.7%	11.0%	8.1%	8.0%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Linxon

The Linxon business is a majority-owned (51%) joint venture with Hitachi ABB Power Grids, which combines SNC's project management expertise with Hitachi ABB's deep technological knowledge (and products) to offer engineering, procurement, management, and construction services to large, high-voltage, alternating current (AC) power substations in various segments, including renewable & conventional power generation, transportation, transmission grids, data centers and battery energy storage. [Note: Linxon segment adjusted EBIT includes the portion attributable to non-controlling interest (i.e., at 100%)].

In the first nine months of 2022, Linxon segment sales increased almost 1% to $427.3 million, as organic growth of ~7.5% was partially offset by foreign currency headwinds, with a 71% decline in adjusted segment EBIT to ~$4.5 million and a ~59% decline in adjusted EBITDA to ~$7.5 million, driven largely by project delays and higher costs at projects in Europe (see Exhibits 1 and 8). The Linxon segment, whose contracts include both reimbursable and engineering services arrangements, as well as standardized EPCM contracts, which are lower-risk compared with standard LSTK contracts, ended 3Q 2022 with a backlog of ~$764 million compared with $1.02 billion at the end of 3Q 2021 and ~$1.04 billion at the end of 2021. (Management indicates that the decline is primarily due to award delays and that its long-term pipeline of opportunities remains strong driven by significant investments it expects in grid infrastructure and renewable power energy across the globe. In fact, the company noted on the 3Q 2022 conference call that its backlog will rebound in 4Q 2022 as the company secured several new project wins subsequent to the end of the September-quarter.) Regarding the outlook, similar to the O&M segment, management has not provided any specific top-line commentary, other than noting a broader growth outlook for SNCL Services of 4%-6%, although management expects the adjusted EBITDA margin profile at Linxon to be in a range of 4%-6% through 2024 (see Exhibit 4). For our part, we project compound annual top-line growth of ~2.5% in 2023E-2024E, with a slightly below-guidance margin profile of 3.0%-3.5%, implying 2024E sales and adjusted segment EBITDA of $593 million and ~$25 million, respectively (see Exhibit 8).

Exhibit 8 SNC-Lavalin: Linxon Business, Selected Financial Items, 2021–2024E

(C$ in millions)

	1Q 2021	2Q 2021	3Q 2021	4Q 2021	2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022E	2022E	2023E	2024E
Sales	**$131.9**	**$143.4**	**$148.9**	**$164.3**	**$588.4**	**$150.5**	**$153.7**	**$123.1**	**$139.7**	**$566.9**	**$578.3**	**$592.7**
Adj. operating income	$6.1	$7.3	$1.6	$3.2	$18.2	($4.5)	$6.5	$2.3	$2.8	$7.2	$17.3	$20.7
Adj. segment EBITDA	**$7.3**	**$8.4**	**$2.4**	**$4.1**	**$22.1**	**($3.1)**	**$7.3**	**$3.2**	**$3.5**	**$10.9**	**$21.4**	**$24.9**
Adj. operating margin	4.6%	5.1%	1.1%	1.9%	3.1%	-3.0%	4.2%	1.9%	2.0%	1.3%	3.0%	3.5%
Adj. EBITDA margin	5.5%	5.9%	1.6%	2.5%	3.8%	-2.1%	4.7%	2.6%	2.5%	1.9%	3.7%	4.2%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Capital

The Capital segment is SNC's investment, financing, and asset management arm, tasked with developing projects, arranging financing and, at times, investing equity, and managing those investments, which are generally infrastructure projects, such as bridges, highways, transit systems, power facilities, and water treatment plants, as well as hospitals (and other "social infrastructure") for optimal returns. (See Exhibit 9.) Anecdotally, SNC generally targets an internal rate of return, or IRR, of greater than 10%. (That said, management indicates that its Canadian projects have historically exceed this target with many reaching the "mid to high-digit percentage teens, IRRs in terms of the return".) At the end of 3Q 2022, the net book value of SNC's Capital investment portfolio was $653 million (compared with $622 million at the end of 2Q 2022 and $620 million at the end of 2021). In terms of fair value, management anecdotally indicates that the current average fair market value assessed by publishing sell-side analysts, which, per Bloomberg, represents a group of roughly 10 firms, is ~$2.4 billion. As well, management notes that its 6.67% stake in 407 International, which operates Highway 407 ETR, a tollway connecting all parts of the greater Toronto area, represents about $1.8 billion of this estimated fair value (although, we note, its net book value on the balance sheet is zero). [Note: in addition to SNC's 6.67% stake, subsidiaries of the Canada Pension Plan Investment Board (CPPIB) own ~50%, and Cintra, a subsidiary of Ferrovial S.A., owns the remaining 43.23%.]

Exhibit 9 SNC-Lavalin: Capital Segment, Investment Portfolio

Project	Description	Held Since	Concession Length	Location	Equity Share
407 EDGGP	32km H407 extension	2012	33	Ontario, CN	50%
Carlyle Global Infrastructure Opp. Fund	Holding investments	2018	-	U.S.	4.5%
Eglinton Crosstown	19km light rail line	2015	36	Ontario, CN	25%
Highway 407 ETR	**108km electronic toll road**	**1999**	**99**	**Ontario, CN**	**6.76%**
Myah Tipaza	Seawater desalination plant	2008	-	Algeria	25.5%
Rideau	Light rail transit system	2013	30	Ontario, CN	40%
SKH	1,227MW gas-fired power plant	2006	-	Algeria	26%
SSL	New Champion bridge corridor	2015	34	Quebec, CN	50%
TC Dome	5.3km electric cog railway	2008	35	France	51%
TransitNEXT	12km light rail line	2019	30	Ontario, CN	100%
Chinook	25km six-lane road	2010	33	Alberta, CN	10%
InPower BC	John Hart 126MW generating station	2014	19	British Columbia, CN	20%
InTransit BC	Rapid transit line	2005	35	British Columbia, CN	6.7%
MIHG	McGill University Health Centre	2010	34	Quebec, CN	10%
Okanagan Lake	Floating bridge	2005	30	British Columbia, CN	20%
Rainbow	Restigouche Hospital Centre	2011	33	New Brunswick, CN	20%

Source: Company reports.

In the first nine months of 2022, Capital segment sales fell more than 13% to ~$60 million, driven by asset disposals and a lower contribution from several investments, more than offset by the $13.5 million contribution from Highway 407 ETR (compared with no contribution in the same period of 2021), with ~18% declines in adjusted segment EBIT and EBITDA to $48 million (see Exhibits 1 and 10). Looking into 2023-2024, while we expect the income statement impact of the Capital segment to be relatively steady, we think investors are best served by considering the underlying value of its investment portfolio, most notably its stake in Highway 407, which will be described in greater detail in the "Valuation" section of this report (on pages #16 & 17).

Exhibit 10 SNC-Lavalin: Capital Segment, Selected Financial Items, 2021–2024E
(C$ in millions)

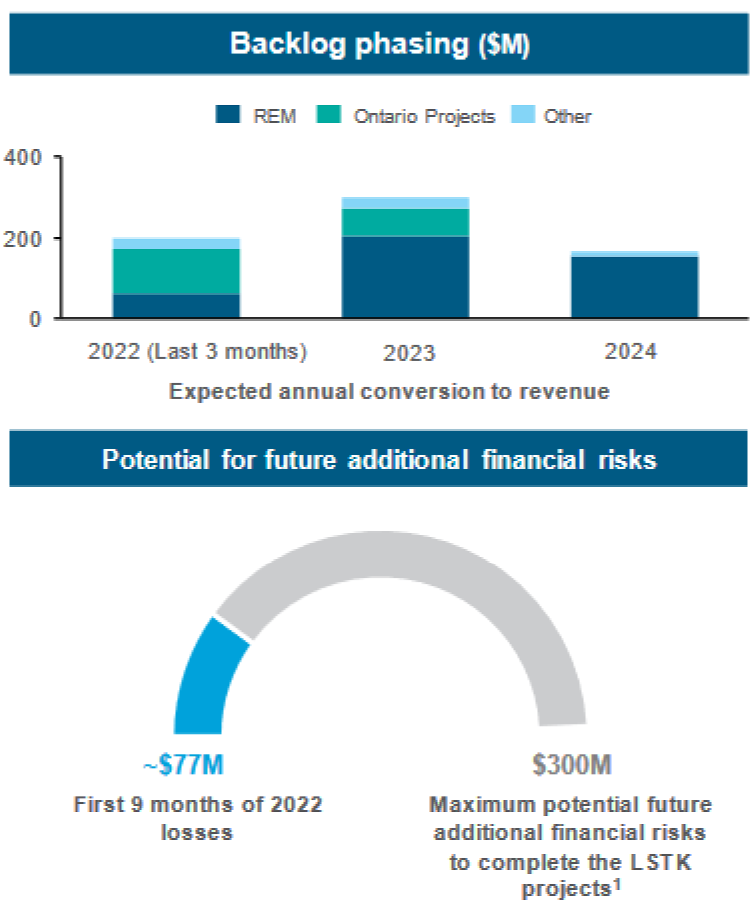
	1Q 2021	2Q 2021	3Q 2021	4Q 2021	2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022E	2022E	2023E	2024E
Sales	**$21.7**	**$19.8**	**$27.4**	**$65.2**	**$134.1**	**$16.4**	**$13.9**	**$29.5**	**$65.2**	**$125.0**	**$125.0**	**$125.0**
Adj. operating income	$18.7	$16.4	$23.6	$60.6	$119.3	$12.4	$10.9	$24.8	$55.4	$103.5	$103.0	$103.0
Adj. segment EBITDA	**$18.7**	**$16.4**	**$23.6**	**$60.6**	**$119.4**	**$12.4**	**$10.9**	**$24.8**	**$55.4**	**$103.5**	**$103.0**	**$103.0**
Adj. operating margin	86.1%	82.9%	86.2%	92.9%	89.0%	75.6%	78.6%	84.1%	85.0%	82.8%	82.5%	82.5%
Adj. EBITDA margin	86.0%	82.9%	86.2%	92.9%	89.0%	75.7%	78.4%	84.1%	85.0%	82.8%	82.5%	82.5%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

LSTK Projects

As described previously, in July 2019 the company announced that it would not bid on any new projects and began to exit/wind-down its lump-sum turnkey (LSTK) construction/contracting business. (The LSTK business employed a model that was ubiquitous in the industry for many years, where contractors submit bids for a project and are solely responsible for the financial risk of any cost overages sustained during the work's completion.) To that end, the company has reduced its LSTK backlog from ~$3.4 billion in 2Q 2019 to ~$664 million at the end of 3Q 2022, a process that it expects to complete by the end of 2024, and has capped potential future losses, excluding overhead costs, at an estimated ~$225 million (see Exhibit 11).

Exhibit 11 SNC-Lavalin: LSTK Projects Segment, Backlog and Financial Risk Snapshot
(C$ in millions)



Source: Company reports.

For context, the remaining backlog is related to three legacy projects, which are expected to be completed by the end of 2024 (with the bulk in 4Q 2022 and 2023; see Exhibit 11): (1) Eglinton, which is a crosstown extension of a light rail system in Ontario, Canada, on which management expects the physical work to be largely completed by the end of 2022 (following which the work becomes moves into testing and commissioning activities); (2) Trillium, a light rail project in Ottawa, Canada, which the company expects to be substantially completed in 2023 (with the bulk of the physical work, again, completed by the end of 2022); and (3) Reseau Express Metropolitain (REM), a light metro rapid transit system in greater Montreal, Quebec, Canada that links downtown Montreal to several suburbs and to the Montreal-Trudeau International Airport, which is expected to be completed during 2024.

In terms of the financial impact, in the first nine months of 2022, LKST Projects segment sales fell ~8.5% to ~$681 million, while the adjusted segment EBIT and EBITDA losses expanded to $111 million and $91.5 million, respectively (see Exhibit 1). As mentioned previously, the company expects to work through its current $663 million backlog, which fell 20% sequentially from $828.5 million in 2Q 2022 and more than 40% year-over-year from ~$1.15 billion in 3Q 2021), through 2024 (with the bulk being completed in 4Q 2022 and 2023). Moreover, the company has consistently reaffirmed its initial expectation, issued at the beginning of 2022, that the maximum potential future additional financial risks to complete its LSTK segment projects would be $300 million, of which ~$77 million has been incurred in the first nine months (not including $34 million of overhead costs). To that end, we expect the ongoing financial impact on SNC to continue to decline in 2023-2024 (with no additional financial impact in 2025 and beyond). (See Exhibit 12.)

Exhibit 12 SNC-Lavalin: LSTK Projects Segment, Selected Financial Items, 2021–2024E
(C$ in millions)

	1Q 2021	2Q 2021	3Q 2021	4Q 2021	2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022E	2022	2023E	2024E
Sales	**$245.8**	**$234.4**	**$263.0**	**$164.1**	**$907.2**	**$214.4**	**$249.4**	**$216.9**	**$201.0**	**$881.7**	**$299.8**	**$174.6**
Adj. operating income	($11.9)	($25.3)	($32.4)	($233.0)	($302.6)	($30.5)	($36.6)	($43.9)	($151.9)	($262.9)	($121.5)	($62.1)
Adj. segment EBITDA	**($6.0)**	**($20.2)**	**($25.0)**	**($226.6)**	**($277.8)**	**($25.5)**	**($31.1)**	**($34.9)**	**($147.4)**	**($238.9)**	**($111.0)**	**($54.2)**
Adj. operating margin	-4.9%	-10.8%	-12.3%	-142.0%	-33.4%	-14.2%	-14.7%	-20.3%	-75.5%	-29.8%	-40.5%	-35.5%
Adj. EBITDA margin	-2.4%	-8.6%	-9.5%	-138.1%	-30.6%	-11.9%	-12.5%	-16.1%	-73.3%	-27.1%	-37.0%	-31.0%

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Balance Sheet & Cash Flow

At the end of 3Q 2022, SNC had net debt of ~$1.499 billion, including cash of $483 million and recourse & limited recourse debt of $1.98 billion (see Exhibit 13). The company had a net recourse & limited recourse leverage ratio of 3.3x, which compares with its 3.75x covenant. The company is targeting a leverage ratio of 1.5x-2.0x by the end of 2024. (Anecdotally, in regards to leverage, on the 3Q 2022 conference call management commented that "we're well below our covenant ratios on our credit facilities and have a high degree of confidence in terms of where we're headed in the fourth quarter, both in terms of the cash generation from the Services business" as well as that "as we come into winter and approach the physical completion particularly on the 2 Ontario projects, we start to get into a glide path with lower cash usage on those LSTK projects. So I'm not concerned at all about where our balance sheet is and our projection of cash flows from here." As well, we note the company is seeking to recover some of the increased costs incurred over the last couple of years at its remaining LSTK projects, primarily Eglinton and Trillium, to which the company contends they are legally entitled; while likely a 2023 event any recoveries would be incremental to the company's operating cash flows.)

Exhibit 13 SNC-Lavalin: Balance Sheet, Selected Items

(C$ in millions)

	2020	2021	2Q 2022	3Q 2022
Cash	**$932.9**	**$608.4**	**$567.4**	**$482.6**
Restricted cash	$29.3	$13.4	$12.2	$28.3
Debt:				
Short-term & current debt	$206.2	$110.9	$631.1	$809.7
Recourse	$175.0	$96.9	$617.7	$783.8
Non-recourse	$31.3	$14.0	$13.4	$25.9
Long-term debt	$1,796.3	$1,553.3	$1,360.1	$1,354.5
Recourse	$996.0	$997.2	$797.1	$797.5
Limited recourse	$400.0	$400.0	$400.0	$400.0
Non-recourse	$400.3	$156.0	$163.0	$157.0
Total debt	**$2,002.5**	**$1,664.2**	**$1,991.2**	**$2,164.2**
Recourse	$1,171.0	$1,094.1	$1,414.9	$1,581.3
Limited recourse	$400.0	$400.0	$400.0	$400.0
Non-recourse	$431.5	$170.1	$176.4	$182.9
Net total debt	$1,069.6	$1,055.7	$1,423.8	$1,681.6
Net recourse debt	**$638.1**	**$885.7**	**$1,247.5**	**$1,498.7**
Net recourse leverage ratio	**3.2x**	**1.7x**	**2.8x**	**3.3x**
Equity:				
Shareholders equity	$2,557.5	$2,973.4	$2,944.8	$2,987.9
Non-controlling interest	$11.2	$20.1	$18.9	$20.2
Total equity	**$2,568.7**	**$2,993.5**	**$2,963.7**	**$3,008.1**

Source: Company reports, Bloomberg and Institutional Research Group estimates.

For full year 2022, the company expects net cash used in operations will be ~$300 million, suggesting the company will generate positive net cash from operations in 4Q 2022, and for capital spending to be ~$80-$100 million (see Exhibit 14). As the aforementioned impact of the unprofitable LSTK contracts continues to dissipate, the company is targeting a free cash flow conversion ratio of 80%-90% (relative to adjusted net income) as well as a "mid-teen" return on invested capital by the end of 2024. Once, the company achieves its leverage targets and an investment grade credit rating the company will look to deploy free cash (i.e., not keen on issuing equity) for tuck-in acquisitions (likely in the "low-$10s of millions" to "low-$100s of millions" range) or distribute it to shareholders, via share repurchases and/or dividend increases.

Exhibit 14 SNC-Lavalin: Sources & Uses of Cash Flow, Selected Items
(C$ in millions)

	2020	2021	9 mos. 2021	9 mos. 2022	2022E	2023E	2024E
Net income	($956.3)	$672.1	$724.7	$65.1	$49.1	$166.6	$250.7
Net cash from operations	**$121.5**	**$134.2**	**$18.8**	**($445.2)**	**($300.0)**	**$227.9**	**$375.5**
Acquisition of prop. & equip.	($75.8)	($106.3)	($59.0)	($75.9)	($100.0)	($100.0)	($100.0)
Payment of lease liabilities	($118.7)	($99.8)	($76.6)	($63.6)	($95.0)	($95.0)	($95.0)
Free cash flow	**($73.0)**	**($71.9)**	**($116.8)**	**($584.8)**	**($495.0)**	**$32.9**	**$180.5**
Acquisitions	-	-	-	-	-	-	-
Dividends	($14.0)	($14.0)	($10.5)	($10.6)	($14.0)	($14.0)	($14.0)

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Exhibit 15 SNC-Lavalin: Public Comparables
($ in millions, except per share amounts; shares in millions)

11/11/2022	SNC-Lavalin Group Inc	WSP Global Inc	Stantec Inc	Jacobs Solutions Inc	AECOM
Ticker	SNC CN	WSP CN	STN CN	J	ACM
Price	$24.29	$160.49	$65.72	$125.72	$77.65
Shares Out	175.6	124.3	110.7	127.6	139.6
M Cap	4,264.2	19,948.5	7,278.2	16,042.6	10,843.8
Net Debt	1,701.8	1,171.5	1,903.1	3,988.5	2,086.7
EV	5,966.0	21,120.0	9,181.3	20,031.1	12,930.5
Revenue					
2022E	7,675.0	8,890.2	4,416.5	14,902.0	13,212.9
2023E	7,378.0	10,324.6	4,710.6	15,028.0	12,539.0
2024E	7,517.1	10,948.5	4,905.7	16,455.0	13,502.6
EV / Sales					
2022E	0.8x	2.4x	2.1x	1.3x	1.0x
2023E	0.8x	2.0x	1.9x	1.3x	1.0x
2024E	0.8x	1.9x	1.9x	1.2x	1.0x
Average		*1.5x*			
EBITDA					
2022E	456.4	1,519.5	702.3	1,361.2	891.3
2023E	680.2	1,798.7	767.4	1,508.5	967.4
2024E	765.1	1,952.5	853.5	1,677.9	1,080.0
Margin	*10.2%*	*17.8%*	*17.4%*	*10.2%*	*8.0%*
EV / EBITDA					
2022E	13.1x	13.9x	13.1x	14.7x	14.5x
2023E	8.8x	11.7x	12.0x	13.3x	13.4x
2024E	7.8x	10.8x	10.8x	11.9x	12.0x
Average		***11.4x***			
EPS					
2022E	$1.30	$5.47	$3.01	$6.93	$3.44
2023E	$1.77	$6.35	$3.42	$7.73	$3.75
2024E	$2.13	$7.19	$3.78	$8.81	$4.43
P/E					
2022E	18.6x	29.3x	21.9x	18.2x	22.6x
2023E	13.7x	25.3x	19.2x	16.3x	20.7x
2024E	11.4x	22.3x	17.4x	14.3x	17.5x
Average		*17.9x*			
Leverage ratio (2022)	3.3x	0.8x	1.8x	2.3x	1.5x
Leverage ratio (2024)	2.0x	0.6x	2.2x	2.4x	1.9x

Source: Company reports, Bloomberg and Institutional Research Group estimates.

VALUATION

SNCL Services Segment

SNC's core SNCL Services business could be mostly aptly compared with Stantec Inc. (STN CN) and WSP Global Inc. (WSP CN), which trade at ~11x 2024E EV/EBITDA, although a broader group of engineering & construction (E&C) peers could also include AECOM (NYSE: ACM) and Jacobs Solutions (NYSE: J), which trades at ~12x 2024E EV/EBITDA multiple (see Exhibit 15). By our calculation, M&A activity in the sector has averaged roughly ~10.5x in recent years (see Exhibit 16).

Exhibit 16 SNC-Lavalin: E&C Sector M&A, Selected Items
(currency in millions)

Announced	Acquirer	Target	EV	EV/Revenue multiple	EV/EBITDA multiple
Jul-22	IBI Group	Arcadis NV	C$873	-	11.5x
Aug-17	Jacobs	CH2M	$3,270.0	0.7x	10.1x
Apr-17	WS Atkins	SNC-Lavalin	£2193.21	1.1x	11.7x
Jul-14	AECOM	URS Corp.	$6,087.6	0.6x	8.5x
Jun-14	Kentz Corp	SNC-Lavalin	£1200	0.7x	9.7x
Avg.				**0.8x**	**10.3x**

Source: Company reports, Bloomberg, Chainbridge Research and Institutional Research Group estimates.

Applying a discounted blended multiple of ~9.5x to SNCL Services segment 2024E EBITDA yields a total value of ~$7.925 million, or ~$45 per share (see Exhibit 17).

Exhibit 17 SNC-Lavalin: Estimated Value of SNCL Services Segment Based on 2024E EBITDA
(C$ in millions, except per share amounts; shares in millions)

		SNCL Services	
2023E Revenue		$6,953.3	
Revenue growth est.		3.8%	
2024E Revenue		**$7,217.5**	
EBITDA margin		11.7%	
2024E EBITDA		**$846.3**	
Applied multiple	8.4x	**9.4x**	10.4x
Enterprise value	$7,079.5	**$7,925.8**	$8,772.1
Diluted shares	175.6	175.6	175.6
Per share basis	$40.33	**$45.15**	$49.97

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Notably, our preceding valuation framework assigns 2024E EBITDA multiples of 9.5x and 10.0x to SNC's Engineering Services and Nuclear business lines, a 7.5x multiple to O&M and a 5.0x multiple to the lower-margin Linxon businesses (see Exhibit 18).

Exhibit #18 SNC-Lavalin: Estimated Value of SNCL Services Business Lines Based on 2024E EBITDA
(C$ in millions, except per share amounts; shares in millions)

		Engineering Services	
2023E Revenue		$4,934.8	
Revenue growth est.		4.0%	
2024E Revenue		**$5,134.1**	
EBITDA margin		12.0%	
2024E EBITDA		**$618.1**	
Applied multiple	8.5x	**9.5x**	10.5x
Enterprise value	$5,254.3	**$5,872.4**	$6,490.6
Diluted shares	175.6	175.6	175.6
Per share basis	$29.93	**$33.45**	$36.97

		Nuclear	
2023E Revenue		$937.3	
Revenue growth est.		4.0%	
2024E Revenue		**$975.2**	
EBITDA margin		16.6%	
2024E EBITDA		**$161.9**	
Applied multiple	9.0x	**10.0x**	11.0x
Enterprise value	$1,457.0	**$1,618.9**	$1,780.7
Diluted shares	175.6	175.6	175.6
Per share basis	$8.30	**$9.22**	$10.14

		O&M	
2023E Revenue		$502.9	
Revenue growth est.		2.5%	
2024E Revenue		**$515.4**	
EBITDA margin		8.0%	
2024E EBITDA		**$41.3**	
Applied multiple	6.5x	**7.5x**	8.5x
Enterprise value	$268.7	**$310.0**	$351.4
Diluted shares	175.6	175.6	175.6
Per share basis	$1.53	**$1.77**	$2.00

		Linxon	
2023E Revenue		$578.3	
Revenue growth est.		2.5%	
2024E Revenue		**$592.7**	
EBITDA margin		4.2%	
2024E EBITDA		**$24.9**	
Applied multiple	4.0x	**5.0x**	6.0x
Enterprise value	$99.6	**$124.5**	$149.4
Diluted shares	175.6	175.6	175.6
Per share basis	$0.57	**$0.71**	$0.85

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Capital Segment

In order to value the Capital segment, we think the most relevant consideration for investors is the estimated value of SNC's 6.7% stake in Highway 407 ETR; in that context, we would note that in August 2019 the company sold a 10.01% portion of its stake in the project to the Canada Pension Plan Investment Board (CPPIB) for $3 billion (plus ~$250 million of contingent payments over the next 10 years). SNC's net after-tax gain on the transaction was ~$2.585 billion. (Notably, in 2010, Ferrovial sold a 10% stake in Highway 407, also to CPPIB, for ~EUR 2.47 billion). Based on most recent transaction, SNC's remaining 6.67% stake could be valued at ~$1.73 billion, after-tax, or ~$9.85 per share (see Exhibit 19). For context, this valuation framework implies an overall Capital segment 2024E EV/EBITDA multiple of ~17.0x and an about 2.65x multiple on the segment's net book value of ~$653 million. (Additionally, we note that, per management, the current average fair market value assessed by publishing sell-side analysts, which, per Bloomberg, represents a group of roughly 10 firms, is ~$2.4 billion or ~$13.65 per share, of which Highway 407 comprises about ~$1.8 billion.)

Exhibit 19 SNC-Lavalin: Estimated Value of Highway 407 Based on Precedent Transaction
(C$ in millions, except per share amounts; shares in millions)

2019 SNC/CPPIB transaction:	
Cash consideration	$3,000.0
Additional consideration	$12.3
Contingent consideration receivable	$56.1
Total consideration	**$3,068.4**
Carrying value	-
Disposition-related costs	($97.6)
Gain on sale, gross	**$2,970.8**
Income taxes	($384.8)
Net gain on sale	**$2,586.0**
Current value based on 2019 transaction:	
Implied total of value Highway 407	**$30,653.3**
SNC's current stake	6.67%
Implied current value to SNC	**$2,044.6**
Transaction costs	($10.9)
Taxes	($305.1)
After-tax value to SNC	**$1,728.6**
Diluted shares	175.6
Per share value to SNC	**$9.85**
Total Capital segment book value	$653.0
Implied book value multiple	2.6x
Total Capital segment 2024E EBITDA	$103.0
Implied EBITDA multiple	16.8x

Source: Company reports, Bloomberg and Institutional Research Group estimates.

For additional context, we would note that more recently, in September 2022, Atlas Arteria (ALX AUS), an Australian-based toll road operator, agreed to purchase a 66.67% interest in the 12.5km Chicago Skyway for US$2.013 billion (equity value), implying a total project value of ~$4.403 billion (enterprise value), or ~43.2x trailing 12-month EBITDA of ~$102 million. If one were to apply a similar valuation framework to SNC's 6.67% stake in Highway 407, it would imply an after-tax value of ~$15 per share. (Further, if one added the net book value of SNC's investment portfolio, excluding Highway 407, to the preceding valuation scenario it could add an incremental ~$1.75-$3.75 per share.)

Sum-of-the-Parts Valuation

Accounting for corporate costs capitalized at the SNCL Services segment average, as well as net debt, future LSTK Projects losses, and non-controlling interests of ~$1.85 billion, yields a total sum-of-the-parts value of nearly $6.6 billion, or ~$37.50 per share (with bull and bear cases of $47 and $27 per share, respectively; see Exhibit 20).

Exhibit 20 SNC-Lavalin: Sum-of-the-Parts Valuation
(C$ in millions, except per share amounts; shares in millions)

	SNCL Services	Capital	Corporate	Enterprise Value	Net Debt, LSTK Losses & Other	Market Cap
2023E Revenue	$6,953.3	$125.0	-			
2024E Revenue	**$7,217.5**	**$125.0**	**-**			
2024E EBITDA	**$846.3**	**$103.0**	**($130.0)**		**($1,854.4)**	
Applied multiple	**9.4x**	**16.8x**	**9.4x**		**1.0x**	
Enterprise value	**$7,925.8**	**$1,728.6**	**($1,217.5)**	**$8,436.9**	**($1,854.4)**	**$6,582.5**
Diluted shares	175.6	175.6	175.6		175.6	175.6
Per share basis	**$45.15**	**$9.85**	**($6.94)**		**($10.56)**	**$37.50**
Bull	$49.97	$15.18	($7.68)		($10.56)	$46.91
Base	$45.15	$9.85	($6.94)		($10.56)	$37.50
Bear	$40.33	$3.72	($6.19)		($10.56)	$27.29

Source: Company reports, Bloomberg and Institutional Research Group estimates.

Summary & Conclusion

In our view, SNC shares are undervalued relative to the underlying value of the SNCL Services business and the Capital segment's portfolio of investments, most notably SNC's stake in the Highway 407 tollway. We think the ongoing wind-down and ultimate completion of the all company's legacy LSTK projects, which have been a significant drag on overall profitability in recent years (but where the incremental financial risk, excluding overhead costs, is estimated to be capped at ~$225 million), should precipitate a re-rating of SNC shares more in line with PS&PM peers, such as WSP Global (WSP CN) and Stantec Inc. (STN CN), which trade at ~11x 2024E EBITDA (compared with SNC's current valuation of less than 8.0x). Additionally, we estimate the value of its stake in the Highway 407 tollway could itself be conservatively worth ~$10 per share after-tax, based on recent transactions (including SNC's own sale of a ~10% stake in the project in August 2019 & the Chicago Skyway transaction in September 2022).

Based on management guidance and commentary as well as peer and M&A valuations, SNC's SNCL Services business and the Capital segment's portfolio of investments could be valued at $45 per share and ~$10 per share, respectively. Accounting for projected future losses from LSTK Projects, corporate costs, projected net debt, and non-controlling interest of ~$17.50 per share yields a base case sum-of-the-parts fair value of $37.50 per share (with bull and bear cases of ~$47 and ~$27 per share, respectively).

Potential catalysts include the roll-off/completion of unprofitable legacy LSTK contracts, the opportunistic monetization of capital investments, better than expected growth/margins at the core SNCL Services business, debt reduction, share repurchases and/or accretive M&A. Risks include management execution, raw material/cost inflation, leverage, competition, currency fluctuations, regulation, legal liability, labor issues, pandemics and/or a recession.