Company: Calian

Conference Title: Calian's First Quarter Results

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Operator: Good day ladies and gentlemen and welcome to Calian's First Quarter 2020 Financial Results Conference Call. As a reminder, this call is being recorded. It is now my pleasure to turn the conference over to Mr. Kevin Ford, Chief Executive Officer. Sir, please begin.

Kevin Ford: Thank you Chelsea and good afternoon ladies and gentlemen. With me today is Patrick Houston, our CFO and we'd like to welcome you to the Calian's First Quarter 2020 Conference Call. I'm very happy with our first quarter results. We again post to the quarterly revenue records of $99.2 million up from Q4 is quarterly record of 90.9 million. While posting our sixth consecutive quarter of record revenue growth, we also reported a 73rd consecutive profitable quarter. The results reflected continued focus on profitable growth as we successfully execute our organic and acquisitive growth strategy. I once again would like to thank our dedicated team at Calian, all of our staff employees for their efforts. It is very much appreciated. I now ask Patrick to review the quarterly numbers and I'll provide some comments at the end, so over to you Patrick.

Patrick Houston: Thank you Kevin. It's exciting to again post record quarterly results reflecting our continued revenue and earnings growth. First quarter revenue gained 24% year over year while EBITDA growth was 47%. The stability of our diversified business was evident in the quarter as Advanced Technologies, Health, and IT posted solid revenue and EBITDA growth compared to the prior year's first quarter. We continue to believe that Calian's diversified profitable growth engine is one of the company's unique strengths.

Consolidated gross margins in the quarter were 20.4% compared to 21% in the Q1 of the previous year. The slight decrease was due to project mix in the quarter. Our focus continues to be the introduction of existing and new products and services into new markets in order to increase our margins. Operating expenses in the quarter were $11.8 million, this compares to $11.2 million in the same quarter of the previous year, a 6% increase. We continue to invest in capabilities to help our growth agenda; this includes augmenting our sales and marketing capabilities, building capacity in our innovation agenda, and strengthening business support to integrate recent acquisitions.

Adjusted EBITDA for the quarter was $8.4 million or $1 per share basic and 103 per share diluted. This increased from $5.7 million or $0.73 per share in the same quarter of the previous year. Adjusted EBITDA in Q1 included a favourable impact of $0.7 million from the adoption of IFRS 16. You can see our reconciliation in the financial statements in MD&A, explaining the change in the accounting. Net profit for the first quarter was $4.3 million or $0.55 per share. This was up from $3.4 million or $0.43 per share in the same period of the prior year. Working capital in the quarter increased by $21 million, this was the result of growth of our business and progress made in our large ground system project.

Working capital demand on the large ground system project in the quarter was approximately $16 million. We expect an additional $6 million of working capital demand in Q2, as we reached the peak demand for that project. Our cash balance ended at approximately $14 million and subsequent to quarter end we expanded our credit facility with RBC from $40 million to $60 million.

Finally, please note that certain information discussed today, it's forward looking and subject to important risks and uncertainties. The results predicted in these statements may be materially different from actual results. I'll now turn it back over to Kevin for his comments.

Kevin Ford: Thank you Patrick. So I just wanted to echo Patrick's comments and again talk about the fact that I was pleased with the results in the quarter. When advanced technology posting very

positive organic revenue growth, 68% from the same period a year earlier obviously is strong contributions from our large ground systems project, and a new mobile wireless product that we've now gone live with for Tier 1 North American mobile provider. Our health revenues rising 10% from year earlier and as demand increased on our clinician services on psychological assessment services. IT similarly posted 9% revenue growth on stronger sales focus for our cybersecurity practice. And learning revenues declined slightly reflecting generally a pace of demand on our core training contracts and focus on security new business going forward.

Post to Q1 quarter end on January 31st we announced the acquisition of health services companies Allphase Clinical Research Services Inc. and Alio Health Services Inc. which was an exciting announcement for our health segments in support of our growth objectives. The companies serve the pharmaceutical and medical device industry, and the broader healthcare sector with clinical trial services, specialty medication support, community care and other services, all enabled by an innovative healthcare delivery management software application. This acquisition supports all four pillars of our growth framework, and specifically helps diversify our customer base in the pharmaceuticals, home care and hospitals, and supports Calian's innovation agenda with services enabled by software.

Continued investment in R&D, M&A, and our own internal innovation will be critical to our long–term profitable growth and continued to push into global markets. Our recent filing of a shelf prospectus is an important step in providing flexibility as we continue on our growth agenda. And closing I'm pleased to see the Calian growth story continuing Q1 following a record performance in fiscal year 2019. We've received very, very positive feedback regarding our reporting aligned to the four segments which we introduced at the end of our 2019 Q4 and full year results.

The four segments of Advanced Technology, Health, Learning, and Information Technology are highlighting our focus going forward, and have helped simplify the company for our shareholders. Our focus within the segments continues to be on inquisitive and organic growth, innovation, and

global markets. I look forward to talking to our shareholders and analysts tomorrow about Calian's diverse business and growth adjustment achievements at our AGM and Annual Investor Day being held tomorrow February 6th at the TMX Broadcast Centre in Toronto, starting at 9:45, and if you're available, please attend.

Lastly, the traditional markets in which Calian operates are stable and management expects organic revenue and earnings growth to most or all of our segments through the successful execution of our growth strategy. However, we must caution that revenues realized are ultimately dependent on the extent and timing of future contract reports as well as customer utilization of the existing contract vehicles. Based on currently available information and our assessment in the marketplace, we expect revenues for fiscal 2020 to be in the range of $380 million to $410 million. EBITDA per share in the range or adjusted EBITDA per share in the range of 425 to 455 and adjusted net profit in the range of $2.50 cents to $2.80 cents per share. So with that Chelsea, I'd like to now open the call up to questions.

Operator: Yes sir. If you would like to ask a question, please signal by pressing star one on your telephone keypad. If you are using a speaker phone, please make sure that your mute function is turned off to allow your signal to reach our equipment. Again, please press star one to ask a question. Our first question will come from Jeff Lavoie[?] with Desjardins.

Jeff Lavoie: Yeah. Good morning gentlemen and congratulation for the strong quarter. I just wanted to start with the guidance. I just wanted to make sure that the increase to the guidance was mostly driven by recent acquisition announced on Friday last week.

Patrick Houston: Yes. We increased the revenue guidance by about $15 million that the bottom and top [inaudible] about three quarters of that was related to the acquisition and about a quarter or it's just continued pace of our existing business we saw a strong Q1 and we're expecting that to continue throughout the year.

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Jeff Lavoie: Okay. So it's on the revenue line but also probably on the EBITDA in the adjusted EPS as well.

Patrick Houston: Yeah, it was similarly down the three – three kind of moved up together, so we're just expecting continued performance of our existing business as well as the impact of the new acquisition.

Jeff Lavoie: Okay, perfect. And when we talk about this acquisition, how should we be thinking Patrick's in terms of amortization of intangibles and also Goodwill for those two acquisitions in the future?

Patrick Houston: Yeah, we have – you know, we just closed the deal last week. So we haven't had the opportunity to do the valuation and at the same point have the auditors go through it. So I have to defer to the next quarter and at that point I can give you some more color, but I would expect it to be similar to our prior acquisitions in terms of ratios of intangibles and Goodwill as an initial kind of point.

Jeff Lavoie: Okay. No, that's good color. Thank you very much. And when we looked at the advent's technologies, I mean the growth was very impressive at about 64% with only about 7% coming from M&E. So I was curious if you could talk a little bit about the key driver of this organic growth. I know there's probably a lot that come from the large satellite contract, but I just wanted to have your view on this one.

Patrick Houston: So two distinct events really obviously progressed on our ground system. We said this was going to be the big year for that one, we're seeing good growth. The other one really is the first shipment of our first wireless product. So we put a press release out announcing that. So we were able to develop this product over the last couple of years. It's being deployed by Tier

1 mobile carrier in North America. So that's really exciting for us, because it's our first foray into that space, but again, shows the capability of our advanced technology. So that contributed as well to that organic growth in Q1.

Jeff Lavoie: Okay. And would it be fair to assume that about 50% came from the ground system and 50% of the organic growth came from a mobile carrier or that mix was a little bit different.

Patrick Houston: More weighted towards the large ground system, but good first quarter on our mobile space and I think that one's going to continue to pick up pace throughout the year.

Jeff Lavoie: Okay, great. And if we look at the learning side, I mean the backlog remain extremely solid, but the revenue growth was a bit impacted by the slowdown in demand. How should we be thinking about demand or organic growth in the quarters to come for that division?

Kevin Ford: Alright. Now, what we're trying to do is across each[?], there's a 5% organic growth. So we're trying to look at that to consistently across each of the segments. So learning is right now with our key defence contracts and we'll move up and down in the quarter depending on demand and scheduling and timing of exercises that we run from the military. We're seeing some good portion on our emergency management services. So again, timing of those will affect it. But I think for modelling purposes, keep it in that 3%to 5% range. I think is realistic organically as we now focus on how do we move that learning segment up to double–digit growth. But for modelling, I think 3% to 5% it's a good way to look at it going forward.

Jeff Lavoie: Okay, perfect. Thank you very much. And maybe a last one from me. On the IT side, the margin was very strong on 9.9%. So would it – so I was wondering what should we expect going through the fiscal '20, should we expect a similar margin? And also I was curious to know if you could provide a little bit more color around the business mix of this segment, so product versus services please.

Patrick Houston: Yeah. So we were really pleased with the increase in margin. It's really been pretty conservative effort between the last couple of years of moving that up in our IT group. So really pleased with the progress that Sandra who's the VP of that group has really been doing with her team. You know, on some of the product we sale and because we don't recognize the full revenue but just the margin that's helping us increase. So right now the product sales is still a small portion, but the margins are much higher than our traditional resource based contracts. So we continue to really look for – to increase that mix over time. And I think as we do that the margins continue. I think in the short term we're hoping to at least hold the margins we've seen in Q1. But again, objective is to continue to increase that in the future.

Jeff Lavoie: That's good color. Thank you very much.

Operator: Thank you. Again, that is star one to ask a question and our next question comes from Deepak Kaushal with [inaudible]. Deepak make sure your phone's not muted. Deepak I think you're on mute. Alright. We'll go to the next question we have from Doug Taylor with Canaccord Genuity.

Doug Taylor: Yeah, thank you. Good evening. The acquisition – the strengthen in advanced technologies and the, and then the recent acquisitions is taking the spotlight off of the IntraGrain and SatService a little bit. But I wonder if you can provide a little bit of an update on how those two acquisitions are progressing since last quarter and perhaps comment on how they're tracking towards future earn–out targets.

Kevin Ford: Yeah, so both, I just did a review of SatService a few weeks ago and IntraGrain the same. Both are actually doing very well. In the context of performance both are seeing orders. They're both coming in from a context of growth that we've seen from last year. As far as earning the targets, we're going to get another quarter, we'll reassess our targets[?] how we're feeling

about that. We'll definitely see more positive momentum than we did the year before. And despite our announcements[?] you know, I am still very confident in those two companies, they're great, both of them have great teams and both of them are doing great things and they're all profitable. So, [inaudible] side, we'll see how that plays out and I'll update that next quarter. But right now I'm very happy and impressed with what they're both collectively doing, both in the context of new sales and orders, as well as progression on integration with our advanced technologies group, so still very positive.

Doug Taylor: Okay. Thank you. The advanced technologies and the large ground system build you provide a lot of color on the working capital impact in Q2. I mean, should we think as Q2 being, that being consistent with the peak revenue quarter for this particular build? And do you expect to recover any of the working capital that you've invested towards the back half of this year or will that be a fiscal 2021 event. And then, you know, in relation to that, perhaps you can talk about the prospects of, you know, filling the backlog for that type of satellite work in behind this large deal.

Patrick Houston: Sure. I mean, the revenue and working capital aren't completely linked as we're doing the revenue on a percentage completion of the entire project. But we have certain payments and milestones that we're expecting from the customers. That's why they're not completely linked. So I think the revenue will be fairly consistent throughout this year. From a working capital, yeah, there'll be another $6 million in Q2 and then likely flat in Q3 and Q4 is when it starts to unwind and not allow unwind over another 12 months after that, to start coming back in.

And then your second question on backfilling, I mean, we've got – we're working on several requests. There's lots of activity that we're seeing in the ground system business. So we've got some fairly nice projects that we'd like to win. And we're hoping to secure those in the short term and if we're able to do that that would contribute to revenue next year, which would help backfill

kind of the reduction on this large ground systems. So we're hoping to hear about those then in the next quarter.

Dough Taylor: Okay. I don't want to steal any more thunder from your event tomorrow, so a nice quarter. We'll see you tomorrow.

Patrick Houston: Excellent.

Operator: Thank you. Our next question comes from Jeff Lavoie with Desjardins.

Jeff Lavoie: Yeah, thank you very much. I just wanted to ask two small questions from a modelling standpoint on the R&D front. So you have spent about $3 to $4 million in the last two years on that R&D level. So how should we be thinking for fiscal year '20?

Patrick Houston: So you saw we've broken out R&D for the first time. So I think certainly as we spend more on that people are getting better visibility. I think for the current year the Q1 run rate will probably continue for the back[?] to the last three quarters. So I think that's what you should model in the short term. And you know, I think it accelerates in future years as we start to identify new projects.

Jeff Lavoie: Okay, great. Maybe lastly on the credit facility, so you mentioned in your opening remarks that you increased it to – from $40 million to $60 million. So I just wanted to make sure when we look at the increase should we – so would it be fair to assume that Calian is still on the lookout for more M&A deals despite the recent transaction announced last week?

Kevin Ford: That – that's correct. You know, from my perspective you know, as most are aware, we've staffed now permanent basic M&A office internally whose job is basically to continue to work with companies out there, whether it's on partnering or M&A opportunities. So yeah, we –

you know, the pace of the 10% growth minimum is something I'm very, you know, sincere and I've got acknowledge I'd like to keep that going, and that'll be both through organic and M&A. So we don't want to slow down M&A for sure, but we're also taking our time to make sure we're taking time to integrate the ones we've done. And we're on the lookout for sure. If you really think about our segments right now, you know, we've done two in Advanced Technologies over the last year. We've done one in the Health segment. Our Cyber Acquisition that we did in IT services that's almost two years ago now. So I think there's capacity there to look at other opportunities because of the capacity for the management team to integrate.

And then our learning business is also something I'm looking at with priority as we look to bring in more innovation into our learning services practices. So yeah, we're not – we don't think we're slowing down, but in the same spirit we're making sure, more importantly that these opportunities are good opportunities for Calian in longer term.

Jeff Lavoie: That's great. Thank you very much for the colors. See you tomorrow.

Kevin Ford: Thank you.

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Operator: Thank you. Again, to ask a question, please press star one. Alright and speakers we have no further questions in the queue at this time.

Patrick Houston: Okay, that's great Chelsea, and I think for – lastly on the forum tomorrow, I'm hoping that I'll be able to say hi in person at our Investor Day and updates. I'm excited about giving an opportunity for other people beside Kevin Ford to speak for a change in the company progress. And I just want to reiterate to my team, thanks again for a great quarter and look forward to providing an update for those that are able to attend tomorrow. And if anyone would like any further information, obviously don't hesitate to reach out. So with that Chelsea will we'll close up

this call and I look forward to giving out an update officially over the next quarter results in a couple of months. And for those attending tomorrow, we'll see you tomorrow.

Operator: Thank you. Ladies and gentlemen, this concludes today's teleconference and you may now disconnect. Please enjoy the rest of your day.