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ATCO Ltd.

Third Quarter 2023 Results

Conference Call Transcript

Date: Thursday, October 26, 2023

Time: 10:00 AM MT

Speakers: **Katie Patrick** - Executive Vice President, Chief Financial & Investment Officer
Lawrence Gramson, Director, Corporate Finance

Conference Call Participants:

Rob Hope Scotiabank – Equity Research
Maurice Choy RBC Capital Markets – Research Analyst
Mark Jarvi CIBC Capital Markets – Research Analyst
Linda Ezergailis TD Securities, Inc. – Managing Director



Operator:

Thank you for standing by. This is the conference operator. Welcome to the ATCO Ltd. Third Quarter 2023 Results Conference Call and Webcast.

As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask a question. To join the question queue you may press star, then one on your telephone keypad. Should you need assistance during the conference call you may signal an operator by pressing star, and zero.

I would now like to turn the call over to Mr. Lawrence Gramson, Director, Corporate Finance. Please go ahead, Mr. Gramson.

Lawrence Gramson:

Thank you, and good morning, everyone. We're pleased you could join us for ATCO's Third Quarter 2023 conference call. With me today is Executive Vice President and Chief Financial and Investment Officer Katie Patrick.

Before we move into our formal agenda, I would like to take a moment to acknowledge the numerous traditional territories and homelands on which our global facilities are located. Today, we're speaking to you from our ATCO Park head office in Calgary, which is located in the in the Treaty 7 Region. This is the ancestral territory of the Blackfoot Confederacy, comprised of the Siksika, Kainai and Pikani Nations, the Tsuut'ina Nation and the Stoney-Nakoda Nations, that include the Chiniki, Bearspaw and Goodstoney First Nations. The City of Calgary is also home to the Métis Nation of Alberta, Region 3. We honour and respect the diverse history, languages, ceremonies, and culture of the indigenous peoples who call these areas home.

Katie will begin today with some opening comments on recent Company developments and our financial results. Following these prepared remarks, we will take questions from the investment community. Please note that a replay of the conference call, a short supplementary presentation and a transcript will be available on our website at atco.com and can be found in the Investors section under the heading Events and Presentations.

I'd like to remind you all that our remarks today will include forward-looking statements that are subject to important risks and uncertainties. For more information on these risks and uncertainties, please see the reports filed by ATCO with the Canadian securities regulators.



And finally, I'd also like to point out that during this presentation we may refer to certain non-GAAP and other financial measures, such as total of segment measures, adjusted earnings, adjusted earnings per share and capital investment. These measures do not have any standardized meaning under IFRS, and as a result they may not be comparable to similar measures presented in other entities.

And now, I'll turn the call over to Katie for her opening remarks.

Katie Patrick:

Thanks, Lawrence, and good morning, everyone. Thank you all very much for joining us today for our third quarter 2023 conference call.

ATCO achieved adjusted earnings of \$81 million or \$0.71 per share in the third quarter of this year. Our non-utility investments delivered exceptional performance, helping to offset the earnings pressure associated with the rebasing of our Alberta distribution utilities and the normalizing inflation profile in Australia.

ATCO Structures and Logistics delivered adjusted earnings of \$28 million, \$10 million higher than the same period last year.

Building on the trend we've been speaking about for a number of quarters now, the key drivers of this earnings growth was the strong performance of our base businesses. Both our space rentals and workforce housing businesses delivered exceptional results in the period. Compared to the third quarter of 2022, we grew our space rentals fleet size by 9 per cent, and our average rental rate by 15 per cent. Our workforce housing division has been successful in refining our fleet and tailoring it to the specific needs of our customers, allowing us to grow our average rental rate by 28 per cent compared to the third quarter of 2022.

Supporting the communities in which we operate is core to our values. During the quarter, we provided support to some of the communities impacted by this summer's wildfires. One of the projects saw us remobilize an existing workforce housing camp in Valemount, BC to help support evacuees displaced by the fires.

As we look ahead to the fourth quarter of this year, we continue to expect our Structures business to deliver year-over-year earnings growth, but with moderation compared to what we had delivered in recent quarters this year. This softening is due to the typical seasonality the business experience in Canada in the later months of the year and the completion of key projects, including the Bechtel Pluto Train II accommodations and our Trans Mountain camps.



On a full-year basis, the strong performance the business has locked in so far this year will allow Structures and Logistics to deliver significant year-over-year earnings growth.

At Neltume Ports, the business delivered strong results, including adjusted earnings of \$7 million in the quarter, \$3 million higher than the same period last year. Favourable foreign exchange and increased ownership at Puerto Angamos and Terminal Graneles del Norte pushed third quarter adjusted earnings higher when compared to 2022.

Subsequent to quarter end, our joint venture with Nautilus, referred to as the Vancouver Bulk Terminal, announced an agreement with Solvay. This opportunity will see us work with Solvay, a global leader in the soda ash market, on a newly designed terminal that will have the capability to annually export more than 2.5 million tonnes of soda ash. Construction of this terminal is expected to begin in 2024, with completion in 2026. This is an exciting opportunity and reiterates our focus on growth and the deployment of capital in Neltume.

As expected, our Canadian Utilities investment saw adjusted earnings decline by approximately \$19 million when compared to the third quarter of last year. This decline was primarily due to the impact of rebasing at our Alberta based distribution utilities as previously mentioned. This rebasing pressure was compounded by year-over-year earnings pressure in the Australian natural gas distribution business, as inflation levels have moderated in 2023 compared to the highs experienced in 2022.

Looking ahead to the fourth quarter, for our Canadian Utilities investment, we expect many of the same themes experienced through the first nine months of the year to continue. While I won't go into too much detail on this point as Brian spoke about it earlier in the CUs call. October saw CU receive two regulatory decisions that helped provide regulatory certainty moving forward, the AUC's decisions on both the generic cost of capital, GCOC, and the third performance-based regulation (PBR) framework.

Our Canadian Utilities investment provides ATCO a stream of stable and reliable earnings and cash flow and these announcements reinforce the prospective and constructive nature of the regulatory system in Alberta as they enter 2024.

Overall, ATCO delivered a third quarter that was in line with our expectations and highlighted the strength of our diversified portfolio. Our non-CU investments delivered very strong results that helped soften the impact of rebasing and downward trending of Australian inflation. With this being a key transition year at our largest investment, CU, we continue to look for opportunities to outperform



across our portfolio of investments. I look forward to sharing our full year 2023 performance on our next call in early 2024.

That concludes my prepared remarks, and I will now turn the call back to Lawrence.

Lawrence Gramson:

Thank you, Katie.

In the interest of time, we ask you to limit yourself to two questions. If you have additional questions, you are welcome to rejoin the queue. I will now turn it over to the conference coordinator for questions.

Operator:

Thank you. We will now begin the question-and-answer session. To join the question queue you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw from the question queue, please press star, then two.

The first question comes from Rob Hope with Scotiabank. Please go ahead.

Rob Hope:

Hello everyone. First question's on the Structures business. Can you maybe speak a little bit more in depth on what the key factors are that are driving the average rental rate upwards and whether you could see some additional upward pressure there? And then secondly, we have also seen utilization tick down a little bit. So is this a price over volume situation?

Katie Patrick:

Yes. Thanks Rob. I'll start just first with the pricing. We are seeing strong demand throughout many of our geographies for our units, so I think that is definitely contributing. Another factor that we're seeing is we have, as you see in the numbers, been increasing our overall fleet size. So we do have a number of new products that we've had that allows us to basically escalate some of the overall rent rates that we're seeing, and the benefit of that is that does apply across the fleet. So the average rate would come up. That is a strong—you know, I think we'll continue to see as we continue to grow that business and provide new products into the market that we'll be able to continue with that, provided that we do continue to see the strong demand spurred by the economic tailwinds that we have.



On the utilization, the corollary of that buildout of the fleet is that you do see a bit of a dip as you're expanding your overall fleet size and the utilization as it takes, first of all, some time to get those units on rent, there is transit in there, there's a few things that—but we're really happy with that number that we have for utilization. We think it allows us to adequately serve all of our customers' needs as well by having a little bit of excess capacity in there to provide our customers units when they need them.

Rob Hope:

All right. Appreciate that. And then secondly, the environment's seeing some infrastructure assets' valuations come down and it does seem like there's a number of assets out there for sale. Can you maybe speak about what the appetite is there on the corporate side to maybe look at M&A? If so, are there any geographies or assets critical that make—are most attractive to you right now?

Katie Patrick:

Yes. As we talked about on the CU call, we do have a strong balance sheet and we want to use that opportunistically to advance our growth. In previous quarters I have said that we hadn't yet seen the private market valuations fall in line with what we're seeing in the public markets. But we are starting to see, as you've mentioned, a bit of a reversal of that trend, which was expected.

So I think we remain open and looking at potential opportunities to acquire some assets. I think the biggest areas of our focus across the whole company right now remain our core markets in Australia and Canada, as well as potentially the US in terms of opportunities that may arise there within the infrastructure categories.

Rob Hope:

Thank you.

Operator:

The next question comes from Maurice Choy with RBC Capital Markets. Please go ahead.

Maurice Choy:

Thank you, and good morning. Maybe I'll stick with the capital allocation discussion since you mentioned a few geographies. Now on a CU level, the utility obviously has amassed quite a bit of clean energy opportunities over the last two or three years. You noted direction in travel towards clean energy hasn't changed. It does feel like the pace is being impacted by higher cost of capital and higher cost overall.



Any thoughts on that? More broadly, what does that mean for ATCO as you allocate capital across the six essential services categories?

Katie Patrick:

Yes. Thanks Maurice. At the CU level, we kind of stated publicly both for our CU and for ATCO investments a percentage of non-regulated assets that is a bit higher than we currently have in our portfolio. So for some time we had significant investment in our utilities which has served us very well and we played a bit of catch-up, particularly with the acquisition of the energy, with the renewables portfolio. That said, we still continue to be, across our portfolio, very focused on investment in utilities where they make sense, and growing that, what we already have in the energy transition portfolio going forward.

So, I think, particularly this year, when you saw the significant acquisitions, probably a little outsized in terms of the capital allocation towards energy transition activities, but you should see a bit more balanced return between the two as you go forward back to the utilities.

Overall, I think, as I said, we're—with Structures doing so well though, we are starting to see that percentage of earnings contribution from the non-regulated side start to inch up, which you can see in the ATCO results is very positive. So, we will continue to focus on a balance between that reinvestment into the utilities as well as some of our non-regulated assets.

Maurice Choy:

Thanks. And maybe finishing off on S&L, and thanks for the color on the rental business earlier, however, I didn't notice any material new contracts being signed at S&L as part of your announcement today. Can you speak to your pipeline of potential projects, types of customers that are advancing towards signing? Maybe just more broadly, what tends to be the top reason why some of these counterparties may be holding back?

Katie Patrick:

Yes. Sure. Thanks Maurice. It's a great question. I'll start just by reiterating what I mentioned in my opening remarks, but our focus on really building that base business so we do have some stability in our earnings profile, which has advanced a lot. I think a strong proportion of our now ever increasing earnings are coming from that base business we're very happy with. That being said, we, of course, like the large projects. They provide meaningful earnings uplift when we can get them.



And the pipeline is very strong. I know that we have not announced. I think the reality is just as—our customers are taking a little longer to make some of these decisions on these large asset builds, and I think that is a function, of course, of the current economic times in terms of the volatility we're seeing in the capital markets and a lot of the other—the markets in general. But I think the economic support in many of these projects is moving forward and so we're hopeful that we'll get some of those in the near term here.

In terms of where they are and who they are, I think it is the geographies that we see the most activity, probably our Australia and in some regions of Latin America that there are some expansion of some of the mining projects in particular that I think could see opportunities for some of those larger accounts.

Maurice Choy:

Great. Thank you very much.

Operator:

The next question comes from Mark Jarvi with CIBC Capital Markets. Please go ahead.

Mark Jarvi:

Yes, good morning. Just coming back to the trends on Structures and Logistics, top line revenues are down year-over-year but margins are very strong. You talked about rental rates being good, customer activity good. With revenues being down, is that just, I guess, mix of types of contracts? Is there something, a conscious decision in terms of what you're looking for in terms of margins, in terms of anything you're bidding on now? Just sort of updated news in terms of how those two dynamics play out in terms of revenue and margins now.

Katie Patrick:

Yes, no, I think part of the revenue drop is probably largely to be attributed to the Bechtel Project, which as you know, obviously larger projects. Overall, I think we are seeing, as you say, an improvement in our margins, which you can see, comes a bit from the average rental rates increasing.

So, I mean, I think the conscious allocation between the businesses towards our base business continues to be the way that we're heading which should help in the long term if we're able to maintain the rental rates that we're seeing that margin profile.



Mark Jarvi:

Okay. And then you updated the normal course issuer bid parameters but it doesn't seem like you've acted on it. Share price is weaker. What would tip you to kind of be more active on the buyback right now? Is it that you're holding back cash because you're seeing more opportunities around private market, new investments, or just what sort of informed the decision not to use the NCIB at this time?

Katie Patrick:

Yes, no, we updated, we increased. We did use up to our maximum that we had approved. It's a small amount. We haven't—we're not talking about a massive NCIB program. We increased it to 2 per cent. So I think as we said in the past and we continue to—how we would utilize that is at times we will see a disconnect between what we think is the true value of our assets and the market pricing and we'll look to opportunistically buy back shares in those circumstances.

So, won't set a specific price to say when that happens or how, but we certainly monitor all the time.

Mark Jarvi:

Okay. Thanks.

Operator:

Once again, anyone on the conference call who wishes to ask a question, may press star, one at this time.

The next question comes from Linda Ezergailis with TD Securities. Please go ahead.

Linda Ezergailis:

Thank you. I'm wondering if you could just give us an update on what discretionary capital is left at the Neltume level once you notionally allocate this latest expansion that you recently announced with Vancouver Port. Maybe comment on what further investment opportunities you see at Neltume, and if and when and to what extent that would warrant kind of a capital call or infusion from ATCO?

Katie Patrick:

Yes. Thanks Linda. We still, as we've mentioned in previous quarters, we still continue to have cash on the balance sheet in Neltume and I think we can get a follow up on the exact number but it's been in around that US\$100 million at the moment that we have or a little bit more on the Neltume balance sheet.



The project in Vancouver, there's a couple of things to note there. We're still working through exactly how we will be financing that, but we will be looking for, obviously, some debt financing considering we have a secured offtake on that. We are also, I might add, 50/50 partner with Nautilus in that venture. So, even after the use of the capital there, we will still have a strong amount of cash on the balance sheet at Neltume to pursue new projects.

So, the theme remains the same in terms of we're looking at the multi-purpose cargo, the smaller ports around the world, and particularly the Americas, with a focus on expansion outside of Latin America into the US.

So, we have a—they have a number of opportunities in that pipeline. In the near term, I would not say that we see a specific need for a capital injection into that business in the next, probably, 12 to 24 months. But, of course, that could always be dependent on a good opportunity at the right moment.

Linda Ezergailis:

That's helpful context. Maybe just following up on your space rental and workforce housing. As you expand kind of into new markets and provide new products, how much would be gaining market share from existing demand versus the market itself growing? What's the runway for continuing to gain market share versus when you start bumping into a competitive response from other incumbents or entrants?

Katie Patrick:

Yes. Thanks Linda. No big surprise, in Canada and Australia in particular, we have a very strong market share position, and we have seen both of those markets grow to an extent. So I think there's a bit of a balance between a small incremental market share gain and overall growth of those two markets in particular.

And the other markets that we operate, I would say there's significant room for us to gain market share in particular. We have seen a good amount of expansion in the US where our market share is very small and we do have the ability to make headways in that, and plus you have the growth obviously overall in the US market. Similar situation in some of the other markets we operate in - Mexico and in Chile. There is—there's plenty of room for us to gain share versus our competitors without necessarily impacting too much market response.



So, I think the dynamics are different by geography, but as I mentioned, particularly in Canada and Australia, we are reaching sort of the top end of what we think is a good market share for those countries.

Linda Ezergailis:

Great. Thank you for that context.

Operator:

This concludes the question-and-answer session. I would like to turn the conference back over to Mr. Lawrence Gramson for any closing remarks.

Lawrence Gramson:

Thank you Operator, and thank you all for participating today. We appreciate your interest in ATCO and we look forward to speaking with you again soon.

Operator:

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