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Jacobs Engineering

Water Solutions Discussion

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CORPORATE PARTICIPANTS

Anna Kaminskaya, *Senior Engineering Construction Analyst, Bank of America Merrill Lynch*

Bob Pragada, *President of Buildings, Infrastructure and Advanced Facilities, Jacobs*

Greg McIntyre, *Executive Vice President and General Manager, Buildings and Infrastructure Americas*

Peter Nicol, *Senior Vice President and Global Water Market Leader*

PRESENTATION

Operator:

This call is not for media representatives or Bank of America Merrill Lynch investment bankers or commercial bankers including corporate and commercial assets. All such individuals are instructed to disconnect now. A replay will be available for Bank of America Merrill Lynch investment bankers and commercial bankers, including corporate and commercial FX. The replay is not available to the media.

Good day and welcome to the Bank of America Merrill Lynch deep dive into Jacobs Water Solutions business conference call. Today's conference is being recorded. I would now like to turn the conference over to Ms Anna Kaminskaya. Please go ahead, ma'am.

Anna Kaminskaya:

Good morning everybody and thank you for joining us on the call today. I am Ana Kaminskaya, Bank of America's Senior Engineering Construction Analyst and I am very pleased to introduce to you senior management from Jacob's Engineering. Today we have with us Bob Pragada, President of Buildings, Infrastructure and Advanced Facilities; Greg McIntyre, Executive VP and General Manager of Buildings and Infrastructure Americas; and Peter Nicol, Senior VP and Global Water Market Leader. Both Greg and Peter joined Jacobs with the CH2M acquisition where they previously held senior roles in CH2M water platform.

You should all have links to the slides of the presentation that you should follow with the call invitation today. If you have any difficult accessing the slides, please send our team and email and we will send you the link. The call invitation also has links to an in-depth report from our thematic research team on global water markets which might also be of interest to read together with today's presentation from Jacobs.

Just wanted to highlight that Jacobs remains one of our top picks for the year as we think the stock price is not fully reflecting ongoing transformation inside of the company with upside to growth and free cash flow over the coming years. We also think Jacobs water platform post CH2M acquisition is still not fully appreciated by the investment community.

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With that, I'll turn the call over to Bob and after the prepared presentation we will have time for Q&A. You can either ask your question live on the call or you can send them over an email to me at anna.kaminskaya@baml.com. With that, Bob, Greg and Peter, I'll turn the call over to you, if you can go through your prepared remarks.

Bob Pragada:

Okay. Anna, thank you. This is Bob Pragada. Thank you, Anna, and welcome all to our Water Solutions Business Call. To start, we wanted to briefly describe our overall Jacobs platform serving multiple end markets and geographies. We are approximately a $15 billion enterprise with over 77,000 employees providing professional services across diverse end markets and clients. Our geographical breakdown as of fiscal Q3 of this year is approximately 60% U.S. based and 40% outside of the U.S.

As Slide 4 depicts, we are organized by end market into three lines of businesses: our Building Infrastructure and Advanced Facilities, BIAF business; Aerospace Technology, Environmental and Nuclear, ATEN line of business; and our Energy, Chemicals and Resources, ECR line of business. Our BIAF and ATEN lines of business provide consultancy, advanced engineering and project construction management services across their respective end markets, while our ECR business is very focused on end-to-end project delivery across both sustaining and project capital programs, predominantly in the industrial space. Our BIAF business represents over 40% of our company's business by revenue and nearly 50% by operating profit.

Turning to Slide 5, we want to describe in further detail our BIAF line of business. We are seeing strong infrastructure demand across the globe, predominantly driven by a couple of few factors: population growth, aging infrastructure and strong urbanization trends. The U.S. is leading the way in this growth trend with the Middle East and Asia showing strong demand.

We'll be focusing our discussion today on our Water Infrastructure business, however our BIAF business is also experiencing strong growth in both the transportation sector spread between highways, rail and aviation, as well as our Advanced Facilities business.

In our growth environment in the Advanced Facilities business, we are seeing a notable uptick in the electronic sector, specifically in the semiconductor manufacturing and data storage sectors. This is being driven by strong technology growth in mobile computing, cloud storage and artificial intelligence.

Our BIAF line of business is pretty evenly split globally with 60% in the U.S. and 40% internationally, and an even 50/50 split between our public and private sector clients. Backlog trends continue to be very strong with over $11.3 billion of business in backlog at the end of fiscal Q3.

Turning to Slide 6, I'll now turn over the presentation to Greg McIntyre. As Anna said, Greg is our Executive Vice President and General Manager of our Buildings and Infrastructure business in the Americas, and was the former Water Business Group President and a board member of CH2M. Greg.

Greg McIntyre:

Thanks, Bob. On Slide 6, the agenda for the rest of the call is we're going to frame the water market and the market drivers as we see them, talk about Jacobs competitive position, also cover our business profile and our global leadership position in technology and delivery. Then I'll turn it back over to Bob who will provide a summary and a wrap up.

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If you move to Slide 7, which is framing the water market, I think we all know the global water market is very large and very fragmented. The first slice we usually take when looking at the market is where is the water consumption by users. This does not necessarily translate to spend. This is just water consumption, and obviously agriculture is the biggest user globally. If you look at the middle pie chart, for developed countries which is really where we are focused as Jacobs, focusing on about 15 countries, it a much more balanced view. As Peter will talk about later, we do serve all users, both ag, industry and municipal, but our focus up-to-date has been on the municipal side and on the industrial side.

The pie chart on the far right is where we begin to look at the actual spend, and this does include the municipal and industrial sectors. As you can see, 80% of the spend is on capital and operating expenses, and about 20% on equipment and chemicals. Our focus at Jacobs is on cap ex and op ex; we do not provide equipment, nor do we sell chemicals.

If you go to Slide 8, I'll dig a little deeper into the addressable market as we see it at Jacobs. As I mentioned, our focus is on cap ex and op ex, and the global market is somewhere between $600 billion and $700 billion a year of spend. This is not need. There's really big numbers thrown out there about the need in the market; this is the view of spend today and you can see the breakdown between capital and operating expenses.

When we look at the addressable market for us, the first thing we focus on is the capital spend in the target countries we're focused on. As I mentioned, we're focused on about 15 countries around the world, and because of that there's some very large markets that, frankly, in the water space we don't play in, example being China or Japan.

The second thing we do is look at the target services that we want to offer in that country. We do provide professional technical services across the world, associated with that capital spend, and they would include services like planning, design engineering, construction management, program management, strategic consulting and asset management. In addition, in the U.S. we focus even more on broader delivery platforms and we do design build services and outsource operations and maintenance. As you can see in the table, in the U.S. we have a lot more granular data about the addressable market by service type, but in summary, we see the addressable market in the U.S. being approximately $15 billion, and outside the U.S. about $8 billion. Of that $23 billion addressable market, our estimated market share is just north of 6%, so we see it, again, a lots of room for growth.

If you go to Slide 9, I'll talk a little bit about the market drivers. On the left-hand column, this is what I call the traditional market drivers, traditional because they're really not new. These drivers have been in place for many years. They include water scarcity and security, Bob already mentioned population and urbanization, but on urbanization, as noted in the Bank of America report, urban water demand alone will increase by 80% by the year 2050.

Obviously aging infrastructure everybody knows about.

Recent and emerging regulations, and here I think it's less federal regulation and real driver we're seeing is state regulatory drivers, such as one of the project examples I'll mention later, the City of Houston, and then in Florida one of the big drivers there is the Ocean Outfall legislation.

Not shown here though is there's always modifiers to these drivers that influence the actual market spend year to year. Those include how's the economy doing, how's the new housing starts and housing growth, what's the tax revenue base in the communities we serve? Those three things combined create the political will to raise rates or not raise rates. Other modifiers include the private capital spend and really the misunderstood value of water.

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Between 2008 and 2014, those modifiers I just mentioned created big headwinds to the market growth. We didn't see a lot of growth. Since 2015, these have become tailwinds. The economy is strong. Housing starts are up. The revenue base is there and the political will to raise rates is there, so it's been a positive market.

Having said all that, the real accelerator today is climate change induced extreme weather events. I'm sure no one on this call, that there isn't anybody that hasn't been impacted by drought, wildfire or flooding. Almost every day the media will be reporting places where there's too much water or there's too little water, and that's really the driver and the big accelerator for the market today.

Now going to turn it over to Peter who's going to talk about our competitive position.

Peter Nicol:

If we move to Slide 10, just looking at the unique competitive position that Jacobs has in the marketplace. Certainly as we explained earlier, we look at all water users. We target the industrial clients, the municipal clients and we provide a range of services to agricultural clients also, because our business really leverages off of clients and the challenges and the solutions that they're looking for, and then the unique skills of the people that we have to be able to work with them to provide those solutions.

Certainly services across the entire water cycle, from the ground water and surface water that are the surface supplies that we're looking at for those clients, the quality challenges, drought resiliency challenges that they're getting into, and then on the treatment side, drinking water reuse and wastewater treatment, and then really trying to put a quality product back into the environment as it goes back into the water cycle with respect to that.

All of this is built on a full-service delivery platform, as Greg talked about earlier with respect to that, and really working with those core clients across certainly our BIAF business, but as Bob talked about earlier with our ATEN and our ECR client base, certainly Jacobs brings us a platform of an expanded group of clients that we can really provide water services to as they look to how do they solve their challenges in dealing with water quality and water challenges around the world.

Certainly a number of industry awards. We're proud of our engineering—sorry, on to Slide 11. We're very proud of our engineering news record recognition with respect to our position in the marketplace in one or two and most of the major components of the water markets. But certainly, the industry recognition that has come through awards such as the Stockholm Industry Water Award; it's been the dubbed the Nobel Prize of water. It's presented in the presence of the king and queen of Sweden, and certainly an internationally acclaimed award from the Stockholm International Water Institute for our leadership in advancing state of the art methodologies and technologies to clean water for potable reuse, as well as increasing public acceptance of recycled water, which has been very important as reuse gains strength around the world. Then, from Global Water Intelligence, the Water Company of the Year Award, we're a past winner of that; also very proud of that.

Greg McIntyre:

Moving to Slide 12, I'm going to spend a few minutes on this talking about our water business profile. First, let's look at it by client type. As I mentioned, very fragmented and a very local market, so very relationship based. Today, Jacobs is primarily focused on the municipal market, but we see a great opportunity to leverage Jacobs industrial client base and relationships to really grow the industrial component of the business.

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If you look geographically, as you can see, we're predominantly in the United States, but as noted on the previous slides, we still see lots of room for growth, even in the U.S. because we're about 8% market share and there's no dominant provider. We also see a great opportunity to leverage Jacobs' global footprint in places like Australia, Southeast Asia and the United Kingdom, to grow outside of the United States.

Then the last pie chart talks about our delivery platforms. We have three main platforms; our consulting business, which I mentioned previous is planning, design, construction management and program management; our design build business and our outsourced operations and maintenance business. We like to maintain a balanced portfolio across here and keep our design build business in the 20% range of our overall business as a way to manage our risk profile, and this is very powerful to have all three delivery platforms so we can provide a full set of services to move projects from concept to operations, and the most important thing here is we're not focused on any particular service offering. We can really listen to our clients, understand what they need, and tailor a solution and be the integrator, and if needed, design, build and operate the solution for our clients.

Let me talk a little bit about our Design-Build and O&M business. In Design-Build, we really differentiate ourselves here based on our process technology expertise. Peter is going to talk about technology in a minute, but that's how we differentiate ourselves in pursing this work. Also, we focus on a less risky progressive design-build approach. In fact, over 90% of our Design-Build portfolio today is progressive design-build where our clients select based on qualifications and experience. Together, you collaborate with the clients to develop the design and then we bid out packages, about 60% design, and we do it in an open book fashion with our clients, so we get market coverage before we agree to a construction price.

On the O&M side, we provide outsourced operations and I want to be clear we do not own the assets here. The clients retain the ownership of the assets and they outsource the operations to us. We operate over 270 water and wastewater plants, serving over 8.7 million people and treating over 1.1 billion gallons per day, predominantly in North America but we do have operations in some other parts of the U.S.

Going to the next slide and talk about global leadership in technology.

Peter Nicol:

Our technology team is a team that's completely integrated within our Water Service Group. We have about 6,000 staff globally that really provide water services to clients, and our technology teams are embedded within those. Certainly we've had a long-term investment in our technology organization, senior technology subject matter experts and icons that we leverage and try to make available to our key programs around the world. We have a technology career path so that people that really aspire and revel in what they do in the technology world have the opportunity to grow within our organization and to really be recognized for what they provide and the skills and capabilities and experience that they bring to the marketplace.

Certainly very proud of a number of technology firsts that we've had the opportunity to partner with clients in over the years, things like the first aquifer storage recovery project in the 1980s in the U.S.; first use of the patented biological nutrient removal process; in the 1990s, the first use of membrane reactors for wastewater treatment. Then, more recently, investment in proprietary processes and modeling tools as we've continued to see digitalization and the availability of some of the computer models that are out there, we've leveraged those to help support our Design-Build business with some of the fast sort of things that we can put together to really take a quick look at a project to understand what might be

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necessary in providing a solution to that client, or some of the things we might be doing on the resiliency side, some of the risk modeling things that we might be looking at from a flood perspective. Also, some of the simulation and optimization analysis tools that we provide to our teams, we've developed those in-house. We make them available to the clients that we work with and we continue to invest and upgrade those as the market continues to move forward with respect to that.

If we look at—moving on to Slide, 14, this is how our Technology organization is organized within the Jacobs platform. We take our water business and we really look at it in the key end markets that we're focused on: drinking water and reuse, wastewater, water resources, and then conveyance and storage, which are really the system that pulls it all together and brings that to a front.

Under those, we've got all the subsets of each of those various marketplaces, and then we've got community of practice. We run about 180 communities of practice across the water platform that really bring all of our people together so that they have an opportunity to share and resource from each other so that we're always sharing best practices across that platform and making them available so that any client has access to what we've done anywhere in the world.

Greg McIntyre:

Moving on to Slide 15, just wanted to dig a little deeper into some key examples. We've got a couple of things highlighted here on some of the key projects that we've worked on and some of the innovations that we've had the opportunity to work with, but, you know, this really starts with our clients. All the clients that are listed here as project examples have been long-term clients of the Jacobs platform and what we've got here. Certainly Lakeview, the membrane technologies that we put there, those are something that we've been working with that client since the 2000s in putting that program together, but that's a client that we've been working with since the '50s, and we've put together the overall plan for the development of that community, and all stages through it we've worked with that client on the wastewater and the water side of things to really develop and continue to put the technologies in place to support that growth and that urbanization as that community developed.

Then down looking at Thames 2100, that's really to protect London and the Thames Estuary from current and future tidal flooding through 2100, so it's really a look at the design and development of a flood management program to incorporate a series of fortifications, embankments, flood gates, pumping stations, outfalls and barriers to protect London, Essex and Kent from tidal flooding from the 175 kilometer tidal river Thames.

There are a couple of other examples listed there and certainly any questions on them we'd be pleased to answer, but we'll move forward and just focus a little bit more on some of our delivery aspects now.

Peter Nicol:

We're on Slide 16, and to wrap up the presentation we wanted to provide some active project examples to highlight our leadership position in delivery. All these projects are active. These are not like cherry-picking the best projects from the last 20 years.

If you looked at the two columns on the right, what we're focused on, we tried to provide a selection of projects that represent the diversity of both our delivery platforms and our end markets. We picked some examples that cover program management. The next one's a traditional design project to the next one, a progressive design build, also a design build to operate in a strategic consulting project, and again, represent the diversity of the end markets that we're in.

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The first example I'll cover is another project in London called the Thames Tideway Tunnel. This is a US$7.5 billion capital program. The driver here is to improve the water quality of the Thames River, which everybody knows is a huge economic, environmental and valued public resource. The solution is to capture the combined sewer overflows where the sewer overflows during rainfall events to the Thames River, by capturing those in 11 connection tunnels, dropping by gravity into two 24-foot diameter tunnels that will run under the Thames River for the length of approximately 20 miles and then we'll collect that at a pump station, a very deep—I think it would be the world's deepest pump station—350-foot deep pump station that would then pump it up and treat it at the existing Beckton wastewater treatment plant.

Our role here—we've been involved since 2010—has been the program manager of the delivery partner for both the conceptual design, design and construction effort. All construction packages have been awarded. We're now in the tunneling phase of this project.

The thing that's really unique here that I want to highlight is how the delivery model evolved since we got started on this project. Thames Water working closely with the U.K. government and regulator, Ofwat, actually moved to a P3 model, a public-private partnership model, and they created a new regulated infrastructure provider just for this single asset tunnel. That company is called Bazalgette Limited, and they (inaudible) to get bids to see who would bring the funding and fund, build, manage the tunnel system, and we've been involved every step of the way so our program team actually was a valued part of going to that new company, and we continue to run the program today.

Greg McIntyre:

Moving to Slide 18, Tuas Water Reclamation Plant. Just wanted to highlight the Singapore Public Utilities Board a little bit first because it's one of the most progressive water utilities in the world today. Certainly for Singapore it's all about water security. They really wanted to develop a program and we've worked with them over the past 25 years. They've been focused on this for probably the last 50 years in trying to make sure that they can leverage everything because they were buying a lot of their water offshore and they continue to have a relationship with Malaysia where part of their water comes by pipeline, but they've also turned the island into a catchment area so that all the rain that they get on an annual basis they can collect, treat and redistribute to their treatment systems. They've also developed a number of desalination facilities, then they take their wastewater plants and they turn them into reuse facilities so that the water can then be recycled back into the water cycle.

Tuas itself is the largest MBR facility in the world when it will be completed. It's currently under design. Separate industrial and domestic use water streams arrive and they'll be lifted 300 feet to the treatment plants so that they're arriving in the deep tunnels. We're going to have two outputs from that; there'll be an industrial water stream and then a new water stream, which again support the holistic approach to managing their water cycle. The treatment processes are all being designed to minimize energy consumption, sludge production and maximize the biocast production to generate electricity because one of the outputs that they're going to have is support their neighbor on the site, which is the Integrated Waste Management facility, so one of their outputs or waste products is going to be the fuel for the other facility as they've tried to integrate some of the services back and forth between those two, and Singapore is looking at this as their Tuas Nexus.

Peter Nicol:

Next example is the Northeast Water Purification Plant for the city of Houston. This will be the largest progressive design project of its kind in the nation, 320 million gallons per day, and it's being delivered over the next seven years by the Houston Waterworks Team, which is a joint venture between Jacobs and the CDM Smith. The driver here was really a state mandate to reduce groundwater withdrawals

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because overpumping of the groundwater was leading to ground subsidence in the Houston area. That was the key driver. Again, we were selected for this project back in 2015. We're currently in the design phase, completing the 60% design and moving into the construction phase.

The next example is again a water reuse example. It's the Agua Nueva—this is on Slide 20. The Agua Nueva Water Reclamation Facility in Pima County, Arizona where we're designing, building and in this case operating a wastewater nutrient removal system that can achieve the high standards for both reuse as well as surface water discharge into the Santa Cruz River. But what's unique here is that the full contract operations for 15 years and really the key differentiator here is there's no other one company that can provide a one-stop shop for an integrated design, build and operate.

The last example will be on non-revenue water.

Greg McIntyre:

Moving to Slide 21, Non-Revenue Water Pilot Program in Gwinnett County. Certainly water utilities for non-revenue water, it's water that either leaks through their systems, inaccurate metering so they don't really account for the water that they are producing and generating and moving through the system, and then we can also have water theft; people that hook up to either hydrants or illegal connections or a variety of other things. It's estimated through a variety of reports and certainly it was highlighted in the Bank of America report that utilities lose up to about $14 billion a year in non-revenue water, and then in the U.S. that accounts for north of $8 billion with a fair bit of that in the small utilities which can certainly least afford it, and then a significant part of that certainly in larger utilities.

Gwinnett County put together this pilot program, really to put in some of the real-time streaming analytics and geospatial dashboards to identify and characterize their non-revenue water so that they could do something about it. How do they do that?

They wanted to deploy both connected meters and advanced algorithms so that they could reduce the cost of water delivery and distribution, improve the management of that scarce water resource that they have, certainly improve their system operations, and then save money for the customers, because if they're already treating this water and distributing it and then not getting paid for it, customers are still paying for it in the rates that they're charged.

Certainly, as we look at non-revenue water across the world, it's a growing volume of water loss through the leaks, overflows and data handling errors, and then unbilled authorized consumption. It's part of the digitalization of water as we see it in the marketplace, and certainly will be a key component of the next phase of the asset management program in the U.K. A number of U.S. utilities are focused on how to do this. A lot of focus through organizations such as American Waterworks Association highlighting this as an issue.

Okay, Bob. Back to you for a summary.

Bob Pragada:

Okay. Greg, Peter, thank you. Just a couple of wrap up comments. As we've articulated, we're really excited about not only the platform that we have now coming together with CH2M, but the opportunities that are ahead of it. We do live in a large, global and fragmented market as it pertains to the water industry, and no one really has any dominant market share. Greg talked about it earlier. At 6% of the addressable market, we have a number one position in the holistic water market, and one that we feel we're uniquely positioned to grow for a couple of reasons. One, as we highlighted today, the market

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drivers are there for continued and sustained growth. Elements and trends such as urbanization, the political will as Greg talked about, as well as something that clearly has been in the news, not just in the recent times, but right now, today. A year ago, we were digging ourselves out of Hurricane Harvey in the Texas area, and just today the folks that are in the Carolinas are dealing with the aftermath of Florence. All of these show that the effects of climate change are here upon us and here to stay.

Coming together with CH2M, our water platform that Jacobs had historically had outside of the U.S. now with a very, very diverse offering, is positioning us for some long-term growth. Part of that growth coming from the diverse and long-term client relationships that Jacobs has had in multiple sectors, as well as leveraging the Jacobs footprint.

Our blend of sustaining and project capital work across the Jacobs business for over 70 years has positioned us to where we are in multiple geographies for the long term. We have not been—we have not had a majority of our portfolio towards large-scale projects where we would go into a geography and depart. When we go into a geography we stay for several years, and we believe that long-term nature of our business will really position us well for long-term growth in this market, and allow us to diversify our delivery platforms, as well as give us ample room for market growth.

We're excited and we look forward to your questions. Anna, I'll turn it back over to you and we'll open it for questions.

Anna Kaminskaya:

Bob, Greg, Peter, thank you so much for the extensive presentation. Anna, would you be able to give us instructions for asking questions, for the audience to ask questions live? Operator?

Operator:

Yes, ma'am. If you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. A voice prompt on your phone line will indicate when your line is open. Again, that is star, one if you would like to ask a question. We'll pause for just a moment.

Anna Kaminskaya:

As I guess we are waiting for some of the questions, maybe I can kick-off with some of my questions. I'm sure everybody is interested about the combination of CH2M and legacy Jacobs. Can you just talk in general what the combination brings to the water platform specifically, and can you contrast legacy Jacobs business versus CH2M business, and maybe where do you see the process of integrating of the two platforms when it comes to water platform of the BIAF platform? Just a general question on the state of integration and what the combination brings for water business growth.

Greg McIntyre:

This is Greg. I'll take the lead on that and Bob can add. When you compare and contrast the two legacy businesses, Jacobs and CH2M, obviously the CH2M water business was much, much larger, but Jacobs had really a strong platform in the U.K., in Australia and then also some in Southeast U.S. But today, I think the main opportunities to continue to drive the end market growth are really the ones that Bob just summarized. It's around really leveraging the industrial client relationships of Jacobs around the world, leveraging that global footprint. I think we're really excited about the footprint we have in Australia and Southeast Asia. Then, also, diversifying the delivery platforms outside the United States, I think there's a

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great opportunity particularly to leverage our O&M business outside of the United States into markets like the U.K. and Australia.

On Design-Build, we'll be very, very selective. We are doing some design-build work in the U.K., but obviously we want to be very selective there.

In terms of the integration, I think the integration is going extremely well. We've got one integrated operating model, one integrated organization and the people are all aligned to that so I think we're well along the way.

Peter talked a lot about the technology organization and that's been the real glue that has brought it all together because that technology organization is a global organization and with the communities of practice that we have we can really get all the people around the world up to speed on our best practices and the latest use of technology.

So, I think it's off to a great start.

Bob Pragada:

I'll just add a couple of comments. The integration, as Greg appropriately said, we're very pleased. We're now effectively three-quarters into the integration and we've already been experiencing the benefits of the combined entity now through growth. Through growth not only in sales in but even in recognized business.

On the power of the combined entity utilizing the platform that Jacobs had had previously, I'd probably characterize it specifically around enhancement of our solutions business. We are in the business, and we said this time and time again, of providing differentiated solutions to our clients to make our client's business better. With the capabilities now that we have in the combined entity, that ride up the value chain has just been accentuated, and we're now seeing our clients recognize us to not only working within what has traditionally been the envelope, whether it be a private sector client or public, the manufacturing or the process envelope, to now looking at all of the enabling works that drive that envelope and having a portfolio that can address it from a solutions standpoint. We're really, really excited about that.

Anna Kaminskaya:

Good. Maybe we can switch to just kind of growth and margin profile for the business as part of specifically Water. I think when you did the presentation CH2M acquisition, the Company was talking about 4% or 5% growth for water end markets. How much can market share add to the growth profile? Do you see upside from some of the regulatory changes? Then where does Water margins stack up relative to the overall BIAF segment?

Greg McIntyre:

I'll again take the lead on that. As we mentioned earlier, we think the overall water market is probably growing 4% to 5% organically year-over-year. Pleased to say that our year-over-year growth at Jacobs is exceeding that so we're taking market share. We're in the 7% year-over-year growth range with the U.S. leading the way over 7%, and international about 5%.

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Probably the most exciting thing to me is that year-over-year growth in the pipeline since we've come together, and our pipeline has grown over 20% now we've come together as one integrated Jacobs Water platform globally.

In terms of the margins, again, Bob could jump in and provide more details, but obviously I run the Buildings and Infrastructure in the Americas and I could tell you that the Water margins are higher than what we do see, particularly on the Transportation side, when we're comparing like services for services such as design or construction management. So, we do experience higher margins in the Water market.

Bob Pragada:

Just a comment there, and I'll profile it to what we at legacy Jacobs had prior to CH2M and what we see now. It kind of goes to that rise up the value chain.

In the water market, we historically had played in probably a low technology-centric, very much driven towards the municipal water market. Now with CH2M and as Peter highlighted, that portfolio of very technology-driven and holistic water solution business has had a nice effect on our unit margins for our offering. So, just broadly speaking, our unit margins around our water offerings business have gone up anywhere from 100 to 300 basis points on those offerings.

Anna Kaminskaya:

Great. Operator, do we have any questions on the line?

Operator:

There are no telephone questions at this time. As a final reminder, that is star, one if you would like to ask a question.

Anna Kaminskaya:

Okay. Then I guess I can continue. Can you just talk about overall U.S. municipal funding? It just seems like water should be a little bit more resilient to economic cycles but doesn't seem to so, right? What do you expect water market to do in the next downturn, and can you talk specifically about some of the regulatory changes that you touched on in your presentation? Kind of how much upside can it provide to the overall end market growth, and as outsiders, what can we track to get a sense of what's happening in the water infrastructure markets? Is it bond issuance? Is it just tax receipts, housing market? Just a broad question on municipal funding and also upside from some of the regulatory changes.

Greg McIntyre:

Okay. On the U.S. municipal funding, I think if you go back to my discussion around those modifiers to the market drivers, the economy, housing starts, which drive new connection fees, which drive capital, and then generally the tax revenue in the really cities, counties and communities we work, when I look at all that as package, I think we're on the front end of a cycle still, even though the spending really picked up at the end of 2015. What we can see into the near-term future looks to remain very positive because of all those underlying positive drivers and modifiers.

I think the important thing that we have always seen in the water market and Peter and I have been through many ups and downs in the cycle, is that the municipal side of the cycle, when the economy turns down, it takes the municipal market two or three years to respond to that. The industrial side will respond

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very quickly on their capital spending, but on the municipal side it could be two or three after a downturn that the cycle continues. I think that's also positive.

In terms of thing we're seeing, in terms of regulatory drivers, I'll make a couple of comments. There's been a lot of recent activity on the Hill in the last week or so which I think are positive signs. I don't think it's going to generate huge funding drivers for us, but the Water Resources Development Act got reauthorized; that's coming through. They still need to go to Appropriation to appropriate the funds, but the fact that they reauthorized that is a very positive signal and there's some big projects connected to that. Then the Energy and Water Bill by the Corps of Engineers is also positive. So, the funding is up, not huge but the fact that they're moving on those I think is a positive thing.

I think everybody is waiting to see if a federal infrastructure bill will come back into the cycle in 2019; we think it will, so that would be a positive thing.

Having said that, what's really driving the market is local, right? I mentioned a couple of examples, Anna, on state regulatory drivers. The City of Houston, that was a state regulatory driver which is driving that huge project. In Florida we have a couple of big programs in South Florida for Miami-Dade and North Miami Beach and some of that's being driven by state ocean outfall legislation because they need to get out of discharging into the ocean by, I think it's 2024—I may have that date wrong. So, there's lots—and California. California has a lot of state drivers around water reuse, non-potable reuse.

So, we see a lot of the action being driven by the states and we're not reliant on federal action on regulatory to drive the needs. I hope that answered your questions.

Anna Kaminskaya:

I think it's super helpful. Then, two questions to follow up. Have you seen much in terms of change from P3 in the water end markets? Because I think there was a lot of enthusiasm about the privatization of certain assets back a few years ago when Donald Trump became the president and there was a lot of talk about infrastructure builds. Secondly, maybe we can touch on international markets because you are talking a lot about the U.K., Australia as an opportunity, but I think it seems like the Middle East and China and Asia would be high growth markets too. Why is Jacobs not excited about those end markets? What are the opportunities there? Do you have to do acquisitions in international markets to get bigger outside of the U.S.?

Greg McIntyre:

Okay. First you talked about the P3 market, and I think—I'll focus on North America. The Canadian P3 market much more mature, established, both driven by the federal government and the provincial government, so we've been active in that market.

The U.S. a lot less mature. I'd agree with you, a lot of hype but we haven't seen a tremendous amount of action in the P3 market in the water market, but there are a handful of key pursuits and big programs that we are positioning for.

I do think we'd like to see a national infrastructure bill come to the forefront in 2019, which would hopefully help spur that market. When we look at the P3 market, it really, to me, comes down to collaborating with the clients or the owners to come up with an investable project with the appropriate amount of risk. That's what the market needs, investable projects that people will really competitively respond to, and the U.S. market is still on the early stages of that development.

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If we look at the international markets, and then I'll turn it over to Peter, but probably my fault on not emphasizing the Middle East. I think the legacy CH business has a strong footprint in the Middle East. We do quite a bit of work in UAE and Kingdom of Saudi Arabia and Qatar, but our footprint in water was bigger than the Jacobs footprint, that's why I wasn't emphasizing that.

Peter, you want to talk a little bit about the international market and what we see?

Peter Nicol:

Yes. Certainly, Anna, just focusing on that, we do see significant opportunities in the Middle East. There's a lot of activity going on in Saudi with their proposed water privatization, and we're talking with them and trying to understand what that model might look like and how do we work within the Jacobs platform to make that happen and carve out a potential role for us.

The UAE continues to have growth in development, and we're working closely with a number of key clients there. Qatar is still moving forward with a variety of things. Kuwait certainly could be on the forefront of a variety of different things, and again, this comes where we would leverage off the Jacobs industrial platform too, because if you look at the water spend in the Middle East—industrially, water spend globally is about 10% of the market. If you look in the Middle East, it's between 40% and 50% of the water spend, and so a lot of the opportunity is really with industrial clients. We think that we're quite excited by the opportunity to really support a number of things that Jacobs are already doing with those clients, and adding water to the platform that we delivered to them.

When we looked at the rest of the world, you spoke about China, and that's a very complex market. Challenging to really work domestically in the municipal market in China, but something that we follow a number of multinationals into, and so we do support our multinational clients in their water piece of their business, the water slice that they might have, but that's historically where we've seen success and we've had the opportunity to leverage growth there.

The combined platform that we now have with Jacobs, India is certainly a key focus of growth for us. We have certainly design resources there that we support the rest of our business globally, and then we have a number of core clients that we're working with, both leveraging our relationships with other clients that are helping India develop as a water platform, but also growing in cities like Bangalore and Delhi and Chennai and a variety of other places like that. We're also working closely with the Delhi Mumbai Industrial Corridor as they look at the industrialization and urbanization of India. Water will be a big piece of that growth and certainly a big factor as to how those communities develop, and we're working on the planning phase of a number of those opportunities, so we'll see where that goes and we'll certainly look to optimize our position and support those clients as they look for solutions to the challenges they're dealing with.

Anna Kaminskaya:

Operator, is there a question on the line before I move on with another question? Just wanted to double-check.

Operator:

There are no telephone questions.

Anna Kaminskaya:

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Okay. I have a couple of emails that I got. Can you talk about risk profile of your backlog? Concentration of certain contracts, what's the average size of a contract in your water backlog? Just as a follow-up, maybe have you had any large losses on a previous water contract? Can you talk about historical risk profile? If we think about potential for losses in the water end market, how large can they get and what went wrong if you had some problem projects?

Bob Pragada:

Greg, why don't I start this one off and then I'll turn it over to you, just to kind of talk about the backlog in its entirety? Anna, just a couple of broad comments and then I'll turn it over to Greg.

We actually are pretty comfortable with the profile of our backlog. We don't necessarily give guidance of the stratification of the backlog, but generally speaking there are no one or two or even a dozen larger jobs that are sitting in that profile. This is literally made up of hundreds of jobs, both sustaining capital as well as project capital work that's in those jobs. So, risk of cancellation or postponement is relatively low.

Now, we do have some larger pipeline jobs that we're looking at that would have a positive effect on that backlog, but today it's a pretty balanced platform backlog that has a nice blend of both sustaining as well as project capital, and that's across our three large geographies: the Americas, Europe and in Southeast Asia and Australia.

Greg, you want to add other comments?

Greg McIntyre:

No, that's a great summary, Bob. I think it goes back to when I was talking about our three delivery platforms. We really try to keep that well balanced with a big focus, 80% or more on low risk, consulting, engineering design services and outsourced O&M services, which is low risk. Certainly I'm pleased to say that in our Design-Build business in the last 10 to 12 years we've had no losses in that portfolio, so that portfolio has performed very well.

Anna Kaminskaya:

Great. Then I have another online question. How do you think about the sustainability of that 7% growth? Just thinking a couple of years out.

Bob Pragada:

We're bullish on it. In fact, we believe that with continued success in our integration and as well as moving up that value chain that we talked about earlier, that we could have a positive effect on it.

Anna Kaminskaya:

Got it. Then one last question from me. I think we're closed to the end of the hour. You highlighted one of your projects, the Digital Solutions business as part of the offering. Just how do you think about the business longer term? When can it start moving the needle for the overall business? Is it just a nice, cool example of new work that you're doing, or is it something that might actually be a meaningful contributor to growth or improving margin in the next couple of years.

Greg McIntyre:

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Let me tackle that one, Anna. Certainly what we see is that digitalization is probably the biggest change, evolutionary change that's going on in the water market space today as the ability to measure more things and to be able to analyze and feedback that information. It's provided our clients with better information to actually run their business, and so it's a key integrated piece of their overall platform. I don't know that it'll move the needle but I think it's going to be a strategic piece of how they make their decision making going forward and how they plan for the future.

What we see is that there's probably going to be a balanced investment in improving their digitalization and their ability to collect the information and understand their systems better versus what traditionally had maybe been that they built an expanded facility or they just replaced an existing asset. There's an awful lot more analysis of the assets that they have. There's a lot more planning going into understanding the asset life and how they maximize that and optimize that, and so certainly we think that it's going to be an integrated piece of every successful water platform going forward, but as a standalone piece of the business I think it will continue to grow, and I think it'll be critical for us to have it as a service offering. In that, I'm just not sure that it's going to be a standalone business that's out there on its own, other than the equipment vendors that are certainly providing a lot of the equipment that's going into that. We're seeing a lot of growth and a lot of investment from them as we partner with them and growing that part of the business.

Anna Kaminskaya:

I think with that we are at the top of the hour. I wanted to thank the entire team for joining us. I think it was very useful. You can contact me for any follow-up questions or Jon Doros who is the head of Investor Relations with any follow-up questions on the presentation or on the company.

With that, thank you very much and we'll speak soon.

Bob Pragada:

Thank you.

Greg McIntyre:

Thank you, Anna.

Operator:

That does conclude today's conference. We thank you all for your participation. You may now disconnect.

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