WILLDAN GROUP, INC.

Moderator: Tony Rossi
May 5, 2016
4:00 pm CT

Operator: Please stand by, your program is about to begin. Good day, everyone, and welcome to the Willdan Group Inc.'s First Quarter 2016 conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to Tony Rossi from Financial Profiles. Please go ahead sir.

Tony Rossi: Thank you, Priscilla. Good afternoon, everyone, and thank you for joining us to discuss Willdan Group's financial results for the first quarter ended April 1, 2016. With us today from management are Chief Executive Officer, Thomas Brisbin; Chief Financial Officer, Stacy McLaughlin; and Mike Bieber, Senior Vice President of Corporate Development. Management will review prepared remarks, and will then open up the call to your questions.

Statements made in the course of today's conference call, which are not purely historical, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The forward-looking statements involve certain risks and uncertainties, and it is important to note that the Company's future results could differ materially from those in any such forward-looking statements.

Factors that could cause actual results to differ materially and other risk factors are listed from time-to-time in the Company's SEC reports, including but not limited to the Form 10-K for the year ended January 1, 2016 and subsequent quarterly reports on Form 10-Q. The Company cautions investors not to place undue reliance on the forward-looking statements made during the course of this conference call. Willdan Group Inc. disclaims any obligation and does not undertake to update or revise any forward-looking statements made today.

On today's call, in addition to GAAP financial results, Willdan will also be providing non-GAAP financial measures that we believe enhance investors' ability to analyze our business trends and performance. Our non-GAAP measures include revenue net of subcontractor costs and EBITDA.

We believe revenue net of subcontractor costs allows for an improved measure of the revenue derived from the work performed by our employees. EBITDA is a supplemental measure of operating performance, which removes the impact of certain non-recurring income and expense items from our operating results. GAAP reconciliations for both of these non-GAAP measures are included at the end of the earnings release we issued today.

With that, I would now turn the call over to Chief Financial Officer, Stacy McLaughlin. Stacy?

Stacy McLaughlin: Thanks Tony. I'd like to add my welcome to those joining us on today's call. I'll start with an overview of our income statement, then our balance sheet and finally our guidance.

Total contract revenue for the first quarter of 2016, increased 1.8%, to $33.9 million, from $33.3 million for the first quarter of 2015. Genesys Engineering, the firm we acquired on March 4, 2016, contributed $3.9 million in contract revenue for the first quarter of 2016. By segment, including both organic and acquisitive revenue, Energy Efficiency Services increases 0.4% to $19 million; Engineering Services contract revenue increased 4.2% to $11.3 million; revenue from Public Finance Services increased 11.9% to $3 million; and Homeland Security Services revenues decreased 25.3% to $685,000 in the quarter.

Revenue net of subcontractor costs was $25 million, unchanged from the year ago quarter. Direct costs of contract revenue were $20.3 million for the first quarter of 2016, compared with $19.8 million in the same period last year. Genesys Engineering accounted for $3.4 million of the direct costs in the first quarter of 2016.

Excluding the impact of Genesys, the direct cost of contract revenue decreased by approximately $2.9 million, as an increase in direct costs associated with Engineering Services was offset by a decrease in direct costs associated with Energy Efficiency Services.

General and administrative expenses for the first quarter were $11.8 million compared to $10.9 million for the prior-year period. The increase in G&A was primarily related to an increase in Professional Services. As a percentage of total contract revenue, our G&A expenses were 34.8% compared with 32.6% in the first quarter of 2015. The increase in this ratio was primarily attributable to higher G&A in the Energy Efficiency Services business due to a delay in the commencement of a significant contract.

Operating income was $1.8 million for the first quarter of 2016, compared with $2.6 million generated in the first quarter of 2015. EBITDA was $2.4 million for the first quarter of 2016, compared with $3.1 million for the first quarter of 2015. EBITDA margin was 7.1% compared with 9.3% in the same period in the prior-year. The decrease in EBITDA margin was due to a slow start for some of our Energy Efficiency programs. We expect our EBITDA margin to improve to more than 8% in the second quarter.

Income tax expense was $711,000 in the first quarter of 2016, compared with $1.1 million in the same period last year. The company is implementing a strategy to reduce its effective tax rates through three methods. First, energy efficiency tax credits at both the state and federal level. Second, R&D tax credits. And third, California State Planning Tax. The effective tax rate in the first quarter of 2016 was 39.7% compared with 43.2% in the same period last year. The difference in the effective tax rate is primarily due to the implementation of the strategies just mentioned.

Net income for the first quarter of 2016 was $1.1 million or 13 cents per diluted share, compared to net income of $1.5 million or 18 cents per diluted share for the first quarter of 2015.

Turning to our balance sheet. We had cash and cash equivalents of $4.8 million at April 1, 2016, down from $16.5 million at January 1, 2016. The decrease is attributable to the $9 million used for the Genesys Engineering acquisition.

Additionally, our accounts receivable days outstanding increased to 85 days compared to 74 days at the end of last quarter. The increase in AR days outstanding is primarily attributable to lower collections in the quarter. Two days of the increase was related to Genesys AR, which accounted for $15.4 million of our total AR. Excluding the impact of Genesys, our AR days outstanding would have been 83 days at April 1, 2016.

We have been focusing our efforts on collecting cash since the quarter ended, and our DSO is now back down to 73 days. As of April 1, 2016, we had no outstanding borrowings under our revolving line of credit, and approximately $1.7 million outstanding on our term loan facility. We have an aggregate total of approximately $8.8 million available for borrowing under these facilities.

Lastly, we are reaffirming our financial and operational targets for 2016. We continue to expect full-year revenue to range between $170 million and $185 million, and we continue to expect full-year EBITDA to range between $14 million and $15.5 million.

I'd now like to turn the call over to Tom. Tom?

Thomas Brisbin: Thanks, Stacy, and good afternoon, everyone. Our performance in the first quarter was consistent with our expectations, with growth in our Engineering and Public Finance segments helping to offset this difficult year-over-year comparison in the Energy Efficiency business.

We made steady improvement as we moved through the quarter with March being a very strong month of activity and giving us excellent momentum going into the second quarter.

Moving to the performance of our individual segments. In the first quarter of last year, the Energy Efficiency business benefited from additional funding in our ConEd contract to address specific load pockets in Brooklyn and Queens. This year with the ConEd contract ramping back up throughout the quarter, our contract revenues in Energy Efficiency were down year-over-year on an organic basis.

We finalized our 2016 contract with ConEd during the first quarter. The value of the contract is $32.8 million. We recognized approximately $6 million of revenue related to this contract in the first quarter and we expect the activity on the contract to increase as we move through the year.

We continue discussions to expand our scope of activity in the second half of 2016, including more programs targeting customer segments such as the Brooklyn Queens area, small business, direct install program and the 100 kW to 300 kW range and multifamily housing. So there is potential upside to the contract later this year and we are keeping staffing levels at an appropriate level to manage the increased scope of activity.

We also expanded our relationship with Puget Sound Energy to include a new two-year $2.8 million lodging direct install program. This builds upon our existing small business direct install program with Puget Sound that has been very successful. As we’ve consistently seen, when you demonstrate that you have the knowledge and expertise to deliver the targeted level of energy savings, it leads to opportunities to win additional programs from our utility customers.

We've also been selected and in negotiations for a number of other energy efficiency programs throughout the country. That should impact the second half of 2016 and our full-year 2017 contract revenues. The most significant new win was a six-year contract we were awarded by San Diego Gas & Electric, which has a total value to Willdan of approximately $90 million. This contract implements a program design to meet their energy efficiency local capacity requirements, or LCR. This is the largest energy efficiency LCR contract awarded to-date in the United States.

To provide a background on this project, after the announcement that the San Onofre Nuclear Power Plant would be permanently retired, the California Public Utility Commission authorized SDG&E to procure between 500 and 800 megawatts of replacement capacity by 2022. Of this amount, at least 200 megawatts must come from energy efficiency. So, on essence, SDG&E will be meeting a portion of the capacity need by actually reducing the amount of energy utilized by its customers. That's where we come in.

Our LCR program builds upon our extensive experience in energy efficiency direct install programs and will implement specific kilowatt-rich HVAC-related energy efficiency measures in commercial buildings. From our perspective, the key to winning this program was the additional direct install capabilities that we brought to the table with our Abacus team. With the addition of Abacus and 360 Energy, we are able to offer utilities the turnkey energy efficiency solutions that they prefer, not just for LCR, but for other types of projects as well.

We believe that the San Diego Gas & Electric energy efficiency LCR has the potential to become a model for other utilities across the country. Clearly our position in this emerging area positions us well to capitalize on additional contract opportunities.

Turning to an update on the New York Prize microgrid competition. We continued to await the awards for stage two of the competition. However two of the communities that we're working with have indicated they intend to proceed with the development of their own microgrid whether or not they are chosen to advance in the competition. We should be part of some of the initial municipal microgrid developments in United States, which will position us well for additional work, as more states and cities look to improve their energy resiliency.

Our most recent acquisition, Genesys Engineering, which closed on March 4, has significantly enhanced our ability to address the microgrid development market. The integration of that acquisition has gone smoothly. They performed well in the first quarter and the outlook for their business is very strong.

Turning to the Energy segment. Revenue was up 4.2% over last year. We continued to see solid demand for our city engineering services in Northern California, our building and safety services in both California and Arizona, and our construction management services.

Importantly, as we expected, we signed new contracts with the City of Elk Grove, California, that essentially continue our existing relationship at its current level. Over the next five years, which consists of a three-year base and two option years, the contract had a combined ceiling of $73 million. The stability of the Elk Grove relationship provides us with an excellent foundation to continue growing our engineering segment.

In Public Finance, our revenues increased 11.9% over last year. We won 78 new contracts with a total value of more than $1.5 million in Q1, so our pipeline of work continues to build. We continue to see strong demand for water rate studies across the country, including the primary markets that we operate in; Texas, California, Florida and the Carolinas.

The pace of residential and commercial development is continuing to pick-up in California resulting in the build-up of a steady backlog in the formation of land-secured financing programs, which bodes well for us.

In Homeland Security, our revenues were down 25% over last year, although over a very small base, approximately $3 million. However we were part of a team that was awarded the US Department of Homeland Security and National Exercise program. Over the next five years of this program, we will be the Regional Coordinator for FEMA Regions IX and X.

This position will provide us with excellent exposure to eight states in the Pacific Islands which we believe will be helpful in generating additional project opportunities. As Stacy mentioned earlier, we are reaffirming our 2016 financial targets. With the renewal of the contracts with two of our largest customers, ConEd and Elk Grove, we feel confident in the stability of our base business. On top of this, we have the contribution of Genesys Engineering and the new energy efficiency contracts we won with SDG&E, Puget Sound Energy and others.

We are seeing very positive trends in the business and we remain confident in our forecast for 2016 and our ability to continue delivering profitable growth in the future.

With that, I would now like to turn the call back to the operator for Q&A.

Operator: Thank you. At this time if you would like to ask a question please press the Star and 1 on your touch-tone telephone. You may withdraw your question at any time by pressing the pound key. Once again, to ask a question today please press Star and 1 on your touch-tone phone. We’ll go first to Al Kaschalk from Wedbush Securities. Your line is open.

Al Kaschalk: Hi. Good afternoon, everybody.

Stacy McLaughlin: Hi Al.

Al Kaschalk: I guess, I want to start with the guidance commentary and the number of moving parts that you have, which a lot of them seem positive, that you would maybe be in a position - is it early in the year that you don't want to modify or move to midpoint of that guidance? Could you just talk a little bit about the nature of - the amount of activity you're seeing and why that doesn't translate into revised financial guidance?

Mike Bieber: You're exactly right, Al. It's early in the year. We don't want to get ahead of ourselves, but we've got good trends in the business. We were on plan for Q1, and we've got a number of new contracts that are ramping up throughout the year. So as we get better visibility coming into the second half, you know, it's possible we can revise upward. But at this point that's premature, so we've stayed appropriately conservative.

Al Kaschalk: To address this, but the Energy Efficiency program's slow start to the year. What was the factors behind that, or what did I not tick up on in your prepared remarks?

Thomas Brisbin: Yes, the start-up of the ConEd contract, I'm going to try to the say this '14 to '15 was not a new contract. It was just a rollover. So we went into '15. We had a lot of activity in the first-half and it ramped down because the new contract was going to be put in place.

Although we knew the new contract was going to be put in place, it was not negotiated until - it was not officially negotiated until the early part of this quarter. We had notice to proceed. We had all that in place. So we ramped down through '15 and now at the beginning of '16, the contract is in place and we are ramping back up.

And as I said, Al, the first quarter is a $6 million. The rest of the year will burn the remaining part of the $32 million or $33 million. And as Mike alluded to, as we get more visibility into the second half, on mods or other areas that will be added to ConEd New York, we'll update.

Al Kaschalk: Okay, very helpful. And then on that same line of thought as things are ramping, could you just address or talk about whether it's utilization rate or billable ((inaudible)), just a little bit more details around the operational part of the business?

Mike Bieber: Utilization is improving, so revenue was coming up. You'll see margin improve into the second quarter as Stacy said in her remarks. We expect margins to improve also, because we are better are absorbing our back-office cost. So, all of the metrics are headed up into the right compared to the first quarter metrics.

Al Kaschalk: Okay. And then that margin discussion was around 8%. Is that what we talked - the commentary was?

Stacy McLaughlin: Yes, it was, Al.

Al Kaschalk: Okay. Finally, thanks for the details on the balance sheet. It looked a little scary there in terms of the size of the build-up in AR. But what I think I heard you say is that you collected nearly $15 million of what was outstanding. Could you talk where cash balance stands today or where are you sitting with cash?

Stacy McLaughlin: As for the $15 million, that was the amount of Genesys' AR in our total AR balance.

Al Kaschalk: Okay.

Stacy McLaughlin: Not what we've collected since year-end, if that's what you were referring to.

Al Kaschalk: Well, what is the accounts receivable balance? You've done a fair amount of collection efforts in this month of April, and I'm just curious what that $34 million number looks like? I thought you had said you moved down a few days, but have you - where does that balance stand, I guess, today is what I'm trying to get at.

Stacy McLaughlin: We are down right now to 73 days for our DSO and we average about 300k a day.

Al Kaschalk: Okay.

Stacy McLaughlin: That could probably increase slightly because of Genesys. But that should give you an estimate of what our collection has been since the end of Q1.

Al Kaschalk: Is Genesys slower paying customer base?

Stacy McLaughlin: They were prior to the acquisition but they have also been putting effort towards the collection of their AR and they have been billing sooner which has been allowing them to collect sooner to be more in line with our DSO figures.

Al Kaschalk: Very good. I'll hop back in queue. Thanks a lot.

Stacy McLaughlin: Thanks, Al.

Operator: And as a reminder if you'd like to ask a question today please press the Star and 1 on your touch-tone telephone. We'll go next to Ryan Cassil with Seaport Global. Your line is open.

Ryan Cassil: Hi. Good afternoon, everyone.

Stacy McLaughlin: Hi, Ryan.

Ryan Cassil: I want to go back to the ConEd contract. So it sounds like that got ironed out late Q1 or the early Q2. So we should we expect that, that ConEd is ramping here in the second quarter or does that start more materially in the second half?

Thomas Brisbin: No, it started in March, the third month of first quarter, we'll be ramping up. So we are at $6 million after the first quarter, and we'll be ramping up to complete the $33 million by the end of the year.

Ryan Cassil: Okay, great. And then - sorry for missing your remarks, but from the release you say you won other significant contracts under negotiation. Can you give any more color on those contracts, maybe the size and scope, if not anything else?

Thomas Brisbin: Not at this time. We will have - I'll be able to release information we believe on two or three of them over the next 30 to 60 days.

Ryan Cassil: Okay. And does - maybe I'll ask you this way. Do you come into any constraints with some of these wins on your human capacity or human capital as you would ramp up some of these projects or contracts?

Thomas Brisbin: Human capital is an issue that we are you addressing, finding the right people to put in the right places. Constraint, no. It's just - when you grow, it's always an issue though. So we are actually ahead in the curve and hiring on some of these new ones I mentioned and that we've got people identified, teams identified so that when they do start we are ahead on the staffing issue.

Ryan Cassil: Okay, great. And then on Genesys, could you talk a little bit about what that business is growing, maybe relative to the legacy business and how the integration is going there? A little more color would be great.

Mike Bieber: Genesys came to us with a very strong backlog, good pipeline into 2016. And they've additionally won several new contracts since they joined us. Genesys is growing much faster than the legacy business of Willdan, and we're able to combine our capabilities with Genesys. We actually started that before the acquisition was closed to win new contracts which we'll be talking more about, as Tom alluded to, in the next 60 days or so.

Ryan Cassil: Okay. So the combination there is helping you win some of those that you were talking about before?

Mike Bieber: They are. Integration is going very well actually. Genesys has been a smooth transaction and a smooth transition. So we'll be moving their accounting system onto Willdan's later this year. Everything is going well.

Ryan Cassil: Okay, great. And then on the microgrids opportunity, it sounds like two potential customers intend to proceed, regardless of how the study goes. Could you just frame that maybe from a financial perspective and then again just on a strategic perspective, how that positions you guys in the future?

Thomas Brisbin: Well, New York Prize is going to give phase one, $5 million - $1 million. Phase three is $5 million per site. So if we can move two of them, it's not real - I've always said this is not a financial play, this is strategic. But let's say you move into the more design phase and then you go into approve phase where it goes $5 million, that's just become a matching fund - it's not even a matching fund, it's incentive to municipalities.

So we estimate if we get to actually design construct which maybe, I don't know, six months, 12 months, 18 months, we thought things would be moving faster but it could go as high as $20 million, $30 million per project for a municipality. So right now, you know, if we go to phase two, it's a $1 million per site. If you go to phase three, $20 million to $30 million per site.

Ryan Cassil: And phase three would be a couple of years down it sounds like?

Thomas Brisbin: No, I don't think couple of years. I hope not.

Ryan Cassil: Okay.

Thomas Brisbin: I hope not.

Ryan Cassil: Okay. All right. Thanks guys. Appreciate it.

Stacy McLaughlin: Thanks, Ryan.

Operator: Thank you. And we'll take a follow-up question from Al Kaschalk with Wedbush Securities. Your line is open.

Al Kaschalk: Tom, could you maybe just clarify on the microgrid aspect. I think you said two potential are now doing a self-development of self-deployment. Can you maybe just add some color around why that's - ramping is not - we should view that in a more constructive view than maybe it comes across?

Thomas Brisbin: More what view?

Al Kaschalk: Constructive.

Thomas Brisbin: Constructive view. So the Department of Defense, every base in the nation is looking at microgrids. In both California and New York, the PUC or rather New York for the PUC here in California, here it's California Energy Commission are looking at funding to help cities put in microgrids. Microgrids is nothing more than a combination of renewable energy, battery storage and distributed generation.

The purpose is for communities that lose their power often. So the idea is both California and New York are moving this forward to have the cities become more resilient. This idea has been on the table for 10 to 15 years. We are now seeing money being spent by the California Energy Commission in the State of New York on studies. We see the Department of Defense putting in pilot programs.

So our objective is to get some of the early municipalities under our belt, so that when funding increases, battery storage becomes more available, renewables become more available. We'll be there to provide the cities with a complete solution, and that city can either be a municipal, states or Department of Defense type facility. Does that help, Al?

Al Kaschalk: It helps. And I guess it doesn't - by definition I guess it shrinks your opportunity side of two potential parties or clients or relationships are going out on doing on their own. They are basically competitors...

(Crosstalk)

Thomas Brisbin: When I said doing on their own, I don't mean doing on their own away from us. Hang on. There are doing - they are going to fund it on their own with us. Boy, I missed that part completely, Al.

Al Kaschalk: All right. I just wanted to make sure that I understood your comments earlier.

Thomas Brisbin: We are excited that they are willing to proceed on their own away from state funding and proceed with us.

Al Kaschalk: And does that - if they are funding on their own, does that maybe increase the likelihood that you see opportunities versus waiting for the government?

Thomas Brisbin: Wait for different government and waiting for municipal versus the state. But the municipality, if they can be very clear - and they are looking at grant money from the Department of Energy and other areas to help fund them, so they are excited enough about to proceed forward and the reason I mentioned is we'll be proceeding with them.

Al Kaschalk: Okay. Finally - well, probably too early unless you have a crystal ball. Do you have any concern if we start to get into the election process here in one or two of them likely candidates are taking more favorable position relative to the other? Does that help or hurt this part of the business, or is that too small to worry about?

Thomas Brisbin: I'd say no effect.

Al Kaschalk: Okay, great. Okay. Thank you for your time.

Stacy McLaughlin: Thanks, Al.

Operator: Thank you. We'll move now to Andrew Gordon from Zeke LP. Your line is open.

Andrew Gordon: Hi. Good afternoon, guys. Congrats on the recent contract wins. Great to see all that progress.

Stacy McLaughlin: Thanks.

Andrew Gordon: I wanted to just ask you, would you mind clarifying the timeline for when you expect to recognize revenue from the three contract wins? I think you had color in the release for San Diego, but I wasn't as clear on Elk Grove and Puget Sound.

Thomas Brisbin: Elk Grove is going on and it was a contract we won six years ago. And so all this is an extension of five more years. So the revenue was running at about $15 million a year. It will continue to run at about $15 million per year for five more years.

Andrew Gordon: Okay.

Thomas Brisbin: San Diego Gas & Electric, the LCR one, does not start until 2017, first part of 2017. And we'll see revenue there. Other wins that we said might impact the second half, we will be announcing over the next 30 to 60 days and we will also give an update on what we expect to see in revenue from it in the second half.

Andrew Gordon: Okay. And Puget Sound?

Thomas Brisbin: Puget Sound wasn't existing contract. They added on and consolidated, and the contract value initially - maybe help me. The $2.8 million is lodging, but how much was the base that we had announced? Was it $7 million something? I think it was $7.5 million and they added $2.8 million on, so it's $10 million and that's over three years.

Andrew Gordon: Got it.

Thomas Brisbin: And you'll have to go back, Andrew. The announcement on the original $7.5 million was announcement about six months ago?

Mike Bieber: Four.

Thomas Brisbin: Four months ago. Yes.

Andrew Gordon: Okay.

Thomas Brisbin: So that's how...

Andrew Gordon: Okay. Great. Yes, thank you for the color. Appreciate it.

(Crosstalk)

Operator: Sir, I'm showing we have no further questions at this time. I'd like to turn the call back to management for any closing remarks today.

Thomas Brisbin: Okay, thank you. I would like to thank all of you for participating on our call today and for your continued interest in Willdan. Have a great day. Thank you.

Operator: This does conclude today's conference. Thank you for your participation. You may disconnect at any time.

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