Company: **WILLDAN GROUP, INC.**

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Operator: Please stand by. Good day, and welcome to the Willdan Group First Quarter 2019 Conference. Today's conference is being recorded. At this time, I would like to turn the conference over to Tony Rossi of Financial Profiles. Please go ahead, sir.

Tony Rossi: Thank you. Good afternoon everyone, and thank you for joining us to discuss Willdan Group's financial results for the first quarter ended March 29, 2019. With us today from management are Thomas Brisbin, Chairman and Chief Executive Officer; Stacy McLaughlin, Chief Financial Officer; and Mike Bieber, President of Willdan Group. Management will review prepared remarks and then we'll 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's 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 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 December 28, 2018 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 disclaims any obligation and does not undertake to update or revise any forward looking statements made today.

In addition to GAAP financial results, Willdan also provides non-GAAP financial measures that we believe enhance investors' ability to analyze our business trends and performance. Our non-GAAP measures include net revenue, adjusted EPS and adjusted EBITDA. We believe net revenue allows for an improved measure of the revenue derived from the work performed by our employees.

Adjusted EPS and adjusted EBITDA are supplemental measures of operating performance which removes the impact of certain expense items from our operating results. GAAP reconciliations for all of these non-GAAP measures are included at the end of the earnings release we issued today.

With that, I'd now like to turn the call over to Chief Financial Officer, Stacy McLaughlin. Stacey?

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 2019 increased 68.1% to $91.8 million, from $54.6 million for the first quarter of 2018. The increase was driven by growth in our energy segment, primarily related to the contributions from our recent acquisitions of Lime Energy, NAM and the Weidt Group.

Net revenue, defined as contract revenue minus subcontractor services and other direct costs, was $40.8 million, an increase of 33.8% from $30.5 million in the year ago quarter. Within the energy segment, net revenue increased by 64.8%. Within the engineering and consulting segment, net revenue decreased by 1.8%.

Direct costs of contract revenue were $65.9 million for the first quarter of 2019, an increase of 87.8% from $35.1 million in the same period last year. The increase was primarily related to the growth in contract revenue resulting from the Lime Energy, NAM and the Weidt Group acquisitions.

Our direct costs of contract revenue were 71.7% of our total contract revenue in the first quarter of 2019, compared with 64.2% in the same period of the prior year. The increase was primarily attributable to the impact of Lime Energy, which has programs that utilize a higher percentage of subcontractors, as well as a temporary reduction in revenue from certain higher margin energy contracts.

General and administrative expenses for the first quarter were $26.2 million compared to $17.6 million for the prior year period. The increase was primarily driven by higher salaries and wages, payroll taxes and employee benefits, largely related to the personnel added through the acquisitions of Lime Energy, NAM and the Weidt Group.

In the quarter, intangible amortization increased by $1.3 million related to our recent acquisitions. We also had stock-based compensation expense net of tax of approximately $1.3 million. Our first quarter results in 2019 included approximately $218,000 in acquisition costs related to the Weidt Group transaction.

We had an operating loss of $234,000 for the first quarter of 2019 compared to operating income of $2 million for the first quarter of 2018. The operating loss was primarily due to the idling of two of our largest contracts in the months of January and February, the LADWP program and the Duke Energy program. Each of these two programs has now been reconfigured and expanded, which Tom will talk more about.

We incurred $1.1 million in interest expense in the first quarter of 2019 compared to $23,000 in the same period last year. The increase was due to the debt utilized to finance the acquisition of Lime Energy. During the first quarter, we recorded an income tax benefit of $927,000, primarily attributable to deductions relating to divesting of performance-based restricted stock units.

Net loss for the first quarter of 2019 was $417,000 or a loss of $0.04 per diluted share, compared with net income of $2.2 million or $0.24 per diluted share in the same period last year. On an adjusted basis, excluding stock-based compensation, intangible amortization and transaction costs, our net income was $2.4 million or $0.22 per diluted share, compared with $4.2 million or $0.45 per diluted share in the same period last year. Adjusted EBITDA was $4.7 million for the first quarter of 2019, compared with $4.5 million for the first quarter of 2018.

Turning to the balance sheet. We had an excellent cash generation quarter. We generated $10.5 million in cash from operations in the first quarter, compared to a loss of $6.7 million last year. We typically consume cash in the first quarter of each year due to a number of payments that occur only in Q1. So this quarter's cash flow performance was truly exceptional. As of March 29, 2019, we had $68.3 million outstanding under the delayed draw term loan, and $14 million outstanding on our revolver - revolving credit facility.

Turning to our outlook. I would like to update our financial targets for fiscal 2019. For net revenue, we have increased the lower and upper ends of the range by $5 million. Our new range is $185 million to $205 million. For adjusted EPS, we have increased the lower and upper ends of the range by $0.05. Our range is $2.40 to $2.50, and effective tax rate of approximately 24%.

I'll note that because of the tax benefit in Q1, we expect the tax rate in each of the next three quarters to be approximately 30%, so that the year averages out to 24%. A diluted share count of 11.7 million shares, depreciation of approximately 4.5 million, amortization of approximately 8.5 million, interest of approximately 4.5 million, and stock-based compensation of approximately 11.9 million.

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

Thomas Brisbin: Thanks, Stacey, and good afternoon, everyone. During the first quarter, we made excellent progress on integrating our acquisitions and collaborating across the organization to drive new business development opportunities. As we indicated on our last earnings call, we expected the first quarter to be somewhat soft due to a lower level of activity from two of our largest clients, LADWP and Duke. As a result, our teams were underutilized in the quarter, which negatively impacted our reported results.

We have completed negotiations for program execution and expansions on both programs. The program expansions that we have been awarded, will positively impact our forecast for 2019. We'll update you further as the programs ramp up. LADWP has added a new program focused on increasing energy efficiency throughout the Los Angeles Unified School District. Duke Energy has been expanded to include additional states.

As we have indicated in the past, when you demonstrate an ability to consistently execute well on programs and deliver the targeted energy savings, there are excellent opportunities to expand relationships with utilities. Both of these relationships come from Lime Energy. And in both cases, we believe the expanded resources and capabilities that the combination of Willdan and Lime can provide, were key elements in the decision by both utilities to award us these new and expanded programs.

Outside of these program wins, we continue to see good success in our business development efforts. For example, we recently signed a contract with the City of New York to address energy efficiency for city owned buildings. Our utility work, Con Ed and National Grid, and work for New York City, has positioned as well to address high rise buildings. There are greater than 50,000 buildings that will be required to become more energy efficient. We've also been awarded a contract by the Port Authority of New York and New Jersey to provide energy and performance contracting for the airports, bridges, tunnels and transportation terminals.

Our latest acquisition, The Weidt Group, just won MidAmerican Energy's commercial new construction program for the third consecutive time. Through this program, The Weidt Group works with developers, architects and engineers throughout Iowa to incorporate high energy efficiency options into new commercial construction projects and major renovations of existing buildings.

We've gotten off to a good start in integrating The Weidt Group's unique technology into our business development efforts across the company, including the New York recompete and California Procurement Opportunities. California will have its own statewide new construction business contract. Again, Weidt and Willdan see this opportunity - see this as an opportunity neither would have had on a stand-alone basis.

In our integral analytical business, we are growing our relationship with Calpine, an independent energy producer. Calpine is using IA software to assist Community Choice (aggregation) efforts. The work we are doing with Calpine is opening up a new market for us serving the needs of independent energy producers.

To provide a quick update on the California Procurement Opportunities, the process continues to advance as we expected. We have submitted abstracts for 11 programs, and we made the shortlist for every program that has made a decision so far. The next step will be submitting full proposals that are due this summer, and hopefully awards by the end of this year.

Looking at trends in the broader energy efficiency market, we continue to see new areas of demand emerging, and more funding becoming available in States that have been slow to embrace energy efficiency. For example, Dominion Energy recently pledged to spend 870 million on energy efficiency programs in Virginia. We don't currently generate revenue in Virginia, but this - but with the stronger presence we have on the East Coast following the Lime acquisition, we believe we have a good opportunity to compete for any outsource programs that Dominion launches in the coming years.

Looking at our M&A program, we continue to have a good pipeline of opportunities that we are evaluating to further expand our capabilities and geographic footprint. Two areas of focus are policy consulting and industrial energy efficiency, which serves industries like heavy manufacturing, defense contractors and data centers.

In closing, we are excited about how this year is shaping up. Our pipeline is very strong, and based upon the rollout schedules for the new programs we have won, we expect to see a significant ramp in revenue and earnings in the second half of the year.

With that, I would now like to turn the call back to the Operator for questions-and-answers. Operator?

Operator: Thank you. And ladies and gentlemen, to ask a question, please signal by pressing Star 1 on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, press Star 1 at this time. And we'll take our first question from Craig Irwin with ROTH Capital Partners. Please go ahead, sir.

Craig Irwin: Good evening and thanks for taking my questions. So I may have missed this in the prepared remarks, but did you share an organic growth number for the first quarter?

Michael Bieber: Craig, it was minus 5% for the first quarter. It's on our investors report.

Craig Irwin: Got it. So then that would be Lime's seasonality and some seasonality in the other projects I'm guessing, slow starts, et cetera?

Thomas Brisbin: Well, we've referenced two of the major contracts with the slow starts because of the renegotiation and the extensions, but overall it's a slow start to the first quarter. So that was - it was a little spread everywhere plus the two big ones.

Craig Irwin: Got it. No, this is construction, right? So I guess everybody is well aware sort of stickiness of starts sometimes. Then if we could talk a little bit more about LADWP and Duke. Congratulations on those expanded contracts. How quickly does this actually come on? I know when you get new scope, new services, new geographies, there's always some finalization of the pricing and local agreements and work agreements and things like this. How soon until we see this actually layering into the P&L for Willdan? Is this a primary driver of your higher guidance for this year?

Michael Bieber: So, Craig, here's the numbers for you first. The LADWP program has expanded by $28 million, and the Duke program has expanded by $14 million. However, we're in discussions with the client about over what period of time we burn that revenue because you're right. You can't just ramp up that quickly and burn all that. So that will not hit at all in 2019. It will extend well out into 2020.

We're currently - we have the contract signed. We're working on finalizing measure pricing, and we'll start sales later this quarter. So that means that revenue would start to hit in Q3, and of course then ramp up in Q4 for those two expansions. And then it'll probably continue to ramp into the first part of next year.

Craig Irwin: Great. Next thing I wanted to ask about is the overall RFA activity out there. Can you comment on how things are moving for the different major utilities? Did the RFA for San Diego actually get released? Is there an opportunity to submit there in the short-term? And how far off do you think credibly some of these awards are? Is this something that we could see potentially this summer, or is it more likely to be sort of toward the end of the year?

Thomas Brisbin: The San Diego Gas and Electric RFP is out. We've been shortlisted for the large and the small programs. The proposals are due around July 1, let's say, and June 15, and award, orals and award are expected in the fourth quarter for San Diego.

Craig Irwin: And then...

Thomas Brisbin: They were first out of the gate on the abstracts, and then came SCE and then came PG&E. We expect PG&E to have a request for proposals out within the next couple of weeks.

Craig Irwin: Excellent. So SCE, same thing, you know, probably toward the end of the year, and PG&E as well, probably toward the end of the year?

Thomas Brisbin: Yes. We - they're doing pretty good.

Craig Irwin: Yes. I'd call that ahead of schedule.

Thomas Brisbin: Yes.

Craig Irwin: Then another market that we maybe talk about a little bit less is New Jersey. I know Adam Procell and the team you brought on with Lime, has some very deep connections there. How are things progressing in New Jersey and local markets like New York? Are you seeing additional scope likely to be awarded this year or maybe at some point in 2020?

Thomas Brisbin: New Jersey, we don't expect to be awarded this year. We expect that in a 2020 timeframe, the competition. What's your question on New York?

Craig Irwin: Con Ed in New York. I know you guys have done business there for quite a while, but how are things progressing? Any update as far as additional scope?

Thomas Brisbin: The 10 years we've been the incumbent, the recompete is out on the Street. We submitted. We're waiting for award, and we expect to ramp up, or an increase in what they're going to do.

Craig Irwin: Excellent. And then maybe, can you comment specifically about the integration of Lime Energy? I know this is largely a bolt-on and largely supplementary services and geographies. There were some very, very conservative assumptions around synergies out of this acquisition. Do you still expect to have minimal synergies given the structure, the way you brought the two companies together?

And is there anything about the progress of the cross integration, maybe bringing not just Willdan services over to Lime customers, but Lime capabilities and services over to Willdan customers? Anything there could be helpful.

Michael Bieber: I would say, Craig, it's going just like we thought it would. We're operating just according to our plan. The integration is going well. We're converting first the ERP system later this year. So that's an internally focused effort. And then externally, the California Procurements will integrate Lime's capabilities, as well as some of the other competitions we're going after around the country.

We've got a number of joint proposal activities that have already occurred and will continue to occur all summer. So I'd say it's happening just like we expect it to, and the demonstration I guess of our early efforts are the expansions of LADWP and Duke. That was good news.

Craig Irwin: Yes. Definitely very good news. Well, congratulations on the progress. I'll hop back in the queue and let one of the other analysts ask questions.

Operator: And once again ladies and gentlemen, if you'd like to ask a question, it is Star 1. We'll take our next question from Moshe Katri with Wedbush Securities. Please go ahead.

Moshe Katri: Hey guys. Thanks. Appreciate the updated guidance for the year. Can you give us some color on how we should think about Q2, and then the progression from there? I think you're talking about a nice potential acceleration during the second half, but it would be great if we can at least get some modeling done into the quarter, and then I have another follow up.

Michael Bieber: Q2 should ramp up nicely. That's already happening right now, Moshe. Q3 should be our biggest quarter. It normally is and this year we would expect that to be true. Q4 will be less than Q3, and then typically we step down in Q1 of next year. So that's kind of how the year unfolds.

And you're right that the progression into Q3 and Q4 this year should be very good, mainly because of the expansions of the existing programs we've already got. We won't - we're starting the work now, but we won't recognize revenue until probably the first part of Q3 and into Q4. So that's how I think it should unfold.

Moshe Katri: Okay. And then again going back to the color that we're looking for, would you expect, I don't know, 45% of your annual revenues to get generated during the first half and then 55% during the second half? Is that a good way of looking at it?

Michael Bieber: I'm doing the math in my head. I would say probably slightly more in the second half than you just indicated. Probably slightly more than ...

Moshe Katri: Okay ((inaudible)).

Michael Bieber: Yes, more like that.

Moshe Katri: ((Inaudible)). Okay. That's fair.

Michael Bieber: And I think that’s probably consistent with a $40 million print on the net revenue for Q1. Yes.

Moshe Katri: Yes. And then how should we think about margins starting in Q2?

Michael Bieber: Q2 margins will increase significantly. Q3 margins should be the highest, probably. That's typically the case. That’s our high utilization quarter. And then Q4 margins come down just a little bit from Q3.

Moshe Katri: Okay, that's helpful. And then apologies if this is a basic question. How do we think, or how should we think about setting up or transitioning or setting up the infrastructure for some of those new deals that are coming on board in terms of cost, personnel? How do these actually work? Are they a bit different than what you're doing typically, and will there be a initial impact on margins as you are kind of setting up or starting to get some scale on some of those new deals?

Michael Bieber: Tom's pointing at me, I'm pointing at him, so. So typically, there are some ramp up costs in new programs. We generally start with a higher percentage of subcontractor work because that allows you to ramp up more quickly. And then as programs mature over the next few years, sometimes in some instances, the percent of subcontractor work comes down. That depends on the program.

Other than that, we have no indication to think that the margins will be any different in the California work than we're currently seeing. There's no indication of that right now, either up or down. So that's kind of where we're at.

Moshe Katri: And typically, does it take a quarter or two in terms of setting up that infrastructure, in terms of kind of ramping or in terms of maybe starting - maybe ultimately winding off the subcontractor lease?

Michael Bieber: In this case, we're already working for these customers and we often have what I'll call a smaller starter program. Other programs are then going to be rolled into what we're procuring. So we have people who are experienced on most of these types of programs. So I don't believe that the ramp up would be as problematic as a brand new customer or a brand new geography.

Moshe Katri: Perfect. Final question. Some color on the integral analytics. How did we do there in the quarter? How does it look for the second half? And I believe when we're marketing, you spoke about a new product/solution that kind of incorporates what these guys are doing. So where are we in terms of trying to monetize it? Thanks.

Michael Bieber: Yes. Integral analytics is by its nature and by the change in the revenue recognition model just last year, going to be lumpy. And so Q4, they had a banner of Q4. Q1 this quarter, they had a weak Q1, and they have a very good pipeline for the rest of the year. So that's the way it will always go with integral analytics. It'll be almost binary way up or way down.

We are integrating integral analytics mathematical tools onto our existing energy efficiency projects. We're doing that in proposals and on pilot scale and we're trying to roll that out across the country to be able to mathematically optimize or target, better target the areas in which you want to put energy efficiency.

Right now most of these energy efficiency programs, sometimes they identify load pockets but they don't get down specifically to the highest value customers. And integral analytics has the ability to tell you exactly where you should target. So we're starting that process and that will roll out over the next year, year and a half.

Moshe Katri: Great. Thanks.

Operator: And there are no further telephone questions at this time. I'd like to turn the conference back over to management for any additional or closing remarks.

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

Operator: And once again, this does conclude today's conference. Thank you all for your participation. You may now disconnect.