WILLDAN GROUP, INC.

Moderator: Tony Rossi
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4:00 pm CT

Operator: Good day, and welcome to the Willdan Group Inc. Fourth Quarter 2015 Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Ms. Moira Conlon. Please go ahead ma'am.

Moira Conlon: Thank you. Good afternoon, everyone, and thank you for joining us to discuss Willdan Group's financial results for the fourth quarter ended January 01, 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 we will then open the call up 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. 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.

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 revenue net of subcontractor costs and adjusted EBITDA. We believe revenue net of subcontractor cost allow us for an improved measure of the revenue derived from the work performed by our employees.

Adjusted 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 like to turn the call over to our Chief Financial Officer, Stacy McLaughlin. Stacy, please go ahead.

Stacy McLaughlin: Thanks Moira. 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 outlook for 2016. Total contract revenue for the fourth quarter of 2015 increased 4.3% to $31.5 million from $30.2 million for the fourth quarter of 2014. The two firms we acquired in January 2015 Abacus and 360 Energy contributed $4.5 million in contract revenue for the fourth quarter of 2015.

By segment including both organic and acquisitive revenue, Energy Efficiency Services increased 3.6% to $15.9 million, Engineering Services contract revenue increased 7.4% to $12.1 million, revenue from Public Finance Service increased 9.4% to $2.9 million, and Homeland Security services revenue decreased 33.6% to $673,000 in the quarter.

Revenue net of subcontract cost was $24.4 million compared with $25.4 million for the year ago quarter. Direct costs of contract revenue were $18.4 million for the fourth quarter of 2015 compared with $17.9 million in the same period last year. The increase was primarily the result of incremental direct cost of revenue of $2.5 million attributable to our acquisitions of Abacus and 360 Energy.

Excluding the impact of the acquisitions, direct costs were lower by approximately $2 million as we had a decrease in direct cost in the Energy Efficiency Services segment resulting from the organic decline we saw in the segment this quarter. This decline was partially offset by higher direct cost driven by the organic growth in the engineering services segment.

Gross margin was 41.5% in the fourth quarter of 2015 which was relatively unchanged from 41% we saw in the same period last year. On a sequential quarter basis, our gross margin improved from the 37.5% that we had in the third quarter of 2015 which was primarily attributable to a lower percentage of our revenue being derived from our recent acquisitions which is more subcontractors.

General and administrative expenses for the fourth quarter were $12.6 million compared to $10 million for the prior year period. The increase in G&A was primarily related to higher RFPs associated with becoming an accelerated filer in 2015. In addition, we had approximately $100,000 of legal costs in the fourth quarter of 2015 related to the acquisition of Genesys Engineering.

As a percentage of total contract revenue, our G&A expenses were 40% compared to 33% in the fourth quarter of 2014. The increase in this ratio was primarily attributable to the higher RFPs as well as the weakness in Energy Efficiency revenues.

Operating income was $456,000 for the fourth quarter of 2015 compared with $2.4 million generated in the fourth quarter 2014. Adjusted EBITDA was $1.8 million for the fourth quarter of 2015 compared with $2.6 million for the fourth quarter of 2014.

Adjusted EBITDA margin was 5.7%, a decrease from 8.4% in the same period in the prior year. The lower adjusted EBITDA margin is primarily due to weak performance in the three utility programs within the Energy Efficiency segment we discussed last quarter. Tom will discuss this later on the call today.

Income tax expense was $210,000 in the fourth quarter of 2015 compared with $366,000 in the same period last year. The effective tax rate in the fourth quarter of 2015 was 35.6% compared with 15.2% in the same period last year.

The difference in the effective tax rate is primarily due to recognition of an income tax benefit for net operating loss carry-forwards that were fully utilized in 2014 and no longer available to offset taxable income this year. Net income for the fourth quarter of 2015 was $380,000 or 5 cents per diluted share compared to net income of $2 million or 26 cents per diluted share for the fourth quarter of 2014.

Turning to our balance sheet, we had cash and cash equivalents of $16.5 million at January 01, 2016, an increase of approximately $1.8 million from the end of the prior quarter. The increase was driven by positive free cash flow generated during the quarter. Our accounts receivable days outstanding were 74 days compared to 73 days at the end of the prior quarter.

As of January 1, 2016, we had no outstanding borrowings under our revolving line of credit and $1.1 million outstanding on our delayed draw term loans. All $7.5 million under the revolving line of credit is available for borrowing. And as we indicated in the 8-K filed last week we have signed an amendment to our credit facility that extends the maturity date by one year to March 24, 2017.

Now turning to our guidance for 2016, we expect full year revenue in 2016 to range between $170 million and $185 million. We also expect full year adjusted EBITDA to range between $15 million and $15.5 million. In addition, we expect our effective tax rate to be approximately 41% although we are currently exploring certain actions we could take to lower our effective tax rate over the next two years. As we move forward with these efforts, we will provide an update on any expected change in our effective tax rate.

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

Thomas Brisbin: Thanks, Stacy and good afternoon everyone. As we indicated on our last conference call, we expected our fourth quarter results to be in line with third quarter, which is generally how things turned out, with regards to Energy Efficiency.

The overall performance of our Energy Efficiency business undermined our overall results as it will take a couple of quarters to work through the issues that surfaced in the third quarter. The most significant issue we are facing in the Energy Efficiency business is adjusting to the baseline level of activity with our largest utility customer.

In the first half of 2015 Con Ed expanded our baseline contracts to provide additional funding to address specific load pockets in Brooklyn and Queens where demand side management was urgently needed. We stepped up to handle these contract modifications and expected the increased scope of activity to continue for an extended period.

However, the ramp-up didn't continue into the third and fourth quarters of 2015. We fell back to the baseline level activity with Con Ed which caused Energy Efficiency's revenue and profit to decline when compared to its first half performance.

We have the extension for 2016 at a value of approximately $33 million. We're prepared to go beyond this baseline and expect to. The good news is that we continue to perform well for Con Ed and as a result we are in discussions to expand our scope of activity in the second half of 2016 to include more programs targeting customer segments, for example, more of Brooklyn, Queens and larger projects, 100 kW to 300 kW in our SPDI program, the type of programs that will include in the larger retail stores and warehouses and more real estate.

The second major drag on the Energy Efficiency business was a slow start up of a new contract. This program required integrating systems and people. This was not our best effort. As a result we generated almost no revenue from this program in the third quarter and generated about $700,000 of revenue in the fourth quarter.

We are now moving in the right direction but obviously not at the pace that we originally planned. The total value of this contract is 7.5 million over a one year period and now that we're starting to get more traction we will -- we still expect to recognize the remainder of the revenue available in this contract during 2016. We have corrected our third problem with hospitals in Southern California.

Outside of these three problems we continue to perform well across the board for our utility customers. And Puget Sound Energy is a good example. We were just awarded another two year contract with a budget increase of 38%. For a small business direct install, refrigeration and logging programs. As we've consistently seen in our Energy Efficiency business if we deliver the targeted level of energy savings, the utilities will come back for more. Increase the level of funding and say we want you to expand what you are doing for us.

We also have two additional wins with New York Power Authority, both Genesys and Willdan were selected to provide Energy Efficiency Services. The two acquisitions we made in 2015, 360 Energy and Abacus are performing well and they have record backlog coming into 2016. The acquisitions have helped us bid on new work that we could not have won without them. We are waiting for the outcome of these significant pursuits. The message here is Willdan is stronger and more diversified with 360 and Abacus.

Turning to an update on the New York Prize micro grid competition, we're approaching the final phase of stage one and completing the feasibility studies for eight communities that we are working with. Approximately 10 of 83 communities will be selected for stage two of the contest later this year, which will consist of engineering design and business planning. We expect to go forward with at least one of the eight communities.

We continue to see more activity and funding for micro grid implementation across the country. We recently submitted a proposal for a micro grid project in California and we're closely monitoring the development of other state sponsored micro grid projects. It looks like Illinois, Massachusetts and Virginia might be the next stage to provide funding for micro grid development.

The increase in demand for micro grids central plants such as boilers and chillers, distributed generation were a primary driver for the acquisition of Genesys Engineering that we announced last week. Over the past few years' we've frequently partnered with Genesys as one of our team members and therefore have firsthand knowledge of their engineering expertise. We are very excited to add the knowledge and skill to the Willdan team.

They are leaders in the development of small to mid-sized central plants primarily used by hospitals, universities and multifamily housing. Genesys also filled another goal of our M&A program which was to expand our East Coast engineering presence.

In this region Genesys was our top target, so we're doubly pleased that they were interested in becoming a part of Willdan. They have demonstrated the ability to consistently grow the business.

We believe the combination of the technical skills will help us capitalize on the continued evolution towards distributed generation and micro grid.

With regards to Engineering, our legacy business, revenue was up 7.4% over last year. Engineering had a very strong year with revenue up 12.8% and profit up 17.5%. Engineering continues to recover with more activities throughout California. We won new contracts in the Bay Area and in the Central Valley as well as a building and safety contract with the City of Phoenix, Arizona, a place where we used to be very strong.

Public Finance Services, in Public Finance Services our revenues increased 9.4% over last year. We won $2 million in new contracts during the fourth quarter which brought us to $13.5 million in new contract wins during 2015. Residential and Commercial real estate development trends continue to be positive which helps drive demand for new financing programs for infrastructure and municipal services.

We continue to see more business coming from Texas and Florida which is providing incremental growth opportunities outside of the historical base business in California. We also expand regulatory changes concerning Property Assessed Clean Energy, PACE funding. This will open the opportunity to cross-sell energy in financial services.

Let’s turn to an outlook for 2016. I want to wrap-up today by talking about 2016. As Stacy mentioned, we’re expecting total contract revenue in 2016 to range from 170 million to 185 million which is an increase of $35 million to $50 million over 2015. Approximately $30 million of the growth will come from Genesys and we anticipate another $5 million to $20 million organic revenue growth. This translates to an applied organic growth rate of roughly 5% to 15%.

Now I want to walk through some data points that will help you understand our projections for 2016. All of our utilities contracts have been extended through 2016. So we have good revenue visibility for the full year. As I mentioned earlier, we are in negotiations with Con Ed to add more programs to our baseline contract.

The addition of these programs will probably put the total revenue from Con Ed about even with 2015 with a bigger contribution coming in the second half of the year. As we indicated the Puget Sound program is increasing in value this year. NIPA has notified us of additional wins that is New York Power Authority. 360 Energy has a current backlog of over $16 million which will lead to solid double-digit growth in their business.

Engineering continues to execute well and produce growth in the mid to high single-digits and Public Finance Services ended 2015 with a backlog of $8.8 million, a 21% increase from where it was at the end of 2014. So this should translate into nice growth for this business in 2016. Given these trends we are seeing in the business, we're confident that 2016 will be a strong year of profitable growth.

We also continue to have an active M&A pipeline and we anticipate completing additional accretive acquisitions. With the last three acquisitions we have significantly enhanced our mechanical engineering capabilities and improved our geographic coverage. Our primary area of focus going forward will be targeting firms that can provide high-end electrical engineering capabilities.

As we indicated in an 8-K filing last week, we have made some amendments to our credit facility that provides us with the flexibility to continue implementing our M&A program. We believe we have strong growth opportunities both organically and through our M&A program and our primary use of capital continues to be focused on investing in initiatives that will drive revenue and earnings.

On a final note, I am confident that we will deliver a strong year in 2016. We continue to have a good position and an excellent reputation in markets that are seeing strong long-term growth. We are very optimistic about our opportunities to create significant value for our shareholders in the coming years.

With that I would now like to turn the call back to the operator for questions.

Operator: Thank you. If you'd like to ask a question please signal by pressing star 1 on your telephone keypad. If you're using a speakerphone please make you're your mute function is disengaged to allow your signal to reach our equipment. And once again that is star 1 to signal for a question. And we'll pause for just a moment to assemble the queue.

And we'll go first to Al Kaschalk of Wedbush Securities.

Al Kaschalk: Hey, good afternoon, guys.

Stacy McLaughlin: Hi, Al.

All Kaschalk: Just to clarify the energy efficiency I think Tom your commentary suggested that the first half'16 you'd see some roll off or some of that work that then materialized and then in the second half we should resume growth in that, and I am talking ex the acquisitions of course?

Thomas Brisbin: What I am trying to say is our baseline will continue into 2016, so where we were in the end of third and fourth quarter will continue. They're adding more Brooklyn Queens work, we have more. They're adding what I refer to as 100 kilowatts to 300 kilowatts type businesses which is larger retail, warehouses and so forth. Those have already been under negotiation, we are anticipating them to start and ramp up maybe earlier than the second half and it's all for Con Ed, so.

Al Kaschalk: But if you put all that together and if I look at the $16 million or $15.9 million that you did in the fourth quarter, understanding that that's generally a little bit slower quarter than others, what's the -- what can you guys share on terms of what the first quarter and second quarter looks like in that segment particularly, or that strategic business unit, well again excluding the recently closed transaction, I'm trying to get out is there sort of so called organic growth in there?

Thomas Brisbin: We think it'll ramp-up throughout the year. So, first quarter we'll be probably where we are and fourth quarter maybe a little better and then by the fourth quarter we're expecting to be doing much better, I think I even said beyond potentially the $33 million that the 2016 contract is for.

Al Kaschalk: Right.

Thomas Brisbin: They've added in larger businesses and they've added in more Brooklyn, Queens. So, you can take our base and say it will ramp-up through 2016 and should be better than 2015 overall.

Al Kaschalk: Thom, if I may ask, the benefit to the revenue mix or to your operation to doing business as a result of larger customers is there such a thing or is there not much in a way of operating leverage or billable pile etcetera?

Thomas Brisbin: It's only operating leverage you get with bigger customers, more customers is probably on the material side. You won't see any leverage onto the people side, so our Professional Services business I mean that's the only -- we either selling people or we're selling to some extent I think I discussed in our results probably ’15 do we know how much material there were around $15 million, maybe $15 million to $20 million in materials through '15. So, as that number grows we have better buying power, but that's about the only thing out.

Al Kaschalk: Okay. Shifting gears on the outlook, you talked about 5% to 15% organic growth, what will get you at the lower end of that range versus the upper end and I realize winning a contract would do one versus the other, but can you give us a little color into, you know, the broader range, you know, is there several contracts that would get you to the $185 million, is there a one that would get you from $170 million to $185 million just a little bit of what you're hunting for in 2016?

Thomas Brisbin: So, if we go from $135 million and we say we're at -- was it $5 million to $15 million? Five million to $15 million, if we perform and deliver all of that one utility for $7.5 million and that gives you $7.5 million that we didn't have in '15. If we get up and go in on the increased size of the 100 to 300 kilowatts in our existing -- these are both existing contracts.

So, when we need to ramp-up we'll give $7.5 million, $6.5 million. Con Ed we're going to ramp-up the 100 to 300 and also the Brooklyn, Queens. So, just those two alone would give you, you know, a solid in the middle $10 million maybe more, so with two existing programs just delivering on them would get you to the mid-range to the high range.

We would have to have some type of unknown event at this time to take place, not to grow because as I said the visibility into 2016 is very good. We have no programs rolling off all we have to do is perform.

Al Kaschalk: Okay. And then my final question if I may, on the, I was wondering perhaps, Stacy, if we could get the cash balance post the closing of Genesys, I think you ended at '16 and cash at the end of the year and then any, the nature of what you used to close that transaction and there was a combination of debt or cash?

Stacy McLaughlin: Hi, Al. After the close of the Genesys acquisition we had approximately$ 9 million left in cash and we only used cash for the close we did not draw on the term loan or the revolver.

Al Kaschalk: Okay. And so that's outstanding as that closed also then would be zero?

Stacy McLaughlin: We have $1.1 million outstanding on the delayed draw term.

Al Kaschalk: Okay. All right that’s all I have. Thank you.

Stacy McLaughlin: Thanks, Al.

Operator: And we'll go next to Ryan Cassil of Seaport Global.

Ryan Cassil: Hi, guys. Good afternoon.

Stacy McLaughlin: Hi.

(Crosstalk)

Ryan Cassil: I guess on my first question just to clarify on the 5% to 15%, does that include if you increase the scope of your work with Con Edison is that what gets you to that 15% organic growth range or would that be incremental in the way you’re building the guidance?

Thomas Brisbin: I am looking at Mike who and we are trying to decide how to answer that, so it's clear. Do you have a clear answer Mike?

Mike Bieber: Tom stated that Con Ed is approximately equal to that of last year. So, the acquisitive growth will be likely driven by other programs including the new programs we’ve already won and are ramping up, Ryan.

Thomas Brisbin: You said acquisitive growth, you meant organic.

Mike Bieber: Organic right.

Ryan Cassil: Okay, so...

Thomas Brisbin: Ryan, did you catch that?

(Crosstalk)

Ryan Cassil: Yes, I think so. Okay. So that would include some of expanding those on some of those new projects with Con Ed to get to that 15% range.

Thomas Brisbin: There is a little expansion in Con Ed there is delivery on the existing one in Southern California and there is a little bit of new programs in there.

(Crosstalk)

Ryan Cassil: And then at the low end, is there -- are you still assuming you get the remainder of this new startup project which I think it has six -- it sounds like just south of $7 million less on that contract, or is that an assumption that you will get all of that in ’16?

Thomas Brisbin: I think we’re being conservative and this time assuming if something goes wrong not -- we’re giving the low end just in the conservative assumptions that might go wrong.

Ryan Cassil: Okay, got it...

Thomas Brisbin: That’s all that is. We gave our self a broader range to be margin for error as Moira said.

Ryan Cassil: Makes sense. Makes sense. In the micro grid study you guys sound confident that you're going to win with at least one of those communities that the move forward, you know, what's giving you the confidence and then or what's giving you the increased confidence. And then on some of those new space I think you said Illinois, Massachusetts and Virginia. Any sense on timing on those and whether one might move forward versus another?

Thomas Brisbin: No, you know, it should be by the end of the year 2016 we should have knowledge of wins or knowledge of responses or under negotiation if we get selected. But with regards to New York if we move one forward, one, it puts us on the map. I mean it is -- what you're looking at is let's say a five year plan of how distributed generation and micro grid start to take over the overall transformation of the utilities.

So for us moving one forward is a big hurdle, I mean it's a big thing for Willdan because I won't to say no one but hardly anyone can point to having implemented a complete micro grid for a municipality.

Ryan Cassil: Right. Could you give us refresh us again on what that revenue opportunity could ultimately lead to on that one project? And then what do you think about that ability, you know, winning that project and how it can help you win additional projects after that?

Thomas Brisbin: It's not a revenue event. I mean the next phase is like $1 million and then the next phase after that I think it's going to be seeded by $5 million to $7 million from the state within municipalities probably looking at coming out with $30 million, $35 million, $40 million.

So again the idea here Ryan is you win, you do it, you go to the next stage, you actually implement it and it puts you on the map in the country that someone who is actually done it.

Ryan Cassil: Right.

Thomas Brisbin: And it's a direction and, you know, the team we have working on it I think I'll refer to before Illinois to technology campus is a complete micro grid. There are potentially a few others that are partial. But for a city to say I've got solar, I've got wind, I've got battery storage, I've got gas fire generators I can island off the grid, you know, for a week or month or, you know, during the high demand times, you know, kick in my other things there is not a real complete city out there that's there.

But it is the direction that seems to be evolving. If you go into New York and listen to Mr. Kaufman he outlines it quite well how utilities is going to look over the next five to 10 years one important role distributed generation and micro grids are going to play energy efficiency also refers to reducing the amount of capital that utilities have to pay.

Ryan Cassil: Okay. Thanks, that's great. Great color on the overall opportunity. The last one from me, you said you have $9 million of cash left post the close of the acquisition could you talk about what the cash needs are, what utility cash needs are at this point in terms of day-to-day operations and where are you comfortable in terms of that cash balance getting to?

Stacy McLaughlin: Hi, Ryan. We're comfortable around the balance we have now, the $9 million we can run efficiently on say approximately $10 million.

Ryan Cassil: Okay. That's the minimum, I was trying to get to the minimum cash balance you would feel comfortable at, do you think that they were kind of bumping up against it or there's some cushion there?

Thomas Brisbin: We're comfortable.

Stacy McLaughlin: Yes.

Ryan Cassil: Okay. Thanks, guys. Appreciate it and look forward to seeing you next week.

Thomas Brisbin: Yes, we'll see you out there. I guess we're going for a tour of a micro grid aren't we?

Ryan Cassil: Yes, yeah. We're pretty excited for it so looking forward to it.

Operator: And again that is star 1 for questions. And we'll go next to Ian Niemeyer of Morehouse Investment Group.

Ian Niemeyer: Hi, Tom. I guess first on just initially following the commentary and looks like an optimistic 2016, I guess my question is on the acquisition strategy and it would be like are you like looking at any specific kind of geographic expansion and are with certain acquisitions going forward or is it going to be in the same sort of geography you guys are in right now?

Thomas Brisbin: Okay, Mike is going to answer that one.

Mike Bieber: Ian, we have only slight electrical engineering capabilities right now, so it's not specifically geographic...

Thomas Brisbin: Hang on a second Mike, somebody got their -- needs to turn their speaker off or Ian? Ian can you hear, I am assuming you can hear us, it helped, I was going to go forward with the answer.

Mike Bieber: All right Ian, we've got only slight electrical engineering capabilities today. So, it's not specific to geography that we want to add additional electrical engineering capabilities. We need both high end electrical engineering consulting services and detailed design services across the

United States right now. The last three acquisitions were focused on mechanical engineering and now we just need to add that electrical capability.

Ian Niemeyer: Okay thank you. And so what are you guys I guess targeting the same sort of like the same size as Abacus and 360 and Genesys or do you think you can go higher or is it just -- it's really dependent on the target?

Mike Bieber: It depends on the target and we could go larger. I think those are representative of what we're looking at but we do have some larger targets as well that we could also pursue.

Ian Niemeyer: Okay thank you.

Operator: And this concludes today's question-and-answer session. At this time I will turn the conference back to management for any additional or closing remarks.

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

Operator: That concludes today's conference. We thank you for your participation. You may now disconnect.

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