# WILIDAN GROUP, INC.

## Moderator: Tony Rossi
## August 4, 2016
## 4:30 pm CT

Operator: Good day, everyone, and welcome to the Willdan Group's Second Quarter 2016 conference call. At this time, all participants are in a listen-only mode. Later, you will the opportunity to ask questions during the question-and-answer session. You may register to ask a question at any time by pressing the star and 1 on your touch-tone phone. Please note that this call is being recorded. I will be standing by should you need any assistance.

It is now my pleasure to turn the floor over to Tony Rossi. Please go ahead.

Tony Rossi: Thank you, operator. Good afternoon, everyone, and thank you for joining us to discuss Willdan Group's financial results for the second quarter ended July 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 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 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 second quarter of 2016, increased 16.3% to $58.9 million, from $36.8 million for the second quarter of 2015. Genesys Engineering, the firm we acquired in March 2016, contributed $15.5 million in contract revenue for the second quarter of 2016.

By segment, including both organic and acquisitive revenue, Energy Efficiency Services increased 97.8% to $42.6 million; Engineering Services contract revenue increased 10.3% to $12.7 million; revenue from Public Finance Services was essentially unchanged at $3 million; and Homeland Security Services revenues decreased 12% to $621,000 in the quarter.

For the purposes of calculating our organic growth in the quarter, we are including the revenue generated by Genesys Engineering that exceeds the revenue recorded in the same period of the prior year. As I indicated earlier, Genesys contributed $15.5 million in total contract revenue in the second quarter of 2016.

In the same period as of prior year, Genesys generated $5.2 million in total contract revenue. The year-over-year difference of $10.3 million is used for the calculation of our organic growth. Since the acquisition, we have one joint program where all the revenue is being reported under the Genesys legal entity.

Thus the growth in Genesys revenue is reflective of our organic business development efforts and is accounted in our organic revenue growth. Without the inclusion of Genesys, Energy Efficiency Services grew organically 26%.

Net revenue defined as contract revenue minus subcontractor services and other direct costs was $27.6 million, an increase of 25.2% from $22.1 million in the year ago quarter. Direct cost of contract revenue were $41.1 million for the second quarter of 2016 compared with $22.9 million in the same period last year. Genesys Engineering accounted for $13.8 million of the direct cost in the second quarter of 2016.

Excluding the impacts of Genesys, the direct cost of contract revenue increased by approximately $4.4 million, primarily as a result of the growth in total contract revenue in Energy Efficiency Services segment.

General and administrative expenses for the second quarter were $13.9 million compared to $11.1 million for the prior year period. As a percentage of total contract revenue, our G&A expenses were 23.6% compared with 30.1% in the second quarter of 2015.

Operating income was $4 million for the second quarter of 2016, compared with $2.8 million generated in the second quarter of 2015. EBITDA was $5.1 million for the second quarter of 2016 compared with $3.3 million for the second quarter of 2015.

EBITDA margin for the second quarter was 8.6% compared with 8.9% in the same period in the prior year. The decrease in EBITDA margin was due primarily to an increase in the use of subcontractors in the current business mix and the resulting increase in direct cost of contract revenues.

Income tax expense was $731,000 in the second quarter of 2016 compared with $1.1 million in the same period last year.

Our effective tax rate in the second quarter of 2016 was 18.6%, down from 40.9% last year. The difference in the effective tax rate is primarily due to an increase in energy tax deductions related to some of the company's energy efficiency activities.

During the second quarter 2016, the company recognized a tax benefit of $0.5 million as a change in estimates related to energy tax deductions earned for the 2015 tax year. The increased use of energy tax deduction is the first three methods we are employing to reduce our effective tax rate. The other two initiatives R&D tax credits in California State Tax Planning are still in process. Once all three methods are fully implemented, we believe, we can further reduce our effective tax rate below our current run rate of 36%.

Net income for the second quarter of 2016 was $3.2 million or 37 cents per diluted share compared to net income of $1.6 million or 20 cents per diluted share for the second quarter of 2015.

Turning to our balance sheet. We had cash and cash equivalents of $10.5 million at July 1, 2016, up from $4.8 million at April 1, 2016. The increase is primarily due to the net income generated during the second quarter and strong collections on accounts receivables. We continue to see strong cash inflows since the end of the quarter. With the strong collections, our DSO declined to 70 days at July 1, 2016, down from 85 days at the end of the last quarter.

As of July 1, 2016, we had no outstanding borrowings under our revolving line of credit and approximately $1.7 million outstanding on our term loan facility.

Lastly, we have raised our financial targets for 2016. We now expect full year revenue to range between $175 million and $190 million. We now expect our 2016 diluted earnings per share will range between $0.84 and $0.91. We expect our effective tax rate to be approximately 36% for the year.

I would now like to turn the call over to Tom. Tom?

Thomas Brisbin: Thanks, Stacy, and good afternoon everyone. We are very pleased with our performance in the second quarter. It's a type of performance that we have been building towards over the last several quarters and we've enhanced our capabilities and expanded our geographic coverage with our recent acquisitions.

Our organic revenue growth was 41% over Q2 2015. The additional expertise we have added in a number of engineering disciplines has improved our business development efforts and we are seeing excellent momentum in winning new projects by cross-selling.

Moving to the performance of our individual segments, I will start with Energy Efficiency. We're seeing strong demand for Energy Efficiency Services across a broad set of customers including public utilities, municipalities, and universities. As a result, we are seeing significant growth and an improvement in the diversification of our revenue mix in this business.

On a year-over-year basis, Energy Efficiency revenue was up 98% in total, as Stacy has said. We had a strong quarter of activity with all of our major public utilities customers including ConEd, SDG&E, Southern California Edison, and Puget Sound Energy.

In addition, the second quarter is a seasonally strong period for 360 Energy, which had its best quarter ever. We expect the third quarter to return to a baseline projection. 360 has increased its worth with higher education clients and is also effectively expanding its business from Kansas to other Mid-Western States.

We have also gotten off to an excellent start in our integration and joint business development efforts with Genesys Engineering by combining our respective strength and experience we have been able to jointly win some significant new pieces of business in New York State and we are seeing a growing pipeline of opportunities with colleges and universities.

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

We also continue to see an increasing level of interest in microgrid development from a diverse set of customers. Most notably the United States Navy recently announced that they are creating a new department to evaluate the development of microgrids and naval facilities.

There is increasing evidence to suggest that overall spending on microgrids will increase significantly in the coming years and we are well positioned to capitalize on this emerging market opportunity.

Looking ahead, we have a strong pipeline of projects that we will be starting up in the second half of the year, most notably the new multi-family program with ConEd. We also have other sizable programs that we have been awarded but are not able to announce yet that will contribute to our energy efficiency revenue in the beginning of 2017.

Turning to the Engineering segment, revenue was up 10% over last year. The recent renewal of our contracts with the City of Elk Grove that covers the next five years continues to provide a stable foundation for growing our engineering revenue.

In addition, we continue to build our roster of three engineering clients, recently adding two new municipal clients in California for Monack and Tulare and one in Arizona.

In Public Finance Services, our revenues were unchanged from last year. We won 49 new contracts with a total value of more than $2.1 million in Q2. One of these areas that we are focused on to grow our public finance business is leveraging our utilities experience to open up new business development opportunities. We recently delivered our first combined utility rate in financial analysis to a client in Virginia and we are currently pursuing other similar opportunities in other states.

And finally in Homeland Security, our revenue was down 12% over last year although this is off a very small base. However, we will be starting work as part of the team that was awarded a five-year contract to implement seamless National Exercise program and we expect this to have a positive impact on future growth in the Homeland Security business.

We expect the positive trends to continue. As I mentioned earlier, we had some significant programs that we will be ramping up in the beginning of 2017 which should enable us to continue delivering strong year-over-year growth in revenue and earnings.

On a final note, I want to touch upon the significance of the tax reduction efforts that Stacy discussed earlier. This is a major corporate initiative that we expect to have a significant impact on the economics of our business model. As we do so our effective tax rate, we expect to see a positive impact on cash flow generation. We believe our overall level of earnings growth will result in significant value creation for our shareholders.

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

Operator: And at this time if you would like to ask a question please press star and 1 on your touch-tone phone. You may remove yourself from the queue at any time by pressing the pound key. Once again to ask a question please press star and 1. We will go ahead and take our first question from Misha Levental with Wedbush. Your line is open.

Misha Levental: Hi, guys, thanks for taking my question and excellent job this quarter. My first question is to the extent you can -- to the extent can you share the composition of the organic growth including the number of contracts whether larger, small and the duration of contracts? In terms of customers, how many were new customers versus existing customers? Thank you.

Thomas Brisbin: Let's take a look at it piece by piece. Within 360 out of Kansas it would probably be three or four new customers at an average value of $2 million to $3 million per customer. With Genesys in New York it would probably range over Elkhart projects because it's under one master service agreement, maybe two master service agreements, five projects at a range of $5 million to $10 million apiece up to high of $40 million.

Within our, I won't say legacy, but our utility business, there are new awards, as I said, Puget Sound was one, Con Edison we had addition of the multi-family program above and beyond the small business direct install and we're looking at more Brooklyn Queens work.

So within our energy business that accounts for most of it. For engineering, the 10% year-over-year is that the economy is still recovering in California, although at a slow rate, so I think we were beaten b it a little bit and we are expanding our existing master service agreements with many of the cities that we've held for 20 to 30 years. So that accounts for most of it.

Misha Levental: Yes, thank you. And direct cost as a percent of contract revenue was nearly 70% versus 62% in the year ago period. Could you maybe elaborate on this, and is does that alter the possibility and/or cash flow profile?

Stacy McLaughlin: Misha, what were you asking on elaborate on the direct cost as a percentage of revenue?

Misha Levental: The direct cost as a percentage of contract revenue being 70% versus 62% in the year ago period. So just maybe if you could elaborate on, you know, the cause for the difference?

Stacy McLaughlin: The increase is related to an increased use in sub-contractor work versus direct salaries and wages in the prior period.

Misha Levental: Okay, okay. Additionally, could you provide utilization rates during the quarter as well as any clarity on backlog?

Thomas Brisbin: In the area that we measured it's probably 75% to 80% in the engineering group and most of our Energy Efficiency Group work it's unit pricing, so it is not really an applicable metric. But where it is, we are in high 70s, 75 to 80.

Misha Levental: And finally, what should be a normalized period tax rate going forward? In dollar terms, how much benefit or lower expense was included in the quarter?

Stacy McLaughlin: For the first part of your question, we expect our effective tax rate to be 36% going forward. And then in the current quarter the change in estimate had about a $500,000 effect on the quarter tax expense.

Misha Levental: Okay. Thanks. That's all my questions. Thank you very much.

Stacy McLaughlin: Thanks.

Operator: And once again to ask a question it is star and 1.

Thomas Brisbin: So if there is no further questions, I would like to thank all of you for participating on our call today and for your continued interest in Willdan. Hold it. We got a question, a last minute, Ryan Cassil.

Operator: And Ryan Cassil with Seaport Global, your line is open.

Ryan Cassil: Hey how are you guys doing?

Thomas Brisbin: You beat the buzzer by like a nanosecond.

Ryan Cassil: I'm sorry jumping on late here, busy afternoon. Maybe if I could just add on to one of the last questions that was asked, the subcontractor revenue just going up year-over-year, you know, that is an easy way, you know, to the extent you guys can do the work to drive earnings in the future, how do you guys think about reducing subcontractor costs or maybe with respect to M&A, I know Genesys you guys used as a subcontract in the past; is that an area you look at in terms of filling in with M&A?

Thomas Brisbin: First, with Genesys right now moving forward, we would not expect to pull additional subcontractor cost into our direct performance. Most of this work is pass-through large equipment and all construction activities we subcontract and will continue to subcontract but it is to going forward that other types of work or other acquisitions will likely have a lower subcontractor cost than Genesys which is very high. So if we were to make additional acquisitions the subcontractor percentage would likely be reduced over time.

Ryan Cassil: Okay. Is there a target you guys would be looking for there over the -- just looking longer-term bigger picture?

Mike Bieber: Thirty or less.

Thomas Brisbin: Thirty-ish-percent.

Mike Bieber: Or less.

Ryan Cassil: Okay, okay. Great. One last okay any update with respect to M&A going forward and I will follow up offline for the rest of my questions.

Thomas Brisbin: Yes. First Genesys is going well, they are integrating well, we will look to integrate the back office systems probably late this year or early next year. So that does put us in a position now to able to consider new deals, cash looks good and we are pursuing other acquisition candidates right now, pipeline looks good.

Ryan Cassil: Okay, great. Thanks for squeezing me in guys. I appreciate it. And nice quarter.

Operator: And we have no further questions at this time. I would like to turn the program back to the speakers for any closing remarks.

Thomas Brisbin: We'll do them again. Thank you all for participating and have a great day.

Operator: And this concludes today's program. Thank you for your participation. You may now disconnect.

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