

WILLDAN GROUP, INC.
Third Quarter Fiscal 2022 Earnings Call
November 3, 2022
(edited)

Call Participants:

Al Kaschalk – Vice President-Investor Relations, Willdan Group
Tom Brisbin – Chairman and Chief Executive Officer, Willdan Group
Kim Early – Chief Financial Officer, Willdan Group

Q&A Participants

Chip Moore, EF Hutton

Presentation

Missy, Operator

Welcome to the Willdan Group third quarter 2022 conference call. I'll now turn the call over to Al Kaschalk, Vice President of Investor Relations. You may begin.

Al Kaschalk, VP Investor Relations

Thank you, Missy (sp). Good afternoon, everyone, and welcome to Willdan Group's third quarter fiscal 2022 earnings call. Joining our call today are Tom Brisbin, Chairman of the Board and Chief Executive Officer, Kim Early, Chief Financial Officer, and Mike Bieber, President. The call today builds on our earnings release we issued after market closed today. You may find the earnings release and the Willdan investor report that accompanies today's call in the Press Release and Stock Information section of our Investor Relations website on ir.willdan.com. Management will review prepared remarks, and then we will open the call up to your questions. Statements made in the course of today's conference call, including answers to your questions, 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 (inaudible) 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 annual report on Form 10-K filed for the year ended December 31, 2021. The company cautions investors not to place undue reliance on the forward-looking statements made during the course of this conference call. Willdan disclaims any obligation and does not undertake to update or revise any forward-looking statements made today. In addition to GAAP results, Willdan also provides non-GAAP financial measures that we believe enhance the investors' ability to analyze the business trends and performance. Our non-GAAP measures include net revenue, adjusted EBITDA, and adjusted EPS. I'll now turn the call over to Tom Brisbin, Willdan's Chairman and CEO.

Tom Brisbin, Chairman & CEO

Thanks, Al, and good afternoon, everyone. Our third quarter shows progress on many fronts. Revenue, earnings, and cash flow were all up as projected. The business overall is good. All business units have gotten past the COVID and restart problems. We have factored in the delays on supply chain. We have collaborated well with Pacific Gas & Electric, San Diego Gas & Electric, and Southern California Gas on the start-ups and negotiation of the California IOU programs. We are in discussions with Southern California Edison to address challenges with these contracts. We have proposed changes that will benefit SCE and Willdan and stakeholders to deliver energy savings. We are affirming our guidance for 2022 that net revenue growth would be greater than 10% and EBITDA margin would be greater than 10%.

For the third quarter, we saw the inflection point that we've been waiting for, for the second half. Third quarter net revenue was up 8% over the prior year. EBITDA margin for the third quarter was 13.5%. Our organic net revenue growth rate was 8% in the third quarter, which is the sixth straight quarter for organic growth. Within the energy segment, our energy consulting, engineering, and design build businesses are contributing strong top-line revenue. E3 has doubled over the last three years and is working with many of the leading jurisdictions on the clean energy transition, which was given a boost by the Inflation Reduction Act. We are looking at how to create synergy with our cities, engineering practice and the clean energy transition. We have previously talked about the New York LL97, decarbonization plan for their 4,000 buildings. We are also working on Denver, Philadelphia, and Boston, helping with decarbonization, primarily electrified clean heat.

Our two largest utility contracts are doing well. Los Angeles Department of Water and Power is adding new measures and expect continued growth in the fourth quarter and next year. We are still working together on catch-up from the COVID pause, and we expect growth in this contract. Con Edison suspended the clean heat program in the second quarter because they successfully ran out of money. They are officially relaunching this program in the fourth quarter. We have participated in a significant way. We managed the program for approximately half their accounts. We expect this heat pump program electrification to be important going forward. Con Ed is making this pivot to electrification. We also see this with PG&E.

FirstEnergy and other client is through the start-up phase and doing well. We expect the program to grow over time. We also won a re-compete with one of our significant Southeast utilities. This was very important to us. We have had this contract since 2013. We are now running multifamily programs for four new—for four New York IOUs. These are programs for low and moderate-income families. As we look at this transition to electrification, we can see that our performance engineering group is also doing well with the New York City Housing Authority, also known as NYCHA, by helping us convert buildings so that tenants can control their heat with electric infrared panel. Again, this is good for the tenants and decarbonization. Our design build unit, who is doing this work, has a strong backlog, and they are now profitable

coming out of COVID. They won \$60 million worth of work in the third quarter with Dormitory Authority of the State of New York.

Our Engineering segment is doing well with strength across both municipal engineering and financial services. Engineering continues to grow. Some of our new assignments include Florida and Texas, although we are just getting a foothold there. For the city of Inglewood, California, we are doing fleet electrification and electric vehicle infrastructure planning. The Californian cities are now thinking about how to electrify. We are again looking to pivot with a clean energy economy.

In terms of the Inflation Reduction Act, we are tracking it in assisting cities. Given the breadth of the provisions of the bill, this has been an important topic of conversation with our clients, many of which are state and local governments and nonprofit entities. Since released in August 2022, we have done a tremendous amount of financial analysis on the bill, including the provisions around energy and climate tax incentives. We are focused on the opportunities that align with our customer base, relationships that Willdan has built over the last 60 years as a trusted adviser here in California.

In summary, we built revenue and earnings momentum in the third quarter. We successfully resolved the major issues with three of the four California IOUs to the mutual benefit of the IOUs, Willdan and outside stakeholders. We're still negotiating with SCE, and there's some progress but no resolution. The rest of the company is performing well. Once again, I want to take a moment to thank the entire Willdan team for their dedication and outstanding execution. I also want to recognize the ongoing support of our customers and long-term stockholders. I would like to turn the call over to Kim for our financial discussion. Kim?

Kim Early, Chief Financial Officer

Thanks, Tom, and good afternoon, everyone. Gross revenue for the third quarter increased by 23.5% over the prior year's Q3 to 121.4 million, while net revenue, net of some contractors, materials, and other direct costs increased 8.2% to 58.9 million. The increased revenue included increases in construction management, California IOU programs, and Engineering and Consulting revenues, partially offset by lower revenues from direct install projects and software licensing. Gross profit for the third quarter of 2022 was 37.5 million, or 30.9% of revenue, compared to 38.1 million, or 38.8% of revenue, in the same period a year ago. The lower gross profit margin was primarily due to the higher mix of construction management revenues, lower software revenues, and higher costs associated with the building of revenue backlog for new California IOU programs.

G&A costs for the quarter were 38.3 million for Q3 of 2022, up 4.3% compared to the prior year, while gross revenues were increasing 23.5%. Interest expense was 1.4 million for the quarter compared to 937,000 a year ago due to an increase in average borrowings outstanding under our credit agreement and the higher average interest rates. The loss before income taxes was 1.5 million compared to income before tax of 600,000 for Q3 of 2021. The income tax

benefit for Q3 of 2022 was 1.5 million compared to a tax benefit of 0.2 million for Q3 of 2021. The resulting net profit was 76,000 for the current quarter compared to a net profit of 840,000 reported for Q3 of 2021.

Adjusted EBITDA was 8.0 million for the quarter compared to 10.1 million a year ago, and the adjusted earnings per share was 0.42 for Q3 of 2022 compared to adjusted earnings of 0.53 per share in 2021. For the nine months to date, gross revenue increased 20.8% to 315.9 million, while net revenue increased 8.2% to 162 million. Gross profit of 100.4 million, or 31.8% of revenue, was down slightly from 101.1 million a year ago. General and administrative expenses increased 1.1% for the nine months to 112.1 million for the period, while gross revenue was increasing 20.8%. The reported net loss for the first nine months of 2022 was 8.0 million compared to a loss of 7.45 million for the same period of 2021. The year-to-date adjusted EBITDA was 11.5 million for 2022 versus 18.1 million in 2021. Adjusted earnings per share was \$0.51 for the current year compared to \$0.99 a year ago.

I'm happy to report the cash flows from operations continued to improve and were positive 8.1 million for the third quarter, bringing the total for the year to 4.5 million provided—compared to cash used of 1.7 million in 2021. Year-to-date, capital expenditures were 7.0 million compared to 4.9 million in 2021. Principal payments on our term loans and earn-out payments resulting from successful acquisition performance were offset by the 20 million drawdown of the delayed draw term loan resulting in cash used in financing activities of \$12,000 to date in 2022 compared to cash used of 17.0 million in 2021. The net decrease in cash was 2.4 million for the first nine months of 2022 compared to a decrease in cash of 23.6 million for the same period last year.

The credit agreement with our five bank syndicate has been amended. Among other things, the agreement amends the minimum adjusted EBITDA threshold and the related total leverage ratio for the remainder of the extended covenant relief period, which extends through March 31, 2023. It also increases the interest rate on borrowings during the remainder of that period and amends maximum borrowings under the revolving credit facility to \$10 million. We do not expect these changes to prevent the company from meeting its obligations or achieving its goals. For fiscal 2022, we continue to expect minimum net revenue growth of 10% over 2021, with a minimum adjusted EBITDA margin of 10% of net revenue. We expect to provide 2023 guidance when we report our fourth quarter and FY 2022 results in March of 2023. Operator, we're now prepared to answer questions.

Missy, Operator

Okay. If you would like to ask a question, you may press star one on your telephone keypad. Again, to ask a question, press star one on your telephone keypad. (Inaudible). Okay, our first question is going to come from Chip Moore with EF Hutton. Chip, your line is open.

Chip Moore, EFHutton

Good evening. Thanks for taking the question. I hopped on a little late, so I apologize if you've covered some of this. But really been a lot of focus on the California IOU business, right, in recent history and nice to see some constructive resolutions there on implementation. But if I think about Willdan, the company is really about much more than just those contracts. Just curious maybe if you step back and think about the electrification opportunity, IRA, some of those drivers over, say, next three to five years, can you maybe just speak to how you're uniquely positioned and really how you think about that opportunity and what it can mean for you?

Tom Brisbin, Chairman & CEO

We're trying to decide who should answer that question, Chip. I'm pointing at Mike. He's pointing at me.

Chip Moore, EFHutton

Maybe both of you.

Tom Brisbin, Chairman & CEO

Well, I don't know how much of the presentation that you heard, but, yeah, we think electrification is going to be the direction for many of the IOUs. And you're right. California IOUs, when they pivot—I mean so far, we've seen a little from PG&E. We're just getting a little started at SCE. We see—within the state, there's this kind of conflict between getting off of gas and getting into electricity for some of the IOUs (inaudible). So, New York has pivoted quite a bit. And I think the future will be both saving energy and electrifying. And so, we're getting early starts with some of these IOUs. And you're right. We've been talking about very recently, is our future really with just California IOUs? Because the strength of what Willdan has as you run through it—if you run through our work with cities electrifying, you run through our performance contracting group that's doing work like NYCHA, large schools, universities, and what they're trying to do is get off of gas and other fuels, and you go throughout all these other contracts. We're going to see a lot of change, and we're pivoting really well. So, thanks for the question, Chip. Did I miss anything?

Chip Moore, EFHutton

No, I think that covers it. Good to hear you're excited and like the position, and I would agree. I'll hop in queue. But that's helpful. Thanks.

Tom Brisbin, Chairman & CEO

I don't know—is there a queue? Are there other questions? I can't see in the screen.

Missy, Operator

As a reminder, if you would like to ask a question, please press star one on your telephone keypad. To ask a question, press star one on your telephone keypad.

Tom Brisbin

That's what I thought. There weren't any more questions, Chip. In summary, we built revenue and earnings momentum in the third quarter. We successfully resolved the major issues with three of the four California IOUs to the mutual benefit of IOUs, Willdan and outside stakeholders. The rest of the company is performing well. I forgot the part about thanking you all. So, thank you all. Once again, I want to take a moment to thank the entire Willdan team for their dedication and outstanding execution. I also want to recognize the ongoing support of our customers and long-term stockholders. I'd like to turn the call over to you Al, if there's anything else.

Al Kaschalk, VP Investor Relations

Operator, this concludes our conference call.

Missy, Operator

Okay. This concludes your call. You may now disconnect.