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CORPORATE PARTICIPANTS

Betty R. Johnson *MYR Group Inc. - Senior VP, CFO & Treasurer*
Jeffrey J. Waneka *MYR Group Inc. - Senior VP and COO of Commercial & Industrial*
Richard S. Swartz *MYR Group Inc. - President, CEO & Director*
Tod M. Cooper *MYR Group Inc. - Senior VP & COO of Transmission and Distribution*

CONFERENCE CALL PARTICIPANTS

Alexander David Dwyer *KeyBanc Capital Markets Inc., Research Division - Associate*
Justin P. Hauke *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate*
Jyotasna Yadav *Stifel, Nicolaus & Company, Incorporated, Research Division - Associate*
David E. Gutierrez *Dresner Corporate Services, Inc. - Head of PR Practice and SVP*

PRESENTATION

Operator

Good morning, everyone, and welcome to the MYR Group Second Quarter 2020 Earnings Results Conference Call. Today's conference is being recorded. At this time, for opening remarks and introductions, I would like to turn the conference over to David Gutierrez of Dresner Corporate Services. Please go ahead, David.

David E. Gutierrez ***Dresner Corporate Services, Inc. - Head of PR Practice and SVP***

Thank you, and good morning, everyone. I'd like to welcome you to the MYR Group conference call to discuss the company's second quarter results for 2020, which we reported yesterday.

Joining us on today's call are Rick Schwartz, President and Chief Executive Officer; Betty Johnson, Senior Vice President, Chief Financial Officer and Treasurer; Tod Cooper, Senior Vice President, and Chief Operating Officer of MYR Group's Transmission and Distribution segment; and Jeff Waneka, Senior Vice President and Chief Operating Officer of MYR Group's Commercial and Industrial segment.

If you did not receive yesterday's press release, please contact Dresner Corporate services at (312) 726-3600, and we will send you a copy, or go to the MYR group website, where a copy is available under the Investor Relations tab.

Also, a replay of today's call will be available until Thursday, August 6, at 1:00 p.m. Eastern Time by dialing (855) 859-2056 or (404) 537-3406 and entering conference ID 4291068.

Before we begin, I want to remind you that this discussion may contain forward-looking statements. Any such statements are based upon information available to MYR group management as of this date, and MYR group assumes no obligation to update any such forward-looking statements. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from the forward-looking statements. Accordingly, these statements are no guarantee of future performance. These risks and uncertainties are discussed in the company's annual report on Form 10-K for the period ended December 31, 2019, the company's quarterly reports on Form 10-Q for the first and second quarters of 2020 and in yesterday's press release.

Certain non-GAAP financial information will be discussed on the call today. A reconciliation of these non-GAAP measures to the most comparable GAAP measures is set forth in yesterday's press release.

With that said, let me turn the call over to Rick Schwartz.

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

Thanks, David. Good morning, everyone. Welcome to our second quarter 2020 conference call to discuss financial and operating results.

I will begin by providing a brief summary of our second quarter results and then turn the call over to Betty Johnson, our Chief Financial Officer, for a more detailed financial review. Following Betty's discussion, Tod Cooper and Jeff Waneka, Chief operating officers for our T&D and C&I segments, will provide an industry outlook and discuss some of MYR group's opportunities going forward. I will then conclude with some closing remarks and open the call up for your comments and questions.

As the COVID-19 pandemic still dominates the headlines and its future impacts remain to be seen, our priority continues to be the health, safety and well-being of our employees, clients and communities. We are closely monitoring and adhering to the latest government recommendations and client protocols as the policies we have enacted to facilitate our ability to adapt to this evolving situation.

We developed plans and contingencies that have enabled us to deliver on our promises, meet the expectations of our clients and return positive results to our stockholders despite these uncertain times.

We are pleased with our second quarter results, highlighted by revenue of $513.1 million, a 14.3% increase over the second quarter of 2019, along with increases in gross profit, earnings per share, net income, EBITDA and free cash flow. Our backlog was $1.55 billion at the end of the second quarter, which marks another record high for MYR.

During the second quarter, bidding and project execution remained active. And we are pleased to announce that we are currently in negotiations to finalize the contract with LS Power Grid New York Corporation I, an affiliate of LS Power to provide procurement and construction services for the Marcy to New Scotland upgrade project in the state of New York.

The project consists of nearly 100 miles of 345-kilovolt transmission construction within the existing utility corridors.

The contract is valued at more than $250 million. This project will ultimately relieve bottlenecks on the New York Power grid to improve system reliability, increase efficiency and facilitate statewide access to renewable energy.

We remain an industry leader in both our T&D and C&I segments. And as always, stayed focused on continually raising the bar to improve our quality and efficiency in project delivery.

Additionally, we continue to have a positive outlook about the future. And despite the ongoing challenges, we are confident in our ability to adapt and grow in the years ahead.

It is especially in times like these, that I am humble and grateful for our incredible team, who seamlessly demonstrates their commitment to safely execute work and deliver quality services to all our clients.

Now Betty will provide an overview of our financial results for the second quarter of 2020.

Betty R. Johnson ***MYR Group Inc. - Senior VP, CFO & Treasurer***

Thank you, Rick, and good morning, everyone. On today's call, I'll be reviewing our quarter-over-quarter results for the second quarter of 2020 as compared to the second quarter of 2019.

Our second quarter of 2020 revenues were $513.1 million. This represents an increase of $64.3 million or 14.3% compared to the same period last year. Our second quarter T&D revenues were $276.8 million, an increase of 8.1% compared to the same period last year.

The breakdown of T&D revenues was $181.2 million for transmission and $95.6 million for distribution.

The T&D segment revenues increased primarily due to an increase in volume in both Transmission and Distribution-related projects. Approximately 50% of our second quarter T&D revenues related to work performed under master service agreements.

C&I revenues were $236.3 million, an increase of 22.5% compared to the same period last year. The C&I segment revenues increased due to incremental revenues from the CSI acquisition, partially offset by a decrease due to the timing of activity on various size projects, along with the impacts related to COVID-19 pandemic.

Our gross margin was 11.9% for the second quarter of 2020 compared to 9.6% for the same period last year. The increase in gross margin was primarily due to better-than-anticipated productivity, an increase in higher-margin work and favorable job closeouts on certain projects.

These improvements were partially offset by decreases in revenue recognized on pending claims and change orders for which we're seeking reimbursement and labor inefficiencies on certain projects.

SG&A expenses were $41.2 million, an increase of $7.3 million compared to the same period last year. The increase was primarily due to the acquisition of CSI, along with higher employee-related expense to support the growth in our operations, partially offset by a reversal of contingent compensation expense related to a prior acquisition.

Second quarter 2020 net income attributable to MYR group was $13.4 million or $0.80 per diluted share compared to $7.2 million or $0.43 per diluted share for the same period last year.

Total backlog as of June 30, 2020, was $1.55 billion, a record high and was 33.5% higher than a year ago.

Total backlog as of June 30, 2020, consisted of $520.8 million for the T&D segment and $1.03 billion for the C&I segment.

Turning to the June 30, 2020 balance sheet. We had approximately $191.4 million of working capital, $82 million of funded debt and $280.2 million in borrowing availability under our credit facility. Free cash flow came in strong for the period at $54.9 million. We have continued to focus on strengthening our balance sheet, which can be seen in our funded debt-to-EBITDA leverage ratio improvements over the last 9 months, since our CSI acquisition improving from 1.85 to 0.7 leverage as of June 30, 2020. We also continued to focus on our free cash flow, controlling our operating and overhead costs and limiting capital exposures to preserve our ability to continue to fund our operations with increased scrutiny of the spend in light of uncertainties around the economic impacts from the COVID-19 pandemic.

However, we do continue to balance this with investing and developing key personnel and in procuring the specific specialty equipment and tooling needed to win and execute projects of all sizes and complexity.

We believe our credit facility, strong balance sheet and future cash flow from operations will enable us to meet our working capital needs, equipment investments, growth initiatives and bonding requirements.

In summary, we had improvements this quarter in revenues, gross profit, net income, earnings per share, EBITDA, free cash flow, funded debt-to-EBITDA leverage and backlog compared to the prior year.

I'll now turn the call over to Tod Cooper, who will provide an overview of our Transmission and Distribution segment.

Tod M. Cooper ***MYR Group Inc. - Senior VP & COO of Transmission and Distribution***

Thanks, Betty, and good morning, everyone. Throughout the second quarter, we experienced active bidding and project execution throughout our T&D operations with minimal impact from COVID-19.

We are very fortunate to be considered a critical and essential business. And as Rick mentioned, we are excited about the potential award of the Marcy to New Scotland upgrade project. Aside from this notable announcement, activity continues to center around small to medium-sized projects, and ongoing work under long-term master service agreements with upticks in bidding for a few larger transmission projects and several EPC and renewable opportunities.

Throughout the Northeast, Mid-Atlantic and Southeast, work continues for several long-term clients, such as Eversource, Dominion and the Tennessee Valley Authority.

The second quarter marks completion of the Coastal Virginia offshore wind project for Dominion, which included building the high-voltage interconnection and providing the ocean boring for future offshore cable installation.

This project was a first for MYR group in the offshore space, and our successful performance should position us well for future opportunities. In June, we were awarded a contract for Phase 2 of Dominion's Mount Storm Valley 500kV rebuilt project in Virginia.

Construction is underway, and the project is expected to be completed in July of 2021. In the Midwest, work progresses on the Connersville Transmission Project for Duke Energy and the Gateway Transmission Project for Ameren, both of which are expected to be completed later this year.

Throughout the Midwest and Texas, we experienced steady transmission, substation and distribution work, much of which falls under our long-term MSAs. Momentum continues for solar, wind and transmission opportunities throughout the West.

Our project team has begun mobilization and start-up efforts on the battle mountain storage and solar project in Nevada and work continues on the Gateway West substation projects for Pacificorp. On the distribution front, a number of utilities are making the ongoing investments in system upgrades to improve asset performance and modernize and strengthen the grid.

Many utilities are relying on outside contractors for much of this work, and our distribution work remains strong from many customers.

Industry headlines continue to reflect the positive market outlook and healthy T&D capital spending projections. Although the magnitude of COVID-19 impacts are still unfolding and could affect future initiatives.

In May, FERC reinforced that electric T&D spending should remain resilient despite weaker economic conditions, key drivers to strengthen grid reliability, replace aging infrastructure and that integrate renewable energy remain intact. And elevated levels of investments are expected to continue for the next 5 to 10 years with most utility customers, maintaining substantial multiyear CapEx plans.

Growth is still expected primarily in small to medium-sized projects and over the next 5 years, with potential for a handful of key large projects to accelerate towards construction in the next couple of years.

Several of our long-term customers made significant spending announcements in the second quarter. Excel announced plans to accelerate $3 billion in clean energy spending in response to the Minnesota Public Utilities Commission and the Department of Commerce request to involve utilities in the state's economic recovery process due to impacts from COVID-19.

In New York, National Grid filed its annual Transmission and Distribution capital investment plan with the New York State Public Service Commission, which includes a proposed $4 billion spend over the next 5 years.

Promising developments on the renewable front included a June report from the International Renewable Energy Agency that reflected significant declines in costs since 2010 for utility-scale solar power, which has dropped 82%, onshore wind which has dropped 39% and offshore wind which has dropped 29%. These declines are expected to continue with improved technology and expanded market participation.

As these energy sources become cheaper compared to new electricity capacity based on fossil fuels, leaders of U.S. hydro, solar, wind and storage industry associations, plan to expand market share over the next decade.

In summary, we are pleased with our second quarter performance and remain optimistic about our future prospects for growth and our ability to persevere through these challenging times. As we strive to bring the best of MYR group to our customers, employees and shareholders, we will carefully monitor and adjust our business operations as necessary to assure that the health and safety of our people and communities remains our top priority.

I'll now turn the call over to Jeff Waneka, who will provide an overview of our Commercial and Industrial segment.

Jeffrey J. Waneka ***MYR Group Inc. - Senior VP and COO of Commercial & Industrial***

Thanks, Tod, and good morning, everyone. Our second quarter performance is reflective of the disruption we faced in resequencing our workflow, and implementing additional safety measures throughout the quarter. Our employees adapted rapidly to new guidelines and continued serving our clients with minimal impact.

We're proud of every team member who took the lead on their respective job site, adhering to the guidelines to keep everyone healthy and safe. We entered 2020 with record backlog that continued to burn at a steady pace through the quarter. The initial decrease in C&I revenue reported last quarter continued to improve in most of our district offices as restrictions were lifted throughout the U.S. and Canada.

While we have not experienced any significant project cancellations, we have faced some delayed project starts and slower ramp-ups as project schedules are adjusted in response to market disruption.

C&I bidding activity has remained active in most of our district offices. Most of the large projects being tracked appear to be moving forward. However, market predictability is likely to remain a concern through the rest of 2020, as COVID-19 cases vary across the country.

We believe that Commercial and Industrial recovery through the balance of the year will continue to be dependent on overall economic recovery, and we remain hopeful that the various approved stimulus packages will offer continued opportunities.

C&I was successful in winning significant projects during the second quarter. These awards provide confidence that our chosen markets will continue to offer solid platform for growth and profitability.

We have continued our investment in building our transportation and infrastructure expertise across all district offices, which we believe positions us favorably for future expansion. We remain encouraged by the possible award of a national infrastructure bill, and believe we will be positioned well when additional spending bills are released.

In addition to transportation and infrastructure, we believe our other primary markets may be somewhat less vulnerable to economic slowing, including health care, data centers, warehousing, renewable energy and water projects.

As always, we remain focused on working safely, productively and in close collaboration with our clients and industry partners.

We expect that our C&I segment will emerge even stronger following the near-term challenges. We are fortunate that most of our operations are considered an essential business and are proud to employ the best field and support services in the industry. Thanks, everyone, for your time today. I'll now turn the call back to Rick, who will provide us with some closing comments.

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

Thank you for those updates, Betty, Tod and Jeff. I want to take a moment to express my appreciation to our employees who continue to inspire me every day. Amidst challenges due to COVID-19's continually evolving impacts, their constant dedication and positive outlook remind me that we are so fortunate to have the best team, talent and culture in the business.

We will remain at the forefront of identifying industry trends and client needs in order to grow our business and provide superior services in order to achieve our long-term strategic targets. And we will continue to make disciplined decisions to move our business forward. Operator, we are now ready to open the call up for your comments and questions.(Operator Instructions)

And your first question comes from the line of Sean Eastman with KeyBanc.

QUESTIONS AND ANSWERS

Alexander David Dwyer ***KeyBanc Capital Markets Inc., Research Division - Associate***

This is Alex on for Sean. Congrats on the strong results. Yes. So first question, I just wanted to touch on the commentary around the project pipeline remaining active for both of your segments and the outlook remaining intact. How would you characterize your visibility and line of sight on actual awards in the second half of the year? And maybe how would this compare to the past at this point in the year?

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

I think it's not as active as it was a year ago, but it has remained active. I think a year ago, we were describing the market as robust. I think on the T&D side remains very active, don't really see much impact there going forward. None of our clients have really said they're cutting back on their budgets. On the C&I, I think it's really, as Jeff was kind of highlighted in the script. It may be changing of the type of work. So will office buildings -- so we didn't have a lot of exposure to that. Will those be being built next year? Well, that stuff, but the data center, the hospital, some of the other areas he highlighted, from everything we see talking to the engineers and our clients out there, those continue to be planned, and it looks like those are going to be moved forward. It's really just the timing of it. And again, with any of our backlog, we've always said in previous quarters, it's lumpy.

We want to make sure we have the right contract in place before we sign it. And again, we don't control the timing of the awards.

So you do see that lumpy in some quarters.

Alexander David Dwyer ***KeyBanc Capital Markets Inc., Research Division - Associate***

Very helpful. And my second question, can you just -- can you give us some color around how you've been able to control costs during this pandemic during the last couple of quarters? And are you able to quantify the magnitude of the impact? And then also, last call, you mentioned $15 million of questionable CapEx. Have your plans for this changed in the past few months? It seems like CapEx has been pretty light this year so far. So that's...

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

We'll start with CapEx. We continue to watch it. We're just -- as we said, we're in negotiations, final negotiations on the LS Power project. That will have us continuing to invest in some capital. So again, we're going to adjust our capital to the book of business we have at hand and where we see the immediate future going. So that can come up and down a little bit, but we've got to make sure we've got the right tools, equipment in place to execute the work profitably.

So again, we'll continue to monitor that. But it probably won't be that high of a cutback on our CapEx, but we will monitor and look at it going forward. So that's on the CapEx side. And your second part of the question -- or your first part of the question, can you repeat that again?

Alexander David Dwyer ***KeyBanc Capital Markets Inc., Research Division - Associate***

Yes, yes. It was just -- I just wanted to understand the cost-cutting during the pandemic for the past couple of quarters.

And if you're able to quantify the magnitude of the impacts.

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

We haven't quantified it. I think when we look at our overall projects, though, immediately, our teams got together and looked at the project, especially on the C&I side that may be pushed out a little bit.

We didn't cut back on the side of where we needed to do additional planning. And I think Jeff can probably add a little bit on what he's done on that planning and where we see some of his productivity based on that. But we've cut -- we're always as a contractor out there, looking at our overhead, looking at what it takes to make us work more efficiently. Developing new plans and procedures that will enable us to hopefully strive a higher profit margin.

And we are in act at all times just not during the pandemic side. Jeff, you want to talk a little more specific about what you've done?

Jeffrey J. Waneka ***MYR Group Inc. - Senior VP and COO of Commercial & Industrial***

Yes. I think initially, we believe there would be a fairly large impact to productivity due to just the safety measures put in place. But we've seen that the additional time talking about the project and protocols and how we're going to go forward with our trade partners has actually benefited us.

So there's clearly some offsetting productivity out there that's been helpful to us. So we see that continuing as some of the projects kind of get pushed out to the right that it's allowing just a lot more collaboration between us and our partners, which is beneficial.

Operator

(Operator Instructions)

Our next question comes from the line of Justin Hauke with Robert W. Baird.

Justin P. Hauke ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

I guess this one is for Betty, but just the -- you called out a couple of things on the margins, some positives and negatives. Maybe to the extent you could help us quantify some of those, specifically, the earn-out reversal that you talked about and then maybe on the offset to that the project closeouts and how that impacted the margins?

Betty R. Johnson ***MYR Group Inc. - Senior VP, CFO & Treasurer***

Yes. I'm going to point to the operating results for C&I, although we haven't quantified very specifically the reversal of the contingent consideration or specifically the job closeouts.

We do, in total, we quantify it. But if you just took those when you think about them as onetime events, basically the reversal of the contingent consideration and then some of the -- maybe some of the offsetting the negative impacts that were onetime in C&I, they've pretty much offset.

So the 3.8% margin that we had in C&I segment this quarter. You can think about that as more of a consistent margin because those 2 did offset.

And just one reminder that we always talk about kind of getting to that 4% or so as is our typical when you take the higher amortization for the acquisitions, mainly CSI, just as we've talked about in the prior quarters. So even with those different events in there, this would have been just above 4% as it has been since the -- this time last year when CSI became part of our operations. And we had that higher amortization, especially for that first year.

Justin P. Hauke ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

Great. Yes, that was going to be kind of what I was going to follow-up on that is just the amortization, is that still in the 100 basis point range in terms of what's running through C&I?

And then what's the time line for that rolling off? Because I know, usually, that's highest in the first year, and you're kind of getting to the point where we're anniversarying the CSI acquisition.

Betty R. Johnson ***MYR Group Inc. - Senior VP, CFO & Treasurer***

Yes, exactly. So this -- the CSI acquisition amortization will definitely come down after this quarter. And it'll be very similar to in the past when we had large amortization and it cutback. So there'll still be some. And you can see in our cash flow the amortization, it's about 0.5% of the C&I business revenue. And it will cut back to probably at least half of that going forward.

Justin P. Hauke ***Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate***

Great. Okay. That's helpful. And then I guess the next question is just on the balance sheet. It is great to see that it's kind of opened up here after a couple of years of it being a little more stretched, at least versus your history.

And I guess the question is, where do you guys want to kind of manage the leverage longer term, assuming kind of a steady state?

And then also, what's the thought process on coming back into the market on the buyback since it's been a couple of years since you guys have done anything on that front?

Betty R. Johnson ***MYR Group Inc. - Senior VP, CFO & Treasurer***

I can start with that, Rick, and you can add. Our leverage, as you know, we talked about down at that 0.7% is even lower than -- we have set that our goal was to get to. Historically, in this last several quarters when it came up with CSI as a company, we've set that we have a -- our comfort zone. And that we talk about on a regular basis goes up to 2x leverage sometimes it could even be higher for the acquisition holiday. CSI took us to the 1.85%. And as a company, from there, our focus was to bring that back down to in that 1% to 1.25% prior to doing another acquisition. And Rick has quoted pretty much for the last year of the focus on the balance sheet and improving operations before we do another transaction.

We've said that we wouldn't be doing one in 2020. But then after that, we would be open to -- we're always looking at transactions. Trust me it is coming across our desk on a regular basis, we'd be more open to a transaction than going into next year as we complete those things that he's talked about.

And when it comes to stock buybacks, we always have that on our discussion list every quarter with the Board. It's always been readdressed. As you know, we don't have a program outstanding right now that is not our first priority of our capital spend, M&A, assuming that there's transactions out there. And based upon today's market, the most likely would be, that would be our first priority. Rick, anything else to add to that?

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

I don't have anything to add. Betty, you covered it well.

Operator

Your next question comes from the line of Jaya Yadav.

Jyotasna Yadav ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate***

This is Jaya on for Noelle Dilts. Congrats on a great quarter. So I just kind of wanted to ask about what you guys are thinking about for the nonresidential construction markets? Recently, the AI consensus forecast came out for the midyear, kind of talking about their expectations for 2020 and 2021. And some of that data was a bit more negative. So I'm just kind of curious about how you guys are thinking about the non-resi construction market into 2021?

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

Yes, I'll let Jeff start, and then I'll add to it.

Jeffrey J. Waneka ***MYR Group Inc. - Senior VP and COO of Commercial & Industrial***

Yes. I'd like to address that. We have found in prior challenging economic times that we're in a pretty resilient position. A lot of our clients during these times turn to their most trusted partners to get their work done.

So we have -- although the -- no doubt there's less work in the pipeline in the design industry. We feel there's plenty of projects out there that are maybe more difficult that our clients are going to be looking for somebody who they absolutely trust to get their work done. They know that other contractors can get stressed during this time. So we believe it starts to put us in a very favorable position and believe we'll push through this pretty well.

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

And as a company, we have little exposure to big box, we don't do that as a company. So we don't do that kind of construction. And we have limited on what I'd call high-rise TI build-out, but we do some of it.

It's not a high percentage of our C&I business. We do more of what we describe as more of the high-tech specialized commercial industrial type work. So again, not a lot of exposure on that, but we constantly monitor the entire market.

And we see some upsides in some potential markets, as Jeff said, with data centers and other areas that are growing.

Operator

(Operator Instructions)

At this time, there are no further questions. I will now turn the call over to Rick Swartz for closing remarks.

Richard S. Swartz ***MYR Group Inc. - President, CEO & Director***

To conclude, on behalf of Betty, Tod, Jeff and myself, I sincerely thank you for joining us on the call today. I don't have anything further, and we look forward to working with you going forward and speaking with you again on our next conference call. Until then, stay safe and healthy, everyone.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.