



Mastech Digital, Inc.
First Quarter 2024 Earnings Call
May 8, 2024

Operator

Greetings, and welcome to the Mastech Digital First Quarter 2024 Earnings Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press star zero on your telephone keypad. As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Jenna Lacey, Manager of Legal Affairs for Mastech Digital. Thank you, Ms. Lacey. You may begin.

Jennifer Lacey

Thank you, operator, and welcome to Mastech Digital's first quarter 2024 conference call. If you have not yet received a copy of our earnings announcement, it can be obtained from our website at www.mastechdigital.com. With me on the call today are Vivek Gupta, Mastech Digital's Chief Executive Officer; and Jack Cronin, our Chief Financial Officer.

I would like to remind everyone that statements made during this call that are not historical facts are forward-looking statements. These forward-looking statements include our financial growth and liquidity projections as well as statements about our plans, strategies, intentions, and beliefs concerning the business, cash flows, costs, and the markets in which we operate.

Without limiting the foregoing, the words believe, anticipate, plans, expects, and similar expressions, are intended to identify certain forward-looking statements. These statements are based on information currently available to us, and we assume no obligation to update these statements as circumstances change.

There are risks and uncertainties that could cause actual events to differ materially from these forward-looking statements, including those listed in the company's 2023 annual report on Form 10-K filed with the Securities and Exchange Commission and available on its website at www.sec.gov.

Additionally, management has elected to provide certain non-GAAP financial measures to supplement our financial results presented on a GAAP basis. Specifically, we will provide non-GAAP net income and non-GAAP diluted earnings per share data, which we believe will provide greater transparency with respect to the key metrics used by management in operating the business.

Reconciliations of these non-GAAP financial measures to their comparable GAAP measures are included in our earnings announcement, which can be obtained from our website at www.mastechdigital.com. As a reminder, we will not be providing guidance during this call, nor we will provide guidance in any subsequent one-on-one meetings or calls.

I will now turn the call over to Jack for a review of our first quarter 2024 results.

Jack Cronin

Thanks, Jenna, and good morning, everyone. During the first quarter of 2024, activity levels, client spending patterns, and economic conditions have all shown promise for the first time since mid-2022, particularly in our IT Staffing Services segment. While some uncertainty still exists in the marketplace with respect to inflation and economic forecasts in general, we're encouraged by our clients' more optimistic views about their prospects and opportunities in today's environment.

With that backdrop, let me address our first quarter 2024 financial results. Q1 revenues totaled \$46.8 million compared to first quarter 2023 revenues of \$55.1 million, representing a 15% year-over-year decline, which is a marked improvement over our Q4 2023 year-over-year revenue decline of 20%. Additionally, on a sequential basis, we achieved revenue growth over Q4 of 2023 of 2%.

Our Data and Analytics service segment reported revenue of \$8.1 million in Q1 2024 compared to \$9.4 million in the 2023 first quarter. On a sequential basis, revenues were essentially flat in Q1 2024 versus Q4 2023. Coming off a record bookings performance last quarter, our Q1 2024 bookings results totaled \$9.6 million, which surpassed last year's Q1 bookings by \$1.2 million. While the "dollar value" of Q1 bookings isn't overly exciting, the fact that many of these new orders came from existing clients who have significantly reduced spending throughout 2023 is very positive.

First quarter 2024 revenues in our IT Staffing Services segment totaled \$38.8 million compared to \$45.7 million in the first quarter of 2023. On a sequential basis, revenues grew by 2%, and our billable consultant headcount increased during the quarter by 6%.

Consolidated gross margins as a percent of revenues in Q1 2024 improved to 25.9% compared to 24.5% in the first quarter of last year and was sequentially better than Q4 2023 gross margins of 24.6%.

In our Data and Analytics Services segment, margins improved to 46.4% compared to 38.5% in Q1 2023 and were sequentially better than Q4 2023 gross margins of 44.7%. This improvement reflected higher project gross margins and improved utilization in the 2024 first quarter. In our IT Staffing Services segment, gross margins were flat compared to Q1 of last year and 130 basis points better than the 2023 fourth quarter.

GAAP net income for Q1 2024 was a loss of \$161,000, or a \$0.01 loss per diluted share, compared to net income of \$261,000, or \$0.02 per diluted share, in Q1 of last year.

Non-GAAP net income for Q1 2024 was \$800,000, or \$0.06 per diluted share, compared to \$1.4 million, or \$0.12 per diluted share in the first quarter last year.

SG&A expense items not included in non-GAAP financial measures net of cash benefits were stock-based compensation and the amortization of acquired intangible assets and are detailed in our Q1 2024 earnings release, which is available on our website.

Lastly, addressing our financial position, on March 31, 2024, we had \$19.4 million of cash balances on hand, no bank debt outstanding, and borrowing availability of \$24.2 million under our revolving credit facility. Our day sales outstanding measurement was 56 days at quarter-end, which was favorable to our target range of 60 days to 65 days.

I'll now turn the call over to Vivek for his comments.

Vivek Gupta

Good morning, everyone. Thank you, Jack, for the detailed financial review of our operating results for Q1 2024.

Clearly, and to Jack's point, we are feeling more positive about the macroeconomic environment today than we were at the end of 2023. During the first quarter of 2024, our clients have shown more comfort with starting new assignments and tackling some of their pent-up IT needs after more than four quarters of reduced spending over economic concerns. While one quarter doesn't make a trend, I'm feeling much better about where the domestic economy is likely headed than I was three to six months ago.

In our Data and Analytics Services segment, Q1 bookings were largely from existing clients who have been very conservative in releasing new orders over the last four to six quarters, and most of these bookings should translate into revenues over the next 12 months. Additionally, I should mention that Data and Analytics gross margins strengthened in Q1 as we continued to focus on improving our delivery performance and utilization rates.

In March, we participated in Gartner's Data & Analytics Summit as a sponsor, which resulted in meaningful, new client introductions and gave us a good platform to showcase our data and

analytics capabilities and go-to-market strategy to a wide audience. This event appears to have favorably impacted our current pipeline of opportunities and is a conference that we will likely participate in again in 2025.

Our IT Staffing Services segment also experienced an increase in demand for its services in the first quarter of 2024. Historically, the IT staffing industry has been somewhat of a lead indicator in both the start of economic downturns as well as the start of economic recoveries. During Q1 of 2024, we increased our billing consultant headcount by 6% and were able to achieve sequential revenue growth of 2%. I'm optimistic that our Q1 performance is a good lead indicator of better times ahead.

Operator, this concludes our prepared remarks. We can take questions now.

Operator

Thank you. We will be conducting a question-and-answer session. If you would like to ask a question, please press star one on your telephone keypad. A confirmation tone will indicate that your line is in the question queue. You may press star two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star key.

One moment, please, while we pull for questions. Our first question comes from the line of Lisa Thompson with Zacks Investment Research. Please proceed with your question.

Lisa Thompson

Good morning. It's great to see some optimism for a change. My first question is about the staffing increase. You said you increased the consultants by 6%. Does that mean that Q2 might be up 6% sequentially?

Vivek Gupta

Hi, Lisa. While, as you know, we don't give guidance, what I can say is that the revenue in Q2 should be better than the revenue of Q1 as a result of this increased headcount.

Lisa Thompson

And how has the headcount trended this quarter?

Vivek Gupta

Well, so far, we've just finished the first month and again, I can say that it has been positive. We've had some net growth in April, so it's a good sign.

Lisa Thompson

Great. Let's see. As far as expenses go, I had thought they would be down a little bit, but they didn't seem to come down that much. Can you talk about what to expect, going forward?

Jack Cronin

They came down 3%, Lisa. You know, but, again, our activity levels increased in Q1 over Q4. We're being very conservative about increasing our expenses, so even if market conditions continue to get better, and there's more opportunity out there, we're still going to be conservative. We'll be adding SG&A costs. But, you know, I think they would trend up a bit.

Lisa Thompson

Okay, so kind of in line with revenues?

Jack Cronin

Yes. Kind of in line with revenues, yes.

Lisa Thompson

Okay. So looking at where you're going, and sequentially, it looks like you should be back to profits by at least Q3, if not Q2, does that make sense?

Jack Cronin

That makes sense.

Lisa Thompson

Okay. Is there anything else we should know about what's going on in D&A as far as the types of projects you're booking?

Vivek Gupta

Sure, Lisa. What I can say is that traditionally, we were doing the D&A businesses more in MDM, their master data management technologies. And we were doing a lot of that. And, over a period of time, over the last couple of years, we've started wading into the broader data modernization areas.

And, I'm happy to say that more and more of new business is coming in that data modernization space, so we are able to then sell and deliver the full spectrum of our offerings in the data and analytics space. And I think that's also the reason why we've been able to do better on all our bookings because our data modernization story is working well with both existing customers and prospects.

Lisa Thompson

Okay. And I guess my final question is you didn't mention anything about stock buybacks. What's the thinking there, and what was the activity?

Jack Cronin

We were in the market for just about every day that we could have been in the market. Our volume, our share volume, has been very low in Q1, which materially impacted the amount of purchases that we can make. We ended up repurchasing a little over 9,000 shares at an average

price of \$8.70. We plan on being in the market in, once we get out of the earnings blackout period.

Lisa Thompson

--Okay, great. Thank you.

Jack Cronin

Yes, we're still keen on the share buyback program. And, the other thing that I would say is we're not opposed to, you know, facilitating a block purchase if that opportunity presents itself, but we're keen on the share buyback program, for sure.

Lisa Thompson

Great. Thank you so much. That's all my questions.

Jack Cronin

Thanks, Lisa.

Vivek Gupta

Thank you, Lisa.

Operator

Thank you. Our next question comes from the line of Tim Call with Capital Management. Please proceed with your question.

Timothy Call

I was hoping you could give us an example of how client interactions and sentiment have changed this year.

Vivek Gupta

Hi Tim. Could you repeat the question?

Timothy Call

I was hoping you could provide an example of how your client interactions, when you're talking to clients about logging new business, how their sentiment has changed, how the conversations have changed this year versus last year.

Vivek Gupta

Sure, sure. So, last year, we saw that the customers were holding back, and they were not willing to give large projects out. They were not willing to spend large amounts of money. The money was being diverted towards keeping the lights on rather than building the business, as we say. And, we've seen that towards the end of 2023, and more in the beginning of 2024, customers are now beginning to open up their wallets and willing to sign projects, much larger projects, the ones that they were holding up for a long time.

And also, you see, when you have four or six, or four to six quarters, of holding back, there is that pent-up IT demand, which doesn't go away. It just stays there and just becomes larger and larger. So, we are seeing that they are now beginning to release funds towards that. So, the conversations, the bookings that we've had, I guess the conversations that we are having with our customers are pointing towards them wanting to now get back onto their IT plans.

And, it's not flood gates yet, but it's looking much more positive. They're looking--customers seem to be much more comfortable. So--and projects typically tend to happen on the data analytics side. On the staffing side, again, the same thing we have seen, that the customers are now--are believed to hire contract staff as well as permanent staff. And the pace and the quantum is picking up at least that's what we've seen in Q1, and right into the last month of April. Does that answer your question, Tim?

Timothy Call

Yes. Thank you. With no debt and cash on the balance sheet being close to 20% of the stock market capitalization, want to congratulate you on getting through the down cycle with such a clean balance sheet and lots of financial capacity. We're looking forward to the multiyear rebound. So, it's great to hear your comments. Thank you.

Vivek Gupta

Thank you, Tim.

Operator

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

Our next question comes from the line of Marc Riddick with Sidoti & Company. Please proceed with your question.

Marc Riddick

Hey, good morning.

Jack Cronin

Hello, Marc.

Marc Riddick

So, I was sort of curious as to--I just want to sort of follow up on that thread the types of projects that folks are beginning to act on. Is there any particular type that you are seeing as far as what those first initial kind of like loosening of funds is being put toward? And then, maybe if you could share whether that's seemingly coming from any particular customer industry vertical that stands out to you as far as being, you know, more willing to put money to work now.

Vivek Gupta

Marc, what we are seeing is more generic and general across all industries, and I don't think it's, you know, some industries more than the other. Banking, of course, as you know, was hit quite badly the banking industry. And they were really holding back quite a bit in the previous year, 2023. And that--they have now started spending on IT services.

Now, what kind of projects they are, there are all kinds out there, but I think I would like to use the same distinction that I made a minute ago, which is, you know, you have to keep the lights on, so you are maintaining what you already have. That never stopped. That didn't stop in 2023 either.

It was really building the bank or building the company or building the enterprise for the future, so the new initiatives, the new developments for competitive advantage and growth, some of those were being held back. And it was beginning to, I guess, impact their businesses. So, customers are now beginning to look at the build the business side of IT. I don't know if that answers your question.

Marc Riddick

No, that's helpful. And then, I wanted to sort of make sure I got this right. So, you mentioned as far as the pickup in consultant count, where did you end the quarter on consultant count?

Vivek Gupta

Jack, do you have the number there?

Jack Cronin

Yes, I do have it. Give me a sec. Yes, for total consultants--for total headcount, for the company, we were a little over 1,700. Our global consultants in our IT Staffing Services was 1,004, up 58 consultants from the previous quarter.

Marc Riddick

Okay, okay, that's helpful. And then, you seemed to signal in an earlier--in one of Lisa's questions that it's maybe a little bit higher since the end of the quarter, correct?

Vivek Gupta

Yes, Yes. I mean, April was positive, yes.

Marc Riddick

Okay, okay, great. And then, I was wondering if you could talk a little bit about the pricing dynamic that you're seeing out there bill rates and the like? I mean, is there much in the way of meaningful push back as far as pricing? Or what are you experiencing now, and has that changed since the year began?

Vivek Gupta

So, the pricing pressures are always there, and I guess they intensified in 2023. They still haven't gone away, but as spending has started, customers do realize that you know, you need--if you're looking for better consultants or better services, then the price point in the marketplace is, you know, because of inflation and otherwise, the rates are going up.

And, by and large, the customers are receptive to looking at that for the right candidates. I'm talking more on the IT staffing side. So, the pricing pressures are there, but they are not what's the word I'm looking for? They are not unduly, impacting our business strength.

Marc Riddick

Okay. And then, the last one for me, the pickup in gross margin in Data and Analytics year-over-year, you know, it was about 800 basis points there. I was wondering if you could talk a little bit about that gross margin pickup. Is that--or how much of that may be--are we talking about--I would imagine there is a little bit of everything. But, you know, how much of that is increased utilization? How much of that is revenue mix? What should be looking at there as far as that gross margin pickup in data and whether that has an opportunity to continue, going forward? Thanks.

Vivek Gupta

So, Marc, there were basically two reasons why our gross margins improved as compared to the same quarter last year. The first one was the actual project execution, so, you know, I said we've continued our focus on the delivery performance. It's looking at, how do we deliver the projects to our customers with better gross margins? And that obviously means better utilization.

Also the second thing which impacted us last year was we had a large bench. So, we are doing very tight bench management, which obviously doesn't mean that, you know, you bring the bench down to zero. You know, you always have to be a little ahead of the need of the people because people have to be brought onboard, they have to be trained and ready for when the projects actually start.

So, I think we are doing a much better job of the bench management, much better job of utilization, and much better job of doing a better--getting better gross margins out of the project in execution. So, it's a bit of many of these things. I don't know if that answers your question. Jack, is there anything else that you'd like to comment on this?

Jack Cronin

Yes, our margins right now are about 46.5%. You know, Q1 of last year was a disaster. It was 38.5%. I wouldn't even use that as a benchmark. We always target 45%, so we're 140 basis points better than, you know, our benchmark target. And I would say, you know, about--if I had to split it between utilization improvement and, you know, just better margins and better delivery, you know, I would say it's one-third utilization and two-thirds project margins.

Marc Riddick

That's helpful. Thank you very much.

Jack Cronin

Yes.

Vivek Gupta

Thank you, Marc.

Operator

Thank you. As a reminder, ladies and gentlemen, if you would like to ask a question, please press star one on your telephone keypad. There appear to be no further questions at this time. I'd like to turn the floor back over to Vivek for closing comments.

Vivek Gupta

Thank you, Alberta. If there are no further questions, I would like to thank you for joining our call today, and we look forward to sharing our second quarter 2024 results with you in early August. Thank you.

Operator

This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.