

Fourth Quarter 2017 Conference Call

February-07-2018

Confirmation #13676079

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Operator: Greetings, and welcome to the Mastech Digital, Inc. Fourth Quarter Earnings Call. At this time, all participants are in a listen-only mode. A 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, Jennifer Ford Lacey, Manager of Legal Affairs for Mastech Digital, Inc. Thank you. You may begin.

Jennifer Ford Lacey: Thank you, Operator, and welcome to Mastech Digital's Fourth Quarter 2017 Conference Call. If you not yet received a copy of our earnings announcement, it can be obtained on 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 our business, cash flows, costs and the markets in which we operate.

Without limiting the foregoing, the words believe, anticipate, plan, expect 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 if 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 2016 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 key metrics used by Management in operating our 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 will we 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 fourth quarter and full year 2017 results.

Jack Cronin: Thanks, Jen, and good morning everyone. Revenues for the fourth quarter—excuse me. Revenues for the fourth quarter of 2017 totalled \$40.5 million and represented a 25% increase compared to revenues of \$32.4 million in the fourth quarter of 2016.

Our Data and Analytics Services segment, which was acquired on July 13, 2017, contributed \$5.1 million of revenue during Q4, or approximately \$1 million higher than revenues reported from this segment in the previous quarter. This sequential revenue increase was due to higher project wins in Q4 versus Q3, and is reflective of a full year of operations—or, excuse me, a full quarter of operations by this segment in the fourth quarter of 2017.

Organic year-over-year revenue growth from our IT Staffing Services segment was 9% in Q4, as our billable consultant base increased by 12% during the year. Demand for our IT Staffing Services remained robust during the fourth quarter, and improved efficiencies at our offshore recruitment center resulted in a higher assignment win ratio in 2017.

Gross profit for fourth quarter of 2017 totalled \$9.5 million compared to \$6.4 million in the same period last year. Our gross margins for Q4 of 2017 were 23.5% of revenues, compared to 19.7% of revenues in the fourth quarter of 2016, and 22.5% of revenues in Q3 of 2017.

Our Data and Analytics Services segment had gross margins of 45.3% in Q4 of 2017, compared to 44.2% in Q3 of 2017. Our IT Staffing Services segment in Q4—our gross margins were 20.4% compared to 19.7% in the 2016 fourth quarter, and 20% in the third quarter of 2017. Lower bench costs in the Data and Analytics segment, and higher direct—higher revenues in our IT staffing segment favourably impacted our gross margins in the 2017 quarter.

SG&A expenses were \$7 million in the fourth quarter of 2017, and represented 17.4% of total revenues compared to \$5.3 million or 16.3% of revenues in the fourth quarter of 2016. Exclusive of amortization of acquired intangible assets, our operating expenses as a percent of revenues were 15.7% in both Q4 of 2017 and Q4 of 2016.

GAAP net income for the fourth quarter of 2017 was \$865,000 or \$0.16 per diluted share, compared to \$640,000 or \$0.14 per diluted share in Q4 of 2016. It should be noted that Q4 net income in 2017 included a \$372,000 charge related to U.S. tax reform, which impacted diluted earnings per share by approximately \$0.07 per share. Non-GAAP net income for the fourth quarter of 2017 was \$1.7 million or \$0.32 per diluted share, compared to \$841,000 or \$0.19 per diluted share in the corresponding quarter of 2016.

Fourth quarter SG&A expense items not included in non-GAAP financial measures net of cash benefits were, one, the amortization of acquired intangible assets; two, stock-based compensation; and in the 2017 quarter, three, an estimated one-time charge related to the impact of U.S. tax reform, and are detailed in our Q4 earnings release, which is available on our website.

Addressing our full year results, 2017 revenues totalled \$147.9 million and represented a 12% increase over 2016 revenues of \$132 million. This increase is reflective of our July 2017 acquisition of the Services Division of Canadian-based InfoTrellis, and organic revenue growth achieved in our IT Staffing Services segment.

Gross profits in 2017 were \$31.6 million compared to \$26.3 million in 2016. Gross margins as a percent of revenues were 21.4% in '17 versus 19.9% in 2016. This improvement was largely due to the InfoTrellis acquisition.

GAAP net income for 2017 totalled \$1.6 million or \$0.33 per diluted share compared to \$2.5 million or \$0.56 per diluted share in 2016. Non-GAAP net income for 2017 totalled \$4.6 million or \$0.92 per diluted share compared to \$3.8 million or \$0.84 per diluted share in 2016.

Full year SG&A expense items not included in non-GAAP financial measures net of tax benefits were the amortization of intangible—acquired intangible assets, stock-based compensation, and in the 2017 year, acquisition transaction costs and an estimated one-time charge related to U.S. tax reform; and in the 2016 year, severance expenses. Again, a detailed reconciliation of our non-GAAP financial measures compared to their comparable GAAP measures is included in our earnings release.

Briefly addressing our financial position, at December 31, 2017, we had \$35.7 million of outstanding bank debt net of cash balanced on hand, and our borrowing availability approximately \$12.9 million under our existing revolving credit line. The increase in bank debt during the year reflected our July 2017 acquisition, which was largely funded with debt.

Lastly, our accounts receivable balance at year end 2017 remains at top quality, and we ended the year with a healthy day sales outstanding measurement of 58 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 2017.

Let me start by saying that 2017 was a watershed year for Mastech Digital. Since joining Mastech in March 2016, it's been my stated objective to transition the Company from a pure-play IT staffing company into a leading player in digital transformation IT services. With the acquisition of the Services Division of InfoTrellis and operating investments in other parts of our business intended to enhance our capabilities and focus on digital technologies, I am pleased to say we are well on course in this journey.

Having said that, 2017 was also a period of great change for our organization, and our dedicated employees rose to the challenges. Our corporate team did an excellent job in completing the acquisition of InfoTrellis from the due diligence phase to its integration, as well as in dealing with the disruption of upgrading our IT systems. Our sales and delivery organizations dealt admirably with change management during the year as we redefined our Services portfolio and go-to-market strategies and how these organizations execute upon them.

Let me take a moment to acknowledge all the hard work and tenacious efforts of our associates during an extremely demanding year. It is thanks to their efforts that, today, we have a project-based Data and Analytics Services segment with capabilities to deliver a wide portfolio of digital transformation services from multiple geographies, and our IT Staffing Services segment has

several promising practice areas and a clear focus on staffing digital technologies, in addition to mainstream technologies skills. It's been quite a ride, and I'm confident that the best is yet to come.

Now let me share with you my expectation for 2018 for our two operating segments. First of all, Data and Analytics Services segment; I believe that this segment is full of opportunities. In 2018, we will endeavour to broaden our capabilities in several high growth areas, including Big Data, analytics, master data management, and data governance. We also plan to make investments in 2018 to expand the size and quality of our sales organization. This initiative will allow us to fully capitalize on our proven delivery capabilities and should help mitigate the historical lumpiness in this segment's quarterly revenue streams. Gross selling efforts and back office optimization will continue in 2018. We've had some success in both of these areas in 2017, and expect to see continued successes this year.

Next, let me talk about the IT Staffing Services segment. I fully expect our IT Staffing segment to grow better than the industry average for 2018. Continued efficiency gains at our offshore recruitment center and successes with digital technologies will be key drivers in this year. I also expect our gross margins to stabilize around 20% in 2018. Clearly, a tight supply of qualified IT resources will continue to pressure margins; however, our focus on advanced digital

technologies should mitigate these headwinds. We will continue with efforts started in 2017 to upgrade our backbone systems and security environments. This initiative will ensure that we have the required infrastructure to support our growth objectives in 2018 and beyond.

As we enter 2018, I can tell you that the morale of our employee base is extremely high, and the confidence levels have continued to strengthen during the year. Collectively, our organization is looking forward to a prosperous and successful 2018.

I will now open the session for your questions.

Operator: Thank you. At this time, 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. The confirmation tone will indicate that your line is in the question queue. You may press star, two if you'd 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 keys. One moment, please, while we poll for questions.

Thank you. We do have a question coming from the line of Louis Moser with Maverick's. Please proceed with your question.

Louis Moser: Good morning. Very nice job, by the way. I was wondering, the stock price being what it is around under 10 somewhere and I know you have a real small capitalization. Do you have any interest in trying to get some analyst coverage because of the apparent momentum that you're achieving now? It would seem to me that you might be able to get a little bit higher price for your stock if you had some coverage and I don't know if you go to various meetings with Executives or trade shows, etc. I think it's undervalued and I think that it would help, so that's my question.

Jack Cronin: This is Jack Cronin. We've been just starting to attend some investor conferences and we're going to continue to do that. As far as a complete IR blitz, I mean, we need to talk to our Board about when that's appropriate.

Louis Moser: Okay. However, I would assume that the momentum of what you're created in your recently announced quarter today will continue on course?

Vivek Gupta: Yes, we are hoping that we'll be able to maintain the momentum that we have gained.

Louis Moser: Okay. Is there anything coming up in the new product that would add to the appeal of the Company?

Vivek Gupta: Are you asking are we introducing any new service lines in the Company?

Louis Moser: Yes. Yes.

Vivek Gupta: Well, at the moment, as I mentioned in my piece, we plan to strengthen the service offerings in our defined areas in the digital transformation services, so we will look at, if there are any missing bits. So anything—investment areas in these space, Big Data, analytics, master data management and data governance. On the IT Staffing side, I think we've come a long way in the last two years by introducing practices specifically focused towards servicing, the digital technologies, and as a result of that in the last seven quarters or so, or eight quarters, we've been able to almost double the percentage of our revenues that are coming from the digital space.

So, sorry I'm giving you a long answer to your question. I mean, there is nothing very—I wouldn't say something very radically different which is going to come out, but we will just strengthen what we have and see that our portfolio becomes more complete.

Louis Moser: Okay. yes, I guess that would, —there was something else on my mind but I can't quite come up with it now, So, I appreciate your answers.

Vivek Gupta: Thank you.

Louis Moser: And, good luck.

Vivek Gupta: Thank you.

Operator: Thank you. As a reminder, ladies and gentlemen, if you would like to ask a question at this time, please press star, one on your telephone keypad. Please hold while we poll for additional questions.

It appears there are no further questions at this time, so I'd like to pass the floor back over to Vivek Gupta for any additional concluding comments.

Vivek Gupta: Thank you. Uh, so if there are no further questions, I would like to thank you for joining our call today, and uh, we look forward to sharing our first quarter 2018 results with you in late April.

Operator: Thank you. Ladies and gentlemen, this does conclude today's teleconference. We thank you for your participation, and you may disconnect your lines at this time.