



Mastech Digital, Inc.
Fourth Quarter 2023 Earnings Conference Call
February 7, 2024

Operator

Greetings, and welcome to the Mastech Digital, Inc. Fourth Quarter 2023 Earnings Conference 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 “*”, “0” 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. Thank you. You may begin.

Jennifer Ford Lacey

Thank you, Operator, and welcome to Mastech Digital's Fourth--Fourth Quarter 2023 Earnings Conference Call. If you have 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 the business, cash flows, costs and the markets in which we operate.

Without limiting the foregoing, the words believes, anticipates, 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 posted in the company's 2022 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 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 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 2023 results.

Jack Cronin

Thanks, Jen, and good morning, everyone. Our fourth quarter 2023 financial results were impacted by economic uncertainty and our current and prospective clients' responses to these challenging market conditions. Fourth quarter revenues totaled \$46.1 million, representing a 20% year-over-year revenue decline. Both of our business segments contributed to this decline.

Our Data and Analytics Services segment reported revenues of \$8.2 million in Q4 2023, compared to \$9.1 million in the 2022 fourth quarter as customers continued to reduce resources on existing projects, albeit at a lower rate in Q4 when compared to Q2 and Q3 of 2023. Also, Q4 order bookings totaled \$19 million, which was one of our best performances since we acquired the Data and Analytics Services segment. Accordingly, we achieved a modest tick up in revenues on a sequential basis, over the third quarter of 2023.

Fourth quarter 2023 revenues in our IT Staffing Services segment totaled \$37.9 million, compared to \$48.1 million in the fourth quarter of 2022. During the quarter, our billable consultant base declined, again, at a slower rate when compared to Q2 and Q3 of 2023. And in a quarter where consultant head count declines are the norm in the industry as clients, historically, seek to complete existing projects and resources, prior to the start of the new year.

Consolidated gross profits as a percent of revenues in Q4 2023 totaled 24.6%, compared to 24.8% in Q4, 2022.

In our Data and Analytics Services segment, gross margins improved, materially, to 44.7%, compared to 37% in the fourth quarter of 2022. This improvement reflects higher utilizations in the 2023 quarter and reduced margins on several significant assignments in the fourth quarter of 2022.

In our IT Staffing Services segment, gross margins were down compared to Q4 of 2022, largely due to a year-over-year reduction in direct hire revenues and unusually high medical claim expenses, related to our self-insured health care program.

GAAP net income for Q4 2023, totaled a loss of \$5.4 million, or negative \$0.46 per diluted share, compared to a profit of \$1.5 million, or \$0.13 per diluted share in Q4, 2022. These GAAP numbers do include a \$5.3 million goodwill impairment charge.

Non-GAAP net income for Q4 2023, was \$1.3 million profit, or \$0.11 per diluted share, compared to \$2.8 million, or \$0.23 per diluted share in the fourth quarter of 2022.

SG&A expense items not included in non-GAAP financial measures net of tax benefits are detailed in our fourth quarter 2023 earnings release for all periods presented, which is available on our website.

Addressing our full year 2023 results, revenues were \$201.1 million, which were down 17% on a year-over-year basis. Again, both business segments contributed to this decline.

Gross margins for the full year 2023 totaled 25.4%, compared to 26.1% in 2022. Our Data and Analytics Services segment gross margin percent increased by 200 basis points, year-over-year, on improved utilization, and our IT Staffing Services segment gross margin percent declined by 140 basis points due to lower direct hire revenues and higher health care expenses.

GAAP diluted earnings per share was a loss of \$0.61 in 2023, compared to a profit of \$0.72 in 2022.

Non-GAAP diluted earnings per share totaled a profit of \$0.44 in 2023 compared to a profit of \$1.13 in 2022.

Throughout 2023, our liquidity and overall financial position remained solid.

Today, we're 100% debt-free with no borrowings outstanding under our PNC facility. Also, we have \$21.1 million of cash balances on hand and have cash availability of another \$22.5 million under our revolving credit facility.

I should also point out that our day sales outstanding measurement on December 31, 2023, improved to 53 days from 59 days, a year earlier. Thus, despite challenging economic

conditions, we prudently managed our accounts receivable credit risk and incurred no bad debt expense in 2023.

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 2023 operating results.

In 2023, macroeconomic headwinds clearly had a significant impact on our financial performance. Concerns over a possible recession, high inflation, increased interest rates as well as geopolitical events, led many of our clients to take a conservative posture with respect to spending on new projects and on new IT initiatives.

While the U.S. economy seems to be entering a recovery mode with positive data points in job growth and GDP expansion, concerns still exist with respect to inflation, high interest rates and the possible escalation of a wider conflict in the Middle East.

Notwithstanding these potential economic issues, we are starting to see some signs of increased customer demand in both of our business segments. In our Data and Analytics Services segment, Q4 order bookings totaled approximately \$19 million, which was one of our best performances on record. Additionally, we had a modest revenue increase on a sequential basis over Q3 of 2023.

In our IT Staffing Services segment, we saw--saw positive billable head count growth for the first time in October and November, after 15 consecutive months of declines. In December, we did see high year-end project ends, but they were largely in line with the seasonal decreases we experienced at year-end. Overall, the Q4 billable head count decline was less than the declines we experienced in the fourth quarter of the prior two years.

We are encouraged by these positive indicators, as we enter 2024.

During the quarter, Michael Fleishman resigned from his position as the Chief Executive Officer of the Data and Analytics Services segment. We thank Michael for his service, and we wish him success in his future endeavors. Until his successor is appointed, the functional heads of this segment are directly reporting to me.

Also, during January 2024, we engaged Primentor, Inc. as a strategic advisory consultant. Primentor is a firm deep experience and knowledge of the broad IT services industry and an impressive track record of strategy and business process improvements for a number of notable clients. We are excited about this engagement and the opportunities that it presents for Mastech Digital.

Finally, despite 2023's difficulties, we believe that our businesses remain fundamentally sound, both operationally and financially, and we are optimistic that we are positioning our businesses for an improved financial performance in 2024.

And that concludes our prepared remarks. Operator, we can take questions now.

Operator

Thank you. We will now be conducting a question and answer session. If you would like to ask a question, please press “*”, “1” on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press “*”, “2” 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 keys. One moment, please, while we poll for questions.

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

Tim Call

Well, it's great to hear that some forward-looking indications are positive. One year ago, the Board authorized a share buyback, uh-uh, program and it's not too big. You have over 20 million of cash on your balance sheet and no debt. So the net cash position is about 22% of your stock market capitalization.

So it seems to be a no-brainer to put 20 million to share buybacks. The Board was very modest and improved a 500,000 share buyback. What's the status of that? And why is it taking a year to make accretive share buybacks when your long-term prospects are so positive?

Jack Cronin

Tim, this is Jack. We are 100% committed to the share buyback program. I mean, I think we think our stock is undervalued compared to the intrinsic, you know, value that it presents. And, we have bought back, I think right now today, we bought back around 60-some-thousand shares in Q4.

We only bought back five and the reason for the 5,000 shares. And the reason for that is we were in an extended blackout period with respect to some of these corporate events.

But we are 100% committed to the share buyback program. And I think you will see us purchase more shares in first quarter of 2024.

Tim Call

There's are some bigger companies that are buying back stock on a more regular basis. And, maybe the person advising you for blackout periods is a little too conservative and, maybe you need a new advisor in that area.

Jack Cronin

I think we would generally we'd be cautious on the conservative side.

Tim Call

--And if you're not expecting--

Jack Cronin

Go ahead.

Tim Call

If you're not expecting any near-term acquisitions, should the Board authorize a larger share buyback authorization. If you have over you know, 20 million cash, it's 22% of your stock market capitalization. If the stock is such a good deal, hopefully, the Board will consider increasing the authorization. I understand you want to get through this first one but hopefully, that can accelerate now.

Jack Cronin

I mean, the Board could once this one has been completed, the Board has the ability to immediately do another buyback. So it's not like, you know, once this is over, all bets are off. We have the ability to be flexible and do more if the Board so desires. But again, the other thing Tim, the other thing is our volume is relatively low.

So that's another headwind where, you know, we'd like to buy, but we're limited on, uh, based on our volume, the--the number of shares that we can buy. But, you know, again, I think the Board management is committed to take advantage of our stock position and buy back shares.

Tim Call

Terrific. And, thanks for your hard work and great to see the indications that business can improve next year.

Jack Cronin

Thanks, Tim.

Vivek Gupta

Thanks, Tim.

Operator

As a reminder, if you would like to ask a question, press "*", "1" on your telephone keypad. Our next question comes from the line of Lisa Thompson with Zacks Investment Research. Please proceed with your question.

Lisa Thompson

Good morning.

Vivek Gupta

Hey.

Lisa Thompson

Again, you people had a very busy fourth quarter.

Vivek Gupta

Yes, supposed to, indeed, Lisa.

Lisa Thompson

So, could you just kind of go through the events that led to the CEO resigning and then you hiring the consultants and exactly what the consultants are hired for? Are the two related or completely unrelated?

Vivek Gupta

They are unrelated, Lisa. So let me pick the first one, first. The Board of Directors and Michael had a series of discussions around the goals and strategies for Mastech, InfoTrellis. And, once it was clear that our long-term goals would not align, Michael felt it was best to resign, and the Board accepted Michael's resignation. So that is what led to Michael's exit.

As regards, the consultant, Primentor coming in, Primentor has deep experience across the global technology and business services industry and, its principles have helped create business value and drive transformational change for a number of large-scale organizations in our industry.

And the Board felt it would be really good to engage Primentor in order to positively impact the organization and provide strategic direction towards significantly improving our business performance and growth. And that's what led to us engaging Primentor to help Mastech Digital.

Lisa Thompson

Okay. So as I read through the documents, I first thought the kind of turnaround improvement guys, and then I got a little concerned that maybe they were hired to sell the company. Can you discuss that?

Vivek Gupta

Well, I can say that, emphatically, that we have not engaged Primentor for selling the company. They have been engaged in order to make that positive impact I spoke about to the organization and provide the strategic direction that would help us with improved performance and growth. That is really the main objective.

Lisa Thompson

Okay. Just checking. Can you talk a little bit about how business is going? Are you feeling these different reactions in different verticals of your base? And I always worry about CGI when I read about banks. Can you talk a little?

Vivek Gupta

So yes, as I said in my prepared remarks that there are some signs that we are seeing that the business is picking up. Last time when we spoke, a quarter ago, we had just completed October and seeing some positive signs. Now, if we exclude December, we've had two quarters--two months of positive activity and also in January, which, just ended, we had a positive net growth.

So three out of four months have been positive. And I think that's really encouraging. It's a positive indicator. And, again, three months don't really guarantee what the rest of the year will look like it's a positive sign direct volume is better than what it was a few months ago.

So, that's the positive side on the IT Staffing side. And on the Data and Analytics side, as we mentioned, we managed to sign a pretty large quantum of bookings adding up to \$19 million. Uh, I must caution everyone that a lot of the business in that is actually multiyear annuity deals. So it doesn't mean that immediately we'll see a jump start as a result of that.

What it does mean is that we've got the right kind of business where we are seeing customers' commitment for multiple years. So there is going to be a steady stream of revenue coming in and just the kind of business we would like to have more and more of.

So, again, for customers to open up their wallets and sign multiyear deals is a very positive sign. But these are only sort of early indicators. We have to now make sure that we maximize what we can from this to the fullest and make sure that 2024 turns out to be a better year.

Lisa Thompson

Okay. So given those signs, do you feel that Q1 will have higher revenues in Q4, then?

Vivek Gupta

Well, yes, I think it should be sequentially higher. Don't want to say how much better it would be. But, yes, it should be.

Lisa Thompson

Alright, that's great. Okay, I think that's all my questions. Thank you so much.

Vivek Gupta

Thank you, Lisa.

Operator

Our next question comes from the line of Ross Davidson with Benetton Capital. Please proceed with your question.

Ross Davidson

Hi, Jack. Hi, Vivek. Thanks for taking the question. Actually, both questions I wanted to ask were asked, already. But the third one I want to ask is just around the goals of InfoTrellis. You alluded to that was sort of the cause of Michael deciding to resign. I'm curious if you could articulate, what is the Board's and your goal for InfoTrellis, you know, the sort of that direction that led to that separation.

Vivek Gupta

I think we will start getting into the weeds a little bit over there. But I think it's suffice to say that what the Board expects or wants for the organization is to take it in a direction where it can scale very quickly to a much larger size and become a bigger portion of the Mastech Digital portfolio.

And, when we're looking at the goals and strategies that were being discussed, there was clearly some misalignment between the two. And we didn't see a clear path in being able to get to where we were hoping to. And it just led to that conclusion where Michael felt that it was best to resign.

Ross Davidson

Would it be fair to say that maybe the goals weren't that far apart? Like, I mean, the idea of growing it quickly, I'm sure Michael didn't want to shrink it, you know, maybe the growth rates are different and more about just the approach to how to accomplish that. I'm sorry, what was the approach was the approach different?

Vivek Gupta

So I would say, yes, it's a mix of both. It's the goals, the strategies and the means to get there. And now that we have Primentor on board, we are actually looking forward to getting some, useful strategic direction about what we could take, what the industry is doing, what our peers are doing and find the right actionable initiatives, which will take us there.

Ross Davidson

Okay, makes sense. Thanks for adding color.

Operator

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

Marc Riddick

Hey, good morning, everyone.

Vivek Gupta

Hey, Marc.

Marc Riddick

So, I was wondering if you could give us an update on the engineering staffing services, you know, the launch from last year and maybe what we're seeing there thus far and maybe some early indication, early reads of what you're getting there.

Vivek Gupta

Good question, Marc. That's one of the initiatives that we are really giving a lot of emphasis on, focus and investment, as well. And, we've seen some virtually quarter-on-quarter, or rather even month-on-month increase in the head count for engineering staffing services. It hasn't quite become, a very, what should I--what's the word I'm looking for? It's not very large growth has not yet happened. But the conversations that we've initiated with our customers are showing you good traction.

So essentially, Marc, there are three groups or, you know, buckets in which we have our opportunities. The first bucket contains customers who are already doing a bit of engineering staffing with us. So the question over there is how do we wrap that up to make it much more than what we have done so far. The second bucket is customers where we are doing IT staffing right now, but we haven't yet done engineering staffing services, getting our message across and making sure that we get invited to the party for any engineering staffing needs that they may have. And the third one, of course, is to go and look for new logos, new customers who have never worked with us in the past or even IT staffing and focus on engineering staffing services there.

So right now, our sales engine is focusing on all the three buckets and making sure our message is understood, heard by other customers. And, we hope to see, as a result of that, the requirement volume will start picking up as the year unfolds, and we should be able to get to the goals that we have set for ourselves.

Marc Riddick

Okay, thank you for that. And I was wondering in a way maybe kind of shifting to the to the new order wins in the 19 million. And I was wondering if you could talk a little bit about maybe, without getting too specific, because you did talk about the frames and the multiyear and the like. I was wondering if there's any particular catalyst or two that you would point to that led to those opportunities that could continue to have legs in the coming months.

Vivek Gupta

Marc, it's basically, you know, the kind of relationship that we've been able to establish with our client accounts, customer accounts, The stellar delivery that our team has had the new offerings that under, you know, data modernization that we have come out with.

And rolling all of that into seeing the customers' needs for the next couple of years, it's been a mix of all of that, which has led to the customers feeling comfortable enough to sign up rather than doing quarter-after-quarter, you know, individual extensions of deals or signing up for new contracts. They felt comfortable enough to commit to a multiyear deals where we know there is a steady stream of revenue, which will keep coming quarter-on-quarter. So, I can't really put a finger on any one of them; it's actually all of them.

Jack Cronin

Yes, Marc--

Marc Riddick

That's helpful. I'm sorry, go ahead.

Jack Cronin

Yes, and you know, as far as major clients, it was a combination of orders from existing clients. And like Vivek said, you know, not a short-term order, you know, six months to a year, it was longer-term orders. And then the other thing that was encouraging is there were some major bookings from new clients and you know, that's very encouraging.

Marc Riddick

Great. And then the last one for me. I was wondering if you could maybe give us an update on maybe what you're seeing as far as overall bill rates and then you know what we would you know if there's much in the way of pushback or as far as rate increases and the like, maybe just sort of give us a little bit on, the pricing environment of what you're seeing, currently. Thank you.

Vivek Gupta

So Marc, it's interesting, and it's a very good question that you asked. In 2023, we did see constant price pressures as customers were trying to come down on the projects and also the costs on each project. And so, we did lose head count as a result of that, but there were pricing pressures all the time. But having said that, we've also been able to increase our bill rates over the year. So, which actually says a lot about the quality of relationships that we have, the quality of deliveries that we have made.

So, that pricing pressure would continue, I would think, even in this year, 2024. But, you know, the higher value services that we are providing, we are able to, in some ways, compensate for that and still be able to maintain and if not increase the bill rates.

Marc Riddick

Thank you very much. No,
that's exactly where I was going. Thank you very much.

Vivek Gupta

Thank you, Marc.

Operator

A final reminder, if you would like to ask a question, press “*”, “1” on your telephone keypad. One moment, please while we re-poll for any additional questions.

Thank you. Mr. Gupta, it appears we have no further questions at this time. I would like to turn the floor back over to you for closing comment--comments.

Vivek Gupta

Thank you, Operator. So if there are no further questions, I would like to thank you for joining our call today, and we look forward to sharing our first quarter 2024 results with you in early May. Thank you very much.

Operator

Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.