



# mastech

**MASTECH**

**Q2 2016 Earnings Call**

**July 27, 2016**

**Confirmation #13642047**

**Operator:** Greetings and welcome to Mastech's Q2 2016 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 Holdings, Inc. Thank you, Ms. Ford Lacey. You may begin.

**Ms. Jennifer Ford Lacey:** Thank you, operator, and welcome to Mastech's Second Quarter 2016 Conference Call. If you have not yet received a copy of our earnings announcement, it can be obtained from our website at [www.mastech.com](http://www.mastech.com).

With me on the call today are Vivek Gupta, Mastech'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 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 listed in the Company's 2015 Annual Report on Form 10-K, filed with the Securities and Exchange Commission and available on their website at [www.sec.gov](http://www.sec.gov).

Additionally, management has elected to provide 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.mastech.com](http://www.mastech.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 second quarter 2016 results.

**Mr. Jack Cronin:** Thanks, Jenna, and good morning, all.

**Mr. Jack Cronin:** First off, I'd like to remind everyone that our June 2015 acquisition of Hudson IT is reflected in our financial results effective as of the acquisition date, and accordingly, has benefited our year-over-year comparables.

With that said, revenues for the second quarter of 2016 totalled \$33.6 million compared to \$29.3 million in the second quarter of 2015. This revenue performance represents a 15 percent year-over-year increase and a 6 percent sequential increase over first quarter 2016 revenue results.

Activity levels during the quarter were up from the previous quarter, and our new assignment win ratio improved. Thus, we were able to expand our billable consultant base by 62 consultants to a total of 916 consultants at quarter-end. This was our strongest quarterly increase in billable consultants since second quarter of 2011.

Gross profit for the second quarter of 2016 totalled \$6.9 million compared to \$5.5 million during the same period last year.

Our gross margins for the second quarter of 2016 were 20.5 percent of revenues and represented 170 basis point increase compared to the corresponding period of 2015. This year-over-year gross margin improvement was due to an increase in our retail client base, which generally carry higher gross margins in our wholesale channel and higher gross margins on new starts in general over the last several quarters.

SG&A expense were \$5.2 million in the second quarter of 2016 compared to \$4.9 million in the second quarter of 2015. It should be noted that second quarter 2015 SG&A expenses included \$549,000 of transaction expenses associated with the Hudson IT acquisition. Adjusting for these transaction costs, our year-over-year increase in SG&A expenses of approximately \$800,000 was reflective of the Hudson IT operations, which were included in second quarter 2016 for the entire period but only in last year's Q2 numbers for 15 days - i.e., concurrent with the acquisition date.

GAAP net income for second quarter 2016 was \$945,000 or 21 cents per diluted share compared to \$382,000 or 9 cents per diluted share in the second quarter of 2015.

Non-GAAP net income for the second quarter of 2016 was \$1.1 million or 25 cents per diluted share compared to \$801,000 or 18 cents per diluted share in the corresponding quarter of 2015.

Second quarter SG&A expense items not included in non-GAAP financial measures net of income tax benefits were, 1), the amortization of acquired intangible assets, 2), stock based

compensation, and 3), 2015's acquisition transaction expenses and are detailed in our second quarter earnings release, which is available on our website at [www.mastech.com](http://www.mastech.com).

Briefly addressing our financial position at June 30, 2016, we had \$13 million of outstanding bank debt net of cash balances on hand. Our borrowing availability at June 30, 2016 was approximately \$10.7 million under our existing revolving credit line. During the quarter, we were able to reduce our outstanding bank debt by approximately \$1.7 million.

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

**Mr. Vivek Gupta:** Thank you, Jack, and good morning, all.

During my first earnings call with Mastech in April, I shared with you my vision and objectives for the Company, which were two-fold – 1), to reenergize our existing business, and 2), to look at ways to expand our offerings into adjacencies. In our efforts to expand beyond IT staffing, I also wanted to explore areas that will allow Mastech to participate in the digital transformation of our customers' systems and business processes. I'm excited to say that we have made good progress on both these fronts during the second quarter of 2016.

First, let me talk about reenergizing. Clearly, our second quarter financial performance reflects our reenergizing efforts. We organically grew our billable consultant base by 62, which is a 7 percent increase in the quarter. Our gross margins improved nicely, both on a year-over-year basis as well as on a sequential basis when compared to the first quarter of 2016; and our bottom-line results showed a material improvement both on a GAAP and non-GAAP basis as we cut operating expenses in areas in which we were not getting the desired payback while investing in training our leadership and improving our operational effectiveness.

During this quarter, we aligned our US sales organization under new leadership, significantly strengthened our marketing capabilities and tweaked a number of our core processes into being more responsive to our clients' and consultants' needs. We will continue this journey of enhancing efficiencies by continuing to assess changes in organizational alignment, internal processes and people during the second half of 2016.

Now regarding the objective of expanding beyond staffing, we have made progress in several areas. First, we have revamped our go-to-market approach in our Salesforce.com practice and have also expanded our capabilities beyond staffing. Today, our Salesforce.com practice has the ability to deliver both staffing and project services as a solutions provider.

Secondly, we have started a new practice around SAP HANA. This is an exciting area of future growth and our first foray into data analytics. In this true transformation technology space, that truly excites me. I will expect to talk further about these initiatives as things progress in the second half of 2016 and beyond.

As I stated on our last earnings call, my ultimate vision for Mastech is to transform it from a pure IT staffing company to a much broader digital technology solutions company. These solutions will include both staffing as it has some turnkey projects and managed services. Towards that end, the revamped Salesforce.com practice and the newly established SAP HANA practice are our first steps in our transformation journey. We have also primarily restructured our offshore recruitment organization to better align with digital technologies. Specifically, we now have a dedicated team which focuses exclusively on securing experienced consultants in these advanced digital technologies. While Mastech's transformation into a broader digital technology solutions company will not happen overnight, we will continue to review and adjust how we conduct our business to better facilitate this ultimate objective.

In summary, I'm pleased with our second quarter accomplishments, not only in terms of financial results but also in terms of strengthening our capabilities and positioning ourselves for the future as a digital technology solutions company.



I will now open the session up 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. A confirmation tone will indicate 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 keys. One moment please while we poll for questions.

Our first question comes from the line of David Polonitza with AB Value Management. Please go ahead.

**Mr. David Polonitza:** Hi Guys. Good morning. Good quarter. Congratulations. I'm hoping you can go a little more in depth on why we had this level of success for the quarter, and was it due to gaining new clients or servicing existing clients better? Any clarity on that would be useful. Thanks.

**Mr. Vivek Gupta:** Thanks, Dave. Nice to hear your voice. There are a number of reasons why this quarter turned out to be the way it is. I think a lot of the credit goes to the team. I came on board toward the end of February and immediately after coming on board, we started looking at ways to reenergize the system and the business and that involved looking at all aspects.

We looked at our sales organization, and felt we needed to unify the various units that we had some which have come to us from the Hudson acquisition, some which were legacy Mastech units. We integrated them under one leadership and we broke a lot of internal barriers and looked at ways of maximizing benefits from the national accounts.

We focused a lot on account management and to fill all the positions which were lying open. We also looked at our delivery capability, which as you know, we have a large center in India where we have almost 125 recruiters and we looked at ways of energizing that capability. We felt that it will be good to change the structure from a dedicated recruiter model to a technology practice based recruitment model.

What that means is that the 125 recruiters that I'm talking about, they were allocated to individual sales channels on a dedicated basis. We've moved away from that, and now we have

these teams organized on technologies. The recruiters are dealing with the similar technologies, the same technologies day in, day out, and they're getting better and faster at it. As a result, our speed of response improved, and we were able to service the June assignments much better.

We also looked at the kind of Client Connect and the Consultant Connect that we have, and we have been working on it, and of course, that's something which we will continue to work on.

It's just tightening a lot of our processes and looking at ways of, breaking barriers, as I call them in quotes, and it really involves getting the entire engine humming in a better alignment, and that has resulted in this kind of headcount growth. Does that answer your question?

**Mr. David Polonitza:** Yes, no, absolutely. I appreciate the further information.

I do have one other question, and I'll go back into the queue here. With the digital transformation of the company, what's your go to market strategy in terms of the value proposition that Mastech has versus competitors? And are you able to leverage kind of the history of the company or existing client base on the staffing side to help potentially grow that business?

**Mr. Vivek Gupta:** Dave, our plan is to expand our offerings. What that essentially means is that we should be able to go to the same customers to whom we have been successfully providing IT staffing services and be in a position to talk to the same customers as a solutions provider, we'll still be servicing the staffing requirements of those customers, but we will be able to talk the language subject matter experts and practice heads understand what the real problems are and to be able to service those requirements in whichever way is necessary. It could be staffing, it could be actually doing the projects fully where we own the deliverable and it could be managed services. It's really not opening up a completely different front and having a different sales force coming in. It's really leveraging the current account relationships that we have and a strong practice and delivery and technology capability subject matter expert who can support the sales people in positioning us as more of a solutions provider. This should help us not only go on the transformation--or the digital transformation services side. It is already showing results in improving our positioning on the staffing side. Does that answer your question, Dave?

**Mr. David Polonitza:** Yes, Vivek. I appreciate that and keep up the good work. Thank you very much.

**Mr. Vivek Gupta:** Thanks, Dave.

**Operator:** Ladies and gentlemen, as a reminder, if you would like to ask a question in today's call, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. One moment please while we repoll for questions.

Our question and answer session has concluded, so I would like to turn it back to management for closing remarks.

**Mr. Vivek Gupta:** Thank you.

If there are no further questions, I would like to thank you for joining our call today, and we look forward to sharing our third quarter 2016 results with you in late October. Thank you.

**Operator:** This concludes today's conference. Thank you for your participation. You may disconnect your lines at this time.