Transcript of TechPrecision
Fourth Quarter 2019 Earnings Call
June 27, 2019

Participants

Brett Maas - Hayden Investor Relations
Alexander Shen - Chief Executive Officer
Thomas Sammons - Chief Financial Officer

Analysts

Howard Brous - Wellington Shields
Ross Taylor - ARS Investment
Mark Gomes - Pipeline Data
Richard Greulich - REG Capital Advisors

Presentation

Operator
Good day, ladies and gentlemen. And welcome to the TechPrecision Fourth Quarter 2019 Earnings Call. All lines have been placed in listen-only mode and there will be a question and answer session following the presentation. [Operator instructions].

At this time, it's my pleasure to turn the floor over to Mr. Brett Maas of Hayden IR. Sir, the floor is yours.

Brett Maas - Hayden Investor Relations
Thank you. On the call today is Alex Shen, Chief Executive Officer; Tom Sammons, Chief Financial Officer. The call is also being simulcast on the company's website, techprecision.com. Before we begin, I'd like to remind our listeners that management's remarks may contain forward-looking statements, which are subject to risks and uncertainties, and management may make additional forward-looking statements in response to your questions.

Therefore, the company claims the protection of the Safe Harbor for forward-looking statements as contained in the Private Securities Litigation Reform Act of 1995. Actual results may differ from those discussed today, and therefore, we refer you to a more detailed discussion of risks and uncertainties in the company's financial filings with the SEC.

In addition, projections as to the company's future performance represent management's estimates as of today, June 27, 2019. TechPrecision assumes no obligation to revise or update these forward-looking statements.

With that out of the way, I'd like to turn the call over to Alex Shen, Chief Executive Officer, to provide opening remarks. Alex?

Alex Shen - Chief Executive Officer
Thank you, Brett. Good day to everyone and thank you for joining us. Our results for the fourth quarter and full year of fiscal 2019 were highlighted by improved gross margins. Net income for the full year was $1.1 million compared to a net loss of $266,000 in fiscal year 2018. Net sales were $16.7 million for fiscal year 2019 and gross margin was 27.4% for fiscal 2019.

Our improving results and higher overhead absorption were a direct result of effective planning and execution, enabled by projects with longer build cycles, timely customer approvals and timely customer releases.

At March 31, 2019, we had a backlog of orders totaling approximately $12.6 million compared to approximately $14 million at March 31, 2018. Backlog at May 31, 2019 was $13.5 million. As a reminder for everyone, at the beginning of fiscal year 2019, we adopted the new revenue recognition guidance issued by the Financial Accounting Standards Board. Under this guidance, we adopted a new revenue recognition model that allows us to recognize revenue over the project duration for most of our customer contracts. Prior period amounts have not been restated and are reported in accordance with the accounting standards in effect for those periods.

Now, I'd like to turn the call over to Tom Sammons to tell us more about our fourth quarter and 12 month year-to-date financial results. Tom?

Thomas Sammons - Chief Financial Officer
Thank you, Alex. Net sales were $4.7 million for the fourth quarter of both fiscal 2019 and 2018. Net sales in our nuclear market increased by $1.1 million on higher customer demand. However, this increase was almost entirely offset by a decline in net sales in our defense and industrial markets in the fourth quarter of fiscal 2019.

Gross profit was $1.5 million in the fourth quarter, an increase of approximately $1.1 million, when compared to the same quarter of fiscal 2018. The increase can be attributed primarily to higher margin product mix and higher overhead absorption due to increased project activity.

Our net income was $538,000 or $0.02 per share, basic and fully diluted for the fourth quarter of 2019 compared with a net loss of $367,000 or $0.01 per share basic and fully diluted for the fourth quarter of fiscal 2018. For fiscal year 2019, our net sales were $16.7 million or $2 million lower when compared to fiscal 2018. Net sales in our defense market decreased by $1.7 million and net sales in our precision industrial market decreased by $0.4 million. Our net sales in our energy market increased by $0.2 million.

Gross profit was $4.6 million or 15% higher when compared to fiscal 2018. Our gross profit and margin benefited from an increase in project activity and higher overhead absorption rates. Income from operations was $1.8 million, a $0.9 million or 90% increase when compared to the same period a year ago. Fiscal 2018 results were dampened by lower overhead absorption, shipments of certain low-margin products and higher selling, general and administrative expense.

In fiscal 2019, we reported tax expense of $423,000. Fiscal 2018 tax expense was higher and included $700,000 of non-cash tax expense, result of re-measured net deferred tax assets to reflect the new 21% US Federal statutory tax rate as provided under the 2017 Tax Cuts and Jobs Act. Our tax expense was primarily a non-cash expense as we continued to utilize our deferred tax assets to offset any tax liability. The company does not expect to make any significant tax payments for the remainder of the 2019 calendar year.

Net income was $1.1 million or $0.04 per share basic and fully diluted for the fiscal year 2019 as compared to a net loss for fiscal year 2018 of $266,000 or $0.01 per share basic and fully diluted. Fiscal Year 2019 EPS is based on an average weighted share count of approximately 28.9 million and 30.3 million per basic and fully diluted shares, respectively.

Turning to the balance sheet, we finished the quarter with $2 million in cash at March 31, 2019. Our working capital was $6.3 million and $4.9 million at March 31, 2019 and 2018, respectively. Cash flow provided by operations was approximately $0.5 million in fiscal year 2019. We used approximately $446,000 of cash to purchase new machinery and equipment that was placed in service during fiscal 2019, and used $752,000 of cash to repay principal under our long-term debt agreements.

With that, I will now turn the call back over to Alex. Alex?

Alex Shen - Chief Executive Officer
Tom, thank you. TechPrecision is proud and honored to serve the United States defense industry, specifically, naval submarine manufacturing through its Ranor subsidiary. We continue to see meaningful opportunities in our defense sector, primarily in the nuclear submarine business for the next 12 months and beyond.

The opportunities we are actively pursuing for the next 24 months are well over 5 times our revenue, somewhere in the $100 million range give or take. We expect to operate at or above current levels during the next fiscal year. I would now like to open up the call for Q&A.

Operator
Thank you. [Operator instructions]. We'll take our first question from Howard Brous with Wellington Shields.

Q: Alex, Tom, congratulations on a very, very good fourth quarter. You just addressed an opportunity of $100 million. Based on the most recent Department of Defense US Navy requirements, they're expected to build three Virginia-class submarines and one Columbia-class submarine starting in fiscal year 2020. What percentage of that $100 million opportunity does this present to you?

Alex Shen - Chief Executive Officer
I don't have a good feel for what percentage this $100 million opportunity that Ranor is actively pursuing matches up against what you just described.

Q: Thank you. That's all I have.

Alex Shen - Chief Executive Officer
I would say that it's a very small percentage compared to what you just described.

Q: Could you explain what you just said a little bit clearer, please?

Alex Shen - Chief Executive Officer
So, the opportunities we are actively pursuing for the next 24 months, right? That's what we're talking about somewhere in the $100 million range.

Q: Correct.

Alex Shen - Chief Executive Officer
Right. So, what you're talking about, I think, was talking about just Virginia-class only, and nothing about Columbia.

Q: Virginia and Columbia, yes.

Alex Shen - Chief Executive Officer
Three Virginia, right, from two Virginia, right? That cadence.

Q: Right.

Alex Shen - Chief Executive Officer
Okay. And then there's Columbia-class. So what I'm saying is what we pursue is a miniscule part really in comparison to another giant submarine being added to the mix as in the third Virginia-class. That was my illustration.

Q: But as a percentage of the $100 million for you over the next 24 months, what does that represent? Is that a miniscule piece of $100 million, or rather a larger part of it?

Alex Shen - Chief Executive Officer
I don't have a good [overlapping voices] in terms how it correlates to the two.

Operator
[Operator instructions]. We'll go next to Ross Taylor with ARS [ph] Investment.

Q: Alex, what I hear you saying without you saying it is that we have reached the tipping point. I think people have for a long time been waiting for the Navy to finally move forward with the Block V Virginia, to move forward with the Columbia-class. And what I'm actually hearing you saying is that over the next two years that you would expect to produce two times to three times the amount of revenue that you've been producing over the prior 24 months. And therefore, that we're at a tipping point and that would seem to fit with the aggressive way in which Electric Boat and Newport News and the like are hiring and trying to build up workforces, which take multiyear training periods and the like.

So am I right that you actually are probably inside screaming happy that we've finally gotten to this point where we should start to see the hard work you guys have put in the last couple of years pay off with meaningfully improving top line?

Alex Shen - Chief Executive Officer
I think you had a very, very long question in there.

Q: I learned that you can have very short answers, Alex.

Alex Shen - Chief Executive Officer
Yes.

Q: So that's it. I wrote the question, so you could answer it. Yes or no? Okay. And so the follow-up to that would be, if that is the case, should we be surprised that you would not be able to produce historic strong business flow operating margins? I don't want you to comment on what they are, because I used to work for a defense contractor and I know you never want to talk about what your margins are. But that we should be able to produce historic type margins going forward?

Alex Shen - Chief Executive Officer
I think this is the point where you know I'm not going to be able to answer because of our defense clients and our clients don't want me to talk about, this is the what I—

Q: I just don’t want you to say no, Alex. You can simply say no comment.

Alex Shen - Chief Executive Officer
Well, I don’t want to no comment it either. So I think it’s really, our clients don’t want me to talk about this. This is that’s where we're at.

Q: And I appreciate that and I don't think you need to. It seems to me that a bouncy question you have $2 million in cash, what's the net debt at this point in time?

Thomas Sammons - Chief Financial Officer
The debt is $4.3 million at the end of March.

Q: The net debt or the gross debt is $4.3 million?

Thomas Sammons - Chief Financial Officer
Total debt.

Q: Total debt, okay. So basically at about $2.3 million net debt and one should expect it going forward, if my read on what's about to happen over the next two years is true, we should move to where we have free cash flow generation that gives you the ability to determine how you want to redeploy that capital for your shareholders, your company [ph] is on record saying you wanted to explore all alternatives to revise value for shareholders. So I would expect that the next two years should be a pretty exciting time for the company overall to take you from you were struggling to survive to where you actually are really going to start to thrive and prosper?

Alex Shen - Chief Executive Officer
Well, I always think it's an exciting time especially since we had a solid year this year. I've been pretty bullish and very focused on really pursuing what we're good at, making big clunky precision machine parts that are very complicated weldments, fabricated weldments that need precision machining. And to really see this come through with true opportunities that we're pursuing over the next 24 months, yes I'm excited, absolutely.

Q: And then my last question is, the first two boats of the Virginia Block V carry a smaller missile payload, the third boat added that shows up in the Navy's documents and the like, that actually carries a higher missile payload, correct?

Alex Shen - Chief Executive Officer
I'm sorry, Ross, there is some—I won't be able to comment on that at this time. My clients don't want me to comment on that one specifically, excuse me.

Q: Okay. Thank you very much. I agree [ph]. Thanks very much.

Alex Shen - Chief Executive Officer
Ross, I do want to talk about that a little bit on what I can say is that as previously stated, the first boat of the ten boat Block V Virginia-class would not have the payload module with additional Tomahawk missile capability. From the second one on the previous plan was to have the additional payload capacity added. I can tell you that was in the previously stated plans.

Q: Correct. Cool. And so we will assume the Navy is moving forward and obviously the need for submarines has grown substantially. I think that it's our belief organizationally and from the people I talk to in the intelligence community that America is falling behind some of our chief global rivals in advanced conventional military technology. And so the sooner the Navy gets to work on its new Block V boats than the new Columbia-class the better for all of us not just TPS shareholders.

Alex Shen - Chief Executive Officer
Absolutely.

Q: Okay. Thank you very much, and congratulations on what you've accomplished in setting up for what you I think are about to accomplish in the next 12 and 24 months.

Alex Shen - Chief Executive Officer
Ross, thank you always for your support.

Q: You're welcome. Thank you, sir.

Alex Shen - Chief Executive Officer
Yes sir.

Operator
[Operator instructions]. We'll go next to Mark Gomes with Pipeline Data.

Q: Thanks for taking the call. Congrats on the progress. Given your statement was that going forward you expect the quarters ahead to be at least at these levels if not above. Does that apply also to your operating metrics? And what kind of commentary can you provide with regard to what kind of operating leverage we might see, particularly on the SG&A line going forward?

Alex Shen - Chief Executive Officer
Tom, I'm going to ask you to field this question first. And I will attempt to provide more color. Tom?

Thomas Sammons - Chief Financial Officer
Can you repeat that question with regard to SG&A?

Q: Just looking for some color commentary on what kind of operating leverage you guys might see as we move forward? So, what kind of need there might be—I know your capacities—just to reiterate your capacity and as revenue ramps up assuming that it does, how much gross margin can flow down to the bottom line?

Alex Shen - Chief Executive Officer
We're not going to be able to answer that, go ahead.

Thomas Sammons - Chief Financial Officer
For competitive reasons, we prefer not to answer that question.

Q: Okay. So going back to my first question, so when you provided the statements that forward quarters will be at least as good as this one, does that also pertain to your operating metrics? Or were you referring to revenue? I'm just looking for clarification on the statement.

Alex Shen - Chief Executive Officer
I'd say it refers to just the overall performance for the year.

Q: Okay, thank you.

Operator
And we'll take our next question from Richard Greulich with REG Capital Advisors.

Q: Thank you. Recently this month, the Congressional Research Service quoted a GAO report from May indicating that some of the problems with the vendor quality issues on the payload module has caused a several month delay and that they were seeking to catch-up with that by accelerating a second vendor manufacturing the tubes. And then they also stated that this approach may increase program costs. Two questions, have you seen any effect of that attempt on their part to accelerate the second vendor? And then secondly, could you elucidate on why that approach would increase program costs?

Alex Shen - Chief Executive Officer
Rich, this is Alex. I have to tell you that 100% every single one of my clients do not want me to talk about this. I'm sorry.

Q: Okay. Alright. But let me ask it one other way. There's nothing that you're aware of that would contradict those statements made by the GAO?

Alex Shen - Chief Executive Officer
Again, I have to repeat my line. I'm hardlined on this. It's not me. Please don't take it the wrong way. But my clients, every single one of my clients, without exception, every single human in there does not want me to talk about this whatsoever.

Q: Okay. I came in the call a minute or two late. Did you indicate what the backlog was at the end of the fiscal year?

Alex Shen - Chief Executive Officer
I did.

Q: Oh, what was that number?

Alex Shen - Chief Executive Officer
Hold on one second. $12.6 million at March, 31, 2019, we had a backlog of about $12.6 million.

Q: Okay. Thank you very much.

Alex Shen - Chief Executive Officer
Backlog at May 31, 2019 was $13.5 million. Those were the statements that I made, Rich.

Operator
And Mr. Shen, there appears to be no further questions at this time. I'll turn the call back over to you for any closing remarks.

Alex Shen - Chief Executive Officer
Thank you, everyone, for your attendance. Have a good afternoon.