

**Transcript of
TechPrecision Corp
First Quarter 2020 Earnings Call
August 13, 2019**

Participants

Jeff Stanlis – Partner and Vice President, Communications-Hayden IR
Alex Shen – Chief Executive Officer
Tom Sammons – Chief Financial Officer

Analysts

Ross Taylor – ARS Investment
Aaron Warwick – US Capital
Mark Gomes – Pipeline Data
Howard Brous – Wellington Shields
Richard Greulich – REG Capital Advisors

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the TechPrecision First Quarter 2020 Earnings Call. All lines have been placed on a listen-only mode. [Operator instructions].

At this time, it is my pleasure to turn the floor over to your host, Jeff Stanlis with Hayden IR. The floor is yours.

Jeff Stanlis – Partner and Vice President, Communications-Hayden IR

Thank you. On the call today is Alex Shen, Chief Executive Officer; and Tom Sammons, Chief Financial Officer. The call is also being simulcast on the company's webcast at www.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 represents management's estimates as of today, August 13, 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, go ahead.

Alex Shen – Chief Executive Officer

Thank you, Jeff. Good day to everyone, and thank you for joining us. Our results for the first quarter of fiscal year 2020 were highlighted by net sales of \$4.3 million and net income of \$221,000. Net income was 34% higher for the first quarter of fiscal year 2020 when compared to net income for the first quarter of fiscal year 2019. We improved liquidity by adding \$1.5 million to our available cash balance in the first quarter of this fiscal year. At

June 30, 2019, we had a backlog of orders totaling approximately \$14 million compared to approximately \$12.6 million at March 31, 2019.

Now I'd like to turn the call over to Tom Sammons to tell us more about our first quarter financial results. Tom?

Tom Sammons – Chief Financial Officer

Thank you, Alex. Net sales were \$4.3 million for the first quarter of fiscal 2020 compared to \$4.1 million in the first quarter of fiscal 2019. Our backlog remains strong, as new orders for components continue to flow down from our prime defense contractors. Cost of sales for the quarter ended June 30, 2019 was \$3.2 million compared to \$3.0 million for the same quarterly period a year ago, resulting in a gross margin of 25.6% for the current quarter. Our margin was negatively impacted by higher unabsorbed factory overhead and increased costs on certain new projects.

Selling, general and administrative increased by \$11,000, primarily due to an increase in professional fees. Interest expense and debt cost amortization was lower for the quarter ended June 30, 2019, and will continue to decrease as we amortize debt principal to maturity.

Income tax expense continues to be a non-cash item, as we are able to utilize our federal net operating loss carryforward to offset taxable income. The company does not expect to make any significant tax payments for the remainder of fiscal 2020.

Net income for the quarter ended June 30, 2019 was \$221,000 compared to \$164,000 in the same quarter a year ago, an increase of 34%. Earnings were \$0.01 per share basic, fully diluted for both quarterly periods.

Moving to the balance sheet. At June 30, 2019 we had \$3.5 million in cash and working capital of \$6.6 million. Cash provided by operating activities was \$1.7 million for the three months ended June 30, 2019 due to favorable timing of shipments and collections during the quarter. Net debt at the end of the first quarter of fiscal 2020 was \$567,000.

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

Alex Shen – Chief Executive Officer

Tom, thank you. TechPrecision remains 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.

I would now like to open up the call for Q&A.

Operator

Thank you. The floor is now open for questions. [Operator instructions]. And our first question comes from Ross Taylor with ARS Investment. Go ahead, Ross.

Q: Thank you. Alex, it appears we're stuck in a waiting for Godot situation here, in that the Navy clearly has a need, and a massively growing need for submarines, but they are not really pushing through, for a variety of reasons, the build of those boats. So can you tell us, has anything changed from your outlook last quarter?

Alex Shen – Chief Executive Officer

So I see that the question is, has anything changed for my outlook since last quarter?

Q: Last quarter, yes. You were very bullish on the last call about the prospects the company had looking out over the next two years. Has anything about that changed?

Alex Shen – Chief Executive Officer

I don't see how our position has changed since last quarter as far as what I see as meaningful opportunities in the defense sector.

Q: Okay. And then can you comment on what level of – I don't know how exactly you would put it, but effectively, I assume that you have a workforce and a factory capability that is sized more for what you expect to be coming than what is currently there. Is that correct?

Alex Shen – Chief Executive Officer

I'm taking my time answering the question, Ross, because there's a portion of competitive nature that causes me to be careful in answering. I hope you'll forgive me.

Q: Okay. No, I will. And perhaps you can simply say, would I be wrong if I assumed the basic premise of my question that you can't answer before?

Alex Shen – Chief Executive Officer

I think the basic question is, do we have more capacity than the business that we're flowing through now?

Q: Yes.

Alex Shen – Chief Executive Officer

If I can rephrase the question in that way, Ranor and TechPrecision has more capacity than the business flowing through now.

Q: Okay. And then will you comment on how you see the competitive environment? It appears that some players that might have been competitors of yours in a variety of areas have run into difficulties providing the proper equipment and the like, or providing things of the right standard or in a timeliness fashion, and in fact some of that might be why the Navy is behind on its build of boats.

Alex Shen – Chief Executive Officer

I can tell you that what you commented on just now is something that I am not going to be able to say a thing on. I can comment on information that's of a more public nature that says, the two shipyards, Electric Boat and Huntington Ingalls in Newport News are busy expanding the landscape of competitors. They need more and they need more capacity, and that is public information. So, more capacity would mean more competitors.

Q: And some of that is because they are looking – are they not looking to outsource business that they used to do in-house on contracts? In essence, boiling down their emphasis and focus to a smaller universe of component structures and things of that nature, and therefore, actually opening up opportunities for you to provide products that in the past might have been provided by the prime?

Alex Shen – Chief Executive Officer

Ross, I'm going to parse your combination question carefully and answer each one.

Q: Thank you.

Alex Shen – Chief Executive Officer

I think it's relevant and I'd like to do that so that I'm clear. So number one, the two shipyards, the main shipyards that are building the submarines are definitely outsourcing more than they have before, more than ever. That is true and that is public information that's available to all of us. The other thing that we can talk about is, what does that mean as far as needing more vendor capability and capacity. And that's the part I was alluding to that the two shipyards are very interested in developing more vendor capability because they're outsourcing. So that means that there's more competitors, simply because there's more capacity that's needed.

Q: Right. So because of that, it's not that you're facing more direct competitors in your spaces, but there's more opportunities moving for you and others, therefore, creating a greater number of aggregate competitors. I think I'm learning to speak, Alex.

Alex Shen – Chief Executive Officer

I think we're both very well versed in dancing with each other. But also I think we're very clear in trying to make sure that the opportunity is very clear.

Q: Yes. And I think there was a Seeking Alpha piece written about you and there were two risks laid that I thought I'd like to address from a perspective. One of the risks was whether the company, TechPrecision, would perform – execute on its contracts. And I would say, from my perspective, I know you can't say this, you've said job one is to execute effectively for your prime customer, and I would say that I can't imagine a scenario in which you would not. It doesn't strike me as anywhere in your personality or the nature of how you run the firm.

And the second is the submarines, and it appears the U.S. is falling, as I said, further behind, in that there's probably a greater risk of the Navy needing more boats as opposed to needing less boats when you start to see everything that's going on in the world and the moves Russia has been making and things of that nature, and China as well. So I'd like to say, we're still waiting for Godot, but as someone just reminded me, Godot does show up in this play, unlike the ones in the book. So thank you very much, and continued good luck.

Alex Shen – Chief Executive Officer

Thank you, Ross, as always, for your continued support.

Operator

Our next question comes from Aaron Warwick with US Capital [ph]. Go ahead, Aaron.

Q: Hey guys, thanks for taking my call. I always enjoy hearing you and Ross dance. I've got a couple of questions for you that are unrelated to each. I'll ask the first one here, it's about the backlog. My understanding from reading the 10-Qs and the 10-Ks is that backlog consists of funded projects that you believe you can complete within a two-year fiscal period, which seems pretty straightforward. But I'm wondering when you consider something like the US Navy submarine programs to be funded and therefore included in backlog, is that only after the passing and signing of the National Defense Authorization Act? Or is there some other event before that that would trigger that work to be considered part of the funded backlog?

Alex Shen – Chief Executive Officer

Excuse me. That was a pretty long question.

Q: Yes. Sorry. For submarine work, like on the Virginia class or the Columbia class, for that to be part of your backlog, does the National Defense Authorization Act have to be passed and signed by the President, or is there some other event or advanced authorization that would trigger that to be considered part of your backlog?

Alex Shen – Chief Executive Officer

My backlog consists of orders that I get.

Q: Okay. Thank you. My second question, you had mentioned with Ross about public information, and there was actually an article in Bloomberg today, it comes out of the BWX Technologies call last week, their conference call, where they had mentioned they have not received any updated orders from Electric Boat, and that they're considering withdrawing from producing those tubes altogether. So that would appear to leave one of your partners a customer to the sole supplier of those tubes in the future, and based on that, I would think the opportunity for you, although, already large, has gotten even bigger since that development. Am I understanding that correctly?

Alex Shen – Chief Executive Officer

I am completely unable to answer that question, for a number of reasons. The primary reason is that every single one of my customers, without exception, has put a lip-lock on me on that subject.

Q: Okay. That's fair. Thank you for your time. I appreciate it, guys. Keep up the good work.

Alex Shen – Chief Executive Officer

Aaron, thank you very much.

Operator

Our next question comes from Mark Gomes with Pipeline Data. Go ahead, Mark.

Q: Good afternoon, gentlemen. Just to rephrase that last question in complete general terms and nothing to do with the specificity of that question, when a vendor on contracts such as this misstep in such a way to create a setback in production, is it fair to say that it's generally a negative sign for the vendor's future as a supplier and therefore, a positive for its competitors? Again, nothing to do with the last question that was asked.

Alex Shen – Chief Executive Officer

Understood, Mark. So you understand I'm also a very careful and conservative person, and I do know that customers listen and replay this as well to see if I'm compliant to their instruction. So I will—

Q: And I respect that.

Alex Shen – Chief Executive Officer

I will not be answering that question, excuse me.

Q: Okay, fair enough. And boiling the ocean down, you did mention your level of excitement and how you feel about the opportunities ahead of you on the last call. Are you generally as excited about your future as you were on our last call?

Alex Shen – Chief Executive Officer

My excitement level remains the same. I am very excited.

Q: Thank you.

Alex Shen – Chief Executive Officer

Thank you for your support.

Operator

Our next question comes from Howard Brous with Wellington Shields. Go ahead, Howard.

Q: Alex, congratulations on the significant increase in balance sheet. It looks significantly better than it did several years ago, so congratulations. In following up a question about purchase orders, if there's a purchase order that extends beyond two years, and this is a generic question, having nothing to do with any particular order, what part is in backlog, or is all of it in backlog?

Alex Shen – Chief Executive Officer

Every purchase order is in backlog.

Q: Okay. So even if it extends beyond two years?

Alex Shen – Chief Executive Officer

There is no time limit. Every purchase order is in backlog.

Q: Okay. Let me ask a hypothetical question. If I go back three years ago in terms of gross margins, those gross margins approached 35%, if I remember correctly. Is that a correct comment?

Alex Shen – Chief Executive Officer

I don't remember back then. I'd have to do some research and—

Q: We'll do that off-line?

Alex Shen – Chief Executive Officer

—answer you exactly.

Q: I appreciate it. That's all I have. Thank you and congratulations, and good luck on the future purchase orders.

Alex Shen – Chief Executive Officer

Thank you, Howard. I appreciate your support.

Operator

Our next question comes from Richard Greulich with REG Capital Advisors. Go ahead, Richard.

Q: Thank you. Alex, the increase in sales to the industrial market, you noted in the 10-Q it was due to completed projects of large medical device components. Is that indicative of any ongoing business that you might be getting over the next four to six quarters?

Alex Shen – Chief Executive Officer

I'm sorry, can you rephrase that question?

Q: Yes. The fact that you've had an increase in medical device companies sales, does that portend any future sales from that area as well?

Alex Shen – Chief Executive Officer

I do not know.

Q: Okay. And was that involved with Mevion?

Alex Shen – Chief Executive Officer

I will not be commenting on individual customers at this time.

Q: Okay. In the 10-Q, when you noted that defense market revenues was lower partly due to timing and related project closing and startup activities, could you shed any light on what you mean by that?

Alex Shen – Chief Executive Officer

Sure. That's a more, probably wordy word to say that we have a lumpy business. That's as much light as I can shed on it. It's lumpy, so certain characteristics go up, certain ones go down. Timing is definitely one of them. We try to mention more than simply just saying it's lumpy and try to tell you guys a little bit more about – there's timing, there's these things, there's other things, but those are all contributors to the business being lumpy.

Q: In the past, let's say, over the last five or six years, when a prime contractor received a contract to supply certain parts of the submarine, is there any general time frame in which that would flow down to subcontractors?

Alex Shen – Chief Executive Officer

I'm not aware of any such timing.

Q: Okay. Thank you.

Operator

And our next question comes from Ross Taylor with ARS Investment. Go ahead, Ross.

Q: Thank you. Alex, given that you sit on the cusp of a substantial uptake in what should be top line, middle line, bottom line free cash flow generation and the like, has the Board begun to have discussions on how it plans on returning capital and the like, and how it plans on investing what should be a substantial growth in the balance sheet? It's already been mentioned how much it's improved, but the simple fact is going forward, as this business really starts to ramp, as you talked about in the prior call and opportunities in front of you, one would expect that you're going to end up generating a lot of cash that doesn't need to go to pay down debt, and the question is, how do you guys plan on using it? Have you thought about instituting a dividend, a share buyback? What are you going to be doing with that capital?

Alex Shen – Chief Executive Officer

So I think the question is what are we going to be doing with the capital, is the question. I don't know that we can answer the question right now. We are considering different things, yes. But I think that's more of a company and Board conversation probably. I'm going to ask Tom to also pitch in. I think we're having a discussion here, not so much a Q&A, but we can tell you what we can tell you.

Tom Sammons – Chief Financial Officer

Yes. I mean our cash goes up and down, so under a scenario where we have large growth we should be generating cash and then we will be – but there's no decision yet as to what do we do with that cash.

Q: Okay. I would only suggest that as you move into that state that the plans and return of capital approach you guys choose to take, because I would assume that whatever you do will involve not inconsequential return of capital likely, that it'd be communicated to investors, because I think it becomes a big part of the investment story going forward. I think this is one that we kind of – as I said, we're stuck in this holding pattern at this point beyond your control, but it's very clear that the need hasn't gone down, the opportunity hasn't gone down. In fact, I'd probably argue – you might even argue that you're more excited this quarter than you were three months ago, although, I know you want to be calm.

Alex Shen – Chief Executive Officer

Yes, I want to be calm.

Q: But you're more excited, aren't you?

Alex Shen – Chief Executive Officer

Boy, he asks such leading questions, doesn't he? That was not a question, right, Ross?

Q: Yes, it was.

Alex Shen – Chief Executive Officer

I have the same excitement level, Ross.

Q: Okay. I think you're more excited. I can tell that in your voice. Thank you very much.

Alex Shen – Chief Executive Officer

Thank you.

Operator

And there appears to be no further questions in the queue.

Alex Shen – Chief Executive Officer

Thank you, everyone, for your attendance. Have a good day.