RCM Technologies, Inc.

First Quarter 2022 Earnings Call

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CORPORATE PARTICIPANTS

Kevin Miller, *Chief Financial Officer*

Brad Vizi, *Executive Chairman and President*

CONFERENCE CALL PARTICIPANTS

Bill Sutherland, *The Benchmark Company*

Min Cho, *B. Riley Financial*

Frank Kelly, *Scopia Capital Management LP*

PRESENTATION

Kevin Miller

Good morning, and thank you for joining us. This is Kevin Miller, Chief Financial Officer of RCM Technologies. I am joined today by Brad Vizi, RCM's Executive Chairman.

Our presentation in this call will contain forward-looking statements. The information contained in the forward-looking statements is based on our beliefs, estimates and assumptions and information currently available to us and these matters may materially change in the future.

Many of these beliefs, estimates and assumptions are subject to rapid changes. For more information on our forward-looking statements and the risks, uncertainties and other factors to which they are subject, please see the periodic reports on Forms 10-K, 10-Q and 8-K that we file with the SEC as well as our press releases that we issue from time to time.

I will now turn the call over to Brad Vizi, Executive Chairman, to provide an overview of RCM's operating performance during the quarter.

Brad Vizi

Thanks, Kevin. Good morning, everyone.

RCM's first quarter results demonstrate a strong start to 2022 as we continue to build on the foundation we've established and drive execution across each of our business units. We also expect continued strength from each of our divisions, with every member of our team steadfast in their commitment to delivering excellence to our clients each and everyday. Once again, all of our units performed well during the quarter. Our Engineering team is seeing robust activity across the board. Our Healthcare Services team continues to expand its client footprint fortifying its presence as the premier service provider for school districts across the country. Lastly, our Life Sciences and IT group is making demonstrable strides toward becoming a leading solutions and managed service provider to the life sciences end market.

I will speak to several of the operational highlights in a moment. But first, I want to thank the team for a job well done and their commitment to propelling RCM to the next level. As proud as I am of the team's historical performance, we must continue to remind ourselves that we are still in the early stages of unlocking the massive potential of our platform. In fact, I believe we are just scratching the surface and remain confident that we have a long runway ahead. The level of collaboration has been contagious amongst the groups, and the shared institutional knowledge has been demonstrably accretive to today's results. Each group brings a unique and valuable skill set the entire firm can leverage when delivering value to our clients.

We are attacking markets with an increasingly holistic approach, and it is resonating with our clients as the level of engagement has never been better. This mindset shift from a solid approach to one of seamless collaboration is a testament to a strong company culture spawned by leadership and embraced throughout the organization. I am convinced the tangible benefits we are seeing today have galvanized the sustainable culture shift that will be one of the hallmarks of RCM for years to come.

Before Kevin dives deeper into the numbers, I want to share a few highlights and discuss several of the exciting initiatives we have underway at some of our top performing business units.

First quarter results represent another step change in performance, further highlighting our team's commitment to the RCM platform. We continue to see strong contributions from each of our divisions. As a company, RCM generated first quarter revenue of approximately $82 million, a 26% increase sequentially and an 84% increase year-over-year. Even more impressive, we posted record profitability during the quarter. In total, EBITDA for Q1 came in at $9.3 million, representing growth of 74% sequentially and well over 400% year-over-year.

I would like to call out a few of our star performers during the quarter and discuss at a high level some of the exciting developments that we expect will move the needle in the future.

First, our Healthcare team continues to execute against our long-term plan through its unwavering commitment to serving the youth of our country and education end market. By introducing new services, serving new schools and increasing penetration of our long-term partners, the team continues to fortify its position in this vital end market. Strength was broad-based, as reflected in the division's financial performance.

Our Aerospace team is doing a tremendous job across the board. Our new teammates sit hand in glove with the rest of the organization. Starting with our unwavering commitment to the client, which is only augmented by their insatiable appetite for innovation. To give you a sense as to the scale of this group's growth pipeline, the team's overall headcount has increased from 107 as of Q4 2020 to 272 currently.

As mentioned on our fourth quarter call, my level of excitement remains unabated regarding the inroads we are making within multiple new ecosystems. The pace of innovation and overall industry activity is impressive and I have conviction that RCM has a definitive role to play in helping our clients make history within some of these emerging markets. Our team has been extremely adept at finding niche skill sets in a tight labor market to help our clients scale. In return, we are increasingly being thought of not only as a vendor but a partner of choice.

Speaking of being a partner of choice, our Energy Services team is also worth highlighting. Their unwavering commitment to the client goes beyond projects in the field. As a reminder, this week, we are presenting in partnership with one of our premier clients at the IEEE T&D Conference in New Orleans. We hope you'll be able to tune in.

Finally, our Life Sciences team continues to gain traction with several blue chip clients as the group pivots to a more attractive managed services model. In particular, our validation practice is seeing robust demand for its services as life sciences industry undergoes a substantial upgrade of its manufacturing capacity. This strong demand backdrop has been precipitated by the pandemic, but is also being driven by the desire of many companies to simplify and secure their supply chains, which has led to a large onshoring effort.

Taken together, their execution is paying off as the group grew revenue by more than 27% year-over-year and increased profitability by approximately 43% over the same timeframe.

It is also worth noting that the outlook is just as robust, with business activity remaining elevated across all service lines. I want to thank Bill and his team for their unwavering commitment to restoring RCM Life Sciences and IT back to the crown jewel status it once held many years ago. It serves as a beacon within our organization and we appreciate the group's tireless efforts towards making RCM a marquee franchise within this vital end market.

In closing, I am proud of the team's focus and execution as we enter 2022. We are committed to building on the successes of last year's robust and broad-based performance. Our strong leadership throughout the organization has each of our groups positioned well for the future, and I look forward to sharing more updates as the year progresses.

Now, I will turn the call back to Kevin to discuss the Q1 2022 financial results in more detail.

Kevin Miller

Thanks, Brad.

Regarding our consolidated results, revenue for the quarter was $82 million, growing over $17 million sequentially and $37.4 million on a year-over-year basis. Adjusted EBITDA in Q1 2022 was $9.3 million, representing a sequential increase of almost $4 million and a $7.6 million increase over Q1 2021 Adjusted EBITDA.

Gross profit expanded to $23.4 million, a 32% sequential increase from Q4 '21 and just over 115% increase from Q1 '21. We are proud of the performance for the quarter as we continue to demonstrate the ability to both benefit from the inherent leverage within our business model, while also keeping an eye on future growth by making strategic investments in our team.

Turning to our Healthcare segment, the group generated revenue of $52.2 million in Q1 '22, which represents a 50% increase sequentially and a 147% increase on a year-over-year basis. The performance was broad-based.

Turning to our Life Sciences and Information Technology segment, the group performed well during the quarter, with revenue and profitability growing on a year-over-year basis. Regarding revenue, we generated $9.9 million in Q1 '22 compared to $8.9 million in Q1 '21. As Brad mentioned, our life sciences team continues to expand its footprint across various strategic accounts. We remain encouraged regarding the success we are having in pivoting the business to a managed service model.

Finally, turning to our Engineering segment, we generated revenue of $19.9 million in Q1 '22, growing both sequentially and year-over-year. After removing the impact of Canada Power Systems from Q1 '21, the group increased revenue by $7.8 million on a year-over-year basis and $1.6 million sequentially. At the unit level, as Brad mentioned, our Aerospace team continues to hit its stride as the group expands into some very exciting end markets.

Another strong performer was our Process and Industrial group. The team's initiatives across carbon capture, decarbonization of supply chains and renewables are all gaining momentum. Although some of these markets are nascent in their development, we are excited about the inroads the group has made by leveraging our existing process equipment technology.

Lastly, our Energy Services team continues to execute well and has laid the groundwork for a strong 2022 as client activity remains high across the electric utility space. As Brad mentioned, as strong as our performance was in Q1, we are excited going forward as the utilization levels and overall pipeline activity remains strong.

This concludes our prepared remarks. At this time, we will open the call for questions.

Operator

All right. We do have a question coming in from Bill Sutherland.

Brad Vizi

Good morning, Bill.

Bill Sutherland

Hey guys. I guess I'll just lead you through what you were maybe going to get into, Kevin, as far as some of the numbers.

Kevin Miller

Sure.

Bill Sutherland

Brad mentioned in Healthcare, growth was contributed to by new services, new schools and also increased penetration. So I'm interested in that. And then, also just the split between education and the travel per diem, the regular business.

Brad Vizi

Yes. I'm happy to start. And Kevin, you can certainly add to the extent that I miss anything. As you mentioned, Bill, a lot of the growth has been driven by new services that had been introduced, new schools that we've been serving, as well as further penetration of schools so that—we've been working with for a long time. A lot of that service offerings that we introduced, they tend to skew more towards the behavioral health end market, special education teachers, etc. So, what you're also seeing is a more rich mix, which is not only are they driving growth in these end markets, but also increased margin, more in line with the education segment.

Kevin, do you have anything to add to that?

Kevin Miller

No, I think that covers it.

Operator

All right. We do have another question. This one is coming from Min Cho.

Min Cho

Sorry about that. Hi. Thank you, gentlemen. Great quarter here. I know you don't provide a lot of guidance, but I was wondering if there's anything kind of one-time in nature in the first quarter, or if these are good quarterly run rates for each of the segments in terms of revenue and margins to kind of use going forward.

Brad Vizi

Yes. I don't think there's anything one-time in the quarter, and every single year, each of our businesses it tasked with growing in the double-digits. We also all aim for double-digit operating margins. Inevitably, what happens is as you scale that starts to show up on a consolidated basis. So, look, our marching orders have not changed. I don't see them changing for the foreseeable future, just given our size relative to the large end markets we play in. So, no, I don't view this quarter as extraordinary in nature beyond, obviously, the efforts of really thousands of employees at RCM.

Operator

All right. We do have another question coming from Bill Sutherland.

Bill Sutherland

I hope there's a way that I can ask more than one question. Kevin, again, in the quarter, because there was such a big upside in healthcare relative to my model, what was the driver of the healthcare, and I'm sort of getting at that by asking about the split between education and...

Kevin Miller

Sure. The growth is frankly broad-based across all of our groups, but obviously, we're heavily concentrated in the school business, right, so that is probably the biggest driver is the penetration and growth in schools, frankly. But we are growing really everything, and we expect to continue to see growth outside of the school business as well.

Bill Sutherland

Yes, I'm just asking because it's becoming clear that the rates are going to start to normalize particularly in the travel business going forward and the volume growth is probably going to moderate as well.

Kevin Miller

Sure.

Bill Sutherland

So, that's why I'm trying to understand how much...

Kevin Miller

Well we really do very little travel, I think you know, and we may do more of that in the future, certainly. We are certainly are interested in doing that. But right now, our greatest focus is on serving our school clients and serving non-travel related business to hospitals, rehab centers, nursing homes, what was our bread-and-butter business before we got into schools many years ago.

So, we're not really—to the extent there's a contraction in rates in the travel business, that's really—I don't expect that to impact us in any material way. This is—we do very little travel. Maybe a couple of million a year right now. That's about it.

Bill Sutherland

Yes. Okay. That's kind of what I needed to find out. Then there's excellent gross margin realization in IT, while revenues were a little light sequentially. Any color on that?

Kevin Miller

Yes, well we had an extraordinary quarter in IT in Q4. We had a big project that we delivered in sort of a short period of time. So, we saw a big jump in the Q4 revenues. It wasn't a big surprise to us to see Q1 revenues sort of more in line with Q3 of last year.

As far as the margins are concerned, that's not by accident. Obviously, we're transitioning our model to more managed services, more higher margin work where we're seeing some of our growth is in life sciences, which if you're in the right niche markets, you should see the kind of margins that we're seeing. At least that's the way we feel about it.

We've also seen a lot of improvement in our Human Capital Services, our HR Services group, which we also typically see pretty good margins as long as we're doing a good job managing our utilization which we have done for the last couple of quarters.

Bill Sutherland

How baked is life sciences as a percent of your IT group?

Kevin Miller

It's probably roughly 70%.

Bill Sutherland

Okay. And then impressive job on the cash. Any updated thinking on capital allocation plans?

Kevin Miller

Nothing to—certainly nothing to announce, but it's a heavy, heavy focus for Brad, the Board and myself in terms of how to allocate capital. It's something we think a lot about. Nothing really to talk about today, but all I can say, and I'm sure Brad will probably want to speak to this because this is something he's incredibly focused on, but we're going to allocate the capital in a way that we think is most efficient and most beneficial to the shareholders.

Bill Sutherland

Got it. Okay. Thanks gentlemen. Congrats.

Kevin Miller

Thank you, Bill.

Operator

All right. Our next question's coming from Frank Kelly.

Brad Vizi

Good morning, Frank.

Frank Kelly

Good morning gentlemen. How are you?

Brad Vizi

Good.

Frank Kelly

It looks like we had another great, great quarter for all the units. I'd like to add my congratulations to all the group heads and to the leadership team up at the top. I have a couple of questions. One is in the SG&A area. It looks like year-over-year it's gone up 55% or $5 million. Can we shed some color as to where those monies are spent?

Kevin Miller

Sure. I mean, at a high level, Frank, we're hiring people and paying them more as they deliver more gross profit. As you know, this is a very labor intensive business, particularly on the recruiting and sales front, and particularly as far as our school business is concerned and all of the credentialing and all of the things that need to go on behind the scenes to put somebody to work. So, we're just investing in our people, we're investing in our systems. Obviously, as gross profit increases, so do commissions and the bonuses and everything else. But what Brad and I and the other leaders in this business here are trying to do is balance investment for the future with good profitability and good cash flow in the present, right? Right now, we're happy with where we are, but we'll continue to keep an eye on SG&A and make sure we're efficiently deploying it.

Frank Kelly

Great. The second question I had was A/R. Do we—is our DSOs—because it looks like it—obviously, with revenue going up, sales going up, we expect A/R to continue, but where are DSOs today versus a year ago?

Kevin Miller

Much improved. We had the best DSO quarter in Q1 than we've ever had in the Company, and Q4 was the best quarter we ever had until Q1 of this year. So, we're well under 70 days. I don't have the exact number in front of me, but I think it's right around 66 for Q1 and we were right around, I think 67, 68 for Q4. So, we're very pleased with where the DSOs are at this point.

Frank Kelly

Great. Great. So, that kind of dovetails into my next point, which Bill brought up as well on the shareholder appreciation program, if you will. We're all looking forward to hearing some good news in that as we see these great numbers trickle through the financials.

Brad Vizi

Well, you're not expecting a different answer than we gave Bill, are you?

Frank Kelly

I am not, but just kind of also reiterating his valid point. I guess he brought it up on the last call as well and would like to hear—look forward to hearing what kind of program that we have or intensions that we have down the line.

Kevin Miller

Great. We appreciate your positive feedback and I think you know that we keep a very close eye on the capital allocation and view it as an incredibly important function of Executive Management here.

Frank Kelly

Great. Great quarter.

Kevin Miller

Thanks, Frank.

Operator

All right. Our next question is coming from Min Cho.

Min Cho

Hi there. Just had a couple more questions. Firstly, did you repurchase any shares in the first quarter?

Kevin Miller

We did. We did. If you bear with me, I'll look that up. I want to say it was around 400,000 shares. But I'll give you an exact number. Hold on.

Brad Vizi

I think that's right.

Min Cho

About 400,000. And how much did you...

Kevin Miller

(Multiple speakers)

Min Cho

Okay. And how much did you spend on that?

Brad Vizi

About $2.7 million, $2.8 million. But Kevin, you can double check on that.

Kevin Miller

Yes. Let's see. Two point eight million. Four hundred and six thousand shares. (Multiple speakers) in the first quarter, our average purchase was $6.84.

Min Cho

Perfect. Also, I think Bill was asking this question as well, but what percentage of your Healthcare revenues is from the school districts? I think you've provided that information in the past.

Kevin Miller

Yes, it's in our Q. In Q1 it was approximately 79%.

Min Cho

I'm sorry, seventy...?

Kevin Miller

Nine percent. Approximately 79%.

Min Cho

Okay. Great. Perfect. Also, in terms of your Engineering business, are you starting to see any benefits from the infrastructure bill in terms of increased bidding pipeline, just anything anecdotally about the infrastructure bill and its impact?

Kevin Miller

I don't think we've seen the impact yet, but we do expect that there will be some impact in the future. I mean, this is kind of something, as I'm sure you would understand, it's a pretty lagging sort of impact, right. We're seeing a lot of demand for T&D services and we were seeing that before the infrastructure bill. I think that there's a lot of—I mean, I think—the big utilities all know that they're going to be spending a lot of money on T&D...

Min Cho

Yes.

Kevin Miller

... and they're gearing up for that. So, I don't think that has really shown up. And frankly, while we're very optimistic about the rest of this year, I'm not sure we're going to see much impact in 2022 specifically from the infrastructure bill, but we do believe it's going to have a major impact to our business over the long term.

Min Cho

Got it. And then also, just a quick question about your carbon capture technology. I know you've talked about it in the past. Can you provide just a little more detail about that? Is this a proven technology? Are customers actually using it or are you still in a testing phase? Just wondering if you had any info on that.

Brad Vizi

No. So, yes, it's very much commercial. But we don't break out process and industrial. It's safe to assume it's well into the eight figures of top line, and generally speaking above average margin. Obviously, it could be project specific. What happens is is as you start to partner with some of the larger players in the space, you're the preferred provider and so there's quite a bit going on in terms of pilot programs that are actually sizable, and we actually think that that entire space is in the very early stages of its development. So, we anticipate benefitting from that over the long term and it's already materially accretive to our results today.

Min Cho

Okay. Then the final question. I know you don't provide a backlog per se, but can you talk about—I'm assuming given your—given kind of the guidance for the year, just general guidance, that backlog trends kind of improve sequentially across all the segments as well?

Brad Vizi

Yes, yes, backlog's very strong. But this might be a good opportunity for me to explain ultimately the mix of our Engineering business.

Min Cho

Mm-hmm.

Brad Vizi

Depending what business you're looking at, backlog is slightly more relevant and in some of our businesses they're a bit more quick turn in nature, so backlog might not be the best indicator. In others, it is a very good indicator. But what happens is as these businesses are growing and the projects that we work on are larger, backlog becomes a little more relevant in nature. That's why it's—we don't break it out and even internally it's not necessarily the best indicator in isolation, but when you take it—you triangulate it amongst a number of other things we look at, you have a really good sense as to how workflow is going.

Min Cho

Great. Understand. All right. Great. Thank you.

Operator

Thank you, gentlemen. I'm not showing any further questions at this time.

Brad Vizi

Thank you, everyone, for attending the RCM Q1 2022 conference call. We look forward to providing further updates going forward. We'll speak to you about Q2 in August.

Operator

Ladies and gentlemen, thank you for joining us. You may now disconnect.