

ATSC Q4 2009 Earnings Call Script

OPENING OF CALL/OPERATOR:

OPERATOR: Welcome to the ATS Corporation 2009 Fourth Quarter and Full Year Conference Call. During the presentation, all participants will be in a listen-only mode. Afterwards, you will be invited to participate in a question and answer session.

Now I would like to turn the program over to Joann O'Connell, Vice President of Investor Relations.

MODERATOR (J. O'Connell): Thank you. Good afternoon and thank you for joining us to review our fourth quarter 2009 and full year 2009 results. With us this afternoon from ATS Corporation are Dr. Edward Bersoff, Chairman, President and Chief Executive Officer, and Pamela Little, Executive Vice President and Chief Financial Officer.

Before I review the structure of this call, I would like to read the safe harbor statement.

This conference call could contain forward looking statements about ATS Corporation within the meaning of the Private Securities Litigation Reform Act of 1995. Forward looking statements are statements that are not historical fact. Such forward looking statements are based upon the current belief and expectations of ATS' management and are subject to risks and uncertainties, which could cause actual results to differ from the forward looking statements. Such risks are more fully discussed in ATS' filings with the Securities and Exchange Commission. The information set forth herein should be considered in light of such risks. ATS Corporation does not assume any obligation to update the information contained in this conference call.

At this time, I would like to outline the agenda for today's call:

- First, Ed will offer opening remarks.
- Next, Pamela will review ATS Corporation's fourth quarter and full year 2009 financial results.
- Finally, Ed will review operating results and offer concluding remarks.
- At the completion of Ed's remarks, the Company will open the call to take your questions.

At this time, I would like to turn the call over to Dr. Edward Bersoff, Chairman, President and Chief Executive Officer of ATS Corporation.

Ed?

OPENING REMARKS:

E. BERSOFF: Good afternoon and thank you all for joining us today to review ATS Corporation's fourth quarter and full year 2009 financial and operational performance.

Before I discuss those results, I would like to first take the opportunity to announce the appointment of our new Executive Vice President and Chief Operating Officer, Sidney Fuchs. As we announced today, Sid will join us officially on April 5, and he comes to us with extensive industry experience that crosses each of our market areas. He was most recently the President and Chief Executive Officer of OAO Technologies, a global provider of IT services to government and commercial companies that was sold earlier this year. He also served as a corporate officer at Northrop Grumman Corporation in two key executive roles, one being the CEO and President of TASC, Inc. when it was a \$1.2 billion Northrop subsidiary and the other as President of Northrop's \$1.4 billion Information Technology's Civilian Agencies Group. We're very excited to have Sid join us next month and we look forward to his participation on future earnings calls.

Now we would like to turn to our fourth quarter results. We are pleased to report solid financial and operating performance in 2009, where we delivered EBITDA near the top of our guidance range and continued to significantly pay down our debt while also executing our share repurchase plan. We began the year facing significant weakness in several of our commercial business areas but proactively managed our cost structure over the course of the year to maintain strong profitability. We continued to perform well on our existing contracts and win all our recompetes in 2009. We believe that our long standing track record with our customers and recompute record as well as our ability to deliver above industry average margins are strong indicators of our high end solution offerings and program execution capabilities; both providing a solid foundation for our long term growth strategy. We are also very pleased to report strong bookings in the fourth quarter of 2009, resulting in an increase in backlog from the previous quarter and a book to bill ratio greater than one. We believe this increase in bookings provides strong momentum for us in 2010, and we have already had a strong start to the year with over \$50 million in new awards so far in the first quarter. We are highly optimistic that our growth trajectory will continue to improve over the course of the year. Finally, we received approval in late December to list on the New York Stock Exchange AMEX and began trading on AMEX January 5, 2010. We believe this achievement will increasingly improve liquidity for our shareholders over time.

I will further talk about our operational accomplishments and challenges for the quarter and the year and outline our priorities and initiatives for 2010, after Pamela discusses our financial results for the quarter and year.

Pamela?

FINANCIAL RESULTS:

P. LITTLE: We will begin with our GAAP results, followed by our Earnings Before Interest, Taxes, Depreciation, Amortization and then explain the difference.

For the quarter ended December 31, 2009, we recorded \$29.2 million in revenue. Revenue for the quarter decreased by approximately 5.5% from fourth quarter 2008 revenue of \$30.9 million.

The operating income and net loss for the quarter was \$1.3 million and \$461,000, respectively, or a loss of \$0.02 per diluted share, compared to an operating income of \$2.6 million and net income of \$785,000, or \$0.03 per diluted share, for the fourth quarter of 2008. In the fourth quarter of 2009, we recognized a \$1.5 million loss contingency based on recent settlement discussions related to our ongoing litigation with Maximus, Inc.

As we have previously disclosed in our SEC Filings, we are a defendant in a lawsuit filed in 2007 asserting breach of contract related to a subcontract we had with Maximus associated with a prime contract between Maximus and the State of Connecticut. As of this time, the State of Connecticut advised Maximus that it was accepting Maximus' settlement offer and we have agreed to the financial terms of a settlement with Maximus. We are currently in the process of memorializing the final terms into a written agreement. Furthermore, based on the claims asserted in the lawsuit and when the Maximus lawsuit is fully resolved, we intend to pursue our indemnification claim against the former principal owners of Advanced Technology Systems, Inc., or ATSI, under the stock purchase agreement governing the transaction in which the Company (then Federal Services Acquisition Corporation) acquired ATSI. We could recover the amount of the expected settlement of \$1.5 million, as well as associated legal fees which through December 31, 2009 were approximately \$800,000. Any recovery of the settlement amount will be recorded as other income, when received.

We had asserted other working capital-related claims against the former principal owners and the former ATSI owners asserted certain counterclaims against us. For those claims, the arbitrator issued an award on June 26, 2009, under which we received \$3.8 million on July 1st 2009. We have provided more details on this matter in our annual report on Form 10-K which was filed with the Securities and Exchange Commission today.

Let me now turn to our internal metrics of performance and highlight how we look at our results. As I said a moment ago, our reported net loss was \$461,000 for the quarter. We incurred depreciation and amortization expenses of approximately \$714,000. Adding back the depreciation and amortization expenses, interest expense of \$695,000, less a tax benefit of \$401,000 results in an EBITDA of \$547,000. Further adding back the \$1.5 million loss contingency

and \$383,000 in non-recurring severance expenses, results in an adjusted EBITDA of \$2.4 million and an associated adjusted EBITDA margin of 8.3%.

The quarter over quarter decline in adjusted EBITDA was driven primarily by a decrease in gross margins from 33% to 30% from Q4 of 2008 to Q4 2009. This drop resulted in lower year over year fourth quarter gross profit of \$1.4 million. A shift in our contract mix, the largest of which was tied to the Coast Guard contract we've reported on previously where we shifted from a prime to subcontractor role, drove the decline.

When combined with the first three quarters in 2009, our revenue and EBITDA for the full year were \$118.7 million and \$11.2 million, respectively. Adjusting EBITDA for the loss contingency and severance expenses discussed earlier, results in an adjusted EBITDA of \$13.1 million and associated EBITDA margin of 11.0% for the full year 2009.

The operating and net income for the full year was \$9.6 million and \$3.1 million, respectively, or \$0.14 per diluted share compared to an operating loss of \$51.1 million and a net loss of \$49.8 million in 2008, or a loss per share of \$2.35. As we have previously reported, we incurred a \$56.8 million non-cash goodwill and intangible asset impairment charge in the third quarter of 2008, which had a significant impact on our earnings for the full year. The impairment resulted from an updated outlook for the businesses acquired in 2007, which led to an adjustment of the estimated fair value of the goodwill and certain intangible assets. Net income for the full year 2008 adjusted for the impairment charge and associated tax benefit was \$2.0 million, or \$0.09 per diluted share compared to \$0.14 per diluted share for the full year 2009.

Other measures of performance that we monitor regularly include backlog and days sales outstanding, or DSO. Our contract backlog at December 31, 2009 was \$166.8 million, of which \$61.0 million was funded.

Our DSO at the end of the quarter was at 66 days. We're very pleased to have reduced our DSO from 86 days at the end of 2008.

As of December 31, 2009, the balance on the revolving credit facility was \$18.7 million, down from \$32.6 million at the end of 2008, and we had approximately \$2.5 million of debt in the form of promissory notes, a decline from \$4.5 million in promissory notes at the end of 2008; both promissory notes were related to the acquisitions we made in 2007. As we have just reported in our 2009 10-K, the \$2.5 million in promissory notes will be further reduced in the first quarter of 2010 to reflect a settlement reached with the sellers of Number Six Software for \$495,000 related to an indemnification claim associated with the acquisition of this business in 2007.

As Ed alluded to in his opening remarks, our financial results for 2009 were mixed. Our revenue contracted in 2009; however, we were able to manage our expenses as necessary to maintain our target EBITDA and exceed our target

EBITDA margins. We were very pleased in our ability to increase our adjusted EBITDA margins from 9.9% in 2008 to 11.0% for 2009. Furthermore, we were able to generate strong cash flow over the course of the year, allowing us to pay down our debt by 43% since December 31, 2008 and repurchase over 400,000 shares of our common stock.

This concludes my review of the financials and I would now like to turn the call back over to Ed.

Ed?

OPERATING RESULTS

E. BERSOFF: Thank you, Pamela.

I'd like to start by commenting on our current market environment and offer our views on the outlook for our operations.

In 2009, we generated 46% of our revenue from federal civilian agencies, 32% from defense and homeland security agencies including our public safety business which has a number of state and local government customers, and 22% from commercial customers.

We remain optimistic about our market positioning as we enter 2010, particularly as we expect procurement activity to accelerate over the course of the year. Our business strategy in the government markets has been to maintain a balanced base of business across civilian and defense agencies. Within our civilian business area, we are encouraged with the latest budget request as our largest and longest standing customer, the Department of Housing and Urban Development, stands to receive one of the largest increases. Within our defense and homeland security areas, we believe there are ample opportunities to expand our business with several of our existing customers and add new customers to our mix in 2010. Furthermore, we have no exposure to a decrease in spending in the Middle East related to cuts for any weapon systems, or in-theater support.

We look forward to leveraging our new Chief Operating Officer's extensive background in the defense and intelligence markets to pursue new avenues of growth in those areas. Particularly, his leadership of TASC and current senior advisory roles in both the defense and intelligence communities will bring tremendous value to ATSC in capturing market share in those markets.

We will continue to monitor our commercial operations closely, which is the area in which we have experienced the most challenges in 2008 and 2009. As we did in earlier years, we will make investments where we see the potential for growth and keep costs in line with top-line performance.

Now I'd like to turn to a summary of some of our operational goals. I am pleased to report that we met many of the objectives we laid out at the start of the year. I would like to take the opportunity now to highlight those achievements in 2009 and outline our priorities for 2010.

Accomplishments in 2009 included:

1. Continuing to win all our re-competed contracts reflecting strong customer satisfaction.
2. Adding new customers such as the Defense Security Service and expanding our market share with one of our largest customers, the Pension Benefit Guaranty Corporation.
3. Achieving a book to bill ratio of 1.5x in the fourth quarter, providing strong momentum for growth as we enter 2010.
4. Exceeding our targeted EBITDA margin of 9% for the year even with declines in revenue and an increase in our investment in business development. Our margin improvement over last year of 110 basis points is attributed to a benefit from the first full year result of cost saving plans and process improvements initiated in 2008.
5. Paying down our debt by 43%.
6. Executing our stock repurchase plan and purchasing over 400,000 shares of our common stock.
7. And finally, receiving approval to list on the New York Stock Exchange AMEX, with trading beginning on January 5, 2010.

Now I will turn to some of the challenges we faced in 2009 and objectives that will remain on our priority list for 2010.

1. First, related to our revenue, we did not achieve year over year organic growth. Much of the year over year decline has come from our commercial business areas. We've seen that business recover over the course of year, as we've discussed on earlier calls, and expect that trend to continue in 2010. On the government side, we expected this decrease, as we've previously discussed, due to the conversion of one of our Coast Guard contracts to a small business set-aside, where we shifted from a prime to subcontractor role. Our number one priority for 2010 is supporting the efforts of our business development organization and committing the resources necessary to increase our bid pipeline in order to achieve our organic growth targets.

2. Second, our year end backlog did not meet our target goal. As we previously reported, a portion of our bookings in recent periods represent a number of imminent recompetes that were delayed. In the first quarter of this year, we have seen some of these recompetes now finally come up for bid and we've won those recompetes in each and every case. So far in the first quarter, we have already added over \$50 million in new bookings. So while the previous incremental extensions to our contracts were to our immediate benefit and we are very pleased that our customers continue to value our work, it did not allow us to achieve the growth in backlog that we expected by the end of the year. We do expect to continue to see procurement activity for most of our recompetes scheduled for bid this year despite the delays we experienced last year. Increasing our backlog from both winning our recompetes and securing new awards are critical components to our business development strategy and organic growth targets.
3. Finally, we had also hoped to pursue an additional acquisition in 2009, but determined that it made more sense for us to use our cash flow generation to pay down debt and preserve our operating flexibility, as well as execute our stock repurchase plan. We will accelerate our M&A efforts later in 2010 with our cleaner balance sheet to pursue accretive acquisitions, which has always been an important element of our longer term growth strategy.

Other initiatives for us in 2010 include:

- Quickly integrating Sid Fuchs, our new COO, into his new role within our experienced executive team, to promptly leverage and benefit from his industry network and operational experience,
- Continuing to maintain a greater than 9.5% EBITDA margin, and
- Achieving recertification of our CMMI Level 3 certification, demonstrating our continued commitment to high quality standards to meet or exceed our customer's expectations.

GUIDANCE AND CONCLUDING REMARKS:

E. BERSOFF: Before we open the call to questions, I'd like to outline the guidance we issued in our earnings release today. We provided a range for 2010 revenue for the year of \$124 million to \$128 million and EBITDA of \$11.8 million to \$13.0 million.

In 2010, we will continue to focus on our top priority to improve the quality of our pipeline and build our bookings and backlog. We plan to continue to increase our investment in business development in 2010 to significantly expand the resources we have dedicated to growing our company.

This concludes my prepared remarks. At this point, we would like to open the call to questions.

AFTER Q&A:

E. BERSOFF: Thank you for your time and attention. We look forward to speaking with each of you over the coming months and thank you again for your support.