

ATSC Q1 2011 Earnings Call Script

OPENING OF CALL/OPERATOR:

OPERATOR: Welcome to the ATS Corporation 2011 First Quarter 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 first quarter 2011 results. With us this afternoon from ATS Corporation are Co-Chief Executive Officer and Chief Financial Officer, Pamela Little and Co-Chief Executive Officer John Hassoun.

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, Pamela will offer opening remarks and review ATS Corporation's first quarter financial results.
- Next, John will review operating results and comment on the Company's performance for the quarter.
- Finally, Pamela will further comment on the Company's outlook for our business as well as offer concluding remarks.
- At the completion of Pamela's remarks, the Company will open the call to take your questions.

At this time, I would like to turn the call over to Pamela Little, Co-Chief Executive Officer and Chief Financial Officer.

Pamela?

OPENING REMARKS:

P. LITTLE: Thank you, Joann. Good afternoon and thank you all for joining us today to review ATS Corporation's first quarter 2011 financial and operational performance.

Our results today reflect our performance in an extremely difficult market environment where funding delays as a result of the continuing resolutions through the quarter and an overall challenging Federal budget environment adversely affected our top-line. For our business, in particular, the market pressures had a more significant impact combined with the heavy recompetes schedule we faced in 2010. We are now transitioning to a number of those recently recompetes and awarded contracts where in some cases there was an initial reduction in revenue due to changes in scope. We do continue, however, to achieve attractive margins despite the revenue weakness and have used available cash to pay down debt by another 21% since the end of 2010.

On April 18 of this year we announced a \$46 million, five-year award for one of our large Department of Housing and Urban Development, or HUD, programs that also includes the potential for an expanded scope of services. We believe this potential increase in our level of work on this contract, as well as for some of our other HUD contracts and existing customers where projects were delayed in the first quarter, will result in revenue growth from the first quarter for the remainder of the year, particularly in our government business.

FINANCIAL RESULTS:

P. LITTLE: Turning to the details of our financial results, 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 March 31, 2011, we recorded \$24.8 million in revenue. Revenue for the quarter decreased by approximately 18.6% from first quarter 2010 revenue of \$30.5 million. Revenue decreased by 10.2% from fourth quarter 2010 revenue of \$27.7 million.

The operating income and net income for the quarter was \$362,000 and \$182,000, respectively, or \$0.01 per diluted share, compared to an operating income of \$2.1 million and net income of \$1.1 million, or \$0.05 per diluted share, for the first quarter of 2010.

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 income was \$182,000 for the quarter. We incurred depreciation and amortization expenses of approximately \$638,000. Adding back the depreciation and amortization expenses, interest expense of \$65,000, and taxes of \$115,000 results in an EBITDA of \$1.0 million. Further adjusting EBITDA for non-recurring expenses related to severance and strategic evaluation-related costs of \$1.1 million and

\$94,000, respectively, results in an adjusted EBITDA for the quarter of \$2.2 million, and an associated adjusted EBITDA margin of 8.7%. Adjusted EBITDA in the first quarter of 2010 was \$2.7 million resulting in an adjusted EBITDA margin of 8.8%. For further clarification and as we have previously reported, first quarter 2010 operating income, net income, and EBITDA were favorably impacted by \$495,000 of other income associated with the adjustment of the sellers' note related to the Number Six Software acquisition, therefore explaining an adjusted EBITDA for the first quarter of 2010 lower than the actual EBITDA.

As I mentioned in my opening remarks, revenue performance was adversely impacted by several factors including the result of the continuing resolutions through the quarter and related Federal budget uncertainties that delayed funding for several of our programs. Our Fannie Mae business also experienced a quarter over quarter revenue decline driven by temporarily reduced staffing levels over 2010 due to delayed project starts. John will discuss the operational challenges we faced this quarter in greater detail in his comments, as well as the recent awards and opportunities we are pursuing to generate revenue growth in the remaining quarters.

Quarter over quarter adjusted EBITDA margins remained in line. We have continued to take steps to achieve attractive margins while we experience revenue weakness by seeking further efficiencies in our administrative processes and reducing overhead expenses to align with the revenue level, while continuing to invest in business development. Ongoing selling, general, and administrative expenses, excluding severance costs of approximately \$1.1 million, declined by 24% from the first quarter of 2010. Additionally, our Fannie Mae business margins are significantly lower than our government and commercial operations, therefore the drop in revenue from Fannie Mae this quarter did not have a material impact on our overall margins.

As we have experienced in previous years, we incur higher expenses in the first quarter related to our accounting for fringe benefits that impacts gross, operating and EBITDA margins as well as other indirect expenses related to audit and public company requirements. As a result, we expect our EBITDA margins to increase in the remaining quarters to our targeted levels for the full year.

Other measures of performance that we monitor regularly include backlog and days sales outstanding, or DSO. Our contract backlog at March 31, 2011 of \$222.2 million, of which \$31.6 million was funded, increased by 10% from March 31, 2010 backlog of \$201.2 million. Backlog as of March 31, 2011 does not reflect the \$46 million contract with HUD that I mentioned earlier, booked subsequent to the end of the quarter.

Our DSO at the end of the quarter was 68 days, in line with the fourth quarter of 2010. As of March 31, 2011, the total debt balance was \$11.4 million, all on our revolving credit facility. Debt is down 21% from \$14.4 million at December 31, 2010.

This concludes my review of the financials and I would now like to turn the call over to John to discuss the operating results.

John?

OPERATING RESULTS

J. HASSOUN: Thank you, Pamela.

I would like to start by commenting on our performance by market segment. Our government business generated revenue of \$19.4 million in the first quarter of 2011, compared to \$24.1 million in the first quarter of 2010 and \$20.3 million in the fourth quarter of 2010. Our commercial business generated revenue of \$3.0 million in the first quarter of 2011, compared to \$2.9 million in the first quarter of 2010 and \$3.6 million in the fourth quarter of 2010. Our government sponsored enterprise or Fannie Mae business generated revenue of \$2.4 million in first quarter of 2011, compared to \$3.5 million in the first quarter of 2010 and \$3.8 million in the fourth quarter of 2010.

The decline in our government business was primarily driven by delayed contract start dates as a result of the challenging Federal budget environment. As Pamela also discussed earlier, some of this drop is attributed to the impact of a number of new starts on recently recompeted contracts where we are experiencing lower revenue due to changes in scope or requirement modifications. We do, however, expect those recompeted contracts to expand in size and scope over their multi-year periods.

We additionally described several other factors that adversely impacted quarter over quarter revenue performance in the Form 10-Q we filed today including a high volume of HUD work in the first quarter of 2010 related to development tasking on a fixed price contract, the loss of one of our contracts with the Defense Logistics Agency in September of last year, and reduced funding on an Air Force contract related to changes in their procurement process. We do expect significant improvement in our government business over the course of the year related to incremental funding from several existing and recently awarded contracts that I will describe in greater detail in a few moments.

The decline in our government sponsored enterprise or Fannie Mae business was related to temporarily reduced staffing levels due to delayed project starts largely driven by Fannie Mae reacting to the mounting negative press in the first quarter of this year. We do anticipate that this business will increase in the second quarter and we expect further improvement in the second half of the year, as Fannie Mae is likely to increase its needs for new contract staff to catch up on its delayed projects. Furthermore, as Pamela mentioned earlier, our Fannie Mae business operates at significantly lower margins than our other business areas, so revenue volatility has less of an impact on our margins.

Our commercial business did not materially change quarter over quarter, and the drop from the fourth quarter of 2010 to the first quarter of 2011 was from higher product sales at the end of the last year which is customary for that business.

Now turning to new awards and a discussion of our government business, our first quarter new bookings totaled \$10.8 million. This amount includes a \$4.8 million, three-year task order under the U.S. Army's Indefinite Delivery, Indefinite Quantity, or IDIQ, contract for human resource solutions and services in Recruiting and Retention to support the U.S. Army Intelligence and Security Command, or INSCOM, in its efforts to recruit highly qualified cyber security professionals. The balance of the new bookings came from additional funding from existing clients.

As mentioned earlier and subsequent to the end of the quarter, the Company booked a \$46 million, five-year award with HUD, for the continuation of our application systems support for HUD's Single Family Computerized Homes Underwriting System or CHUMS and FHA Connection. This contract has the potential for an expanded scope of services in the second half of the year. With this early second quarter award, incremental funding on several additional HUD and other existing defense and homeland security customer contracts, as well as new awards such as the INSCOM task order, we estimate our government business performance will improve significantly over the course of the year.

As we have previously reported, the majority of bookings for the last few quarters have come from recompleted or follow-on government contracts, which has now secured much of our business for the next four to five years. We faced a very heavy recomplete schedule in 2010, where in most cases the new awards resulted in a change in scope and required skill set for delivery. We have now won thirteen of those follow-on contracts submitted in 2010 and are very pleased with this track record of defending our business base, particularly in this highly competitive marketplace we're operating in today.

Now turning to our business development initiatives, our current pipeline stands at a total of \$2.0 billion, of which \$468.1 million are qualified opportunities. Of that amount, we have approximately \$75 million in proposals awaiting award. We are also aggressively pursuing a number of new tasks under existing IDIQs such as the Army R&R mentioned earlier and our GSA Alliant vehicle; none of which are reflected in these numbers. We believe these IDIQs, in addition to new IDIQs we have submitted and are pending award, will be critical vehicles to support our long-term growth plans. These pipeline amounts also exclude our commercial and Fannie Mae opportunities. Business development remains our number one priority as we continue to invest in the initiatives that build our strategic pipeline and backlog.

And now I will turn the call back over to Pamela.

P. LITTLE: Thank you, John. Before we open the call to questions, I'd like to outline the revised guidance we issued in our earnings release today. Based on the continuing effects of a challenging Federal budget environment, we revised our guidance to reflect a range for 2011 revenue for the year of \$105 million to \$115 million and EBITDA of \$14 million to \$16 million.

As John discussed earlier, we expect an increase in award activity and acceleration in our level of work with HUD and other customers in the second half of the year. Furthermore, as we have proven in earlier quarters, we will continue to closely monitor the alignment of our expenses with revenue levels and manage our business to achieve our targeted EBITDA margin.

Finally, I would like to briefly comment on our announcement from earlier this year that we began a process to evaluate strategic alternatives. As we mentioned in our last earnings call, while the process continues, we do not intend to disclose specific developments regarding the consideration of strategic alternatives unless and until the Company's Board of Directors has approved a transaction or otherwise concludes its review of strategic alternatives.

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

AFTER Q&A:

P. LITTLE: 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.