

ATSC Q2 2011 Earnings Call Script

OPENING OF CALL/OPERATOR:

OPERATOR: Welcome to the ATS Corporation 2011 Second 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 second 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 second 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 second quarter 2011 financial and operational performance.

The results we will discuss today will tell a mixed story, as our backlog, second quarter bookings, profit margins and borrowing capacity are all at or near all time favorable levels for us. Our backlog is a record high at \$271.1 million, which is up 34% over June 30, 2010 and we booked over \$72 million in new awards in the second quarter representing a book to bill ratio of over 3x. We won two sizeable contracts this quarter at the Department of Housing and Urban Development or HUD and the Pension Benefit Guaranty Corporation or PBGC where we expect significant growth in the second half of the year as both contracts begin to ramp. We also continued to achieve industry leading EBITDA margins and paid down our debt to \$7.9 million or by another 31% since the end of the first quarter of this year.

Despite these positive fundamentals, we continued to face challenges with our revenue this quarter. As we have described previously, our government revenue has been negatively impacted as we manage through the simultaneous transition of a number of recompleted contracts in the midst of a very challenging Federal budget environment. Furthermore, our Fannie Mae business continued to decline as a number of planned projects were delayed. We will discuss both issues in greater detail later on the call.

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, and Amortization and then explain the difference.

For the quarter ended June 30, 2011, we recorded \$23.1 million in revenue. Revenue for the quarter decreased by approximately \$6.1 million from second quarter 2010 revenue of \$29.2 million.

The operating income and net income for the quarter were \$2.6 million and \$1.6 million, respectively, or \$0.07 per diluted share, compared to an operating income of \$2.2 million and net income of \$1.1 million, or \$0.05 per diluted share, for the second 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 \$1.6 million for the quarter. We incurred depreciation and amortization expenses of approximately \$630,000. Adding back the depreciation and amortization expenses, interest expense of \$53,000, and taxes of \$946,000

results in an EBITDA of \$3.2 million. Adding back non-recurring expenses related to strategic evaluation-related costs of \$14,000 results in a slightly higher adjusted EBITDA for the quarter also rounding to \$3.2 million, and an associated EBITDA margin of 13.8%. EBITDA in the second quarter of 2010 was \$2.8 million resulting in an EBITDA margin of 9.7%.

When combined with our first quarter results, revenue and adjusted EBITDA were \$47.9 million and \$5.4 million, respectively, resulting in an adjusted EBITDA margin of 11.2%. In comparison, revenue and EBITDA for the first six months of 2010 were \$59.8 million and \$5.5 million, respectively. Operating income for the first six months of 2011 was \$2.9 million and net income was \$1.7 million, or \$0.08 per diluted share, compared to operating income of \$4.3 million and net income of \$2.2 million, or \$0.10 per diluted share, for the first six months of 2010.

As I mentioned in my opening remarks, revenue performance was adversely impacted by several factors including managing the transition of a number of recently recompleted contracts where in some cases funding was delayed on several of our programs. Our Fannie Mae business also continued to experience declines 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 second half of the year.

Quarter over quarter adjusted EBITDA margins increased from 9.7% to 13.8%. This increase is the realization of efforts to improve efficiencies in our administrative processes and reduce overhead expenses, while continuing to invest in business development. Ongoing selling, general, and administrative expenses declined by 35% from the second 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 and discussed on last quarter's call, 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, EBITDA margins increased from 8.7% to 13.8% from the first quarter of 2011 to the second quarter of 2011. In the second half of 2011, we expect our indirect expenses and gross margins to remain comparable to the second quarter. Therefore as the revenue recovers, we expect EBITDA margins to further increase.

Other measures of performance that we monitor regularly include backlog and days sales outstanding, or DSO. Our contract backlog at June 30, 2011 of \$271.1 million, of which \$31.1 million was funded, increased by 34% from June

30, 2010 backlog of \$201.2 million and 15% from December 31, 2010 backlog of \$236.1 million.

Our DSO at the end of the quarter was 66 days, in line with the first quarter of 2011. As of June 30, 2011, the total debt balance was \$7.9 million, all on our revolving credit facility. Debt is down 45% 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 \$72 million in bookings this quarter, largely comprised of the two sizeable awards Pamela mentioned in her opening remarks.

As we discussed during our last call back in April, we were awarded a \$46 million, five-year award with HUD for the continuation of the Company's application systems support for HUD's Single Family Computerized Homes Underwriting Management System or CHUMS. Within this program we have built systems to process single-family mortgage insurance applications for securely handling high daily transaction volumes. While we have been involved with the evolution of this program for HUD for nearly 30 years, this contract has the potential for an expanded scope of services in the second half of the year as HUD begins to accelerate its IT transformation initiatives to modernize many of the applications we've built and maintained for it over our long partnership.

In June, we were awarded a follow-on single award contract with a \$30 million ceiling over 5 years with PBGC for the software development, maintenance, and operational services of the Benefit Management Applications (or BMA) suite of solutions. The purpose of BMA is to manage participant and beneficiary information and disbursement of pension benefit payments exceeding \$440 million each month. We've been working on the predecessor contracts to this award for nearly ten years, supporting large scale, complex modernization efforts. Similar to the HUD contract, we expect this new award to ramp up significantly in the second half of the year as development projects are funded.

While both awards were follow-on contracts to ATSC, they represent the strength of our sustained relationship with our two largest customers.

Now I'd like to turn to a few comments on our financial performance by market. Our government business generated revenue of \$38.1 million in the first six months of 2011, compared to \$46.5 million in the first six months of 2010.

Our commercial business generated revenue of \$5.6 million in the first six months of 2011, compared to \$5.8 million in the first six months of 2010. And our government sponsored enterprise, or Fannie Mae business, generated revenue of \$4.3 million in the first six months of 2011, compared to \$7.4 million in the first six months of 2010.

The decline in our government business was primarily driven by delays in contract awards as well as temporarily postponed funding for HUD and PBGC development tasks. We anticipate the development tasks to start in the August timeframe, which will significantly improve the financial performance of our government business over the course of the year. Offsetting the declines in HUD and PBGC in the first half of this year, we experienced strong growth from other key government customers – such as the Defense Technology Security Administration or DTSA and the Nuclear Regulatory Commission or NRC. With DTSA specifically, we are seeing increased demand for our expertise to support the current administration's export reform initiative. We expect continued growth from both customers in the future.

We also described several other factors that adversely impacted 2011 year to date revenue compared to the same period in 2010 in the Form 10-Q we filed today including the loss of one of our contracts with the Defense Logistics Agency in September of last year, and reduced funding on an Air Force project related to changes in its procurement process.

Our government sponsored enterprise or Fannie Mae business continued to experience declines this quarter related to the organization delaying projects in reaction to political pressures in redefining Fannie Mae's mission to provide liquidity, stability and affordability to the U.S. housing and mortgage markets. We believe that as Fannie Mae operations begin to stabilize, it will increasingly need new contract staff to catch up on the delayed projects. Being a top tier vendor at Fannie Mae with a long standing relationship, we expect to continue our role as a critical partner and see our business return to historical levels. Furthermore, as Pamela mentioned earlier, our Fannie Mae business operates at significantly lower margins than our other business areas, so its revenue volatility has less of an impact on our margins.

Our commercial business has remained relatively stable and we anticipate that to continue in the second half of the year.

Now turning to our business development initiatives. Our current pipeline stands at a total of \$2.1 billion, of which \$619 million are qualified opportunities. Of that amount, we have approximately \$100 million in proposals awaiting award. With the heavy contract renewal schedule we faced last year now behind us, we are also aggressively pursuing a number of opportunities new to the Company under both single awards and new tasks under existing IDIQs or GWACs. We have secured access to a number of new IDIQ vehicles this year, such as the Army R&R that we discussed on last quarter's call as well as ITSS for Department of Justice opportunities, and T4 for Veterans Affairs opportunities.

We believe these IDIQs, in addition to several other large prime proposals awaiting award with the National Oceanic and Atmospheric Administration, the Department of Homeland Security, and National Institutes of Health, will be critical vehicles to support our long-term growth plans.

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 reiterate our guidance we announced in our first quarter earnings release and call, reflecting 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 anticipate recovery in our revenue in the second half of the year primarily driven by the ramping of several recently awarded recompetes, where we experienced downturns in the second quarter as they transitioned to new contracts and new development related funding was temporarily delayed. We also expect to enhance current customer growth with several new business wins from pursuits where we expect a number of awards before the end of the government fiscal year.

Finally, as we discussed on last quarter's call, I will briefly comment on our announcement from earlier this year that we began a process to evaluate strategic alternatives. While this 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.