Volt Information Science
FY2017 Fourth Quarter Conference Call Transcript
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Good morning and thank you for joining us today for Volt Information Sciences' Fiscal 2017 fourth quarter and full year earnings conference call. On the call today is Michael Dean, President and Chief Executive Officer, and Paul Tomkins, Senior Vice President and Chief Financial Officer.

Before beginning today's call, let me remind you that some of the statements made today will be forward-looking and are made under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projected or implied due to a variety of factors. We refer you to Volt Information Sciences' recent filings with the SEC for a more detailed discussion of the risks that could impact the Company's future operating results and financial condition.

Also on today's call, our speakers will reference certain non-GAAP financial measures, which we believe will provide useful information for investors. A reconciliation of those measures to GAAP is included in the earnings press release issued this morning, January 12, 2018.

With that, it's now my pleasure to turn the call over to Volt's President and Chief Executive Officer, Michael Dean. Michael?

Michael Dean, President and CEO

Thank you, Lasse.

Good morning and thank you for joining us today for our fiscal 2017 fourth quarter and full year earnings conference call.

I will begin today's call with an overview of our results from this past quarter, along with an update on our ongoing turnaround strategy. Paul Tomkins, our Chief Financial Officer, will then discuss additional details about our fourth quarter and full year financial results, including the status of our financing and our balance sheet and liquidity position.

Looking at our fourth quarter performance, net revenue of $288.5 million decreased 15.5%, from $341.6 million in the fourth quarter of fiscal 2016. On a same-store basis, net revenues decreased 11.3% compared to a year ago, when excluding businesses we exited or divested over the prior twelve months and fluctuations in foreign currency exchange rates. A significant portion of the year-over-year decline was related to lower revenues from a single large customer in our North American Staffing segment. And while we continue to maintain a very strong, positive relationship with this client, changes to their overall human resources strategy dramatically reduced their overall spend on temporary staffing. Excluding this customer from the current and prior periods, revenue declines over the past several quarters have been relatively steady.

Notwithstanding the lower revenue, Volt's fourth quarter results showed continued evidence of improvement in several key financial and operational metrics. In this quarter we've effectively maintained our notable margin improvement for the fiscal year 2017. For the full year, we successfully expanded gross margins by 52 basis points—an accomplishment in our industry. In addition, our ongoing focus on achieving operational efficiencies and cost containment has continued to deliver lower selling, administrative and other operating costs. And at the bottom line, fourth quarter net income from continuing operations of $39.8 million benefitted from a gain on the sale of our quality assurance business, known in the industry as VMC, with fourth quarter adjusted EBITDA of $0.1 million.

Since Paul will discuss our financial performance in more detail in his remarks, my comments today will focus on the progress we made in fiscal 2017 executing our turnaround plan, along with our key priorities for fiscal 2018. As a quick reminder, the Volt turnaround has been focused on three key pillars:

- First, strengthening our balance sheet and company foundation;
- Second, streamlining our business and improving our cost structure and margins;
- And third, achieving top line growth.

Overall, we have made strong headway on these initiatives over the past two years. As is generally the case in a business turnaround of this magnitude we are undertaking at Volt, our progress has been uneven. We have made significant advances in many aspects of the turnaround and I will share with you the progress we have made since our last quarterly conference call. However, the progress we achieved earlier this year on the final pillar, bending the revenue curve, has stalled. Addressing this lone pillar of our plan is our top priority as we enter the new fiscal year 2018, and I will provide more detail on this in a minute.

With respect to improving our balance sheet and simplifying our corporate structure, we had another productive quarter. At the end of the fourth quarter, we completed the sale of the quality assurance business, which is part of our Technology Outsourcing Services and Solutions segment, and provides production development, quality-assurance testing and customer support to companies primarily in the video gaming and mobile industries. The sale did not include the call center services unit of this segment, which Volt will continue to own and operate.

Suffice it to say, we are very pleased with the outcome of this value-creating transaction. The quality assurance business was our lone remaining non-core asset representing approximately 5% of Volt's global revenues, but its sale generated net proceeds of $66.8 million, or the equivalent of more than $3 per share of Volt common

stock. In other words, we roughly sold 5% of the Company for about 140% of Volt's entire market capitalization before the deal's announcement. This transaction further enhanced our balance sheet liquidity and financial flexibility and allowed us to pay down $50 million of outstanding debt while utilizing some of our significant tax loss carryforwards. With this divestiture complete, Volt is now a focused, pure-play staffing company where we are best positioned to create long-term shareholder value.

Also during the quarter, we completed a settlement agreement with NewNet Communication Technologies related to our December 2014 sale of Volt's Computer Systems segment to NewNet. The net result is that Volt received cash proceeds of $5 million, as well as a $1 million promissory note due later this month. Overall, we are very pleased to have successfully resolved this on favorable terms and put this matter behind us.

And finally, we have a signed commitment letter from a lender and expect to close shortly on a new financing program that provides Volt with enhanced financial flexibility. Paul will discuss this in more detail in his remarks, but overall we are pleased with this new program that solidifies our balance sheet, and at the same time extends the runway to execute our turnaround plan.

Turning now to our objective of improving our cost structure and operational efficiencies, during this past quarter, we continued to make progress in right-sizing our administrative support functions. During the fourth quarter, selling, administrative and other operating costs improved by 1.0%, compared with the fourth quarter last year. For the full year, we were able to reduce SG&A costs by a net total of $6.8 million, or 3.3%, through ongoing cost reduction activities. This is on top of the net total of $27.1 million, or nearly 12% reductions that we achieved for the full year in fiscal 2016. It is worth noting that these cost savings are net of significant cost headwinds, including our investments in people and technology. The year-over-year reduction in SG&A also resulted from the sale of Maintech in March.

We are also making investments in our business that we believe will further lower overall costs and improve efficiencies going forward. Early in the year, we deployed new company-wide technology that we have discussed on previous calls. After years of deferred spending prior to the arrival of the current management team, this technology was a significant undertaking and going forward, will be essential to Volt's future competitiveness. As you recall, this system was deployed across most of the entire company and included front-end-of the business ERP functionality as well as a back office financial suite. As we reported last quarter, we did experience some customer billing issues during the post-implementation phase that negatively impacted our liquidity position at the end of the third quarter. However, I am pleased to report that all material issues associated with the deployment have been resolved. With this behind us, our teams are focused on implementing the enhanced functionality, improved operational efficiency and other competitive benefits that this technology now offers. We continue to anticipate this will generate cost savings of approximately $5 to $7 million annually in 2018 and beyond.

Over the past two years, our success in executing the first two pillars of our turnaround plan has helped us address many challenges facing the business. We believe we have achieved the primary goals and objectives we established for improving Volt's balance sheet and right-sizing the business. Furthermore, I feel we are in lock-step on the measures required to maintain the momentum of these pillars going forward. Therefore, we will consider our efforts here to simply be part of our regular course of business in fiscal 2018 and beyond.

With this foundation in place, entering fiscal 2018 we are now focused on the third pillar of our turnaround strategy, which is to drive revenue growth. To start, we have already achieved progress in our efforts on several fronts. Within our Technology Outsourcing Services and Solutions segment, after the sale of the quality assurance business, the remaining call center services business has achieved 10% year-over-year revenue growth and is our fastest growing business. In addition, our

International Staffing segment revenues adjusted for foreign exchange and businesses sold or exited, ended the year down only 2.3% despite being significantly impacted by the UK economic downturn. And VCG, our MSP business that now comprises the majority of Volt's 'Other' segment, produced strong momentum in the second half of fiscal 2017 and is poised to generate growth in fiscal 2018.

The remaining segment, and by far Volt's largest, is North American Staffing. While we made significant headway bending the declining revenue curve in fiscal 2016 and early this year, our progress has been stalled in the last several quarters.

A key to getting this business back on track is to appoint a permanent replacement to lead the North American Staffing segment. To this end, we have identified a top staffing industry executive with an extremely successful track-record. We are addressing a non-compete issue with this individual's previous employer before we move forward, and with the exact timing yet to be determined.

In the meantime, we are continuing to execute the strategy we articulated last quarter that we call 'Win, Fill, Grow': To win more new clients, to efficiently fill all the orders and opportunities that our current engagements offer, and to grow by finding better ways to expand with our existing clients. Let me take a moment to discuss our progress so far with each of these.

First, we need to win more new business through focusing, expanding and training our salesforce. This quarter, we have focused our local salesforce including rolling out a new sales playbook defining roles, responsibilities and expectations. And despite a challenging labor market, in this quarter we reduced attrition and expanded our salesforce, and we expect to hire many more in the next few quarters. Furthermore, we have refined and expanded our training of our sales team. And, in terms of wins, again this quarter we brought in 4 new clients, each with expected annual revenue in the millions.

The second imperative to grow revenue is to fill our clients' needs efficiently and with high quality candidates. Since our last earnings call, we have invested in and expanded our internal recruiting team by 19 people, in an effort to better capitalize on existing opportunity with current clients. Additionally, since our last call, we have completed over 600 hours of training for 500 branch employees at 64 locations on how to capitalize on our recently launched front end applicant tracking system. We believe this will provide advantage relative to our peers, of which many have older, less robust tools.

And the last piece of our win, fill, grow strategy is to grow our business with our existing roster of clients. To this end, this quarter we invested in, and executed, a global Strategic Sales Training program, to better capitalize on finding growth through our existing clients. This is but one part of our current efforts to focus and realign our overall sales efforts.

While we have not yet slowed the revenue declines in this business, I believe that these and other efforts and investments that we are making are intended to have a positive impact on revenue in quarters to come.

Lastly, let me say that the turnaround strategy that we have executed over the past two years has successfully helped us address many of Volt's operational challenges. The Company is today on solid footing, with a clear pure-play focus and streamlined operations. Now our entire team is focused on the final phase of our strategy, which is achieving top line growth. I look forward to successfully overcoming Volt's remaining challenges and emerging as a stronger company.

With that, I'd like to now turn the call over to Paul for a more detailed discussion on our fourth quarter and full year financial results. Paul?

Paul Tomkins, SVP & Chief Financial Officer

Thank you, Michael.

Good morning. Today I will provide additional details on our fourth quarter and full year financial results as well as discuss the status of our financing and our balance sheet and liquidity position.

Our revenue in the fourth quarter was $288.5 million, a decrease of $53.1 million, or 15.5% on a year-over-year basis. The decrease was primarily driven by a reduction in our North American Staffing segment of $31.0 million and a $17.9 million decline in our Other segment as a result of the sale of Maintech in March. Excluding the impact of non-core businesses sold or shut down during this past year, as well as normalizing for the impact of foreign exchange, the year-over-year revenue decline would have been 11.3% on a same-store basis.

Looking at the full year, net revenue in fiscal 2017 was $1,194.4 million, down $140.3 million, or 10.5%, compared to fiscal 2016. Excluding the impact of non-core businesses sold or shut down during this past year, as well as normalizing for the impact of foreign exchange, the year-over-year revenue decline would have been 6.6% on a same-store basis.

Turning now to our revenues by segment…

Revenue for our North American Staffing segment, which provides a broad spectrum of contingent staffing, direct placement, recruitment process outsourcing and other employment services, was $224.2 million in the fourth quarter, down 12.1% on a year-over-year basis. Revenue in this segment was impacted by decreased customer demand in the aerospace industry as well as with a large customer that changed its human capital strategy and significantly decreased overall spend on temporary

staffing. As Michael discussed in detail, the North American Staffing segment is the final focus of our turnaround. We remain firmly dedicated to our “Win, Fill, Grow” efforts in this segment with an increased focus on improving top-line performance. As discussed on previous calls, it is imperative that we further expand our sales and recruiting talent in order to improve VWS’ revenue performance. While we made progress on this front during the quarter, there is still additional work to be done. It is abundantly clear that getting VWS back on track is key to our turnaround effort.

Revenue for our International Staffing segment, which includes the Company’s contingent staffing, direct placement and managed program businesses in Europe and Asia, was $30.2 million in the fourth quarter, down 4.9%, from a year ago. The year-over-year decline was attributed to increased economic slowdown in the United Kingdom as well as the impact of foreign exchange fluctuations of $1.1 million.

Our Technology Outsourcing Services and Solutions Segment revenue, which includes quality assurance, business intelligence and analytics and customer service support for companies in a variety of industries, was $26.4 million in the fourth quarter, down 13.7% year-over-year. As Michael discussed, at the end of the quarter, we sold our quality assurance business, which was part of this segment. We are retaining the call center portion of this business, which primarily services a prominent technology company. While the overall segment was down year-over-year in 2017, our call center business revenue grew in 2017 and also on a sequential quarter basis.

And finally, looking at our Corporate and Other businesses, which is now primarily comprised of VCG, our North American Managed Service Programs business, revenues were $9.7 million in the fourth quarter, down 65.0%, versus last year. The year-over-year revenue decline was primarily driven by the impact of the sale of Maintech, which occurred early in the second quarter of 2017. On a same-store basis, excluding the businesses sold or exited of $17.6 million, VCG decreased $0.3 million, or 3.1%,

year-over-year due to lower volume as well as contracts that were not renewed in the latter half of fiscal 2016.

Overall, our total company gross margin percentage during the fourth quarter was 16.5%, relatively flat year-over-year. Excluding the businesses sold or exited, gross margin in the fourth quarter this year decreased 22 basis points on an apples-to-apples basis.

Turning to our cost and expense performance, selling, administrative and other operating costs in the fourth quarter decreased $0.5 million, or 1.0%, versus last year. This year-over-year decrease was primarily due to ongoing cost reductions in all areas of the business and due to the sale of Maintech. This improvement was above the $3.3 million of higher depreciation and software license expenses related to completion of the first phase of the upgrade of our back-office financial suite and information technology tools.

We incurred restructuring and severance costs of approximately $0.3 million in the fourth quarter as a result of the cost cutting initiatives we implemented beginning in the first quarter last year. The fourth quarter expense run-rate includes the majority of the $17 million of cost saving impact from these initiatives.

On an annual basis, gross margin percentage was 15.7%, up 52 basis points year-over-year. For the full year, our SG&A declined by $6.8 million, or 3.3%, despite being impacted by approximately $7.0 million of higher depreciation and software license expenses related to completion of the information technology updates in the back half of the year, including some one-time costs we incurred addressing issues with our payroll and billing systems during the upgrade. The year-over-year reduction in SG&A also resulted from the sale of Maintech in March.

While revenue generation remains a key focus, leveraging our SG&A to maintain profitability is also a top priority and we are pleased with our continued progress in fiscal 2017. Since 2015, excluding businesses we have sold or shutdown, our SG&A has reduced from $220 million to a run rate of $184 million as we enter into 2018. Looking ahead to fiscal 2018, we expect to continue to make improvements in our cost structure as we realize the full functionalities of our IT upgrade and focus on intelligent changes to our business processes.

Turning to our total company profitability for the quarter…

Income from continuing operations in the fourth quarter of 2017 was $39.8 million, compared to $2.8 million in the fourth quarter last year. The year-over-year increase was primarily due to the $48.0 million gain on the sale of the quality assurance business during the fourth quarter of 2017.

For the full year, income from continuing operations was $28.8 million, compared to a net loss of $14.6 million in the prior year. The year-over-year increase is primarily attributed to gains on the sale of our non-core businesses, Maintech and the quality assurance business. We are pleased to have completed these sales which significantly enhanced our liquidity and financial flexibility and further refocused Volt into a pure-play staffing company.

Adjusted EBITDA, as highlighted in our earnings press release, was a positive $0.1 million in the fourth quarter of fiscal 2017, compared to $8.0 million in the year ago period. For the full year, Adjusted EBITDA was a negative $0.9 million, compared to a positive $6.0 million in the year ago period.

Now let's move on to the profitability of our core segments.

Operating income in our North American Staffing segment was $5.5 million in the fourth quarter of 2017, compared to $10.6 million a year ago. We expect this to improve over time through a combination of operating efficiencies and revenue growth initiatives Michael discussed earlier in his remarks.

Looking at the other segments, the Technology Outsourcing Services and Solutions business generated operating income of $2.3 million, while our International Staffing Segment generated operating income of $0.9 million.

Our total company operating income for the fourth quarter of 2017 was $43.8 million, an improvement of $39.1 million compared to operating income of $4.7 million in the prior year period, primarily as a result of gains from divestitures.

Turning now to our balance sheet and liquidity position, our total debt balance at the end of the year was $50 million, down $50 million from the prior quarter and down $47.1 million from prior year. At October 29, 2017, we had a total of $94.8 million of global liquidity, up from $33.4 million in the third quarter. As of January 5, 2018, our global liquidity was $87.4 million.

The significant decrease in our debt balance and improved liquidity position were consistent with our ongoing efforts to divest our non-core assets and de-lever our balance sheet. The previously discussed sale of our quality assurance business during the quarter resulted in net cash proceeds of $66.8 million, and the settlement agreement we reached with NewNet Communication Technologies also improved our cash balance. As part of the settlement, NewNet paid off a Note more than a year early for $7.5 million and we also agreed to settle our outstanding working capital adjustment and other indemnity claims for $1.5 million. The net result was a cash receipt of $5 million and a promissory note of $1 million maturing no later than January 31, 2018. These cash inflows were primarily used to pay down debt, further improving our balance sheet and financial flexibility.

And finally, we expect to further solidify our balance sheet by refinancing our debt. We have executed a commitment letter on a new Accounts Receivable Securitization arrangement. We are currently working on definitive deal documentation, as the lender has successfully completed its due diligence. We anticipate closing shortly on the new financing program, which will improve our debt maturity profile, providing additional runway to execute our turnaround plan.

In terms of managing our liquidity, our top priorities remain consistent. We are focused on ensuring there is adequate liquidity for working capital purposes to effectively manage our business on an ongoing basis, as well as investing in the necessary tools and technology that are required to support our growth plan, and returning capital to shareholders.

In closing, again, I'd like to thank the entire Volt team for their continued focus and commitment to the success of our business. We are fully focused on driving top-line revenue growth and confident we are on the right track to returning Volt to profitable growth.

Thank you for joining the call and at this time I'd like to turn the call back over to Michael Dean. Michael?

Michael Dean, President and CEO

Thank you Paul. Now, I'd like to reiterate some remarks we made when we announced the sale of VMC in late October. We highlighted then that the disposition of those non-core assets, in addition to enhancing our liquidity, would allow us to focus on our core staffing business where we are best positioned to create long-term shareholder value. We also said, at the time, that the Board of Directors and Management continue to review a broad range of options to drive shareholder value

and advance the Company's plan for growth. If and when such initiatives warrant disclosure, we will share them with our shareholders. I continue to believe the stock is significantly undervalued and that projects underway have potentially positive outcomes; however the Company, Board and Management continue to be restricted from buying shares. Accordingly, we will forego questions today after these prepared remarks, but look forward to publicly updating the market and our shareholders on developments as they arise.

To everyone on this call, thank you for your support and for joining us today. We look forward to speaking with you again when we report our fiscal 2018 first quarter results in March.