

LGLIR512
Greg Anderson
The LGL Group, Inc.
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Operator: Good morning everyone and welcome to the LGL Group Q1 2011 Earnings Report. At this time, all participants are in a listen-only mode. Later, you will have the opportunity to ask questions during the question-and-answer session. You may register to ask a question at any time by pressing * and 1 on your touchtone phone. You may withdraw yourself from the queue by pressing the # key. This call also has a visual PowerPoint component in addition to the conference call. To view the PowerPoint, please click on the Join the Meeting link you see in your invitation and included in the press release announcing today's call. If you need assistance seeing the presentation, please press *0 on your touchtone phone and an operator will assist you. I'll be standing by if you should need any assistance. It's now my pleasure to turn the conference over to the company's Chief Accounting Officer, Mr. LaDuane Clifton. Please go ahead.

LaDuane Clifton: Good morning and welcome to today's call. Joining me today is our President and CEO, Mr. Greg Anderson. Before we get started today, we prepared a slide presentation for your reference that may be viewed as part of today's web conference. The presentation materials are also available from our website at lglgroup.com. We ask that you locate these and use them as a reference for our call today. This call will be recorded and will be available for playback later today on our website as well. Other financial information and recent press releases are posted on our website for your reference. Please note that our comments today are covered by the safe harbor statement. During this call, we may include certain forward-looking statements within the meaning of the Private Securities

Litigation Reform Act of 1995. In addition, non-GAAP financial measures may be presented as well. These statements are based on management's current expectations and are subject to uncertainty and changes in circumstances. Actual results may differ materially from these expectations due to changes in global, political, economic, business, competitive, market, and regulatory factors. More detailed information about those factors is contained in the LGL Group's filings with the SEC. If at any time you need assistance during the call and the web conference, please press *0 for the operator. At this time, I'd like to introduce our present CEO, Mr. Greg Anderson.

Greg Anderson:

Thank you, LaDuane, and good morning. Thank you all for joining our call this morning. Again, take a look at our agenda on slide 3, if you will. Pretty traditional. We'll cover our business highlights, cover up on the financials and our capital structure. We would like to give a one-page update on the impacts of Japan and what it means to our company, touch our strategic growth initiatives that we talked a lot about in these past quarters, and then certainly leave time for Q&A. From a business highlights perspective, we'll first cover sales and revenue, and as we had alluded to in our last call, we were not expecting a strong quarter from a revenue perspective. It's quite similar to many of our customers and whether those are the OEMs or the contract manufacturers, I think we're consistent with the trends that they have seen. I would like to say that in the first quarter, we did demonstrate a positive book-to-bill and it really took place late in the quarter and we did show some nice strength. New orders for the quarter were strongest in the telecom segment. MISA continues to lag over all its performance for 2010. It's notable that we did have a very nice increase in our backlogs. We've achieved \$12.2 million and that's about 14% of where we were at the end of the fourth quarter of last year. As I've mentioned, revenues for the first quarter were \$9

million; that's a 15% decrease as compared to the first quarter of 2010. It's really just softening the market, we believe, in the cycle that we've gone through. From an efficiency perspective, our operating efficiencies resulted in margins of 32.6%. That's comparable to where we were a year ago. We've clearly had some impact there by volume and I think we've – if you read our press release, we certainly have a margin component to additional revenue. Net income as well is \$241,000.00 with [unintelligible] with earnings per share of \$0.10. Again, cost containment efficiencies, we were satisfied with revenue as really the driver of the overall performance for income and earnings. We did have EBITDA of \$593,000.00, and it was nice to see that we generated cash from operations of \$1.1 million. As we look ahead to the second quarter and really the back half of 2011, we're getting mixed reports out of our OEMs. Many of them are running with some good backlog. Others are reporting growth but not the kind of growth that they had previously reported. Overall, I think we are showing some signs out there of improved market conditions. From the EMS, the Electronic Manufacturing Services Group, nearly all of those reported a soft first quarter similar to us. They are projecting revenue growth for the sustaining quarters of 2011, which is encouraging for us. I don't think that's also a sign that this inventory correction that we've all talked about has really worked its way through, so we're optimistic that that has taken place. I mentioned earlier that repeat orders from our existing customers, especially in the telecom market, have really strengthened. Overall, the semiconductor industry is predicting growth in 2011. Some of that is a pricing thing based upon what took place in the Japan disaster but nevertheless, they are projecting a growth year. From a financial highlights and capital structure perspective, here's our quarterly income chart, I'll call it. It has got revenue in the bars. The top line is gross margin. The bottom line is the EBITDA percentage. We have extended our positive earnings to six sequential quarters now. Our growth

margins, I'm going to restate, were at 32.6% and frankly, for the kind of revenue we have, we believe that that's a fairly good sign that we're operating efficiently. I mentioned the backlogs and the trends, so here is a twelve-quarter sequence of our backlogs. I mentioned that they did rise to \$12.2 million. That was up almost \$1.5 million over fourth quarter of 2010. Again, the strengthening in the back half of the quarter of new orders is really what drove that. From a trend perspective, we're getting back to the kind of levels that we like to run this business at.

From a capital structure perspective, our working capital is now at \$19 million. We've got just a little over eleven in cash, very little debt, and untapped line of credit, and all that was really the work from cash generated for operations. We also went through the capital raise in February of this year. At present, the strength of our balance sheet is where we want it to be. We think it gives us the kind of flexibility that is needed as we look ahead at the number of our strategic initiatives as well as in reinvesting into our core business. An update on the Japan disaster. Previously, we had a press release probably a month ago or so now that was fairly nondescript. I think today we've got enough experience behind us that we can speak more clearly to the impacts and really they've been very minimal. From an LGL perspective, we're really mostly [touched] by Japan really in the supply chain of our raw materials and we do have a good number that does come out of that region, obviously. Today, we've had no direct impacts on the supply chain. We have experienced some delays early on one to three or four weeks as some of these factories were interrupted by utilities. Today, those factories frankly have done a very nice job of coming back online, and really the whole area for us has now been stabilized. Because frankly we were in a favorable position, we're also able to respond to some urgent customer requests and some of our OEMs obviously had suppliers – I'll say competitors to us that had more

direct impacts. We were able to quickly respond and frankly, in the month of April, have gained some share, at least in one key customer as it looks to roll out some next generation mobile infrastructure.

At this time, it doesn't appear that there will be any significant negative impacts at least to our near-term financials as we take a look at what took place in Japan and how it impacts LGL. Regarding our growth initiatives, obviously we're working these things in parallel. Today, it's primary for the company to really drive our organic business through this cycle that we're in, so we're spending a great deal of time making sure we get that back to the healthy business levels that we had in mid-2010. We continued to work the joint venture aspects, the M&A mostly from the acquisition perspective, and look at anything that is Greenfield or near or adjacent to the frequency control space that might be very nice acquisitions to go under the LGL umbrella. We are organized. We do have a strong effort in that regard and today, we don't have anything to report but as soon as we do, obviously, the investors will be the first to hear. At present, I think at this time, Operator, we'd entertain taking calls from our participants.

Operator:

Thank you. At this time, if you wish to ask a question, please press * then 1 on your touchtone telephone. Once again, that's * then 1 if you wish to ask a question. If another caller asked your question or you wish to withdraw from the queue for any reason, you can do so by pressing the # key. We'll pause one moment to give everyone an opportunity to queue. Our first question comes from Krishna Shankar with ThinkEquity. Go ahead, please.

Krishna Shankar:

Yes. Given the environment in terms of [ensuing] backlog, can you give us some sense for the revenue growth trajectory going into the June quarter and what the outlook might be for the rest of 2011, given what you're seeing both on the telecom and the MISA segments?

Greg Anderson: Good morning, Krishna. This is Greg. Thanks for your question. I don't think you'd be satisfied if I just say it looks stronger but at this point, I think we're going to still remain pretty cautious on the June quarter. I think I spoke a number of times on these calls that the nature of the backlog, even though it's growing, predicting the nurture and revenue has a number of dynamics to it and frankly, I think we're just not at a point where we think that we want to share that openly. We get more mature in understanding our business and the cycles that we go through. I think that's more of a future kind of guidance, if you will, Krishna. What kind of correction we went through, how sustained it will be - those are all things that are uncertainties. We're certainly encouraged and positive about the facts that the order trend has changed as of late.

Krishna Shankar: Is it fair to say that the March quarter could potentially be the bottom in terms of the near-term revenue cycle? Even though you may not quantify the growth, should we expect some growth going forward or could that be a...?

Greg Anderson: I think so. Frankly, it feels like the bottom, yes. What I don't want to share is it's going to be X million for the June quarter and X million for the quarter after that. We believe that we are positioned to get back to the kind of levels that we saw last year. Really, our customer positions are strong. Our contracts are good. We think now we've worked through most of that inventory correction, so I do believe that it feels like we've hit bottom, Krishna, in that it should be an uphill road or a growing road ahead for the quarters ahead.

Krishna Shankar: What is the mix of telecom with these MISA revenues for the quarter, and can you talk about the impact of repeat versus new products in the telecom segment going forward?

Greg Anderson: Let's talk about Q1 to begin with. The actual revenue split was pretty even, so I can't say that there was a large - just from a shipments perspective, they were pretty balanced between our two segments. As we look ahead, telecom is where we've won some recent wins and those are driven largely frankly for LTE build out, so in the base station aspects of the wireless infrastructure. Those are what's building our backlog. I'll call it beyond our heed orders so they're clearly new orders. How well we perform on those over the next coming months I think will determine our ability to turn those into repeat orders like we've talked about in the past. We've clearly had some notable wins. I'll use the word "significant" and I think I used that in the press release as well. They were nice wins. There were some entries for us into that market. The technology that we had, we did have to respond quickly with our factories and our engineering organizations. Right now, we're frankly where we'd like to have it.

Krishna Shankar: The final question, LaDuane, what was depreciation and capital spending for the quarter and what do you expect that to trend for the year?

LaDuane Clifton: Depreciation amortization was about the same as it has been, running just around 200,000 or so. When you see the detail on the queue, you'll see that come through. Then I think, Krishna, you were asking about - did you say taxes?

Krishna Shankar: Capital spending?

LaDuane Clifton: Okay, capital spending, yes. In first quarter, capital spending was approximately 560, and it was a little bit more by design. You may have heard us talk about before that we've been considering going through the process of evaluating our existing ERP systems and we have in fact launched into a product to implement a new ERP system consolidated for all of our operations. A component of that spending, a significant amount

of the 560 I mentioned, is really purchasing the software for that initiative. Then there was some additional unusual capex that was related to consolidation of some of our operating sites, sort of a completion of some of the initiatives that we've had under way as we look to optimize. Capex spending going forward will be similar to prior years, so Q1 was a little bit more because of those two initiatives.

Krishna Shankar: Great. The tax rate for the rest of the year?

LaDuane Clifton: The tax rate, we're back pretty much to a normalized tax rate. During Q4, you recall that because of our projection to where we believe we would be, it was appropriate for us to remove the valuation allowance that had been there the prior year. So we're not really shielded by that allowance any longer, and so you'll see a normalized tax rate. For Q1, it was 36.6% and that's probably indicative of the full year.

Krishna Shankar: Thank you.

Operator: Thank you. Our next question comes from Hendi Susanto with Gabelli & Company. Go ahead, please.

Hendi Susanto: Good morning.

Greg Anderson: Good morning, Hendi.

Hendi Susanto: First question, you contributed a relatively high gross margin in the quarter to operating efficiencies. Besides operating efficiencies, is there some contributions from – let's say – favorable products mix as well?

Greg Anderson: I would have to say yes. We really look at – not just us – but we look at our gross margin from a perspective of what we'll call variable cost or prime cost, the cost of going directly into raw materials and the labor that actually takes to build the product. Those are favorable for the quarter.

That can be both a mix as well as how well we operated. Frankly, our factories ran well. Their efficiencies were good. The yields were good. I do believe there was some favorable mix, but I did mention that it's not so segment oriented. Our revenues between our two major segments were pretty evenly split. I wouldn't say that it was favorable. I would say it was at least probably more driven by the fact that yields and operating efficiencies were improved.

Hendi Susanto: Okay. Then last quarter, you mentioned that you have active discussions on the IP joint venture. Any update on that?

Greg Anderson: None that I can share, other than they're still active. I wish I could but at present, it's just not in the public domain but it's certainly still active, I think.

Hendi Susanto: Okay. Then you mentioned that you are seeing order strength in the telecom segment and then you mentioned like LTE base station. Do you see that order strength to continue into second quarter of 2011?

Greg Anderson: We're going to certainly realize some revenues in the second quarter. I think it's a question of for the back half of the year, frankly, how well we've performed. One of our key customers was impacted by another – I guess I'll call it a competitor. We were able to jump in, gain some share. Our ability to deliver on time and execute, I think, will demonstrate and deliver some opportunity for follow-on orders. We will realize some of those revenues in the near term here and as far as the repeat orders against them, I think that's really how well we perform. Right now, we're feeling comfortable with where we're at.

Hendi Susanto: My last question is about new products. In the last earnings call, you mentioned about the new timing devices for [G Backhaul], and then also like two GPS products targeting commercial markets. Do you have any

update on the timeline and whether the timeline is still the same, considering what we are seeing in the market?

Greg Anderson: I think those are both still consistent. Backhaul aspect is still growing for us. Frankly, this near-term opportunity with regard to LTE, we did shift some gears there and for us, frankly, they were new products for us and they really did generate new bookings. Right now, we see a significant amount of opportunity in that infrastructure. For the next couple of quarters, we're probably going to – we've been presented some real opportunities by our customers, and so we're probably going to shift gears towards that a little bit from the development aspect. We think that fits us pretty nicely and so strategically, it has been presented and we're going to turn our internal resources that way for at least the next couple of quarters. I would say that if in the last quarter I wasn't able to update call, I wasn't able to speak that clearly to it, obviously a lot has taken place and it presented some opportunity for us.

Hendi Susanto: Thank you and great job on the gross margin.

Greg Anderson: Thank you, Hendi.

Operator: Thank you. At this time, there are no further questions in queue, but we'd like to give everyone another opportunity. If you do wish to ask a question, please press * then 1 on your touchtone phone. It appears there are no further questions at this time. I'd like to turn it back to our speakers for any closing remarks.

Greg Anderson: Thank you for joining our call this morning. We are encouraged by our rising backlogs. We are encouraged by our operating efficiencies and our ability to maintain structural cost during the down part of this cycle. We are looking forward to doing a little bit of a road show here in the weeks ahead, so hopefully we'll get a chance to come on out and visit some of

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you in your offices. Thanks again for the call and we look forward to speaking to you in the weeks ahead. Thank you.

Operator: This ends the LGL Group Q1 2011 Earnings Report. If you have any further questions, please send an email to Greg Anderson at ganderson@lglgroup.com or to LaDuane Clifton lclifton@lglgroup.com.

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