HC2 Holdings, Inc. (HCHC) CEO Wayne Barr on Q1 2021 Results - Earnings Call Transcript

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HC2 Holdings, Inc. (NYSE:HCHC) Q1 2021 Earnings Conference Call May 7, 2021 8:30 AM ET

Company Participants

Matt Chesler - FNK IR

Wayne Barr - CEO

Mike Sena - CFO

Conference Call Participants

Kevin O'Brien - Imperial Capital

Brian Charles - R.W. Pressrich

Richard Faulk - Centris

Operator

Greetings. Welcome to the HC2 Holdings' Inc. First Quarter 2021 Earnings Call. At this time all participants are in a listen-only mode. A question and answer session will follow the formal presentation. [Operator Instructions] Please note this event is being recorded.

I would now turn the conference over to your host Matt Chesler with Investor Relations. You may begin.

Matt Chesler

Good morning. Thank you for being with us to review HC2's first quarter 2021 earnings results. We are joined by Wayne Barr Jr., CEO of HC2; and Mike Sena, HC2's Chief Financial Officer.

As usual we have posted our earnings release and our slide presentation on our website at hc2.com. We will begin our call with prepared remarks to be followed by a Q&A session. This call is also being simulcast and will be archived on our website.

Now for some pre-disclaimers. During this call, management may make certain statements and assumptions which are not historical fact, will be forward looking and are being made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

Any such forward looking statements involve risks, assumptions and uncertainties, and are subject to certain assumptions and risk factors that could cause HC2's actual results to differ materially from these forward looking statements.

The risk factors that could cause these differences are more fully discussed in the cautionary statement that is included in our earnings release and a slide presentation, and further detailed in our Form 10-Q and other filings with the SEC.

In addition, the forward-looking statements included in this conference call are only made as of the date of this call and as stated in our SEC reports. HC2 disclaims any intent or obligation to update or revise these forward-looking statements, except as expressly required by law.

Management will also refer to certain non-GAAP financial measures such as adjusted EBITDA. We believe these measures provide useful supplemental data that while not a substitute for GAAP measures allow for greater transparency in the review of our financial and operational performance.

Finally, results for the insurance segment which is pending for disposition are excluded from today's discussion and analysis of performance for the comparable period.

At this point, it's my pleasure to turn things over to Wayne Barr.

Wayne Barr

Thanks Matt. Good morning and thank you all for joining us today. The first quarter was a pivotal one and what we expect to be a transformational year for HC2. We believe that HC2 is in the best position it has ever been to realize the inherent value in our underlying businesses. Our efforts to date have provided us with additional runway to execute our strategy and we believe strongly that each of our operating segments represents unique market opportunities to grow value in this evolving new economy.

This is all coming about at a time when each of our operating segments is at a pivot point in its respective business lifecycle. DBMG is on the verge of expanding its geographic footprint at an optimal time. Pansend R2 technologies launched its first commercial FDA cleared device and Spectrum having substantially built out the nation's largest broadcast station group is focusing on generating revenue from this unique platform. Starting with some areas of near term focus, we are working to close two previously announced M&A transactions, each of which represents an important element of our strategy versus DBM's previously announced acquisition of Banker Steel like DBM's own chuffed steel Banker is one of the leading fabrication and erection companies in the country known for their large urban high rise projects in the New York metropolitan area, as well as work up and down the East Coast. Banker will add significant scale and breadth to DBM's operational footprint and enable DBM to provide fabricated steel for the entire East Coast construction market without detracting at all from its legacy markets primarily in the western half of the country. Banker brings with it a strong backlog and pipeline which we believe will result in even stronger more accelerated growth at DBM.

In addition, the acquisition of Banker will increase cash flow available to the holding company, which is one of the key objectives of our balance sheet enhancement strategy. Banker's about half the size of DBM with similar profitability and is expected to substantially increase DBM's revenue and adjusted EBITDA and we anticipate the acquisition to be accretive from day one. In anticipation of closing the DBM and Banker teams are already working together to assess which of their operational systems and processes will be chosen as best of breed to be used by the combined organization as part of their commitment to operational excellence. The teams will continue to explore additional operational synergies that may be realized as a result of the increased scale and geographic diversity represented by the combined company.

The acquisition is clear staff review and will largely be financed at the DBM level within the confines of our new 8.5% note indenture. We look forward to being able to announce the closing of this transaction in the weeks ahead and welcoming Banker Steel to the HC2 family.

The second near term goal is the sale of our insurance segment. At the very end of March, we reached an agreement to sell our continental insurance business to Continental General Holdings LLC, an affiliate of our board member Michael Gorzynsk for a total consideration of $90 million. As we previously announced, Mike presented us with a non-binding indication of interest in December 2020. Subsequent to our announcement we received and the disinterested members of our board evaluated additional proposals with the assistance and advice of outside counsel and an independent financial advisor. The disinterested board members ultimately selected Continental General Holdings' proposal and we entered into a stock purchase agreement on March 29, 2021. We now await regulatory approval.

In addition to sharpening our strategic focus the sales expected to bolster our liquidity position, including through receiving gross cash proceeds of $65 million, extending the maturity by five years of approximately $16 million of our series A and series A2 preferred stock, returning other

HC2 affiliate securities to HC2. With the refinancing of our balance sheet we completed in February and the closing of these two pending transactions in the weeks and months to come. We have made and continue to make significant progress towards improving our capital structure and increasing our financial flexibility, while positioning the company to execute on a more focused strategy in each of our three remaining operating segments. Managing our businesses now becomes even more front and center in each of these three operating segments had important developments in the first quarter.

Let's walk through the details. In infrastructure in addition to the pending Banker Steel acquisition, DBM CEO, Rustin Roach and his team are actively working to take advantage of the expected recovery in commercial, industrial services, and public sector projects. The backlog has returned to growth and we're seeing an uptick in the number of larger project opportunities in the market. We expect this return market momentum to continue. Regarding the backlog in the first quarter DBM's backlog increased by over $100 million to levels not seen since well before the pandemic. In particular, structural Steel was awarded the nine figure fabrication and erection contract to supply steel to a global technology company establishing a manufacturing plant in the western U.S. is part of a mega site that will be constructed in multiple phases. It's another tombstone project that continues a string of successful builds by DBM for tech companies on the West Coast. These tech company builds have included Apple's corporate headquarters in Cupertino, and an expansion of Facebook's headquarters in Menlo Park, as well as projects for Tesla, Google and Intel. It is also a fast track project which means a good portion of the backlog for this project should burn off into revenue in 2021.

The market for commercial opportunities has been characterized lately by predominantly small to medium sized jobs up to $50 million to $60 million on the high end. This tech company project as well as some additional large commercial projects in our pipeline increases our optimism that the market is now starting to open up for bigger projects. We are feeling increasingly comfortable with the outlook and fabrication and erection. However, as we've said in the past, our industrial services business has yet to see such increased activity and is still feeling the impacts of the pandemic.

We are also optimistic that we will actively participate in public sector capital spending that may be fueled by substantial infrastructure bill which will provide incremental tailwind to our performance. The addition of Banker Steel to the DBM arsenal is expected to further bolster

DBM's ability to participate in infrastructure capital projects as well as growth in the commercial and industrial construction markets.

In life sciences, we are excited about the commercial launch in the U.S. of R2's first product the FDA cleared Glacial Rx device. As we have discussed Pansend portfolio company R2 technologies is a dermatological technology company led by a world class team and guided by David and Cherien R2 has been able to bring to market a new device using new technology and launching commercially during a pandemic, which is a monumental accomplishment. I'd like to acknowledge David and Cherien and especially R2's CEO Tim Holt and his entire team for their hard work and deserved credit.

The pre-order process for Glacial RX was a success in the early demand from aesthetic providers and the first month of commercialization is in line with our expectations. With delivery the new devices underway R2 held its national sales team kickoff, hired a seasoned manufacturing executive out of Zeltiq and is moving towards commercial quantity manufacturing. Additionally, Glacial RX won a packaging design award from GD USA Magazine for its in treatment kit and topicals at the 58th Annual American package Design Awards in April. Glacial RX is designed with selected from 1000s of entries produced by the best design firms and departments representing leaders in every major consumer and B2B category, and further demonstrates the strength of this team and how well-positioned they are to market the product effectively coming out of the pandemic.

Next step for R2 is the commercial launch of a second product Glacial Spa, which is scheduled for this summer in China. Meanwhile, R2 continues to build out its portfolio of products which also includes an autonomous cooling spray treatment that delivers whole body skin lightening delivered robotically using AI technology. All told, with these developments R2 is now a revenue generating asset within the Pansend portfolio. Meanwhile, MediBeacon, which is revolutionizing kidney health, with the first of its kind novel technology that allows for real time monitoring the kidney function is on track to perform a U.S. pivotal study in the second half of 2021. At the conclusion of the pivotal study that will pursue the final process to potential FDA approval.

As a reminder MediBeacon was granted a breakthrough device designation by the FDA, which indicates that it may experience an accelerated process with the FDA, but we can't say precisely what that will translate into. Additionally, MediBeacon platform technology may have applications in other large clinical markets such as inflammatory bowel disease. The company is currently conducting a clinical study in patients with Crohn's disease, and we look forward to updating you as more developments from MediBeacon warrant.

In spectrum, we own and operate the nation's largest network of LP TV and class a television stations which represents a neat national distribution platform to reach households that receive their TV signals over the air. We are kept capitalizing on these over the year opportunities, which we can make available to over 60% of the nation's population by selling access to this audience to third party providers of digital content through leasing digital channels on our spectrum, or entering into revenue sharing agreements for advertising sales. As an example, beIN SPORTS is a relationship that began two years ago, and we are now expanding market coverage for beIN SPORTS extra to more than 40 stations. And on May 1, we launched a new Spanish version of beIN SPORTS Extra and more than 35 channels. We recently completed a carriage deal with Tegna as a launch partner for Twist. Their new multicast network for women which is currently carried on over 38 HC2 broadcasting stations and represents yet another example of a major broadcast network utilizing HC2's large OTA platform to reach audiences in markets in which they do not have coverage.

There are now more than 80 networks taking advantage of the HC2 distribution platform. We are also experiencing an increase in the number of discussions with additional networks and content providers interested in our platform, further demonstrating the attractiveness of the broadcast footprint we provide. From a plant standpoint, we've taken some additional steps to bolster our robust national platform.

We recently relocated the media gateway from Little Rock to Miami and now have 207 of our 228 stations managed out of a tier 3 certified data center. The media gateway enables us to control and monitor all of our stations from one central location. We are able to be responsive to content providers, monitor broadcast signal quality, and identify and correct outages with carrier class precision, making the station group a compelling distribution platform for a variety of content providers.

In addition to our efforts to optimize our podcast quality, we have identified 17 new stations that we plan to build during 2021. We are in the beginning stages of the station builds. After pending and potential station sales and after the build out of the 17 construction permits we will have approximately 240 stations in our network. The average build out costs based on our historical experience is approximately $180,000 per station. We were able to monetize a million dollars worth of our construction permit portfolio through the sale of 61 construction permits that are scheduled to expire in July. Working with the various buyers of these permits, we have filed construction deadline extension applications, thereby giving our buyers additional time to construct the permits that they're purchasing from us.

We will be using the proceeds from the construction permit sales to help defray construction costs associated with the 17 new stations we plan to build. As you can see in our first quarter numbers our Spectrum segment was adjusted EBITDA positive for the second quarter in a row, demonstrating that the business can be profitable in its current form. There are strong operating leverage in the model given the fixed cost nature of the operating structure and we are pleased to see that our increased efforts to utilize capacity represented by the station group are producing positive results. We are also starting to have discussions with colleagues in and outside of the industry as we continue to evaluate opportunities that take advantage of next generation technology such as ATSC 3.0 that offers expanded capability and uses of our spectrum, which we believe should translate into additional revenue opportunities.

So to recap, we believe the new HC2 Holdings is increasingly coming into focus. With a successful refinancing of our balance sheet in February, we put HC2 on a stronger financial footing, which allows us to better support our assets and drive their organic and inorganic ambitions. During the first quarter, we exited our clean energy business and reached an agreement to sell our insurance segment. What remains our best in class assets and infrastructure, life sciences and Spectrum. These are exactly the assets we want to own in the new economy. All three of our businesses have recently reached important milestones in their growth and we believe each is well-positioned to deliver meaningful growth and value creation in the years ahead.

With that, I'll turn it over to Mike for a review of our financials and capital structure.

Mike Sena

First, let me review our financial performance. And then I walk you through key changes to our capital structure to help you bridge the quarter and the two transactions that have taken place so far in early 2021. Please note that our insurance segments operating results have been reclassified to discontinued operations and are therefore excluded from our discussion of the company's results from continuing operations. Consolidated total revenue for the first quarter of 2021 was $171.8 million a decrease of 7.9% compared to 186.6 million in the prior period. The decrease was driven by our infrastructure segment, which had lower revenues and structural steel fabrication and erection due to the timing of project work under execution and changes in backlog mix, as well as a decrease in power and industrial maintenance and repair work performed.

Net income attributable to common and participating preferred stockholders for the first quarter of 21 was $12.2 million or $0.15 per share, compared to a net loss of 83.5 million or $1.82 per share in the prior year periods. Total adjusted EBITDA which excludes discontinued operations was 1 million in the first quarter 2021, up from an adjusted EBITDA of loss of 2.9 million in the prior year period. We saw improvement at infrastructure as well as spectrum partially offset by life sciences.

Now onto some color for each of our three segments. At infrastructure revenue decreased 8.6% to $161.3 million from $176.5 million in the prior year quarter. As discussed earlier, this decline was due to lower revenues from our structural steel fabrication and erection business and a decrease in power and industrial maintenance and repair work performed. Infrastructure adjusted EBITDA for the first quarter of 2021 increased from 9 million in the prior period to 11.3 million. The EBITDA improvements were achieved through optimization of execution strategies, more favorable timing and mix of fabrication and erection project work and contribution from DBM. DBM's construction modeling detailing and digital engineering company.

The Infrastructure segment continued to experience additional costs of 3.9 million during the quarter related to certain measures to comply with COVID protocols and consistent with prior periods we had excluded them from our adjusted EBITDA. We expect these costs to continue to trend down over the first half of 2021 as we burn off the remaining pre-pandemic backlog.

As of March 31, 2021 reported backlog was 523 million up from 395 million at the end of the fourth quarter 2020. Adjusted backlog which takes into consideration awarded but not yet signed contracts was 768 million, up from 608 million at the end of last year. While backlogs still has a larger mix of smaller to medium sized projects than we have had historically we continue to see larger project opportunities starting to materialize in the market. This prospect combined with a robust backlog of the business are providing greater visibility as we look into the future.

At life sciences the increase in adjusted EBITDA losses was primarily driven by the scaling of operations that R2 technologies ahead of the commercial launch of the Glacial RX and Spa products, as well as continued development of its product platform. In April R2 commence the official launch of Glacial RX it's FDA approved device utilizing patented, cryoaesthetic technology and we expect to see revenue generation from R2 this year.

At Spectrum revenue increased 4% to 10.5 million driven by an increase in the number of OTA stations in operation and digital content networks on the distribution platform partially offset by lower revenues from the Aztech network, which experienced a reduction in local market advertising spending driven by unrepeated political campaign expenditures and U.S. Census advertising campaigns in the comparable period.

Spectrum delivered adjusted the butt of 0.8 million in the first quarter compared to an adjusted EBITDA loss of 1 million in the prior year quarter. Results reflect continued efforts to improve operations and cost reductions which have led to the second quarter of positive adjusted EBITDA. The current corporate expenses were 4 million for the first quarter of 2021, down from the first quarter of 2020. The reduction was the result the decrease bonus expense and savings across our other overhead categories from prior year cost saving initiatives.

At the end of the first quarter, the company had 54.2 million of cash and cash equivalents compared to 43.8 million at the end of December 31, 2020. On a standalone basis as of March 31, 2021 the corporate segment had cash and cash equivalents of 36.4 million compared to 27.5 million at the end of 2020. As of March 31, 2021, HC2 had total principal outstanding indebtedness of 549.4 million, down 27.2 million for where it stated at the end of 2020 driven primarily by the February refinancing of our 11.5% senior secured notes.

During the quarter, we saw the Clean Energy segment and refinance the holding company debt. The sale of the assets in January generated 70 million in net proceeds to HC2 reflecting our 61% economic share on a fully diluted basis of 169 million gross transaction price less outstanding debt customary closing costs adjustments and transaction fees. In February, we completed a $330 million offering of 8.5% senior secured notes due 2026, which was used to retire existing 11.5% senior secured notes through 2021 and to repay the 15 million outstanding under our revolving credit agreement. We also entered into exchange agreements with certain holders of 51.8 million of the outstanding 7.5% convertible senior notes extending the maturity date to August 2026. 3.2 million of the old converts remain due in 2022.

Separately, we amended our revolving credit facility extending the maturity from September 2021 to February 2024 increasing the maximum credit commitment from 15 million to 20 million and lowering the current borrowing weight under the agreement by 100 basis points. We have no current borrowings on the line.

In conclusion, the actions we have taken including the rights offering last fall, the asset sales over the past year and the refinancing in February have all contributed to sharpening our strategic focus and enhancing our capital structure.

The next near term piece is the sale insurance segment which when completed, is expected to put the company in even stronger position combined we are confident that the new HC2 set up to deliver attractive growth and build long term stakeholder value. We remain focused in the intermediate term on the three business segments to support their growth and unlock value.

With that, operator, we'd now like to open up the call for questions.

Question-and-Answer Session

Operator

At this time, we'll be conducting a question and answer session. [Operator Instructions] And our first question is from Kevin O'Brien with Imperial Capital. Please proceed with your question.

Kevin O'Brien

Good morning, gentlemen. I wonder if we could focus a little bit more about the pending acquisition of Banker Steel, specifically out of that $145 million purchase price, I'm sure you're currently looking at a couple of different financing options but given those scenarios is there a range of cash that might be needed to be contributed to get this over the goal line from the HC2 level and if that's the case, is there a range of cash needs that you might expect to utilize?

Mike Sena

Kevin. It's Mike. thanks for the question. What I would say is that we're still working through the financing it's largely going to be financed down that at DBM and we're still working through the final throes of that as soon as we do have more clarity on that as we go through the final negotiations there with potential lenders we will certainly disclose that.

Kevin O'Brien

Understood, thanks. I guess post close, assuming a successful close can you maybe talk about a little bit more about Banker Steel and how its East Coast based sort of what the growth prospects you're expecting are and maybe specifically addressing sort of the backlog perspective that they currently have? Is it a similar profile to what you have where backlog is kind of shifted to a small and medium sized business? Or are there larger projects in there currently, that can sort of offset the mix and how does the mix change going forward?

Wayne Barr

Yes. sure. Kevin this is Wayne Barr. Good to talk to you again. So it's a very similar business to sub-steel, except for kind of the geographic diversity that they bring to the table. They are focused very heavily in the metropolitan New York area. So as a consequence some of their projects are high rises and large residential as well as office spaces that necessarily are just very-very big projects. And so from not only the existing projects they're working on but the backlog they tend to have larger projects in the backlog as well as the current things that they're working on. So I don't see that changing too much. They are experiencing a similar uptick as I understand it in the number of inquiries and projects that are that are out there. And I would assume that the nature of the projects is going to kind of stay very similar to what they've been doing already. They have a couple of very large marquee projects that they just finished up including one over at Hudson yard as well as one Vanderbilt and those are the types of projects that I would expect them to continue to bid on and win.

Kevin O'Brien

Great. Thank you. I guess one last question from me is switching to Spectrum. I want to understand I understood the dynamic correctly, the plan is for 17 new stations and if we use sort of the historical cost per station at about 180,000 per, that's about a $3 million price tag, but offsetting some of that is actually the sale of some of the licenses you had. Is that correct? So that might offset some of that cost to the tune of about a million dollars? Is that what I understand from the comments?

Wayne Barr

Yes. The offset is definitely correct. We have a very large portfolio of construction permits that enable us to petition the FCC use those construction permits, and convert those into stations. We got some press about the sales of those construction permits. They weren't really built out stations. We were selling the construction permits. We raised about a million dollars by doing that. And we're going to be using that million dollars to defray the expense of building out or converting 17 construction permits to actual on air stations.

Kevin O'Brien

Great. I understand maybe just one last quick one. I think your nearest term maturity is actually in Spectrum correct with about $16 million of term loan left over. Any thoughts on how you might address that maturity there? I guess specifically you obviously found earlier in the year four non-core assets that you were likely to sell are you pretty satisfied that what you have going forward? Or is there some additional asset sales that could be you utilize to chip away at that $16 million at that?

Wayne Barr

Yes. So the near term maturity of the broadcasting debt is obviously a high priority. We are in the initial stages of putting together presentation to go out and obtain refinancing of that really liked the momentum that Spectrum is showing. As we've indicated, the last couple of quarters, we've got the station group built and we've been focusing on generating revenue. And I think we're going to be able to enter the market for refinancing from a very good position. We do have approximately $4 million of additional non-core asset sales that are in the pipeline and we haven't made any further decisions on selling additional non-core assets at Spectrum. But to the extent that we do and we have something to come back to you all we certainly will.

Kevin O'Brien

Great. Thanks. That's all I had. I will jump back in the queue. Thanks.

Operator

And our next question is from Brian Charles with R.W. Pressrich. Please proceed with your question.

Brian Charles

Thanks just one or a couple of follow up questions of some things you touched on before regarding the acquisition of Banker Steel and the timing in terms of potential cash needs to complete that acquisition. What's the timing relative to the insurance sale? Are you expecting to close it before the insurance segment is sold or afterward and maybe use some of the proceeds from that sale?

Wayne Barr

So the Banker deal has gotten through Hart-Scott-Rodino review and I think right now we're working through just the remaining requirements on both sides including the financing contingency. We haven't really thrown out an estimated closing date but I'm thinking about it in terms of weeks. The insurance transaction has progressed very nicely. It's with the regulator right now. And we just had not felt comfortable making any kind of concrete closing date estimate for that just given the fact that the regulator has to go through its process.

Brian Charles

Okay. That's fair enough. So it sounds as if I can venture a guess that you don't need the proceeds from the insurance segment to close this transaction or at least that's not what you're counting on. It sounds like you've got things circled around enough to close the Banker Steel by itself.

Wayne Barr

With our current thinking about how the financing is going to work at DBM as well as just kind of our focus on the liquidity position at the holding company I think we're fairly comfortable right now and that the way the timing could line up Banker was to go before insurance I think we'd be in a position to handle it from a liquidity perspective.

Brian Charles

Okay. Good enough. And one other general question I have had a few questions posed to me about this on the life sciences segment I know it's still generating negative EBITDA but you're comfortable you don't need to put any more investment cash into those businesses and over time they will, they're certainly generating value. Is there a timing of which you might think about monetizing those? I don't know if you've discussed that before but is this a couple years down the road or is it a long-term holding?

Wayne Barr

So I will talk a little bit about R2 just because they did initiate the commercial launch and we will be generating revenue this year. It is a startup company. The team Tim Holt has done a great job. It's an experience management team that has brought a device and technology to the market before and typically we point people to this management's prior experience with Zeltiq and if you take a look at kind of the history of Zeltique with it being sold and with it going public and then being sold we're thinking about liquidity event for R2 in very much the same way.

Brian Charles

Okay. Good enough. Thanks. Let's see actually that's all I have got for now. Thank you.

Operator

[Operator Instructions] Our next question is from Richard Faulk with Centris. Please proceed with your question.

Richard Faulk

Well my question has already been answered and I want to thank you guys for being very open and transparent with this focused direction. I look forward to hearing better quarters in the future and keep on it.

Wayne Barr

great. Really appreciate it Richard. Thank you for your support.

Operator

And we have reached the end of question and answer session. I will now turn call over to Wayne Barr for closing remarks.

Wayne Barr

Thank you so much. So we really appreciate everybody waking up this Friday morning to join us for this quarterly earnings call. We look forward to coming back to you all at the appropriate time when we're able to close these two exciting M&A opportunities and available to answer any further questions. If you need to get in touch with Matt through our IR please go ahead and do. So hope everybody has a great weekend.

Operator

This concludes today's conference and you may disconnected lines at this time. Thank you for your participation.