HC2 Holdings, Inc.'s (HCHC) CEO Wayne Barr on Q2 2021 Results - Earnings Call Transcript

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HC2 Holdings, Inc. (HCHC) Q2 2021 Earnings Conference Call August 6, 2021 8:30 AM ET

Company Participants

Anthony Rozmus - Investor Relations

Avie Glazer - Chairman

Wayne Barr - Chief Executive Officer

Mike Sena - Chief Financial Officer

Conference Call Participants

Brian Charles - R.W. Pressrich

Derrick Wenger - Concise Capital

Operator

Good morning. And welcome to HC2 Holdings Second Quarter 2021 Earnings Conference Call. Today's call is being recorded and we have allocated one hour for prepared remarks and Q&A.

At this time, I'd like to turn the conference over to Anthony Rozmus, Investor Relations for HC2. Thank you. You may begin.

Anthony Rozmus

Good morning. Thank you for being with us to review HC2's second quarter 2021 earnings results. We are joined by Avie Glazer, Chairman of HC2; 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 brief 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 our cautionary statement that is included in our earnings release and a slide presentation, and further detailed in our 10-K 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 was sold on July 1st, are excluded from today's discussion and analysis of performance for the comparable periods.

At this point, it is my pleasure to turn things over to Avie Glazer.

Avie Glazer

Good morning, everyone. I'd like to thank you all for joining us today as we provide some exciting updates on our company's progress. We believe that our excellent second quarter results, including record backlog of DBM, record adjusted EBITDA at Spectrum and strong progress on the commercial launch of Glacial RX in Life Sciences are a preview of the long-term power and potential of our strategic plan.

First, let's talk about Infrastructure. A key milestone for our company was recent closing of our acquisition of Banker Steel, which added an industry leader to DBM, expanding the size and geographic footprint was already one of the largest steel fabrication and erection companies in the U.S.

With the addition of Banker Steel, DBM reported a record project backlog of $1.6 billion at the end of the quarter and this does even include another $300 million of contracts that have been verbally awarded, but not yet officially signed, which makes our total adjusted backlog $1.9 billion.

In fact, I have some additional good news to share with everyone today. DBM was just last week awarded a contract for the Inglewood Basketball Event Center, the new home of the NBA Los Angeles Clippers.

Please note that given the award was after the end of the quarter, this project is not included in a $1.9 billion of adjusted backlog. Deal erection [ph] for this project was planned to start in the summer of 2022 and we look forward to keeping you posted on the progress of this new arena.

DBM is an outstanding asset, with its expanded size and geographic reach, it is very well positioned to capitalize on this record backlog of projects in the quarters ahead. In addition, we believe the potential Infrastructure Spending Bill before Congress can only be viewed as a positive.

Second, let's talk about Pansend in our Life Sciences portfolio. Shortly after quarter end, we increased our stake in R2 Technologies, which recently launched its first commercial offering and is working towards second product launch Glacial Spa in the coming months.

For those of you who don't know what R2 does, R2 makes revolutionary devices to lighten and brighten skin in the $22 billion aesthetic dermatology market. R2's revolutionary system is the first age spot removal treatment that uses patented cooling technology to freeze melanin at the source, soothing skin while effectively removing age spots.

R2's product Glacial Rx disrupts conventional heat based laser treatments, which often cause inflammation and other painful side effects. We are tremendously optimistic about these new product developments and the team that supports them. We are also excited about the long-term prospects for other innovative companies in the Pansend portfolio.

Third, we are beginning to reap the benefits of our Spectrum assets, which also had a record performance reporting $2.7 million in adjusted EBITDA, a dramatic reversal from the negative $1.2 million in adjusted EBITDA for the same quarter just one year ago.

Operational improvements along with increased OTA or over-the-air broadcast revenues and the expansion of station group footprint with new station construction, position this business to drive continued growth alongside the rise of OTA broadcaster access in homes across the country.

And finally, as you all know, we plan to change the name to INNOVATE Corporation during the third quarter. INNOVATE is a platform of best-in-class assets, we believe are poised to thrive in the new economy. INNOVATE is who we are and INNOVATE is what we do. This is an exciting time for everyone involved in company, employees, stockholders and customers. We are energized to begin our next chapter as INNOVATE and for more color on all our growing businesses, I am pleased to turn the call over to Wayne Barr Jr., CEO of HC2.

Wayne Barr

Thanks, Avie, and thank you all for joining us today. We are pleased with our second quarter results, which we believe demonstrate our company's continued evolution and the strength and potential of our assets, which set us further along the path to succeed with our long-term strategy.

Our quarter goal is to identify unique market opportunities that will grow and value in today's evolving economy, and we made a number of strategic decisions in the second quarter that have advanced that objective. The team is excited and engaged. But we know there's more work to be done to grow our business segments and unlock meaningful value for stockholders.

Importantly, we achieved the near-term goals we highlighted for you last quarter. As Avie mentioned, we closed our acquisition of Banker Steel, increasing our backlog to record level $1.9 billion. We also closed on our sale of Continental. These two transactional milestones were significant steps forward and provide us with enhanced liquidity to ramp up our strategy and support our businesses.

Additionally, concurrent with the completion of the Banker Steel acquisition, and facilitated in part by the enhanced liquidity and other improvements of H2, DBM entered into a new credit facility, which was used to fully repaid DBM's existing debt obligations under portion of the Banker Steel acquisition and provide additional working capital capacity.

More recently, we announced that we provided an additional $15 million in Series C funding to R2 Technologies through Pansend, our Life Sciences segment. The additional investment will allow R2 to continue the rollout of new products, as well as fund the further development of Glacial Spa, Glacial AI and other cutting edge aesthetic dermatological products.

I will now provide you an update on each of our three business segments. At Infrastructure, we completed the acquisition of Banker Steel in May. Banker Steel's leading presence on the East Coast is an ideal complement to DBM's primarily West Coast focus footprint and the addition of Banker Steel to our portfolio more than doubles the size of our contracted backlog fairly significant.

Our total adjusted backlog for DBM was $1.9 billion at quarter end, comprised of $988 million in legacy DBM backlog and $911 million of backlog at Banker Steel. The backlog at Infrastructure has grown in line with our expectations as we are starting to see the market rebound from COVID disruptions.

We are taking advantage of the recovery seen in commercial, industrial services and public sector projects, as the economic environment continues to evolve and believe that our current backlog provides good visibility and runway for the next couple of years.

We are also keeping an eye on the various Federal Infrastructure Bills as a catalyst and significant opportunity for DBM. We anticipate we would see the impact of potential new projects associated with the bill in the 12-month to 18-month period following final passage.

In addition to an Infrastructure Bill's direct impacts on our DBM business, we believe the current emphasis on Infrastructure will be a boom for the construction industry generally and given the size, experience and expertise of DBM, we would expect to benefit from any increased demand for DBM services that occurs.

We also acknowledge the presence of industry-wide challenges in the short-term, including elevated steel prices, labor constraints and supply chain issues. However, we have not seen a significant impact from these challenges and we continue to find successes in our operational efficiencies and business development efforts.

Turning now to Life Sciences, our plan remains on track and we infused an additional $15 million in R2 to further grow that business. The funds will be used to accelerate U.S. commercialization of Glacial RX. The investment will also fuel global growth and fund further innovation and product development at R2.

Given the tremendous growth potential of R2, we were very pleased to be in a position to provide the additional financial resources to accelerate the revenue driving phase following the commercial launch of Glacial RX, and more broadly, to support the development of innovative technologies and global expansion being pursued by this world class team.

We are applying the lessons learned from the Glacial RX launch to the launch of Glacial Spa in China. We gained a number of important insights around manufacturing and shipping that will help to ensure a successful launch of Glacial Spa, which we now expect to take place during the second half of this year.

We also remain excited about prospects at MediBeacon. The U.S. pivotal study is on track to begin in the fourth quarter and we are in constant dialogue with the FDA to ensure we are doing everything we need to begin the study on time. We are happy with the progress made across the Pansend portfolio and optimistic about our ability to capitalize on the ongoing growth opportunities in this business.

At Spectrum, we achieved record level adjusted EBITDA of $2.7 million, and with improved operations, cost cutting and revenue improvements, we saw both our network operations and station group contributing to the third straight quarter of positive adjusted EBITDA results.

On the station group side, we reached an agreement with Scripps Networks to broadcast all nine of their networks on 47 stations, which represent 143 channels of programming and the meaningful annual revenue contribution for broadcasting. These networks comprise nine of the 81 networks using our platform today.

We are in ongoing discussions with Scripps and other content providers about broadcasting additional diginets on our platform as we seek to take advantage of the increased interest these content providers are exhibiting in our extensive distribution platform.

While the Scripps agreement is a fixed rate lease arrangement, this environment is also provided broadcasting with more opportunities to structure our business deals as revenue shares, which we believe present more revenue upside.

We have previously disclosed the broadcasting is in the process of constructing new stations using our portfolio of construction permits. As of today, we are targeting 25 new station builds, which are on schedule for completion by the end of the first quarter 2022. These 25 new stations will bring us to a total of 252 stations in the station group once completed. We plan to fund the construction of these new stations from the proceeds of asset sales including construction permits, as well as cash from operations.

Overall, we are seeing the benefits of innovate sharpen focus on our three operating segments and we entered the third quarter with strong momentum. All three businesses continue to reach important milestones in their business life cycles and we remain confident in their ability to deliver meaningful growth and value creation in the years ahead.

We are highly confident in the value of our current assets and we believe that our businesses are exceptionally well-positioned to benefit from the growth catalysts that are emerging as part of the new economy.

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

Mike Sena

Thanks, Wayne. I will first review our financial performance and then I'll walk you through key changes to our capital structure to help bridge the quarter and the key transactions that have taken place in the first half of 2021.

Consolidated total revenue for the second quarter of 2021 was $243.8 million, an increase of 34.1%, compared to $181.8 million in the prior year period. The increase was driven by our Infrastructure segment, due primarily to DBM's recent acquisition of Bankers Steel, as well as from higher revenues across DBM service offerings attributable to timing and project work under execution and backlog mix.

Net loss attributable to common and participating preferred stockholders for the second quarter of 2021 was $23.7 million or $0.31 per share, compared to net income of $12.7 million or $0.25 per share in the prior year period.

Total adjusted EBITDA, which excludes discontinued operations was $6.5 million in the second quarter of 2021, down from adjusted EBITDA of $10.6 million in the prior year period. The decrease was driven by margin compression at Infrastructure combined with the timing of work under execution and increased spend at our Life Sciences segment. This was offset by continuing improvement in our Spectrum segment.

Now onto some color for each of our three operating segments. At Infrastructure, revenue increased 34.6% to $232 million from $172.3 million in the prior quarter. As discussed earlier, this increase is due to the acquisition of Banker Steel, as well as higher revenues cross DBM service offerings.

Infrastructure adjusted EBITDA for the second quarter of 2021 decreased from $19.1 million in the prior year period to $13.9 million. The decrease is driven by the timing of project work under execution and the change in backlog mix, including the impact of market pressures on point-of-sale margins in the current year period, partially offset by the contribution from Banker Steel.

As we have previously discussed in our fourth quarter, lack of new work being released due to uncertainty during the peak of the pandemic was putting downward pressure on point-of-sale margins and we're burning off the backlog signed during the height of the pandemic.

While we have signed in a number of large projects into our backlog, we continue to see larger, more complex projects come into the market. Larger long-term projects do give us greater opportunity to improve margin through optimization of execution strategies.

The Infrastructure segment continued to experience additional costs of $4 million during the quarter related to certain measures to comply with COVID protocols and consistent with prior periods we have excluded them from our adjusted EBITDA. While these costs remained elevated in the second quarter, we expect COVID-related costs add backs to be minimal for the remainder of the year.

As of June 30, 2021, reported backlog was $1.6 billion, 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 $1.9 billion, up from $608 million at the end of last year.

Banker Steel acquisition added roughly $911 million of backlog. We are beginning to capture some larger project wins mentioned by Wayne over the past two quarters and expect to be running at a high capacity in the second half of 2021 and into 2022 as we burn off the record level backlog.

We generated nearly $400 million of sales into backlog in the quarter for DBM, exclusive of the backlog added by the Banker Steel acquisition, which highlights the continued strength of our pipeline.

In addition, we are starting to see improvements in point-of-sale margins as we see more and more construction projects being awarded. This prospect, combined with the robust backlog of the business are providing greater visibility as we looked into the future.

At Life Sciences, the increase in adjusted EBITDA losses were primarily driven by scaling of operations at R2 Technologies, including the increase in sales and marketing expenses. To support sales revenue growth and further commercialization efforts, as well as continue the development of its product platform and an increase in spend at MediBeacon as they prepare for their final pivotal study.

At Spectrum, revenue increased 11.6% to $10.6 million, driven by high station revenues, as we continue to increase utilization across our stations from both new and existing customers, which more than offset loss revenue from the sale of non-core stations.

Spectrum delivered adjusted EBITDA of $2.7 million in the second quarter, compared to an adjusted EBITDA loss of $1.2 million in the prior year quarter. Results reflect SG&A cost reductions, continued cost savings in the network business and exiting high cost non-core stations combined with the revenue improvements described above.

Non-operating corporate adjusted EBITDA losses were $5.7 million for the second quarter of 2021, up from the second quarter of 2020 by $2.1 million. The increase is largely driven by acceptance of a mediators’ proposal with the former Chairman, President and CEO regarding a separation from the company.

In addition, the prior year second quarter reflected a benefit from changes to the executive compensation plan that went into effect in the comparable period, which reversed executives and employees bonus accruals recorded in previous periods.

At the end of the second quarter, the company had $18.1 million of cash and cash equivalents, compared to $43.8 million as of December 31, 2020. On a standalone basis, as of June 30, 2021, the corporate segment had cash and cash equivalents of $2 million, compared to $27.5 million at the end of 2020.

During the quarter, we used $25 million of cash to fund a portion of the Banker Steel acquisition. In addition, we made an initial draw on our revolver, which requires a minimum balance of $5 million and use the proceeds along with cash on hand to redeem $10.6 million of our Series A and A2 preferred stock.

Subsequent to the quarter, on July 1st, we closed on the sale of Continental Insurance and received $65 million in cash, as well as an exchange of approximately $16 million of the remaining HC2 preferred shares, which were owned by Continental, the new classes of preferred shares with an extended maturity to 2026.

Our indenture allows us to use the first $50 million of asset proceeds from the Continental sale for working capital and combined with the expected cash flows from our Infrastructure segment, and availability under our credit line, we remain confident in our ability to execute our strategy across our business segments.

As of June 30, 2021, HC2 had total principal outstanding indebtedness of $679.6 million, up $103 million from $576.6 million at the end of 2020, driven primarily by Infrastructure financing related to the Banker acquisition.

As Wayne mentioned earlier, concurrently with the Banker acquisition, Infrastructure entered into a new credit agreement that provides for senior secured debt of DBM in the total amount of $220 million, comprised of $110 million term loan, which will mature on May 31, 2026, and $110 million revolving credit facility, which will mature on May 31, 2024.

This new credit agreement significantly reduces DBM’s cost of capital and will provide us with continued liquidity and flexibility to operate efficiently. The additional borrowing capacity will meet working capital requirements of the business and support continued growth.

In conclusion, the second quarter results and more recent milestones will provide a good momentum going forward. While there’s still more work to be done, we have accomplished a lot over the last year and we’re very happy with our progress in building value across our segments. We’re looking forward to the launch of a new name and branding in the third quarter and we remain optimistic about the back half of the year and beyond.

With that, Operator, we’d now like to open the call up for questions.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] Thank you. Ladies and gentlemen, our first question comes from the line of Brian Charles with R.W. Pressrich. Please proceed with your question.

Brian Charles

Thanks. Thanks for taking my question and congratulations on the quarter. Good quarter and congratulations on the Banker Steel acquisition as it is very nice to see that backlog. I just got a couple of questions, though. Could you give me a little more color on the second quarter EBITDA and maybe how that Infrastructure and how that progress is going forward in the context of this backlog? I imagine it was down a bit and I know your comments, you also had a market pressures on point-of-sale contracts, as well as other construction delays? Is that clearing up or is there kind of a trend you can give us on EBITDA might be going looking at or how might be looking going forward?

Mike Sena

Yeah. I would say a couple a couple points on that. This is Mike. Thanks for that question. One is that we are starting to see point-to-sale margins coming back, just based on the level of work that's coming into the market. So that's a positive sign.

And when you look at the backlog and you look at -- when that comes in. If you -- around $1 billion of that backlog is going to burn off over the next 12 months and we're in the early stage of ramping up these projects.

As -- and we've also talked about, as we start to sign some of these larger projects versus the small to medium-sized projects that we've been working on the last couple of years, you see opportunities to find execution improvements over the over the bigger, longer, more complex projects.

Brian Charles

Okay. Okay. I am thinking and I guess we've talked about in the past, I had a sort of a run rate of about $90 million of EBITDA and I am inclined to think that with this backlog over the next couple of years, that's something I'm still comfortable with it and even maybe growing from there. I don't know if you have any guidance on that?

Mike Sena

Well, we can really just talk about, what we've done historically from EBITDA perspective and when you combined, we've said also that Banker Steel is roughly half besides DBM and you are looking at what DBM has done over the last 12 months, you can get there.

Brian Charles

Okay. Good enough. Thanks. All right. My next question then I'll get back in queue, just for housekeeping. With the sale of the insurance subsidiary, understand $65 million of cash and the remainder, so $25 million of HC2 securities that I think were characterized in a press release as broadcast securities, is that correct or is there a combination of that $25 million, I think you mentioned also HC2 preferred, I don't know if I am…

Wayne Barr

Mike, what…

Mike Sena

Yeah.

Wayne Barr

It's for you.

Mike Sena

That's right. You have it right. We talked about in the press release the securities that came back were related to broadcasting. There was some preferred there and also some common down there that we -- that was returned. The insurance company also holds HC2 pref, so if you look at in 8 -- the 8-K we filed in early July, that pref was set to had a redemption date of May 29, 2021. We entered into exchange agreements with virtually the same terms that extended the maturity or the redemption date out to 2026.

Wayne Barr

But -- hey, Brian, it's Wayne. The pref that did come back though was the DBM broadcasting pref.

Brian Charles

Okay. Okay. Good enough.

Wayne Barr

I'm sorry…

Brian Charles

Okay. Thank you.

Wayne Barr

I am sorry, the HC2 broadcasting pref. Yeah. Sorry.

Brian Charles

All right. Good enough. Thanks again.

Wayne Barr

Sorry.

Brian Charles

That's it for me.

Operator

Thank you. [Operator Instructions] Thank you. Our next question comes from the line of Derrick Wenger with Concise Capital. Please proceed with your question.

Derrick Wenger

Yes. Thank you. If I could just drill down on Brian's second question, the $25 million of securities that you got, can you delineate what those are and how they will be paid off?

Wayne Barr

So those are securities of our underlying subs and broadcasting. They -- right now they were received -- the insurance company was owned by HC2, so those securities were transferred up to HC2 and they're being held at that level for the time being.

Derrick Wenger

And what is the breakdown of the $25 million.

Wayne Barr

It's primarily HC2 be preferred shares.

Derrick Wenger

Which will be paid off bullet in 2026 or?

Wayne Barr

We have not, it's intercompany. So from a consolidated basis for HC2 it's all eliminated in consolidation and all within the same house.

Derrick Wenger

Okay. Thank you.

Operator

Thank you. [Operator Instructions] Ladies and gentlemen, that concludes our question-and-answer session. I'll turn the floor back to Mr. Glazer for any final comments

Avie Glazer

Thanks. I want to, excuse me, I want to thank everyone for joining us on the call this morning. I'm sure you are as excited as we are about the future of INNOVATE and I look forward to speaking with you again on our next call. Thanks for joining us.

Operator

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