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Q2 2023 Orion Group Holdings Inc Earnings Call

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David Wright *Henry Investment Trust - Analyst*

PRESENTATION

Operator

Good day and welcome to the Orion Group Holdings second quarter 2023 earnings conference call and webcast. (Operator Instructions) Please note this event is being recorded. I would now like to turn the conference over to Margaret Boyce, Investor Relations for Orion. Please go ahead.

Margaret Boyce ***Orion Group Holdings Inc. - IR***

Thank you, Dustin, and thank you all for joining us today to discuss Orion Group Holdings second quarter 2023 financial results. We issued our earnings release after market last night. It is available in the Investor Relations section of our website at oriongroupholdingsinc.com.

I'm here today with Travis Boone, Chief Executive Officer of Orion, and Scott Thanisch, Chief Financial Officer. On today's call, management will provide prepared remarks and then we'll open up the call for your questions.

Before we begin, I would like to remind you that today's comments will include forward-looking statements under the federal securities laws. Forward-looking statements that are identified by words such as will, be, intend, believe, expect, anticipate or other comparable words and phrases. Statements that are not historical facts are forward-looking statements.

Our actual financial condition and results of operations may vary materially from those contemplated by such forward-looking statements. Discussion of the factors that could cause our results to differ materially from these forward-looking statements are contained in our SEC filings, including our reports on Form 10-Q and 10-K.

With that, I would now like to turn the call over to Travis. Travis, please go ahead.

Travis Boone ***Orion Group Holdings Inc. - President & CEO***

Thank you, Margaret, and welcome to everyone joining our call today. In the second quarter, we made substantial progress against our strategic plan, and Scott and I will cover the details in our prepared remarks.

Before that, I wanted to give you more context around our second quarter performance. As you saw in our press release, revenue came in at $182.5 million. Our loss per share was $0.01 and adjusted EBITDA was $3.7 million. Last quarter, we told you that we expected second quarter results to be better than the first quarter. And they are at a significant improvement over the last quarter, reflecting the progress we are making to improve our long-term performance. We expect continued improvement through the back half of the year.

I'll start with our concrete business. As you've heard me say before, our immediate priority was to improve concrete's profitability. When Scott and I came onboard, the concrete business had been losing money for too long. Since we started the transformation of our company in September, we implemented disciplined bidding processes, made leadership changes, added more rigor in our project delivery, exited the unprofitable central Texas market and focused our resources on our Dallas and Houston markets.

As a result of these actions, our concrete business returned to profitability in March. That profitability continued in April, May, and June, and we expect that trend to be sustainable. Right now, we have a large volume of work that has been bid, which reflects very strong demand in our core markets. We won't win all that work, especially if it doesn't meet our bid margin thresholds and some customers are delaying decisions up until the cost of capital stabilizes.

Even so, we feel concrete is in a strong position for the rest of 2023 and beyond. While concrete was a bright spot this quarter, our volume challenges in the marine business continued, primarily in our dredging operation. For context, our dredging business has historically been roughly 20% of our revenue and 30% of our profit. When that business is slow and we don't have work to bid, it has a big impact on us.

The Army Corps of Engineers has the responsibility, the mandate, and the funding to maintain US waterways along the Gulf Coast. They are very aware of the pressing need to dredge major shipping channels to keep commerce moving efficiently along the coast and to the ports. Delay of this maintenance activity has far-reaching consequences on the Gulf economy in the US supply chain, potentially disrupting shipping, goods handling, warehousing, and ground transportation. While we are excited about the potential to see significant opportunities in this space in the long run, our near-term bidding opportunities continue to be limited relative to historical levels.

In this environment, our focus is on carefully managing our costs and maintaining bidding discipline. In the second quarter, we were successful in winning a $27 million dredging contract from the Corps. And just last week, we won another $18 million contract with the Corps for dredging in Louisiana. These wins will help to get our dredges busier in the latter half of the year. We have several large outstanding bids for marine construction, and we remain confident that our opportunities to grow will continue.

The $1.2 trillion Infrastructure Act was passed two years ago, and while only a very small portion of the work has started, it is coming. Our project to build a drydock at Pearl Harbor is underway, and we are mobilizing equipment and resources to Hawaii. We expect our portion of the work on this $435 million contract to continue over the next 2.5 years. Orion is now fundamentally stronger and better positioned for accelerated profitable growth.

We laid out our three point strategic plan earlier this year, and we have made substantial progress in a short time. We are committed to doing what we say we will do and delivering on our plan to transform our business. We began with a long checklist and have ticked off many of the boxes, all focused on de-risking the business to clear the path for long-term and sustainable growth. We shored up our balance sheet and liquidity. In many ways, this was one of the most critical objectives we faced.

We secured a new $103 million ABL credit facility and have thus far monetized $25 million of assets with substantially more under contract. We have attracted great talent to focus on business development and growth. Building stronger customer relationships is a critical element in driving future growth. [Casey Stavinoha] has joined us to lead business development for our efforts in Louisiana, which is an important state for us, considering that $50 billion is earmarked for Louisiana coastal restoration.

Alan Eckman joined us in July to lead corporate growth and strategy reporting directly to me. These individuals bring years of experience and proven results to Orion. We will continue to invest in key resources focused on growing our business. We're also investing in training and tools that will allow our people to reach their full potential. Our goal is for our people to clearly understand our business objectives, embrace a growth mindset, and speak about the business in the same way. This is an important step in strengthening our culture, leveraging best practices, driving synergies, and cross-selling capabilities.

Looking ahead, we are extremely excited about the future. In the remaining months of 2023, we will continue to build momentum in the execution of our strategic plan and expect quarter-over-quarter improvements in performance. After establishing a foundation for the new Orion this year, 2024 will be a very different year for the company. We are fortunate to have the most exceptional people in the industry and two businesses with different catalysts for growth, concrete, more driven by the private sector and marine by the public sector. They can balance one another during challenging times where both are performing well, as we expect in 2024, they can deliver dramatic growth.

Now I will turn the call over to Scott for his review of the financials and operations.

Scott Thanisch *Orion Group Holdings Inc. - EVP & CFO*

Thanks, Travis. I'll cover some highlights and then review the second quarter results. The main headline of the second quarter is the progress we've made strengthening our balance sheet and improving the company's liquidity. As we announced on May 15, we closed on a three year $103 million ABL credit facility, which includes a term loan of $38 million and a revolving credit facility up to $65 million. By extending our debt maturities and increasing our access to capital, Orion will be in a position to make the most of our market opportunities.

In addition, we closed $25 million in equipment and real estate sale leaseback transactions in the quarter. We're pleased to deliver progress on our asset monetization goals, and we remain focused on opportunities to unlock value on our balance sheet. In April, we signed a $36 million contract to sell our East West Jones property. And then in June, we signed a contract for the sale and partial leaseback of our Baytown Pipe Yard for $8.3 million.

We expect these transactions to complete in the third and fourth quarter, respectively. While our balance sheet is stronger and that is the headline for the quarter, I'm more excited about the transformation of our concrete segment performance, which, as Travis mentioned, hit positive adjusted EBITDA this quarter for the first time in two years. This was a $3 million improvement over both the prior year and the prior quarter. These margin improvements are sustainable and are supported by both operational process enhancements and more disciplined bidding leading to higher margin in our backlog.

Moving on to our financial results, Orion produced $182.5 million of revenue in the second quarter, up 14.7% sequentially and down 6.2% from the prior year. The year-over-year decline was largely due to our exit of the central Texas construction market, partially offset by increased revenue in our marine segment, driven by our Hawaii drydock project.

Second quarter gross profit was $13.8 million or 7.6% of revenue compared to $14.3 million or 7.4% of revenue in the prior year period. Gross margin percentage increased due to our actions to improve concrete segment margins, partially offset by lower equipment and labor utilization in our marine business.

Turning to more detail on our segments. Our marine segment reported second quarter revenue just over $100 million, up 22.1% over the prior year. Adjusted EBITDA was $3.5 million or 3.4% adjusted EBITDA margin. This compares to adjusted EBITDA of $8.7 million and an adjusted EBITDA margin of 10.6% in the second quarter of last year. This decrease in adjusted EBITDA was primarily related to lower labor and equipment utilization. Second quarter concrete revenue was $82 million, down 27% from the prior year. Adjusted EBITDA was $264,000 or 0.3% of revenue compared to negative $3 million or negative 2.7% margin last year. As I mentioned, we expect these margin improvements to be sustainable moving forward.

SG&A expenses for the second quarter were $18.1 million or 9.9% of revenues compared to $17.2 million or 8.9% of revenues in the prior year. SG&A grew due to increased compensation expense, partially offset by lower consulting expense related to the management transition. Net loss for the quarter was $0.3 million or a loss of $0.01 per diluted share compared to a net loss of $3.1 million or a loss of $0.10 per diluted share in the prior year. This result included $4.3 million or $0.13 diluted earnings per share of non-recurring items. Excluding these items, second quarter 2023 adjusted net loss was $4.5 million or $0.14 loss per diluted share. EBITDA for the second quarter was $7.6 million and adjusted EBITDA was $3.7 million.

Turning to bidding metrics, in the second quarter, we bid on approximately $762 million worth of opportunities, and won $534 million with our Hawaii drydock project added to backlog. This resulted in a contract value weighted win rate of 70% and a book to bill ratio 2.9 times for the quarter. As of the end of June, our backlog was $818.7 million, a 75% increase over the backlog at the end of the first quarter.

Breaking out our second quarter backlog, $614.9 million of this was in our marine segment with $203.8 million in our concrete segment. Furthermore, we have been awarded over $84 million for new project work, not included in our backlog at the end of the second quarter. Of this, approximately $39 million is related to marine, with $45 million related to concrete.

Moving on to our balance sheet. As of June 30, we had approximately $8.9 million of cash and $36.9 million of outstanding debt.

In relation to our new debt facility, we incurred $5.9 million of debt issuance cost that will be amortized over the life of the agreement. As of the end of the quarter, we had no outstanding borrowings under our revolver. As we look ahead to the second half of the year, we're optimistic. As Travis said, we expect to see quarter-over-quarter improvements throughout the year as we realize the benefits of our strategic initiatives. While the low bidding volume in the dredging market continues to impact our industry, our recent wins will enable us to get more of our fleet to work in the coming months, and we are excited as Hawaii ramps up and contribute significantly to our second half.

With that, we'll open the call to your questions, Dustin?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Joe Gomes, Noble Capital.

Joe Gomes ***Noble Capital Markets - Analyst***

So I just wanted to just clarify some stuff here on the concrete segment. You talked about it being profitable basically since March, but if I'm looking at the tables in your release, it says concrete segment had an operating loss of about $1.5 million in the quarter. So when you say profitability, you're just talking about on the adjusted EBITDA basis and when do you forecast that on an operating income basis, the concrete segment will turn profitable?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***

Yeah, Joe, that's right. We're thinking about it on an adjusted EBITDA basis. In terms of when it might turn profitable on an operating income basis, I don't know that. I'm going to call a month there, but I do think that we can see continued improvement in that business. We think that the opportunities in front of it are pretty significant. And the strides that we've taken to improve the margins there, as we've said, we think are going to stick. So we expect continued improvement in that business, and we'll close that gap over time.

Joe Gomes *Noble Capital Markets - Analyst*
Okay. Thank you for that. And are you completely out of central Texas or is there still a few more things that you need to finish up there?

Travis Boone *Orion Group Holdings Inc. - President & CEO*
We're wrapping up. I think we have two, maybe two or three projects kind of in the final throes of completion here. They should be wrapped up, I believe, in the next month or so. We're almost out.

Scott Thanisch *Orion Group Holdings Inc. - EVP & CFO*
Yeah, the punch list work, there's not really any significant backlog associated with central Texas remaining.

Joe Gomes *Noble Capital Markets - Analyst*
Okay, great. And one more, if I may. You talked about some of the monetizations, East West Jones, Baytown, Port Lavaca South, when all of those are said and done, how much cash do you think they're going to bring in on the balance sheet?

Scott Thanisch *Orion Group Holdings Inc. - EVP & CFO*
Yeah, so I think we've talked about the $25 million already that we did this quarter between the outstanding contracts that we have. And other things that we see as potential opportunities on the balance sheet, I think there's probably another $40 million to $50 million that we anticipate as realizable in the near term. So that's kind of what we're working towards in our goals right now.

Joe Gomes *Noble Capital Markets - Analyst*
Okay, great. Thanks. I'll get back in queue.

Operator
Julio Romero, Sidoti.

Julio Romero *Sidoti & Company - Analyst*
Hey, I wanted to start on the marine segment on how much revenue in the second quarter did you see from the Pearl Harbor drydock project and how much revenue do you expect to realize from that project in the third quarter?

Scott Thanisch *Orion Group Holdings Inc. - EVP & CFO*
Yeah, we don't talk on specific contracts really, but it was a pretty significant contributor to revenue in the second quarter and it should be more in the third quarter. I think that in the second quarter it was several tens of millions, but it's going to be more going forward. We'll have a more significant ramp in

the beginning of next year as we really start to start driving [parts].

Julio Romero ***Sidoti & Company - Analyst***
Okay. I appreciate the color that you can give there. And it was nice to see the $45 million of dredging contracts that you won recently for Texas and Louisiana. But your commentary, Travis, on the prepared remarks sounded a little bit kind of pessimistic on the pipeline of dredging bids. I don't know if you can just talk about that if it has gotten maybe a little better, worse or same as 30 months ago?

Travis Boone ***Orion Group Holdings Inc. - President & CEO***
I don't know if it's better, worse or roughly the same as it was three months ago. It's just been slow, quite frankly, slower than historic volumes to be clear. And that, as you know, it really impacted us in the second quarter. We had dredges sitting around, waiting there, waiting to go to work. Fortunately, we have -- we'll get most of our dredges busy with the contracts we've won recently. But we need to keep the bids go in so that we can keep those things moving when they are certain that currently it costs us a lot of money.

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
We are in an active dialogue with the Army Corps of Engineers, and we will certainly continue that. They understand both the need and the value to their purchasing program. It's getting a bit [flip-flopped] and getting the market in a more stable position.

Julio Romero ***Sidoti & Company - Analyst***
Got it. And just one clarification question. You talked about the dredging historically has been 20% of revenue and 30% of profit. I assume those metrics are for the marine segment standalone and not for Orion overall. Is that correct?

Travis Boone ***Orion Group Holdings Inc. - President & CEO***
It's actually overall.

Julio Romero ***Sidoti & Company - Analyst***
Oh, really. Okay. That's great to clarify that. Excellent. All right, well, thanks very much for taking my questions.

Operator
Dave Storms, Stonegate Capital Markets.

Dave Storms ***Stonegate Capital Markets - Analyst***
I'm just hoping we could touch on the burn rate for the backlog. I know the last quarter, you had mentioned that it's in the high $300 million. Is that expected to remain constant, maybe another $300 million or so the rest of the year? Is there any comment you can give on that?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***

Generally speaking and looking at our backlog, it's for the next 12 months, probably two-thirds. And I think that over the next six months now that two-thirds, it's probably the majority of that two-thirds. But I think that we typically are looking at backlog out longer than just the next few months. So where we see it right now in kind of a similar place and having a similar profile in terms of how it's going to schedule out is what we have typically seen in our business.

Dave Storms ***Stonegate Capital Markets - Analyst***
That's very helpful. Thank you. And then just sticking with the backlog, is there any sense that you could give us on what the margin expansion may look like specifically on the concrete segment in that backlog or -- do you want to comment on that?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
Well, in terms of how we're bidding jobs we've not given a whole lot of details around that. But our historical approach to bidding jobs, we are at several points higher than that in terms of how we're approaching our value in the marketplace right now. And we are being successful at those higher bid rates. So we'll see in our backlog over time, the rates coming up from our historical over the last 12 months up another kind of two to three points over those historical rates, I think is what we'll see is that kind of bears out.

Travis Boone ***Orion Group Holdings Inc. - President & CEO***
Yeah, as we burn off the backlog with some of those lower bid margins.

Dave Storms ***Stonegate Capital Markets - Analyst***
That's very helpful. Thank you. One more, if I could. You mentioned that in your concrete segment, you're kind of waiting for the cost of capital to stabilize before you think the bidding environment picks up again. Aside from the Army Corps of Engineers kind of changing their stance, are there any catalysts that you're keeping an eye out for, for the marine segment to maybe pick up?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
I'm not sure if you had a question on the concrete side there specifically, but I'll just clarify, you know, we've seen quite a few bid opportunities on the concrete side. It's a matter of projects actually moving forward. We're bidding work. The projects tend to are lagging longer before -- before we get notice to proceed and things like that as developers and move forward with projects.

On the marine side, there's quite a few different catalysts active right now that we see with bidding opportunities picking up.

All the ports are scrambling on the eastern part of the US to expand because of the expansion of the Panama Canal. So bigger ships are able to come to the Panama Canal. So all the ports that utilize ships coming through there are scrambling to increase whether it's increased shipping channel depths or the size of their ports to bring bigger and bigger ships. And then with that, the private sector does the same, right?

All of the -- whether it's industrial, petrochem companies all along the Gulf and East Coast that they utilize ships that come through there, they're also scrambling to be able to bring in bigger ships. So they're all in the same boat with needing to expand the facilities. So you have that catalyst. Defense spending is continuing pretty rapidly, especially in the Pacific so that we expect that to continue ramping up. And then we've got the Infrastructure Act, IIJA, that's -- money -- we expect money to start flowing to projects in the relatively near future. So there's several catalysts on the marine side that we're very optimistic about.

Dave Storms ***Stonegate Capital Markets - Analyst***
That's incredibly helpful. Thank you for the clarification and thank you for taking my question.

Operator
(Operator Instructions) Alex Rygiel, B Riley FBR.

Alex Rygiel ***B Riley FBR - Analyst***
Can you -- first on the Hawaii project, is the profit recognition along the same trajectory as the revenue?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
In terms of physical progress, it's a little bit different. The revenue recognition has a few different drivers. Physical progress is kind of that 2.5 year fairly steady as we drive pile over that timeframe. And we can report on that as we go, but revenue recognition largely aligned, but there'll be some differences early in the project as we have some mobilization related revenues.

Alex Rygiel ***B Riley FBR - Analyst***
Okay, and then can you talk a bit about the cash needed for working capital in the Hawaii project?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
Sure. Yeah. In terms of our expectations of the level of working capital investment needed, I think we've talked before about between $5 million to $10 million of working capital investment. When we were negotiating those contracts, we were very careful to include in that good cash dynamics and terms for us both with the JV partner and the JV with the Navy. So we have a fairly short period of time that we have to wait for some of our revenues, and that helps to ease a little bit of the depth necessary for working capital.

Alex Rygiel ***B Riley FBR - Analyst***
And then lastly, what's your CapEx budget for this year and next?

Scott Thanisch ***Orion Group Holdings Inc. - EVP & CFO***
Good question. This year, I would say that our year-to-date CapEx is relatively low, considering where we have historically been. I think historically you would typically see us around $15 million of annual CapEx. I think that that's probably a good number for us on a normal year. And I would expect that we'll get a

little more spending in the back half of the year, although we won't quite approach that level for this year. Next year, I expect we'll probably see a little bit more spending and we're working through the plans on that right now, not quite ready to talk about it, but we'll get there closer to the end of the year.

Alex Rygiel *B Riley FBR - Analyst*
Perfect. Thank you very much. Nice quarter.

Operator
(Operator Instructions) David Wright, Henry Investment Trust.

David Wright *Henry Investment Trust - Analyst*
Good morning. There was a press release from the company not quite two years ago about a couple of contracts. One is State Road 405 Indian River Bridge and the other was Berth 6 Expansion. There were a couple of nice-sized contracts that were supposed to go on for two or three years. I was wondering, could you give us an update on the status of each of those and whether you've had any snags or not?

Travis Boone *Orion Group Holdings Inc. - President & CEO*
Quite frankly, I've only been here nine months, I'm not familiar with either one of those projects. Those press releases were reported before my time and they must be complete because I'm not familiar with them at all. So wish (multiple speakers) so I had a better answer for you. They must be complete or something. Because I'm -- or maybe we know them by different names, right? I'm not familiar with those two projects.

David Wright *Henry Investment Trust - Analyst*
The first $125 million over the NASA Causeway near Cape Canaveral --

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Travis Boone *Orion Group Holdings Inc. - President & CEO*
Oh, yes. Thank you. That's helpful. I know that when that's not the Causeway one in our terminology. So that project is going really well.

We reached a big milestone here a couple of months ago with -- there's two -- it's a side-by-side bridges so we completed the first bridge here a couple of months ago ahead of schedule. And there's actually quite a bit of press from Florida DOT about that one. They were really excited to get that one open. We're now in the demo phase of the existing bridge and expect to get to the second bridge open ahead of schedule as well. So that project is going very well.

David Wright *Henry Investment Trust - Analyst*
Okay. The other one, maybe you'll notice Port Arthur? Port Arthur, Berth 6 Expansion project, $67 million?

Travis Boone *Orion Group Holdings Inc. - President & CEO*
Yep, it's under construction right now. We're making good progress on it. And I'm not sure if I have more

details on that other than we're making good progress on that project.

David Wright ***Henry Investment Trust - Analyst***

Well, great. Thanks for updating those two large contracts and good luck as you continue moving forward with your turnaround plans. Thanks for taking my questions.

Operator

(Operator Instructions) And with that, being said, there are no further questions at this time. Mr. Boone, I turn the call back over to you.

Travis Boone ***Orion Group Holdings Inc. - President & CEO***

Thank you. I just wanted to close with we are really proud of the progress we've made with transforming this business to be healthier, profitable incentive for future success. We've been doing what we said we would do, and the results are starting to show. Our team has been working hard to make it all happen, and we appreciate all of their efforts to make us a stronger company.

Operator

This now concludes today's conference call. You may now disconnect.
