Acorn Energy

Q1 2021 Earnings Conference Call

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CORPORATE PARTICIPANTS

Tracy Clifford - *Chief Financial Officer, Chief Operations Officer, Omni Metrics Subsidiaries*

Jan Loeb - *Chief Executive Officer*

PRESENTATION

Operator
Good day ladies and gentlemen. Welcome to the Acorn Energy First Quarter Conference Call. At this time all participants are in listen-only mode. Should you need assistance, please signal conference specialist by pressing star, then zero. Later, we will conduct a question and answer session and instructions will be given at that time. As a reminder, today's conference is being recorded.

I would now like to turn the conference over to Tracy Clifford, CFO of Acorn Energy and COO of its Omni Metrics Subsidiaries. Please go ahead.

Tracy Clifford
Thank you and welcome everyone, to today's conference call. As a reminder, many of the statements made in today's prepared remarks are in response to your questions may be forward looking. These statements are subject to various risks and uncertainties. For example, the operating and financial performance of the company in 2021, and future years is subject to factors such as risks associated with disruptions to business operations and customer demand, resulting from the impact of the COVID19 pandemic, executing the company's operating strategy, maintaining high renewal rates, growing our customer base, changes in technology, changes in the competitive environment, financial and economic risks as well is having access to sufficient capital for growth.

Forward looking statements are based on management's beliefs as well as assumptions made using information currently available to management pursuant to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995. There are no assurances that Acorn or Omni Metrics will be able to achieve their growth goals in 2021, nor in future years. The company also undertakes no obligation to disclose any revisions to the forward looking statements to reflect events or circumstances after the date made. A full discussion of the risks and uncertainties that may affect the company is included in risk factors on Acorn’s form 10-K as filed with the Securities and Exchange Commission.

Now, I'll turn the call over to Jan, Acorn’s CEO. Jan?

Jan Loeb
Thank you, Tracy. Good morning. And thank you all for joining today's call. Acorn is off to a strong start this year, building on our progress in 2020, which is 27% revenue growth in the first quarter, as well as positive profitability on a consolidated basis, representing both year-over-year and sequential improvements. And once again, we were operating cashflow positive. We believe are improving performance in recent quarters confirms that the company is well positioned to achieve continued profitable growth and to generate positive cash flow throughout fiscal 2021 and moving forward.

Q1 revenue increased by $367,000 over Q1 2020, and we were able to bring more than 80% of that increase to the bottom line. This performance demonstrates the leverage of the business model we have built, as well as our disciplined lean cost structure. Importantly, we have achieved our goal of positioning Acorn as a growing cash generating and self-funding business with attractive margins and recurring revenue streams. Our gross margin improved to 71% in Q1 2021 from 69% in the prior year period, due to higher margin product sales from next generation products such as our Hero-2 pipeline monitor, and our premier industrial and commercial generator monitor, True Guard Pro.

We continue to invest in R&D and new product initiatives, which extend our technology leadership and competitive advantage and help drive long-term sales growth and margins. Other recent new product launches include our smart enunciator for critical electrical systems, and an upgraded release of our Omni Pro data management software for pipelines. We believe that the outlook for our products will improve as we progress through fiscal 2021, as the impact of COVID-19 subsides and business conditions gradually normalize.

To position ourselves for the reopening of the economy, we added two new sales engineers in the first quarter to support business development efforts in both our power generation monitoring and corrosion protection of our pipeline monitoring segments. We are already seeing benefits from these hires and the opening of businesses both in terms of customer dialogues and meetings. And we also are taking steps to support sales of our Air Guard air compressor monitor solution, which is still in its early stages of commercialization.

Our financial position remains strong with catch of approximately $2 million and no outstanding credit line debt. We generated $68,000 of net cash from operating activities and paid off our receivables factoring line in the first quarter, eliminating the outstanding balance of $149,000 at year end 2020. And we chose to not renew the line upon its expiration. We feel we have developed a strong financial footing on which to grow our business and to consider value enhancing growth opportunities, which could include partnerships or possible tuck in acquisitions to strengthen our position in the IoT space.

We are very disciplined in considering such opportunities in order to ensure that they meet our risk reward profile and are accretive to earnings and shareholder value within a reasonable period of time, if not immediately. Given our steadily improving operating results, financial strength, and the significant and under penetrated markets in which we operate, I am very enthusiastic about our business and about our prospects. We also think we are in somewhat of a sweet spot, considering the environmental benefits of our business model and the Biden Administration's renewed focus on environmental issues and infrastructure.

Having moved the business into profitability, we are also position with a large NOL of nearly $70 million to shield our taxable income and enhance our cash flows. And the NOL tax asset could become even more valuable if corporate tax rates were to increase. Ultimately, the strength of our business derives from the substantial value and environmental benefits that our remote monitoring solutions delivered to customers versus alternatives, which are typically expensive, ongoing physical inspection by teams out in the field, or even worse, little or no monitoring of critical assets. We feel that we offer a strong value proposition to commercial, industrial and residential markets, where remote monitoring solutions still have relatively low levels of penetration.

Certainly the reopening of the economy and more normalized business activity should provide a springboard for our growth plans. As a result, we see significant near and long term growth opportunities and believe we can grow the business at an average annualized rate of 20% or more in 2021, and for years to come, while maintaining our operating discipline and generating very attractive cash flows and net income. Historically, Q1 tends to be our slowest quarter in terms of business volume, and we see no reason why 2021 would be any different. Sales of new hardware units fueled our growth in Q1 partly due to the snap back from lower levels of equipment spending experienced last year, as well as to our sales initiatives at Omni Metrics. And we expect this trend of stronger equipment sales to continue in coming quarters. In fact, we are seeing positive growth trends across the business in early Q2.

With that overview, I'll turn the call back to Tracy Clifford, our CFO, to review our financials in more detail. Tracy?

Tracy Clifford
Thanks, Jan. As most of you know, today, we released our first quarter 2021 results in a press release and also filed our 10-Q with the SEC. I'll review some financial highlights compared to the first quarter of 2020. Omni Metrics revenue grew 27% to $1.7 million in Q1 ‘21 from $1.3 million in Q1 ‘20 due to a 57% increase in hardware revenue and a 13% increase in monitoring revenue. The increased hardware revenue was due in part, to the sale of custom units designed to one specific customer specifications to allow them to monitor these units themselves and an increase also in the sale of accessories. These revenues are recognized at the point of sale and not deferred over the life of the unit, based on the fact that they are sold uniquely by themselves.

There was also an overall increase in sales of next generation monitors including our Hero-2 pipeline rectifier monitors. The increase in monitoring is due to a growing number of installed and billable connections that results from new hardware sales, shift in our sales concentration from residential to commercial and industrial that we've talked about for several quarters, and the restructuring of our data plan. Gross Profit increased 31% in Q1 ‘21 versus Q1 ’20 driven by, as I noted previously, an increase in sales to commercial and industrial customers versus residential customers. And that increase I noted in accessory sales, leading to higher hardware margins combined with growth in high margin monitoring revenue.

The gross margin on monitoring increased to 86% in Q1 ‘21 from 84% in Q1 ‘20 with a higher concentration of the commercial and industrial revenue segment. Gross margin on hardware increased to 49% in Q1 ‘21 from 39% in the prior year period due to increase sales of next generation monitors and customized units that provide higher margins due to enhanced features, functions, and customer value. Omni Metrics' operating expenses decreased 3% to $943,000 in Q1 ‘21, principally due to $55,000 decrease in SGA expenses related to travel and tradeshow expenses, which were partially offset by a $23,000 increase in R&D bringing product development.

We expect SG&A expenses will increase in future quarters as travel and tradeshow activities return to pre COVID levels and we continue to spend more dollars on upgrades and enhancements to our IT infrastructure. Omni Metrics generated operating income of $267,000 in Q1 ‘21 versus a loss of $53,000 in Q1 ’20, due to the increased revenue and strong gross margin and our lean operating structure. Acorn's corporate cross increased $20,000 to two $241,000 in Q1 ‘21, principally due to increased noncash stock compensation and audit and tax accounting fees, partially offset by a decrease in travel expenses.

Due to the improved performance at Omni Metrics, Q1 ‘21 net income attributable to Acorn shareholders improved by over $300,000 to $20,000, or zero cents per share from a net loss of $283,000 for a loss of $0.01 per share in Q1 ’20. As you may know, Acorn looks at cash basis sales to supplement our GAAP revenue metrics and particularly for insight regarding (INAUDIBLE). Cash sales differ from GAAP revenue because we generally defer and recognize revenue from hardware sales over the life of the unit, typically a three year period, and we defer and recognize revenue for monitoring contracts over the period of service, typically one year.

In Q1 ’21, our cash basis sales grew 23% to $1.6 million from $1.3 million in Q1 ‘20. By segment, cash basis sales for PG increased 27% to $1.4 million in Q1 ‘21 versus $1.1 million in the prior year period. CP cash sales increased 3% to $205,000 versus $200,000 in Q1 ‘20. Cash generated from operating activities was $68,000 and Q1 ’21, exceeding consolidated net income of $22,000, primarily due to non-cash expenses. Cash provided by operating activities was less than the same period in the prior year due to the timing and collection in the first quarter of 2020 of several significant customer receivable balances that we're outstanding at December 31st, 2019.

Also, during the first quarter of 2020, we aggressively focused on receivable collections and extending payables payment terms to conserve cash in the beginning phase of the COVID-19 pandemic. We had consolidated cash of approximately $2 million at the close of the quarter compared to $1.4 million last March and $2.1 million at yearend December 31st, 2020. As I noted previously, and as also Jan mentioned, we did pay off our AR credit line and elected not to renew that line following its February 28th expiration. We may in the future seek a revolving line with more favorable terms, but at this time, we believe the company's current cash and expected cash flow provides sufficient liquidity to finance our existing operations for the foreseeable future.

I’d just like to conclude my remarks by saying that we are very excited about how 2021 has started and we have the full confidence in our knowledgeable and seasoned sales and marketing team, our depth of engineering expertise and continuing to expand our product line, and the dedication of our support teams to customer service to execute successfully towards our growth goals, now that we're getting out from under the burden of COVID-19.

With that, I'd like to turn the call back to the operator to give you all an opportunity to ask any questions. Operator?

Operator
We will now begin the question-and-answer session. To ask a question, you may press star, then one on your touch tone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed, and you would like to withdraw your question, please press star, then two. At this time, we will pause momentarily to assemble our roster.

Our first question is from Richard Sosa, who's a private investor. Please go ahead.

Richard Sosa
Hi, Jan, Tracy, good morning. How are you?

Jan Loeb
Good morning, Richard. Good. Thank you.

Richard Sosa
Great. I just had a few questions. First, just wanted to make a statement. Nice work. I mean, I know you guys made money in the fourth quarter, but this quarter feels like it's the first true quarter of a positive net income. It's been a long journey and I just wanted to note that. And it's

hopefully something we can see in the foreseeable future. And from what I'm looking at right now, that is the case. So, just a few questions. One, I joined five minutes late. So, you might have mentioned it. What was the cash sales number for the quarter?

Jan Loeb
Tracy?

Tracy Clifford
Let me pull that. Hold on just a second. Let me get it out of my folder. Our cash sales were $1.6 million, compared to $1.3 million. And then, if you'd like it on a segment by segment basis, $1.4 million for PG versus $1.1 million, and then on CP, $205,000 versus $200,000 compared to the prior quarter.

Richard Sosa
Okay. That's great. Just on the—you had mentioned on the travel, do you expect conferences and things like this, have you seen them in person conferences happening? I mean, I know that's a big driver for sales. Are they starting again? I mean, I know this is the season for the CP units to go out there and go to these nice conferences and things. Have they been picking up?

Tracy Clifford
We have seen them picking up as far as plan date for the fall. There's also been some online conferences, but we are seeing more of the routine annual conferences occur being scheduled late summer and early fall. Jan, do you have anything to add to that?

Jan Loeb
Yes. I just want to point out that three weeks ago was the EGSA conference, which was the electrical generator conference. And it was held to 200 people and we attended, a number of our salespeople and our CTO attended, which was very good, because none of our competitors were there. And we were exhibiting and so, we picked up a number of very good leads there. So, the answer to your question is, they are picking up. They're not anywhere near where they used to be, but we think it's a great opportunity, and our sales forces going there and participating.

Richard Sosa
And it's my last question, you had mentioned the press release, about one specific sale to a group, a hardware sale, why did they choose not to use the monitoring? And is that something that you do often or is it a onetime thing?

Jan Loeb
Let me just answer the why they did this, and then Tracy can answer about the onetime thing. And they are very careful about their firewall, and they want to have everything behind the firewall. So, that's why they, A, chose our technology, because we have the best technology. But they want to set it up that it's only monitored internally, not through our systems. So, it's a security issue with this very large customer. And I'll Tracy handle about ongoing sales with them.

Tracy Clifford
We did have sales from this customer in prior periods, just not to the level that we had in first quarter. And we do expect future sales from them throughout the remainder of 2021. We just

don't have any committed POs at the moment to provide any specific quantities. But we feel like they're a long-term partner.

Richard Sosa
That is a PG customer?

Tracy Clifford
Correct.

Richard Sosa
Perfect. All right. That's great. Thank you very much.

Operator
As a reminder, if you have a question, please press star, then one to be joined into the queue. The next question comes from Jeff Moore with Oak Capital. Please go ahead.

Jeff Moore
Hi, guys. I was curious if you could give an update or just general thoughts on the NASDAQ up listing that y'all had mentioned in prior presentations?

Jan Loeb
No real update right now. We do intend to do it. We hope to do it in this year. But it most probably will be done in conjunction with some other things. So, stay tuned, but it is still our game plan to have it done this year.

Jeff Moore
Okay. When you say in conjunction with some other things, what are those other things?

Jan Loeb
Most likely an acquisition or partnership or something like that. And also, the same thing, we would do a--in conjunction with that, we must--probably would do a reverse stock split. Get us over $5 a share. So, a number of things like that. We want to do it all in one shot.

Jeff Moore
Okay. So, you're thinking probably in the next seven months or so, I'm guessing?

Jan Loeb
Well, being that we are in May. But your math is good, but I would hope that it's sooner than December 31st, 2021.

Jeff Moore
Okay. Thank you. And then also, have you guys given any consideration to share repurchases before the NASDAQ up listing?

Jan Loeb
No, we have not.

Jeff Moore
Okay. That's it. Thank you.

Operator
The next question comes from Jack Mayer, who's a private investor.

Jack Mayer
Hello?

Jan Loeb
Good morning, Jack.

Jack Mayer
Good Morning. Congratulations. And let's think, been a very good quarter. A couple of questions. Can you comment on what you're doing geographically? Are you trying to expand outside North America at all, if you can just comment on that, generally?

Jan Loeb
It is not a focus of ours. I said on a previous call, that we have some orders in from Italy. They liked our technology and would like to become a distributor of ours in Italy, and maybe Southern Europe. We have some business in Mexico. But it's not a focus of ours. It requires a significant investment. There's a big time difference. People really like us for our customer support. And to set up a customer support with the time difference requires a decent investment. And right now, we feel that there's enough growth opportunity in North America, that that's where our efforts should be focused.

Jack Mayer
Excellent. When you talk about 20% plus growth, possibly. Do you view that in light of possible acquisitions, or do you think you can do that organically, separate from acquisitions?

Jan Loeb
That that is all organic.

Jack Mayer
That's all organic, excellent. The issue that was talked about before about this onetime event, with the customer wanting to retain the monitoring behind the firewall, is this something that you've come up with before? Is it a concern dealing with larger people altogether, if you can just comment on that?

Jan Loeb
We have come across it before. And we anticipate coming across it in the future. And for us, it really is a big positive for us. Because we charge the customer, since it's customized, we charge the customer more than what we would charge a customer for obviously a non-customized type product. Its impact is only, just to explain the accounting, it’s impact is while normally on a gap basis, we take in our revenue over, I’m talking about on equipment sales, over a three year period. So, you don't see the impact so much on this, because it's a non-monitored product. But we recognize the revenue as it's shipped.

So, it's a great deal for us. We're very happy the customers very happy with us. And I think we've done this in the past. It hasn't seen such an impact because it all wasn't necessarily in one particular quarter and it wasn't the magnitude of this order. But we expect to see it on an ongoing basis.

Jack Mayer
Got it. And then, finally, with respect to NASDAQ. You explained that you'd like to do it in conjunction with other things. But leaving that aside, are there any requirements that you need to make to be able to up list that you don't have at the moment? Would you need to raise more capital? Would you need to do anything, if you just wanted to up list?

Jan Loeb
Well, we would need to reverse with our stock, unless our stock goes over $5, just because people think our value is such. And yes, our capital base would need to be enhanced. Otherwise, we're good.

Jack Mayer
Got it. Okay. Thanks very much.

Jan Loeb
Thank you.

Operator
As a reminder, if you have a question, please press star, then one to be joined to the queue.

The next question comes from Bill Jones of Catalyst IR. Please go ahead. Mr. Jones, your line is open.

Bill Jones
Can you hear me?

Jan Loeb
Yes, I can hear you now.

Bill Jones
Okay. Thank you. We have a question that was emailed from a private investor. And the question is, it's known that some small and bigger tech firms are facing problems in their supply chain for chips, semiconductors. Are there any issues that you have, or do you have any plans to mitigate those impacts?

Jan Loeb
Yes. So, it's well known that there is some issues in semiconductor production in the United States. So, there's two things that I think we've done pretty well. Number one is, I think we were early in recognizing what the issues were. And so, we put in a significant amount of orders into our vendors very early on in 2021, ahead of our requirements for that particular quarter or what we would normally do. So, I think we have good POs at our vendors.

Now, obviously, we have to stay on top of our vendors to make sure that the vendors are getting the product that we've ordered, and so, we're doing that. And then also, we have tweaked our boards, and we have the ability to tweak our boards in order to use alternative parts. So, our engineers have that flexibility and we have done that in a certain instance and continue to do that. So, at least right now, I don't see a problem with us getting parts. But that's at least for now, and we certainly have to stay vigilant and on top of our vendors to make sure that they are producing the boards that we need.

Operator
At this time, I would like to turn the conference back over to Jan Loeb for any closing remarks.

Jan Loeb
Thank you. I just would like to conclude by saying, that although we're not out of the woods regarding COVID19 and economic uncertainties, we are off to a very good start in 2021. We are returning to more normal growth trends and expect to be net profitable on a consolidated basis for the year. We continue to see growth opportunities both internally and in adjacent markets, although we will always be prudent regarding find the right complementary and accretive opportunities. Again, I thank you for your interest in Acorn. We appreciate the support of our shareholders and I'm happy to speak with any potential investors about the company. You can contact our investor relations with any questions or to set up a call with me. Thank you again for your time today.

Operator, I believe this concludes our call.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.