Global Water Resources, Inc.
First Quarter Conference Call
May 9, 2019
CORPORATE PARTICIPANTS

Ron L. Fleming, President & Chief Executive Offer
Michael Liebman, Senior Vice President & Chief Financial Officer
Heather Krupa, Controller

CONFERENCE CALL PARTICIPANTS

Gerard “Gerry” J. Sweeney, Roth Capital
Jon Jung, Trailhead Asset Management

PRESENTATION

Operator:

Good morning, ladies and gentlemen. Thank you for standing by. Welcome to the Global Water Resources, Inc. 2019 First Quarter Conference Call. At this time, all participants are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue up for questions. If anyone has any difficulties hearing the conference, please press star, zero for Operator assistance at any time. I would like to remind everyone that this call is being recorded on May 9, 2019 at 1:00 p.m. Eastern Time.

I would now like to turn the conference over to Heather Krupa, Controller. Please, go ahead.

Heather Krupa:

Good morning, everyone, and thank you for joining us on today's call. Yesterday, we issued our 2019 First Quarter Financial Results by press release, a copy of which is available on our website at www.gwresources.com. Speaking today is Ron Fleming, President and Chief Executive Officer, and Mike Liebman, Chief Financial Officer. Mr. Fleming will summarize the key events of the quarter, following which Mr. Liebman will review the financial results for the quarter. Mr. Fleming and Mr. Liebman will be available for questions at the end of the call.

Before we begin, I'd like to remind you that certain information presented today may include forward-looking statements. Such statements reflect the Company's current expectations, estimates, projections and assumptions regarding future events. These forward-looking statements involve a number of assumptions, risks, uncertainties, estimates and other factors that could result—that could cause actual results to differ materially from those contained in the forward-looking statements. Accordingly, investors are cautioned not to place undue reliance on any forward-looking statements, which reflects Management’s views as of the date hereof and are not guarantees of future performance.
Ron Fleming:

Thank you, Heather. Good morning, everyone, and thank you for joining us today. We are very pleased to report our first quarter 2019 results. First and foremost, in the quarter, we again extended our employee safety and regulatory compliance non-recordable incident streaks, having now achieved over 631 consecutive days without a recordable safety accident and nearly 1,128 days since our last compliance violation. These remarkable achievements show the dedication and care of our employees as we deliver exceptional performance, both financially and operationally.

Further financial and operational highlights include, despite abnormally high precipitation levels, revenues increased 4% to $7.7 million. Net income increased $0.3 million or 102.8% to $0.6 million or $0.03 per share; continued our monthly dividend payouts equating to an annualized $28.6 per share; we collected the final payment due of $1 million dollars for the Loop 303 contract, which we sold in 2013, which is reflected in other income. For the trailing 12 months, total active connections increased 11.7% to 44,152 as of March 31, 2019, with organic connections are up for 4.8% in that period. In Q1, our annualized growth rate was 4.3%.

Moving on, I want to highlight permitting activity which is a precursor to organic growth. For 2018, single-family dwelling permits in Maricopa and Pinal counties were up to 22,437 units or 13% over 2017. The forecast remains strong for 2019 projected to see approximately 25,000 single-family dwelling permits. Importantly, the data for the City of Maricopa submarket continues to be strong. In 2018, permit growth was up another 18% over 2017 with 1,022 permits issued. This was the first time we have seen greater than 1,000 permits in the City of Maricopa since before the great recession. This acceleration supports our long-stated position that as sustained growth continues, we will get a larger and larger market share of new homes based on the significant amount of lot and infrastructure capacity that exist.

Before turning the call over to Mike to review the year-end 2018 financial performance in greater detail, I want to again layout our primary objectives. Global Water will continue to meet our primary mandates to provide safe, reliable and sustainable service to our customers and partners, while taking a disciplined approach to growth and value creation. We will do this through the following means: we'll work to grow recurring EBITDA by driving top-line revenue growth and while creating operational efficiencies in managing controllable expenses; we will make targeted capital improvements when necessary; as appropriate, we'll process great applications and see great recovery for all expenses and a return on all investment capital; we'll routinely analyze our dividend policy; and finally, we will pursue accretive acquisitions with consolidation benefits. Accretive tuck-ins such as this will complement the strong position and growth of our core regional assets. We're committed to continue to pursue similar opportunities, both big and small. Additionally, as proven by our recent acquisitions, this consolidation can help improve our industry as a whole and provide many benefits to the customers and communities we have the privilege to serve.
I will now turn the call over to Mike.

**Michael Liebmian:**

Thank you, Ron. Hello, everyone. Total revenues for the Quarter were $7.7 million, which was up $300,000 or 4% compared to Q1 of 2018. This increase is primarily driven by the organic connection growth, in addition to acquisition connection growth from Turner Ranches and Red Rock. These benefits were offset by a reduction to revenue as a result of tax reform, as well as higher precipitation in Q1 2019 versus Q1 of 2018. Specifically, we saw 4.2 inches of rain in Q1 of 2019 compared to half an inch in Q1 of 2018.

On tax reform, if you remove the reduction to revenue or the impact of tax reform, revenues would have increased by $526,000 or 7.1%. Operating expenses in Q1 of 2019 were $6.5 million compared to $6.1 million in Q1 of 2018. This is an increase of $463,000 or 7.6%. Notable changes in operating expenses include increased operating and maintenance costs of $273,000. This increase was primarily driven by the additional costs associated with the Turner Ranches and Red Rock acquisition of $177,000, as well as an increase in utilities, property tax and contract services, which all increase as revenue increases. Additionally, we had increased depreciation expense by $212,000 due to increase in fixed assets associated with the capital expenditure plan, as well as the acquisitions of Red Rock and Turner Ranches.

Now to discuss other expense. Other expense for Q1 of 2019 was $208,000, which was a decrease of $695,000 compared to 2018. The decrease was primarily due to the $1 million of other income received from the Loop 303 contract, offset by a decrease in the Valencia earn out of $219,000. Turning to net income, Global Water had a net income in Q1 of 2019 of $649,000 or $0.03 per share compared to $320,000 or $0.02 per share in Q1 of 2018.

Adjusted EBITDA, which adjust for non-recurring events, such as Loop 303 proceeds and also adjusts for option expense and our equity investment in Fathom, was $3.4 million in Q1 2019, which is down $251,000 or 6.8% compared to Q1 of 2018. Adjusted EBITDA was down primarily due to the impacts of tax reform of $231,000, and the lost income from Valencia earn out of $219,000.

Additionally, to have a precipitation in Q1 of 2019 versus 2018 was another factor. These reductions were offset by increases in organic growth of 5.2%, as well as the acquisition growth from Red Rock and Turner Ranches. One subsequent event that I'd like to point out is that we were able to extend $8 million line of credit until April 30, 2022. Previously, it was set to expire on April 30 of 2020, so we extended the line an additional two years. This line is currently unused.

This concludes our update on Q1 2019 results. I'll now pass the call back to Ron.

**Ron Fleming:**

Thank you, Mike. It is clear, excluding the revenue reductions caused by abnormal precipitation, federal tax reform and corporate rate reductions, and the slowdown of our Valencia earn out, all items that are beyond our control, Global Water's top line in connection growth rates continue to be very strong. As we handle the cycles, we intend to remain at the forefront of the water management industry and advance our mission of achieving efficiency and consolidation. We truly believe that expanding our platform and applying our expertise throughout our regional service areas into new utilities will be beneficial to all stakeholders involve. We appreciate your investment and support of us as we grow Global Water to address important utility, water resource and economic development issues in Arizona and potentially beyond.
These highlights conclude our prepared remarks. Thank you. Mike and I are now available to answer your questions.

Operator:

We will now begin the question-and-answer session. During the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you're using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

The first question is from Gerry Sweeney with Roth Capital. Please, go ahead.

Gerry Sweeney:

Hey, good morning, Ron and Mike. Thank you for taking my call.

Ron Fleming:

Hey, good morning, Gerry.

Gerry Sweeney:

On the precipitation side, will you—would you be able to sort of bracket out maybe how much it affected volumes within your main operations?

Michael Liebman:

Yes. Gerry, on the residential side, in 2018 customers we’re using roughly 58,000 gallons—or 5,800 gallons on average each month, and in 2019, it was 5,300 gallons. It was about 540-gallon less usage on the residential side. Obviously, hard to pinpoint specifically how much it's behavior versus precipitation, but we believe it's precipitation related. If you try to extrapolate that out to a dollar, just coming somewhere in that $150,000 to $200,000 is a good estimate.

Gerry Sweeney:

Okay, yes. I've seen precipitation hit some other utilities in the past. I mean, it does play a role and so it actually makes sense. Then just two other quick ones. Obviously, Valencia, I mean, it had faster growth in the past. Real estate ebbs and flows, but have you been watching the permitting activity over in their section of suburban Phoenix? Have you seen anything or any thoughts on maybe—there maybe a shift at some point in the future?

Ron Fleming:

Yes, no. Permitting data in that specific area remains down. It is interesting, Gerry, because we're overall, through the stats we talked about earlier on the call, Metro Phoenix as a whole and in certain pockets is still continuing to see the same type of permit activity we've seen for the last few years, if not accelerating. But in that exact area where we sell the utility, it is down and it remains down. We do think based on its location and based on kind of growth patterns and the fact—that happened is—that's why the earn out was so high for few years. They blew through all available lot so fast that they basically have run out and Guelph (phon) has move to a few other surrounding communities while land developers get the next communities ready.
We think it's only a matter of a year or two before they can get those, right? Can't build a home where they're not a lot. They're getting those lots prepared and we'll start to see that growth pick back up. But at this point, we would say it's probably a few years away.

Gerry Sweeney:

Yes, that makes sense. Juxtapose to that, I mean, you're seeing there's a lot of growth in Chandler and Gilbert. I think a bunch of companies are moving into those areas as well which should benefit Maricopa, correct?

Ron Fleming:

Absolutely. Yes, there is no doubt. Chandler is—and Gilbert and all of—then Tempe—all those Southeastern cities that are the next concentric ring north of Maricopa that we benefit from. They are all doing amazing things. We feel pretty good about the growth rate that we're seeing in Maricopa for the foreseeable future.

Gerry Sweeney:

Just another one, a quick one for Mike—the line of credit, can you give little details? I know it’s undrawn, but how much was it for and just interest rate, just for…

Michael Liebman:

Yes, it's an $8 million line and it's at LIBOR plus 2.25%.

Gerry Sweeney:

Got it.

Michael Liebman:

Just the rate.

Gerry Sweeney:

Thank you, guys. Really appreciate taking my call. Thank you.

Michael Liebman:

Sure.

Operator:

The next question is from Jon Jung with Trailhead Asset Management. Please, go ahead.

Jon Jung:

Good morning, Mike and Ron. Good job on the quarter. I appreciate what you're doing for shareholders. Wonder if you could give us any estimate on what you think the Fathom asset is worth. It's not shown, I don't think, of any value on the books, so it is kind of a hidden asset, isn't it?
Michael Liebman:

Yes, that's correct, Jon. We have it on our books for less than $100,000 I think at this point in time, so it's not showing. But clearly, there is—based on our understanding and what we've seen happen in the past, there's clearly value there. Depending on what's to come with Fathom, if and when they do another capital raise, et cetera, it will give us a better perspective, but we do believe there's value there, yes.

Jon Jung:

What would the value be at the last capital raise that they did of the 7% that you own today?

Michael Liebman:

Yes. Ron, you can correct me if I'm wrong, but I think the last time I remember, I think the valuation was about $80 million or so, is when the last capital raise was done, somewhere around there.

Ron Fleming:

Yes. I think it was around $80 million.

Michael Liebman:

Yes.

Jon Jung:

The 7% would be worth $5 million or $6 million?

Michael Liebman:

That's the math, yes.

Jon Jung:

That's good math. I don't think a lot of people recognize that that still doesn't show up on the books, but hopefully at some point in time, that will provide some growth capital for the Company.

Ron Fleming:

Absolutely, Jon. It's what we believe as well.

Jon Jung:

Good. Are there any color or updates you can give us on your acquisition activity or is there anything in the pipeline now? I haven't seen anything announced recently.

Ron Fleming:

Yes. Look, I mean, I think we haven't talked about the pipeline for a while because we've been talking about the several that we closed just late last year. But those—the way we described it in the past is still the way it exists today, which is we basically sorted through the criteria that we're looking for, with all of
the opportunities throughout the state. We ranked the top few dozen and started conversations with a dozen of them and we got four. It was pretty good success right there.

Now, we're circling back and going back through that list. I would just say, in general, sure, there's half dozen, dozen utilities that are worth continuing to talk to. With these things, they are kind of slow by nature, so I don't like to get too much out in front of it. But I think if we can continue to get, 5%, 10% connection growth rate on the acquisition side and 5%—4% or 5% on the organic growth side and be north of our low double digits, that would be something that we're attempting to do.

Jon Jung:

Okay. All right. At this point in time, you have not—is it correct that you haven't gone outside of the Arizona state for looking at acquisitions?

Ron Fleming:

That's correct. We thought we'd see through our efforts here first before doing that.

Jon Jung:

Okay.

Michael Liebman:

Jon, that doesn't mean…

Jon Jung:

All right, great. All right, great.

Michael Liebman:

If the right opportunity presented itself, we'd obviously be open to it in determining if it's a good play to make it into a different state, but we're going to focus first on what's in Arizona.

Jon Jung:

All right. Thank you.

Ron Fleming:

Thanks, Jon.

Operator:

This concludes the question-and-answer session. I would like to turn the conference back over to Ron Fleming, President and CEO, for any closing remarks.

Ron Fleming:

Yes. Thank you, Operator. I would like to thank everyone for participating on this call today and for your ongoing interest in Global Water. Thank you and we look forward to speaking with you again.
Operator:

This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.